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BOARD OF DIRECTORS' REPORT

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This report was prepared with Word for Windows 6.0. All tables were created in Excel 5.0 and either embedded in the document or linked to master spreadsheets. Additionally, most of the channel and product group tables were generated via automation from the general ledger. Each of these automated tables is made accurate in its calculations by using data at a lower level than the rounded amounts shown in this report. These lower level amounts are used to calculate variances and are then rounded and displayed in this report. Therefore, individual amounts are rounded perfectly but totals and variances may not foot precisely. All other tables have individual numbers that may be rounded. While these individual numbers may not be precisely to supporting schedules, they will foot exactly as shown in this report.

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Results of Operations

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COMPARISON WITH PLAN

Income Statement

Q94-2 (in millions)

	Actual		Plan		Variance	
	\$	%	\$	%	\$	%
Net revenue	\$1,129	100.0 %	\$1,106	100.0 %	\$23	2 %
Cost of revenue	185	16.4	193	17.5	8	4
Gross profit	944	83.6	913	82.5	31	3
People expenses	273	24.2	302	27.3	29	10
Facilities expenses	83	7.4	93	8.4	10	11
Marketing expenses	103	9.1	109	9.9	6	6
Other expenses	70	6.0	74	6.7	4	5
Total expenses	529	46.9	578	52.3	49	8
Contribution margin	415	36.8	335	30.3	80	24
Nonoperating income	23	2.0	23	2.1	0	0
Income taxes	149	13.2	122	11.0	(27)	(22)
Net income	\$289	25.6 %	\$236	21.3 %	\$53	23

FYTD94 (in millions)

	Actual		Plan		Variance	
	\$	%	\$	%	\$	%
Net revenue	\$2,112	100.0 %	\$1,933	100.0 %	\$179	9 %
Cost of revenue	344	16.3	328	17.0	(16)	(5)
Gross profit	1,768	83.7	1,605	83.0	163	10
People expenses	536	25.4	606	31.4	70	12
Facilities expenses	160	7.6	184	9.5	24	13
Marketing expenses	191	9.0	197	10.2	6	3
Other expenses	123	6.0	148	7.7	25	17
Total expenses	1,010	47.8	1,135	58.7	125	11
Contribution margin	758	35.9	470	24.3	288	61
Nonoperating income	42	2.0	42	2.2	0	0
Income taxes	272	12.9	173	8.9	(99)	(57)
Net income	\$528	25.0 %	\$339	17.5 %	\$189	56

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Results of Operations

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COMPARISON WITH PLAN

RESULTS OF OPERATIONS SUMMARY- QUARTER (IN MILLIONS)

Channel

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$417	103 %	\$318	99 %	\$170	106 %	\$115	119 %
Europe FG	324	87	273	89	173	90	114	91
ICON FG	61	75	44	72	20	62	7	42
Far East FG	54	118	40	120	19	159	1	NM
OEM	268	138	249	133	229	133	161	182
Other	6	81	20	464	(5)	NM	17	122
Worldwide	<u>\$1,129</u>	<u>102</u>	<u>\$944</u>	<u>103</u>	<u>\$606</u>	<u>109</u>	<u>\$415</u>	<u>124</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	37 %	37 %	76 %	80 %	41 %	40 %	28 %	24 %
Europe FG	29	34	84	82	54	52	35	33
ICON FG	5	7	73	76	34	40	12	22
Far East FG	5	4	74	73	35	26	3	(15)
OEM	24	18	93	96	85	88	60	45
Other	1	1	332	58	(84)	(202)	276	184
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>54</u>	<u>50</u>	<u>37</u>	<u>30</u>

Product Group

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$488	92 %	\$403	93 %	\$288	90 %	\$182	90 %
Database & Dev. Tools	85	92	69	93	25	98	6	118
Consumer	98	145	76	141	44	216	25	335
Workgroup	26	114	23	122	8	299	1	NM
Systems	419	112	350	109	239	124	169	142
Advanced Technology	3	64	2	55	(10)	NM	(11)	NM
Other	10	93	21	296	14	306	42	212
Worldwide	<u>\$1,129</u>	<u>102</u>	<u>\$944</u>	<u>103</u>	<u>\$608</u>	<u>111</u>	<u>\$415</u>	<u>124</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	43 %	48 %	83 %	81 %	59 %	60 %	37 %	38 %
Database & Dev. Tools	8	8	81	80	29	28	7	6
Consumer	9	6	77	79	45	30	26	11
Workgroup	2	2	90	84	32	12	5	(15)
Systems	37	34	84	86	57	51	40	32
Advanced Technology	0	0	70	82	(333)	(324)	(365)	(356)
Other	1	1	213	67	139	42	418	182
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>54</u>	<u>50</u>	<u>37</u>	<u>30</u>

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COMPARISON WITH PLAN

RESULTS OF OPERATIONS SUMMARY - YEAR TO DATE (IN MILLIONS)

Channel

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$704	103 %	\$541	99 %	\$275	117 %	\$178	139 %
Europe FG	585	93	488	94	303	100	197	104
ICON FG	127	91	97	92	50	106	27	122
Far East FG	114	125	86	128	42	165	8	NM
OEM	523	140	493	137	453	138	317	189
Other	58	467	62	862	(4)	NM	31	(120)
Worldwide	<u>\$2,112</u>	<u>109</u>	<u>\$1,768</u>	<u>110</u>	<u>\$1,120</u>	<u>123</u>	<u>\$758</u>	<u>161</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	33 %	35 %	77 %	80 %	39 %	34 %	25 %	19 %
Europe FG	28	33	83	82	52	48	34	30
ICON FG	6	7	77	76	39	34	21	16
Far East FG	5	5	75	74	37	28	7	(12)
OEM	25	19	94	96	87	88	61	45
Other	3	1	107	58	(7)	(254)	54	(210)
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>53</u>	<u>47</u>	<u>36</u>	<u>24</u>

Product Group

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$869	101 %	\$725	103 %	\$525	107 %	\$336	110 %
Database & Dev. Tools	164	93	127	89	48	98	12	118
Consumer	152	137	119	135	64	291	35	3,521
Workgroup	46	115	41	122	12	NM	(1)	NM
Systems	811	113	687	112	475	130	341	150
Advanced Technology	5	73	3	61	(18)	NM	(20)	NM
Other	64	337	65	506	29	372	54	NM
	<u>\$2,112</u>	<u>109</u>	<u>\$1,768</u>	<u>110</u>	<u>\$1,134</u>	<u>125</u>	<u>\$758</u>	<u>161</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	41 %	45 %	83 %	82 %	60 %	57 %	39 %	35 %
Database & Dev. Tools	8	9	77	81	29	28	7	6
Consumer	7	6	78	80	42	20	23	1
Workgroup	2	2	89	84	25	(1)	(1)	(27)
Systems	38	37	85	86	59	51	42	32
Advanced Technology	0	0	68	82	(353)	(458)	(385)	(490)
Other	3	1	102	68	45	41	84	(148)
	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>54</u>	<u>47</u>	<u>36</u>	<u>24</u>

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COMPARISON WITH PLAN

REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

Q94-2

	Revenue			Licenses			Revenue per License		
	Actual	Budget	% Var	Actual	Budget	% Var	Actual	Budget	% Var
WIN Office	\$260	\$182	43%	760	571	33%	\$342	\$320	7%
MAC Office	23	19	20%	65	54	20%	357	356	0%
Excel PU *	55	82	(33%)	267	477	(44%)	205	171	19%
Word PU *	99	122	(19%)	614	706	(13%)	161	172	(7%)
Graphics PU *	8	8	3%	51	47	9%	160	169	(6%)
Project PU	23	19	17%	66	63	6%	344	309	11%
DAD BU New Users **	<u>468</u>	<u>432</u>	8%	<u>1,823</u>	<u>1,917</u>	(5%)	256	226	14%
WIN Office	49	26	87%	311	130	140%	157	202	(22%)
MAC Office	3	3	(6%)	18	14	27%	178	241	(26%)
Excel PU *	9	35	(75%)	149	548	(73%)	57	63	(10%)
Word PU *	41	49	(16%)	487	529	(8%)	84	92	(9%)
Graphics PU *	0	1	(88%)	8	93	(91%)	19	14	34%
Project PU	1	2	(43%)	10	29	(65%)	108	66	63%
DAD BU Existing Users **	<u>103</u>	<u>116</u>	(12%)	<u>983</u>	<u>1,343</u>	(27%)	105	87	21%
Basic PU	16	14	14%	110	94	17%	145	148	(2%)
Database Mgmt (Access) PU *	29	31	(9%)	216	172	26%	132	183	(28%)
Fox Database PU *	13	24	(48%)	18	116	(85%)	705	210	236%
Languages PU's	18	18	(4%)	112	100	12%	156	183	(14%)
DBDT BU *	<u>75</u>	<u>88</u>	(15%)	<u>457</u>	<u>483</u>	(5%)	164	183	(10%)
Entry PU	43	24	80%	1,278	640	100%	34	37	(10%)
Multimedia Publishing PU	21	9	130%	365	153	138%	56	58	(4%)
Works PU	24	29	(15%)	425	396	8%	57	73	(21%)
Consumer BU	<u>88</u>	<u>62</u>	43%	<u>2,068</u>	<u>1,189</u>	74%	43	52	(18%)
Hardware BU	<u>38</u>	<u>48</u>	(21%)	<u>650</u>	<u>692</u>	(6%)	59	69	(16%)
MS-DOS BU	<u>46</u>	<u>34</u>	37%	<u>2,406</u>	<u>688</u>	250%	19	49	(61%)
Windows BU	<u>70</u>	<u>54</u>	29%	<u>1,273</u>	<u>847</u>	50%	55	64	(14%)
Win NT Family	5	42	(89%)	28	192	(86%)	171	220	(22%)
Win NT Adv. Server Family	7	10	(31%)	10	14	(26%)	679	725	(6%)
Win NT Server (SQL,SNA)	8	10	(12%)	28	9	206%	298	1,040	(71%)
Other Operating Systems PU	8	5	48%	31	22	43%	258	248	4%
Advanced Systems BU	<u>28</u>	<u>67</u>	(58%)	<u>98</u>	<u>237</u>	(59%)	289	284	2%
Workgroup BU *	<u>16</u>	<u>15</u>	1%	<u>399</u>	<u>199</u>	101%	39	78	(50%)
Digital Office Systems PU's	0	3	(88%)	3	23	(87%)	96	110	(12%)
ACT and APD PU's	3	5	(36%)	149	143	5%	21	34	(38%)
Other PU's	1	4	(80%)	1	43	(97%)	763	96	694%
Other	<u>4</u>	<u>12</u>	(63%)	<u>153</u>	<u>208</u>	(26%)	28	55	(50%)
Finished goods revenue	936	929	1%	10,311	7,802	32%	91	119	(24%)
Other materials	<u>13</u>	<u>0</u>	n/a	<u>0</u>	<u>0</u>	n/a			
Total FG gross revenue	<u>948</u>	<u>929</u>	2%	<u>10,311</u>	<u>7,802</u>	32%			
Press	9	8	4%						
OEM gross revenue	257	195	32%						
Revenue adjustments	<u>(85)</u>	<u>(26)</u>	230%						
Net Revenue	<u>\$1,129</u>	<u>\$1,106</u>	2%						

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* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

Note: The Office revenue related to the Office Guarantee Program is included in the detail and the deferral amount is then pulled out through the revenue adjustments line.

COMPARISON WITH PLAN

REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

FYTD94

	Actual	Budget	% Var	Actual	Budget	% Var	Actual	Budget	% Var
WIN Office	\$415	\$308	35%	1,172	939	25%	\$354	\$328	8%
MAC Office	41	34	21%	112	94	19%	362	358	1%
Excel PU *	120	133	(10%)	635	754	(16%)	189	177	7%
Word PU *	182	189	(4%)	1,161	1,089	7%	157	174	(10%)
Graphics PU *	17	16	5%	112	96	16%	150	167	(10%)
Project PU	44	39	12%	136	127	7%	325	310	5%
DAD BU New Users **	<u>819</u>	<u>720</u>	14%	<u>3,328</u>	<u>3,098</u>	7%	246	232	6%
WIN Office	60	42	45%	414	210	97%	145	198	(26%)
MAC Office	5	6	(13%)	40	24	69%	127	248	(49%)
Excel PU *	18	47	(61%)	279	672	(59%)	66	69	(6%)
Word PU *	59	70	(16%)	679	745	(9%)	86	94	(8%)
Graphics PU *	1	2	(71%)	23	107	(79%)	31	22	40%
Project PU	2	3	(27%)	37	38	(4%)	62	81	(24%)
DAD BU Existing Users **	<u>145</u>	<u>169</u>	(14%)	<u>1,471</u>	<u>1,796</u>	(18%)	99	94	5%
Basic PU	35	28	24%	268	199	35%	129	141	(8%)
Database Mgmt (Access) PU *	47	55	(15%)	514	280	84%	92	198	(54%)
Fox Database PU *	31	55	(43%)	199	277	(28%)	157	199	(21%)
Languages PU's	34	30	10%	240	173	39%	140	176	(21%)
DBDT BU *	<u>147</u>	<u>169</u>	(13%)	<u>1,222</u>	<u>928</u>	32%	120	182	(34%)
Entry PU	65	40	62%	1,781	989	80%	36	40	(10%)
Multimedia Publishing PU	25	13	102%	447	213	110%	57	59	(4%)
Works PU	44	48	(7%)	764	665	15%	58	72	(19%)
Consumer BU	<u>135</u>	<u>101</u>	34%	<u>2,992</u>	<u>1,868</u>	60%	45	54	(16%)
Hardware BU	<u>75</u>	<u>92</u>	(19%)	<u>1,248</u>	<u>1,293</u>	(3%)	60	71	(16%)
MS-DOS BU	<u>64</u>	<u>64</u>	1%	<u>2,886</u>	<u>1,275</u>	126%	22	50	(55%)
Windows BU	<u>125</u>	<u>97</u>	29%	<u>2,244</u>	<u>1,491</u>	51%	56	65	(14%)
Win NT Family	24	81	(70%)	116	389	(70%)	210	209	0%
Win NT Adv. Server Family	12	18	(34%)	18	27	(31%)	665	691	(4%)
Win NT Server (SQL,SNA)	11	20	(47%)	65	22	199%	161	898	(82%)
Other Operating Systems PU	19	13	49%	81	60	36%	234	214	9%
Advanced Systems BU	<u>66</u>	<u>132</u>	(50%)	<u>281</u>	<u>497</u>	(43%)	235	266	(12%)
Workgroup BU *	<u>30</u>	<u>27</u>	9%	<u>837</u>	<u>377</u>	122%	36	73	(51%)
Digital Office Systems PU's	1	5	(83%)	8	45	(82%)	104	110	(5%)
ACT and APD PU's	5	7	(28%)	249	206	21%	21	35	(40%)
Other PU's	3	7	(62%)	8	69	(88%)	306	97	214%
Other	<u>9</u>	<u>19</u>	(54%)	<u>265</u>	<u>320</u>	(17%)	33	59	(45%)
Finished goods revenue	1,615	1,590	2%	16,772	12,941	30%	96	123	(22%)
Other materials	32	0	n/a	1	0	na			
Total FG gross revenue	<u>1,646</u>	<u>1,590</u>	4%	<u>16,773</u>	<u>12,941</u>	30%			
Press	14	14	(1%)						
OEM gross revenue	487	375	30%						
Revenue adjustments	<u>(36)</u>	<u>(46)</u>	(21%)						
Net Revenue	<u>\$2,112</u>	<u>\$1,933</u>	9%						

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* excludes allocation from sales of Office bundles
 ** includes database and MS Mail products sold through Office bundles
 Note: The Office revenue related to the Office Guarantee Program is included in the detail and the deferral amount is then pulled out through the revenue adjustments line.

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COMPARISON WITH PLAN

Q94-2

Revenue

- Worldwide OEM net revenue exceeded plan by \$74 million driven by demand for personal computers, while Worldwide FG net revenue fell below plan by \$51 million. Win Office 4.0 shipped in October and billings of \$60 million were deferred. These will be recognized as revenue when earned through shipments of Excel and PowerPoint upgrades.
- Desktop Applications, Consumer, MS-DOS, and Windows Business Units more than offset the below plan gross revenue from Database and Development Tools, Hardware, and Advanced Systems Business Units in Finished Goods.
- The Win Office 4.0 October release helped drive Desktop Applications' 4% positive gross revenue variance. The Excel 5.0 schedule slip to December and Word 6.0 sales performance offset the Win Office gains by \$53 million and \$31 million respectively.
- Consumer Business Unit had a strong quarter in sales. Even with aggressive sales planned for this quarter due to the holiday season, Consumer exceeded this plan by 43%. Flight Simulator sales in North America accounted for over half of this variance while Encarta 5.0 which was released in September, exceeded its plan by 229% and accounted for 25% of the positive variance.
- Database & Development Tools gross revenue was below plan primarily due to the Fox Database product unit. Japanese versions of Access and Visual C++ were released this quarter, driving strong sales in the Far East (Access sales were above plan by 242% in the Far East) and partially offsetting the shortfall.
- MS-DOS Business Unit exceeded its gross revenue plan by \$16 million due to strong sales of MS-DOS 6.2 in North America (and net of 335,000 MS-DOS 6.0 returns in North America).
- Windows for Workgroups 3.11 shipped in November. Windows 3.1 continued to have stronger than planned revenue.

Cost of Revenue

- Cost of revenue, as a percent of net revenue, was less than plan primarily due to decreased product costs for Desktop Applications in Europe. This was enough to offset the increased OEM costs. OEM costs increased from plan by 3% due to higher than anticipated Mouse sales, while the cost of FG revenue was 20%, as planned.

Controllable Expenses

- Controllable expenses remained below plan due to a positive headcount variance of 1,701, or 10%. All major groups were below plan: research and development (682), sales and marketing (650), general and administrative (198) and manufacturing and distribution (171).
- People expense was less than plan due to salaries (\$12 million), employee fringes (\$7 million) and supplies (\$3 million). Facilities was below plan due to depreciation (\$6 million) and telecommunications (\$2 million).
- Marketing was seasonally low, and underspending for other expenses consisted of a favorable variance for product development (\$16 million) offset by negative variances for miscellaneous expenses (\$7 million) and bad debt (\$6 million). The bad debt variance resulted from reserves for high risk OEM accounts.

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COMPARISON WITH PLAN

FYTD94

Revenue

- Worldwide OEM net revenue was \$149 million over plan as higher unit sales by the established OEMs continued to be spurred by aggressive competitive pricing for PCs.
- Worldwide Finished Goods gross revenue was 4% above plan. Desktop Applications, Consumer, and Windows Business Units more than offset the below plan revenue from the Database and Development Tools, Hardware, and Advanced Systems Business Units.
- The Desktop Applications Business Unit was 8% ahead of plan due to strong Win Office 4.0 sales (NA 35%, Europe 38%, ICON 26%, and FE 54% over plan). Office revenue more than compensated for the 23% and 7% shortfall to plan of Excel and Word Product Units, respectively.
- Consumer Business Unit was the leader of all business units in exceeding planned gross revenue on a percentage basis (34%, \$34 million better than plan). Flight Simulator and Encarta in North America accounted for 59% of the positive variance as strong sales were experienced through the holiday season.
- Windows Business Unit experienced strong sales in North America with Win 3.1 accounting for a \$28 million favorable revenue variance.
- Advanced Systems business unit was below plan by \$66 million. The resources required to run Win NT (16 megabytes of memory) seemed to be a bigger issue than anticipated when Win NT sales were planned. In addition, the wide array of applications needed to exploit Win NT are just now beginning to enter the market.

Cost of Revenue

- Cost of revenue, as a percent of net revenue, was less than plan primarily due to European product costs. Desktop Applications in Europe were lower than plan due to a higher than plan mix of licensed product.

Controllable Expenses

- Headcount has remained approximately 10% below plan throughout FY94.
- The favorable variance within People expenses included salaries (\$25 million), employee fringes (\$12 million) and travel and entertainment (\$12 million). Within facilities, depreciation was below plan by \$10 million. Telecommunications (\$5 million) and maintenance and repairs (\$3 million) were also below plan.
- Marketing was below plan driven by Q94-2. Product development was below plan by \$39 million, primarily in Systems (\$18 million), Advanced Systems (\$7 million), Database & Development Tools (\$5 million) and Consumer (\$5 million). In contrast, bad debt expense exceeded plan by \$11 million due to provisions for high risk OEMs.

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Results of Operations

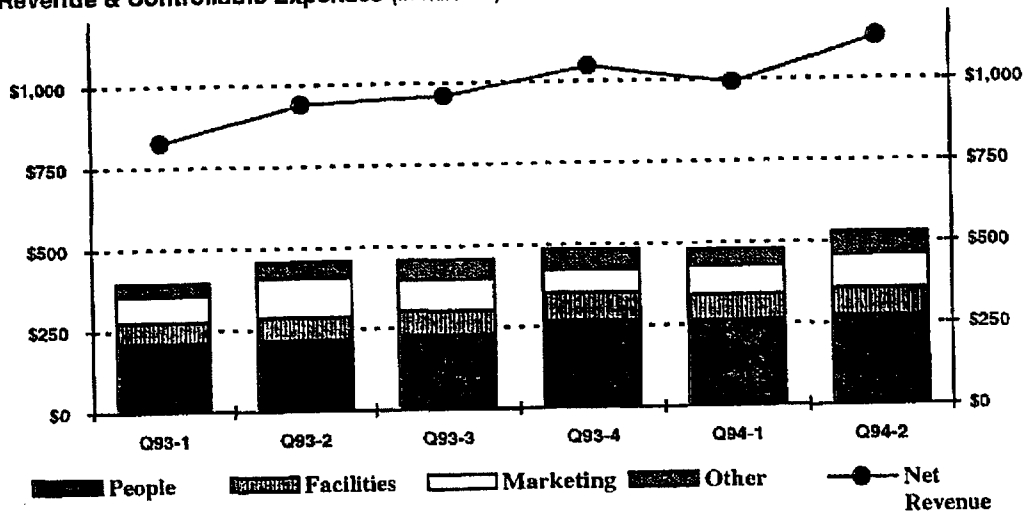
COMPARISON WITH PLAN

METRICS SUMMARY (DOLLARS ANNUALIZED IN THOUSANDS)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Net revenue per employee	\$275	\$299	\$287	\$294	\$271	\$308
People expense per employee	69	68	66	71	73	74
Facilities expense per employee	23	23	23	26	21	23
Marketing expense % net revenue	39%	49%	40%	27%	36%	37%
R&D expense % net revenue	51%	47%	48%	53%	54%	53%
PSS Expense % net revenue	19%	18%	18%	20%	22%	20%

TREND ANALYSES

Net Revenue & Controllable Expenses (in millions)



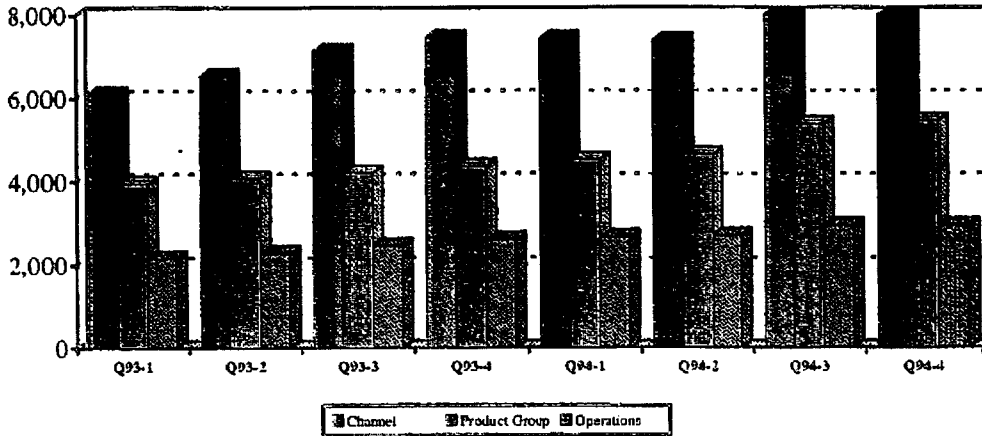
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- Q93-1 included favorable foreign exchange rates (\$34 million) and continued growth for Windows applications offset a reduction in Windows 3.1 revenues. Q93-2 revenues increased from \$818 million to \$938 million due to strong sales of Office which increased \$46 million, and the release of Access. Q93-4 was the first quarter to break \$1 billion in revenue due to the late March release of the MS-DOS 6.0 Upgrade.
- Q94-1 revenue decreased as there were no major product releases, except for Win NT, which was not expected to generate significant revenues during the quarter.
- Q94-2 net revenue increased \$146 million, or 15%, over Q94-1. Office revenue increased \$95 million (net of deferrals for unreleased suite components). The MS-DOS Business Unit added \$38 million due to release of version 6.2, mainly in North America FG, where sales increased by \$32 million.
- Q94-1 total expenses of \$481 million were \$86 million higher (22%) than Q93-1, and slightly less (\$5 million) than Q93-4. As a percent of net revenue, Q94-1 expenses were as follows; people (27%), facilities (8%), marketing (9%) and other (5%).
- Q94-2 controllable expenses increased to \$529 million, or 10% from \$481 million in Q94-1. Although average headcount only increased 1%, people expenses grew by 4% due to increased salaries and incentive compensation. Marketing was up 18% over the prior quarter. Other expenses grew by \$17 million, or 34%, and included increases for product development (\$7 million) and professional fees (\$5 million) due to litigation and patent protection.

COMPARISON WITH PLAN

Headcount



The above chart uses actual headcount from Q93-1 through Q94-2, and then budgeted headcount for the remaining two quarters of fiscal 1994.

- o Microsoft headcount at quarter-end Q94-2 was 14,737. The percentage of total each group represented were; Channel 50%, Product Group 31%, and Operations 19%.
- o The Channel headcount plan from Q94-2 to Q94-4 is for relatively flat headcount.
- o The Product Group headcount plan from Q94-2 to Q94-4 is for relatively flat headcount with the exception of Advanced Technology.
- o The Operations headcount plan from Q94-2 to Q94-4 assumes flat headcount.

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BALANCE SHEETS AND CASH FLOWS

Balance Sheets (in millions)

	Dec. 31, 1993		Sep. 30, 1993		Change	
Assets						
Current assets:						
Cash and short-term investments	\$2,796	62%	\$2,532	63%	\$264	10%
Accounts receivable - net	460	10	364	9	96	26
Inventories	130	3	95	2	35	37
Other	96	3	82	2	14	17
Total current assets	3,482	78	3,073	76	409	13
Property, plant, and equipment - net	913	20	891	22	22	2
Other assets	91	2	84	2	7	8
Total assets	\$4,486	100%	\$4,048	100%	\$438	11
Liabilities and Stockholders' Equity						
Current liabilities:						
Accounts payable	\$ 242	5%	\$ 214	5%	\$ 28	13
Accrued compensation	99	2	66	2	33	50
Income taxes payable	211	5	183	5	28	15
Other	188	4	118	3	70	59
Total current liabilities	740	16	581	15	159	27
Stockholders' equity:						
Common stock and paid-in capital	1,232	28	1,149	28	83	7
Retained earnings	2,514	56	2,318	57	196	8
Total stockholders' equity	3,746	84	3,467	85	279	8
Total liabilities and stockholders' equity	\$4,486	100%	\$4,048	100%	\$438	11

Cash Flows (in millions)

	Quarter Ended	
	Dec. 31, 1993	Sep. 30, 1993
Cash flows:		
From operations	\$ 348	\$ 316
Used in financing	(4)	(6)
Used for investments	(78)	(62)
Net change in cash and short-term investments	266	248
Effect of exchange rates on cash	(2)	(6)
Cash and short-term investments, beginning of period	2,532	2,290
Cash and short-term investments, end of period	\$2,796	\$2,532

Stock Repurchases

	Shares adjusted for all splits	Amount (millions)	Average Cost
FY90	1,785,375	\$ 46	\$26.14
FY91	5,469,750	197	35.96
FY92	1,979,828	135	68.18
FY93	3,128,500	250	79.92
Q94-1	966,500	72	74.47
Q94-2	1,152,500	92	79.66
LTD	14,482,453	\$792	54.70

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CASH AND SHORT-TERM INVESTMENTS

CASH AND SHORT-TERM INVESTMENTS

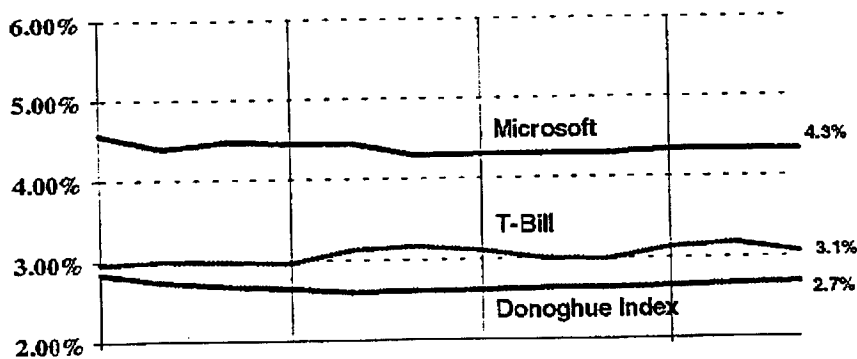
- Cash and short-term investments increased \$264 million during Q94-2.
- Short term interest rates were stable during Q94-2.
- At December 31, the portfolio was in compliance with all investment guidelines.
- The MS portfolio maintained a 1.2% yield advantage over the 90-day T-Bill and a 1.6% advantage over the Donoghue Index benchmark. Investment in municipal securities was increased this quarter to capture higher pre-tax yields.

Cash and Investment Portfolio Balances (in millions)

	Dec. 31, 1993		Sep. 30, 1993	
US \$ investment portfolio	\$ 2,587	92%	\$ 2,345	93%
Foreign currency investments	74	3	98	4
Operating bank accounts	135	5	89	3
Worldwide cash and investments	<u>\$ 2,796</u>	<u>100%</u>	<u>\$ 2,532</u>	<u>100%</u>

US\$ Portfolio Characteristics

MS US\$ Portfolio Pre-Tax Yield versus 90-Day T-Bill



US\$ Portfolio by Security Type (in millions)

Security type	Dec. 31, 1993			Sep. 30, 1993		
	Cost	%	Yield	Cost	%	Yield
Municipal bonds	\$ 1,173	45%	4.9%	\$ 1,035	44%	4.9%
Commercial paper	398	15	3.4	299	13	3.2
Treasury securities	270	10	4.0	194	8	4.0
Floating rate notes	195	8	3.3	210	9	3.8
Money market preferred	175	7	4.0	141	6	3.6
Certificate and time deposits	170	7	3.7	184	8	3.1
Corporate bonds	156	6	4.6	190	8	4.5
Other	50	2	5.0	92	4	3.3
US \$ investment portfolio	<u>\$ 2,587</u>	<u>100%</u>	4.3	<u>\$ 2,345</u>	<u>100%</u>	4.3

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US\$ Portfolio by Investment Type (in millions)

	Yield	% of Portfolio
Tax exempt municipals	4.9%	45.0%
Tax advantaged preferred stock securities	4.4%	2.0%
Taxable securities	3.7%	53.0%
	<u>4.3%</u>	<u>100.0%</u>

US\$ Portfolio by Credit Rating (in millions)

Credit Rating	Dec. 31, 1993		Sep. 30, 1993	
	Amount	%	Amount	%
AAA	\$ 767	30%	\$ 605	26%
AA	988	38	891	38
A	655	25	624	26
BBB	110	4	132	6
MS rated	67	3	93	4
US \$ investment portfolio	<u>\$ 2,587</u>	<u>100%</u>	<u>\$ 2,345</u>	<u>100%</u>

US\$ Portfolio by Industry (in millions)

Industry	Dec. 31, 1993		Sep. 30, 1993	
	Amount	%	Amount	%
Municipalities	\$ 1,173	45%	\$ 1,035	44%
US treasury	373	15	296	13
Banking/finance	322	13	306	13
Other	213	9	204	9
Automotive	101	4	85	4
Utilities	88	4	44	2
Natural resources	73	3	60	2
Food/beverage	68	3	40	2
Retailing	60	2	43	2
Securities	57	2	80	3
Medical	30	1	30	1
Services	29	1	45	2
Industrial	0	--	77	3
US \$ investment portfolio	<u>\$ 2,587</u>	<u>100%</u>	<u>\$ 2,345</u>	<u>100%</u>

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ACCOUNTS RECEIVABLE

ACCOUNTS RECEIVABLE

Ten Largest Worldwide Accounts Receivable (in millions)

	Total	Percent	Aging Summary			
			Current	1-30	31-60	Over 60
Ingram	\$107	17%	\$67	\$37	\$2	\$1
Merisel	71	12%	51	16	3	1
Computer 2000	29	5%	27	1	1	0
Egghead	21	3%	18	3	0	0
Corporate Software	15	2%	12	1	2	0
Olivetti	15	2%	11	3	1	0
Softmart	10	2%	9	1	0	0
Veba	10	2%	10	0	0	0
Software Spectrum	8	1%	8	0	0	0
Macrotron	8	1%	8	0	0	0
Total ten largest	294	47%	221	62	9	2
Other	326	53%	227	41	11	47
Total Q94-2	\$620	100%	\$448	\$103	\$20	\$49
Total Q94-1	\$493		\$328	\$98	\$27	\$40
Ten largest percentage	100%		75%	21%	3%	1%

Worldwide Accounts Receivable (in millions)

	DSO		Total		Aging Summary			
	Q94-1	Q94-2	Q94-1	Q94-2	Current	1-30	31-60	Over 60
Retail								
USFG	55	43	\$161	\$233	\$158	\$59	\$7	\$9
International	51	58	236	299	246	32	8	12
			397	532	404	91	15	21
OEM	32	24	81	68	30	10	4	24
Other	84	81	15	20	14	2	1	4
Total accts receivable	48	45	\$493	620	\$448	\$103	\$20	\$49
Aging Percentages					72%	17%	3%	8%
OEM GAAP Adjustments				114				
Sales returns reserve				(91)				
Customer deposits/deferred rev.				(44)				
Reseller rebates				(42)				
Allowance for doubtful accounts				(97)				
Accounts receivable-net				\$460				

Worldwide Net Receivables (in millions)

	Net Receivables	DSO	Allowance		
			Dollars	% of AR	
Q94-2	\$460	45	\$97	16	
Q94-1	364	48	83	17	
Q93-4	338	46	76	18	
Q93-3	438	54	68	13	MX3078539
Q93-2	339	46	62	15	CONFIDENTIAL

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INVENTORIES

INVENTORIES

Inventories by Location (in millions)

Location	<u>Q94-2</u>	<u>Q94-1</u>	<u>Change</u>
Subsidiary warehouses	\$37	\$35	\$2
Campus North	78	54	24
Ireland	14	4	10
Puerto Rico	1	2	(1)
	<u>\$130</u>	<u>\$95</u>	<u>\$35</u>
Subsidiary			
Japan	\$9	\$7	\$2
France	7	3	4
Australia	6	3	3
Sweden	2	1	1
Germany	2	5	(3)
Others	11	16	(5)
	<u>\$37</u>	<u>\$35</u>	<u>\$2</u>

Raw Materials, Finished Goods and Allowances (in millions)

Consolidated Inventories	<u>Q94-2</u>	<u>Q94-1</u>	<u>Change</u>
Raw materials	\$61	\$58	\$3
Finished goods	87	62	25
Allowances	(18)	(25)	7
	<u>\$130</u>	<u>\$95</u>	<u>\$35</u>

- Inventories at the end of Q94-2 increased \$35 million or 37%, compared to the prior quarter. Campus North inventory increased substantially in anticipation of shipment demand for Excel 5.0.
- Inventory turnover has remained consistent, staying around four turns per year.

Days Sales (\$ in millions)

	<u>Q94-2</u>	<u>Q94-1</u>	<u>Q93-4</u>	<u>Q93-3</u>	<u>Q93-2</u>
Inventories	\$ 130	\$ 95	\$ 127	\$ 119	\$ 102
Days sales	88	84	86	97	73

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PROPERTY, PLANT AND EQUIPMENT

PROPERTY, PLANT AND EQUIPMENT

December 31, 1993

Property, Plant and Equipment (in millions)

	Land	Buildings	Leasehold Improvements	Furniture & Equipment	Computer Equipment	Total
Beginning balance, Sep. 30, 1993	\$144	\$400	\$92	\$154	\$450	\$1,240
Additions	--	18	6	8	25	57
Retirements	--	--	--	(1)	(2)	(3)
Ending balance, Dec. 31, 1993	144	418	98	161	473	1,294
Accumulated depreciation	--	(44)	(28)	(69)	(240)	(381)
Net property, plant, and equip.	\$144	\$374	\$70	\$92	\$233	\$913

	Quantity Purchased	Cost (millions)	Q94-2 Avg Price (thousands)	Q94-1 Avg Price (thousands)
Domestic personal computers				
Dell 486 computers	982	\$ 4.1	\$ 4.1	\$ 4.1
Other servers	81	2.3	29.0	40.9
Pentium servers	127	1.8	14.1	19.5
Compaq portable 486 computers	224	1.7	7.6	7.4
Gateway 486 computers	435	1.6	3.7	3.5
Other Compaq servers	141	0.9	6.5	9.9
Compaq desktop 486 computers	186	0.8	4.1	4.1
Other 486 computers	125	0.8	6.4	5.1
Other pentium computers	82	0.5	6.0	7.7
Apple computers	85	0.4	4.4	4.5
RISC computers	16	0.1	7.9	15.8
	<u>2,484</u>	<u>15.0</u>		
Other computer equipment				
Subsidiaries		2.6		
Peripherals		1.6		
Networking equipment		3.2		
Retirements		(2.0)		
Other		4.1		
Net change		<u>\$24.5</u>		

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OTHER ASSETS

OTHER ASSETS

(in millions)

	Cost			Market Value	
	Dec. 31, 1993	Jun. 30, 1993	Change	Dec. 31, 1993	Jun. 30, 1993
Financial assets					
Santa Cruz Operation	\$ 20	\$ 20	\$ --	\$ 23	\$ 27
Dorling Kindersley	19	19	--	55	49
MicroUnity	15	--	15	--	--
Monotype	4	4	--	--	--
Natural Language Inc.	2	2	--	--	--
Citrix Systems	2	2	--	--	--
	<u>62</u>	<u>47</u>	<u>15</u>	<u>78</u>	<u>76</u>
Valuation allowance	<u>(33)</u>	<u>(28)</u>	<u>(5)</u>	--	--
	<u>29</u>	<u>19</u>	<u>10</u>	--	--
Intellectual property rights					
Consumer Software, Inc.	13	13	--	--	--
Other	52	49	3	--	--
	<u>65</u>	<u>62</u>	<u>3</u>	--	--
Accumulated amortization	<u>(39)</u>	<u>(32)</u>	<u>(7)</u>	--	--
	<u>26</u>	<u>30</u>	<u>(4)</u>	--	--
Miscellaneous	<u>36</u>	<u>38</u>	<u>(2)</u>	--	--
	<u>\$ 91</u>	<u>\$ 87</u>	<u>\$ 4</u>	--	--

- Financial assets are equity and equity-related investments. Microsoft maintains a valuation allowance to cover operating losses at investee companies and potential losses on disposition. The provision is charged to non operating income in the financial statements. Market value is shown above for all public companies.
- Intellectual property rights represent purchased code or other intellectual property and rights. Their cost is amortized over periods of up to five years. Amortization is generally charged to research and development expense.
- Miscellaneous assets include other long-term assets, primarily lease and other deposits and patent rights.

Santa Cruz Operation, Inc.

Income Statement Data (in millions, unaudited)

	Year Ended Sep. 30, 1993	Year Ended Sep. 30, 1992	Change	Change
Net revenues	\$ 178	\$ 164	\$ 14	9 %
Cost of revenues	<u>59</u>	<u>61</u>	<u>(2)</u>	<u>(3)</u>
Gross profit	119	103	16	16
Controllable expenses	<u>105</u>	<u>94</u>	<u>11</u>	<u>12</u>
Net income	<u>\$ 14</u>	<u>\$ 9</u>	<u>\$ 5</u>	<u>56 %</u>

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OTHER ASSETS

Balance Sheet Data (in millions, unaudited)

	<u>Sep. 30, 1993</u>	<u>Sep. 30, 1992</u>	<u>Change</u>	<u>Change</u>
Cash	\$ 56	\$ 14	\$ 42	300 %
Other current assets	43	33	10	30
Property and other	12	13	(1)	(8)
Total assets	<u>\$ 111</u>	<u>\$ 60</u>	<u>\$ 51</u>	<u>85 %</u>
Current liabilities	<u>\$ 38</u>	<u>\$ 41</u>	<u>\$ (3)</u>	<u>(7) %</u>
Long-term liabilities	2	2	--	--
Stockholders' equity	71	17	54	318
Total liabilities and equity	<u>\$ 111</u>	<u>\$ 60</u>	<u>\$ 51</u>	<u>85 %</u>

- Recent results at SCO have continued to be disappointing due to slow revenue growth and increased operating expenses. The company has initiated several headcount reductions and a restructuring to improve its operating margins but the benefit of these actions has yet to be demonstrated in the financial results. The chief financial officer and the SVP of operations have both resigned in the last three months.
- For its first fiscal quarter ended December 31, 1993, SCO reported revenues of \$41.6 million compared with \$44.8 million for the comparable quarter in fiscal 1993. Revenues were below expectations due to weakness in the US and Latin American markets primarily due to high inventory in the channel. In addition, revenues for the year earlier period included \$7.0 million from a federal contract which was completed in that quarter. Net income for the quarter was \$1.5 million with EPS of \$0.05 per share compared with \$3.6 million with EPS of \$0.13 per share for the first quarter of fiscal 1993. Our target minimum selling price of \$7 per share was not reached. We are re-evaluating our minimum disposition price.
- SCO's stock price fell to a recent price of \$5 3/8 compared with \$8 3/8 last quarter. The "lockup" restrictions on Microsoft's stock expired in late November 1993.
- SCO is the leading producer of Intel-based UNIX software.

Dorling Kindersley

Income Statement Data (in millions, unaudited)

	<u>Year Ended</u> <u>Jun. 30, 1993</u>	<u>Year Ended</u> <u>Jun. 30, 1993</u>	<u>Change</u>	<u>Change</u>
Net revenues	£ 87	£ 71	£ 16	23 %
Cost of revenues	59	48	11	23
Gross profit	28	23	5	22
Controllable expenses	22	18	4	22
Net income	<u>£ 6</u>	<u>£ 5</u>	<u>£ 1</u>	<u>20 %</u>

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OTHER ASSETS

Balance Sheet Data (in millions, unaudited)

	<u>Jun. 30, 1993</u>	<u>Jun. 30, 1993</u>	<u>Change</u>	<u>Change</u>
Cash	£ 19	£ 3	£ 16	533 %
Other current assets	58	42	16	38
Property and other	4	3	1	33
Total assets	<u>£ 81</u>	<u>£ 48</u>	<u>£ 33</u>	<u>69 %</u>
Current liabilities	£ 38	£ 33	£ 5	15 %
Long-term liabilities	3	3	--	--
Stockholders' equity	40	12	28	233
Total liabilities and equity	<u>£ 81</u>	<u>£ 48</u>	<u>£ 33</u>	<u>69 %</u>

- DK's shares have recently fallen to 283p from a high last fall of 351p due to the resignation of Richard Harmon, group managing director, and the company's warnings of declining profits in the current quarter. DK attributed the profit decline to continuing problems with Tiptree, the distributor of DK's Family Library series, and weakness in the DK Education division.
- In November, Microsoft and DK signed an amendment to their current licensing agreements to resolve certain contractual differences. Pursuant to this amendment, DK repaid to MS £390,000 of royalty advances. Microsoft's right to combine images in titles was confirmed and DK is now allowed to create multimedia titles from its print titles subject to certain royalties to Microsoft.
- Microsoft cannot liquidate its equity position until DK's fiscal 1994 financial statements are released, which should be in October.

MicroUnity Systems Engineering, Inc.

- MicroUnity remains in the development phase. In January, MicroUnity completed its fab on-time and within budget. Also this month, headcount reached 100 and the company began taking shipment on equipment.
- MicroUnity raised \$75 million in 1993 with investments from Microsoft, TCI, Time Warner, Cox Cable and Comcast. The funds were raised primarily to produce a 128-bit RISC microprocessor for a digital, interactive cable set-top box.
- Microsoft owns 6.5 million shares of convertible Series D Preferred Stock at a cost of \$14.95 million (\$2.30 per share) and a warrant to purchase 2.0 million shares of Series E Preferred Stock at a cost of \$50 thousand (which is exercisable for \$3.75 per share). Assuming conversion and/or exercise of all preferred stock, warrants and options, Microsoft owns approximately 6% of the fully-diluted common stock. If the performance of MicroUnity's chips exceeds certain performance benchmarks, Microsoft's position could be diluted. Concurrent with its investment, Microsoft signed agreements with MicroUnity and the other Series D Preferred investors which grant Microsoft access to certain technical specifications for the cable chip and other future developments.

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OTHER ASSETS

Monotype Typography Limited

Income Statement Data (in millions, unaudited)

	9 Months Ended Dec. 31, 1993	6 Months Ended Sep. 30, 1993	Quarter Ended Dec. 31, 1993
Net revenues	\$ 6.1	\$ 4.3	\$ 1.9
Cost of revenues	<u>1.9</u>	<u>1.4</u>	<u>0.5</u>
Gross profit	4.2	2.9	1.3
Operating expenses	<u>4.8</u>	<u>3.6</u>	<u>1.1</u>
Net income	<u>\$ -0.5</u>	<u>\$ -0.7</u>	<u>\$ 0.2</u>

- The company achieved an 11% profit margin in its 3rd quarter on sales of approximately \$1.9 million. The improved performance was attributable to a reduction in the cost of revenues and headcount reduction measures embraced earlier. Management's cost containment focus resulted in expenses declining aggressively to approximately 60% of revenues in the current quarter.
- Year to date revenues for the nine months ended December 31, were \$6.1 million, with \$3.4 million generated by overseas operations (UK and China Type Design Limited) and \$2.7 million generated by US operations. During this period, the company suffered a loss of approximately \$500 thousand, with a loss of \$700 thousand in its overseas operations and a profit of \$200 thousand in the US. The overseas loss figure included approximately a \$350 thousand reserve in the UK for restructuring and layoffs. With a -21% net margin, the overseas operations continued to lag the +6% net margin US operations. Looking forward, in 1994, the company continues to expect pricing pressures.
- Monotype's liquidity continued to remain tight.
- Microsoft's \$4 million investment included the purchase of Monotype's font library, warrants for approximately 36% of the company, which under certain performance conditions can amount to 85% of the company, and a working capital loan of \$1.2 million. Currently, the loan balance is \$900 thousand.

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Natural Language Incorporated

Income Statement Data (in millions, unaudited)

	Quarter Ended Dec. 31, 1993	Quarter Ended Sep. 30, 1993	Change	Change
Net revenues	\$ 0.4	\$ 0.7	\$ (0.3)	(45) %
Cost of revenues	<u>0.1</u>	<u>0.1</u>	<u>(0.0)</u>	<u>(7)</u>
Gross profit	0.2	0.5	(0.3)	(55)
Operating expenses	<u>0.8</u>	<u>0.9</u>	<u>(0.0)</u>	<u>(3)</u>
Net income	<u>\$ (0.6)</u>	<u>\$ (0.4)</u>	<u>\$ (0.3)</u>	<u>75</u> %

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OTHER ASSETS

Balance Sheet Data (in millions, unaudited)

	<u>Dec. 31, 1993</u>	<u>Sep. 30, 1993</u>	<u>Change</u>	<u>Change</u>
Cash	\$ 0.1	\$ 0.3	\$ (0.2)	(72) %
Other current assets	0.6	0.7	(0.1)	(21)
Property and other	<u>0.2</u>	<u>0.2</u>	<u>0.0</u>	<u>1</u>
Total assets	\$ <u>0.9</u>	\$ <u>1.2</u>	\$ <u>(0.4)</u>	<u>(30) %</u>
Current liabilities	\$ 3.7	\$ 3.5	\$ 0.2	7 %
Long-term liabilities	0.0	0.0	0.0	41
Stockholders' equity	<u>(2.9)</u>	<u>(2.3)</u>	<u>(0.6)</u>	<u>28</u>
Total liabilities and equity	\$ <u>0.9</u>	\$ <u>1.2</u>	\$ <u>(0.4)</u>	<u>(30) %</u>

- Revenues have declined on both a quarter-to-quarter and year-to-year basis because the market continues to be slow to embrace end-user querying tools and does not adequately perceive the difference between Natural Language and the various point-and-click tools that are positioned as providing ease of use. NLI has had some recent successes using sales seminars and plans to shift more resources toward this method of selling.
- The company's strategic focus has shifted toward providing Windows solutions and it is becoming a Microsoft Solution Provider. In addition, the company is completing ports of Natural Language to Fox and Access. The Fox and Access teams have expressed initial interest in entering into some sort of bundling arrangement with NLI.
- Microsoft, along with most of NLI's venture investors, invested an additional \$97,000 in the company in the quarter via demand notes sold in October and December to bolster its short-term cash position
- The company is the process of down-sizing in order to stabilize cash flow and recently terminated seven of its 35 employees. A proposal to raise an additional \$500,000 of equity has been made. Under this proposal all the existing debt and equity would convert to a new class of shares. Microsoft has not yet decided whether to participate in this round and it is not clear the company will survive if we do not.

Citrix Systems

Income Statement Data (in millions, unaudited)

	<u>Year Ended Dec. 31, 1993</u>	<u>Year Ended Dec. 31, 1993</u>	<u>Change</u>	<u>Change</u>
Net revenues	\$ 5.0	\$ 1.8	\$ 3.2	178 %
Cost of revenues	<u>0.9</u>	<u>0.4</u>	<u>0.5</u>	<u>125</u>
Gross profit	4.1	1.4	2.7	193
Controllable expenses	<u>6.8</u>	<u>-4.5</u>	<u>11.3</u>	<u>-251</u>
Net income	\$ <u>-2.7</u>	\$ <u>-3.1</u>	\$ <u>0.4</u>	<u>-13 %</u>

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OTHER ASSETS

Balance Sheet Data (in millions, unaudited)

	<u>Dec. 31, 1993</u>	<u>Dec. 31, 1993</u>	<u>Change</u>	<u>Change</u>
Cash	\$ 1.1	\$ 0.3	\$ 0.8	267 %
Other current assets	1.1	0.6	0.5	83
Property and other	<u>0.1</u>	<u>0.1</u>	<u>0.0</u>	<u>--</u>
Total assets	\$ <u>2.3</u>	\$ <u>1.0</u>	\$ <u>1.3</u>	<u>130</u> %
Current liabilities	\$ 1.8	\$ 1.3	\$ 0.5	38 %
Long-term liabilities	0.0	0.0	0.0	NM
Stockholders' equity	<u>0.5</u>	<u>-0.3</u>	<u>0.8</u>	<u>(267)</u>
Total liabilities and equity	\$ <u>2.3</u>	\$ <u>1.0</u>	\$ <u>1.3</u>	<u>130</u> %

- Citrix continues to position itself as a supplier of remote solutions to the Fortune 1000. In its fourth quarter, Citrix added Tech Data as distributor and re-signed several new national accounts including Motorola, Westinghouse and UPS.
- In December, Citrix's WinView 2.2 product received a technical excellence award from PC Magazine and was a runner-up in the networking category (to NT Advanced Server). In addition, WinView received favorable reviews at Comdex and Lotusphere.
- Citrix's liquidity remains adequate and the company is on the verge of signing a credit line with Bank of Boston.
- Citrix develops client and server software for Windows, Windows NT, Netware and OS-2 LANs. Other significant shareholders include Intel, Olivetti, Kleiner Perkins, Mayfield Partners and Sevin Rosen.

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TAX MATTERS

TAX MATTERS

This section addresses only tax-related financial reporting issues. Tax issues which are privileged and confidential are reported in the Law and Corporate Affairs briefing.

Tax Rate

- Taxes were provided at 32% for FY93. New 1993 tax legislation raised corporate tax rates 1% for FY94 and future years and included a 0.5% retroactive rate increase for FY93. The retroactive increase for FY93 is properly accounted for in FY94, and our corporate tax provision to increase to 34% for Q94-1 and Q94-2. Our corporate income tax rate for Q94-3 and Q94-4 is expected to be 33%.

"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):

	<u>FY93</u>		<u>FY94</u>	
	<u>Spread</u>	<u>Tax Benefit (34.5%)</u>	<u>Spread</u>	<u>Tax Benefit (35%)</u>
Q1	\$ 137	\$ 47	\$ 77	\$ 27
Q2	396	137	153	54
Q3	114	39		
Q4	<u>166</u>	<u>57</u>		
	<u>\$ 813</u>	<u>\$ 280</u>	<u>\$ 230</u>	<u>\$ 81</u>

- Unless the stock shows tremendous strength in the remainder of the year, the "spread" is not likely to produce a tax benefit for FY94 that approaches the benefit enjoyed in FY93. In FY93 a spike in the stock price coupled with the anticipation of increased individual income tax rates resulted in an unusually large "spread", particularly in Q93-2.

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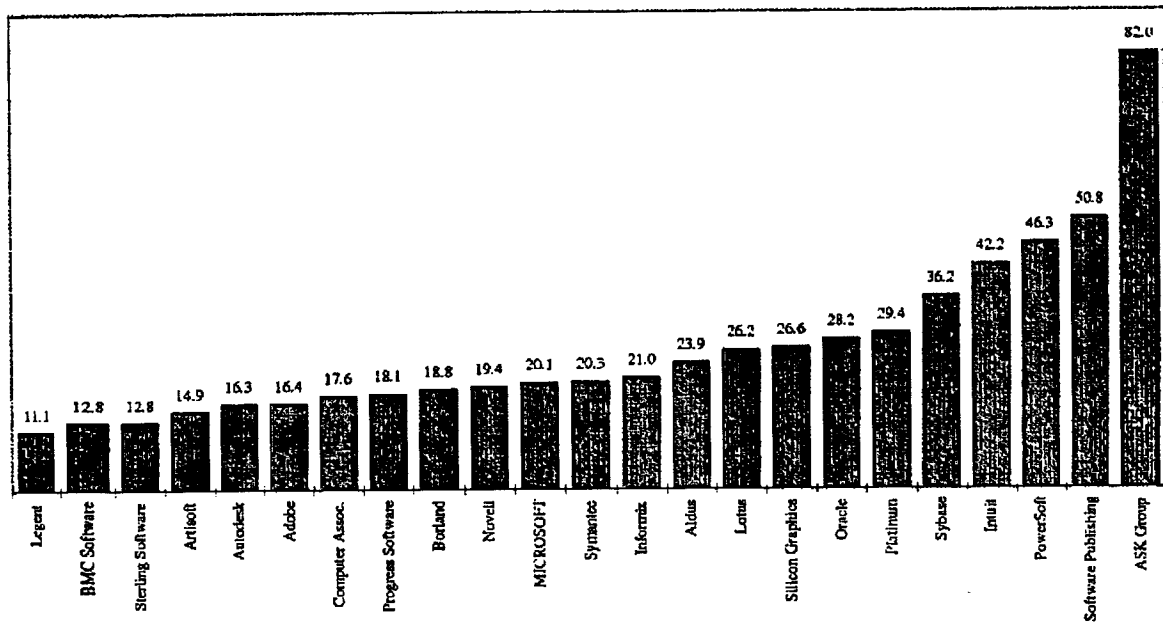
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SOFTWARE INDUSTRY FORWARD P/E RATIOS



Forward P/E ratios are calculated based upon December 31, 1993 stock prices and analysts's consensus estimates for the next four quarters.

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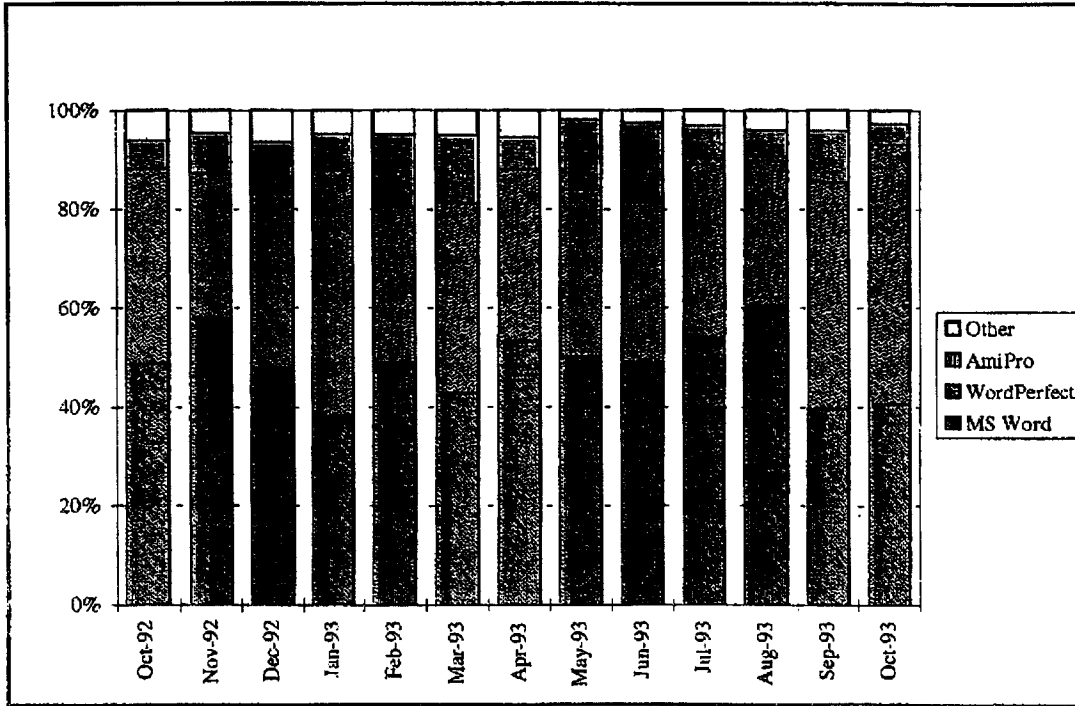
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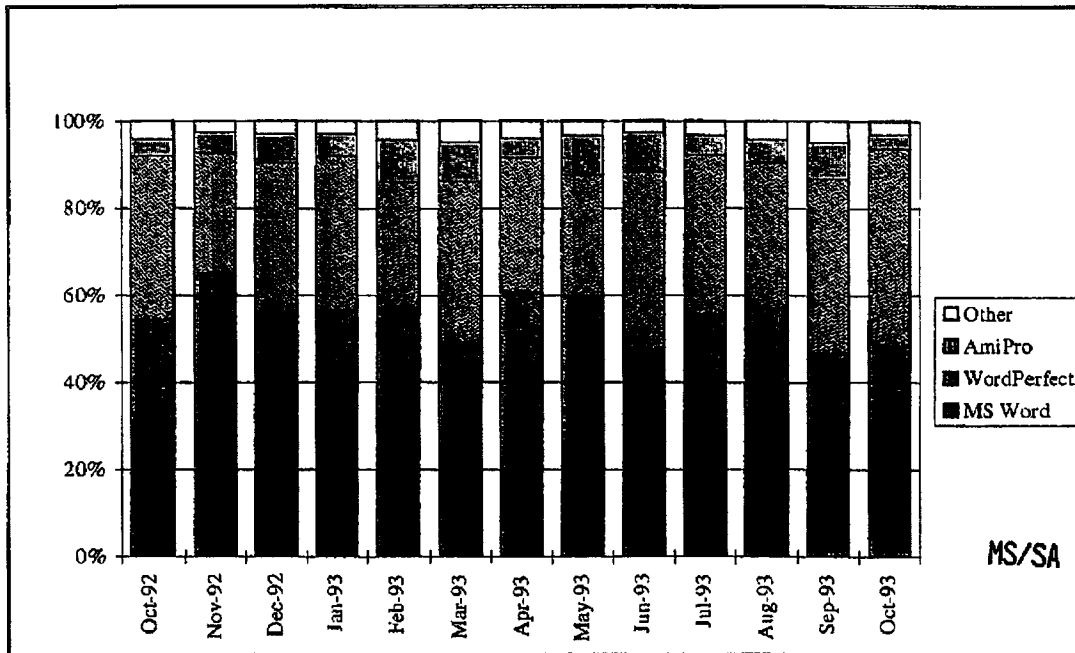
WORLDWIDE MARKET SHARE

WORLDWIDE MARKET SHARE

Word Processing (Units)



Word Processing (Revenues)



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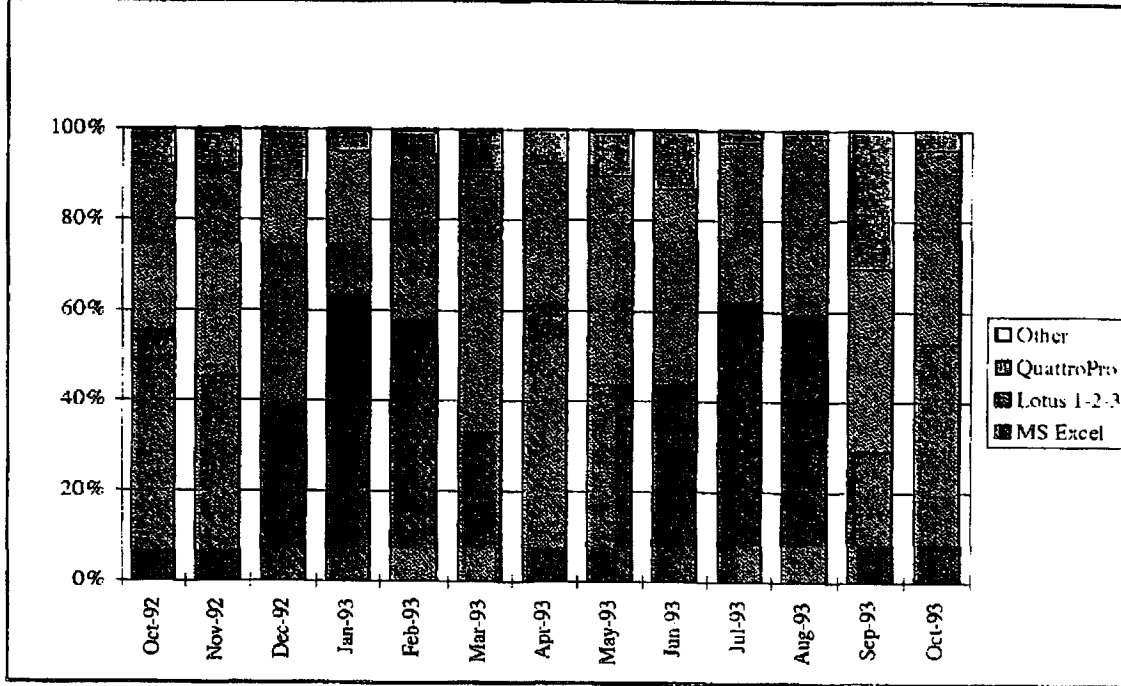
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Information presented includes MS-DOS, Windows, and Macintosh environments on a worldwide basis. Three month rolling averages. Market share is calculated by Microsoft Office marketing personnel. Market share data for competitors is estimated based on SPA, IDC, and DataQuest information.

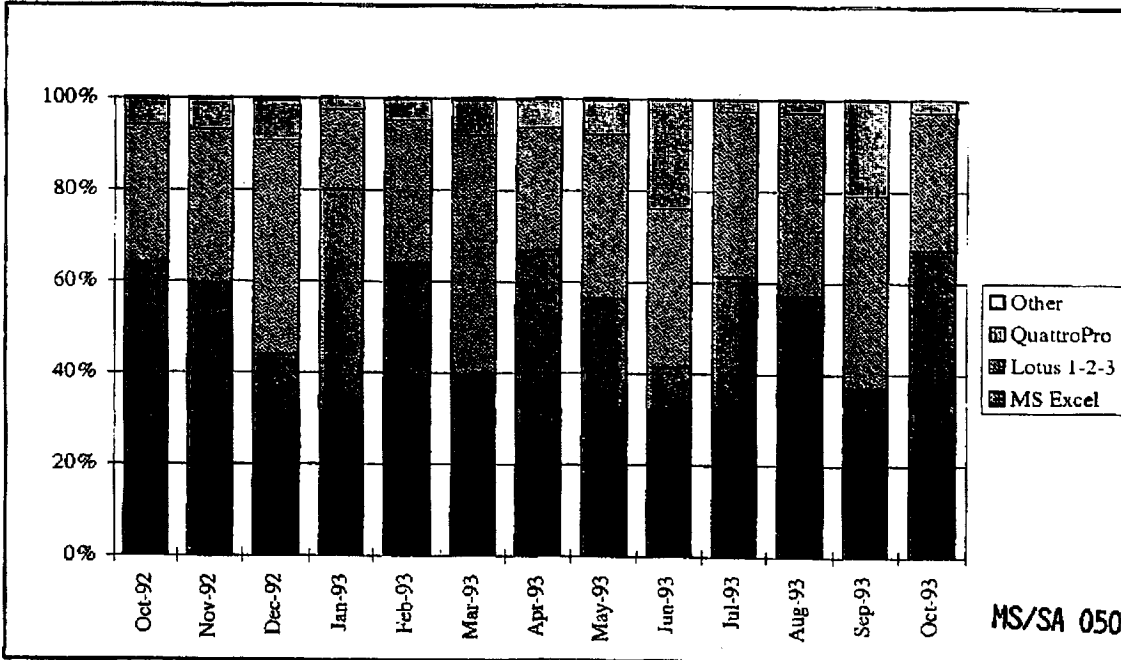
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WORLDWIDE MARKET SHARE

Spreadsheets (Units)



Spreadsheets (Revenues)



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Information presented includes MS-DOS, Windows, and Macintosh environments on a worldwide basis. Three month rolling averages. Market share is calculated by Microsoft Office marketing personnel. Market share data for competitors is estimated based on SPA, IDC, and DataQuest information.

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Industry

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SOFTWARE COMPETITION

SOFTWARE COMPETITION

Recent Financial and Corporate Items

Novell - Closing stock price: 12/31/93 \$20 3/4

- Channel inventory of NetWare has been significantly reduced.
- Cash and short-term investments increased \$40 million to \$664 million.
- Company completed the repurchase of 11 million shares of its common stock.
- The courts rejected Novell's motion to declare invalid the patent of Functionally-Structured Distributed Processing Systems allegedly infringed by NetWare. This ruling advances toward trial a \$220 million lawsuit brought by Dr. Roger Billings and the International Academy of Science.
- Novell DOS 7 slated for release by the end of January.

Lotus - Closing stock price: 12/31/93 \$55

- Common stock price increased 180% in 1993.
- Lotus terminated an agreement which gave up an estimated 25% of Notes revenues to IBM. This could mean as much as \$60 million in additional revenue for Lotus in the coming year. In return, Lotus renewed its commitment to develop products for OS/2.
- IBM will now sell and support Lotus SmartSuite for OS/2 through its sales channel.
- William Gray III was named to the BOD. Gray is president and CEO of the United Negro College Fund and a former U.S. Representative (D-Pa.).

WordPerfect - Privately Held

- Alan Ashton will step down as chief executive and become co-chairman with co-founder Bruce Bastian. Adrian Rietveld, 39, will become chief executive officer and president.
- WordPerfect 6.0 shipped in October.
- WordPerfect and Borland released Borland Office 2.0 for Windows, which includes Quattro Pro, Paradox, and WordPerfect.
- The company announced it will discontinue free telephone support.

Borland - Closing stock price: 12/31/93 \$14 7/8

- David Liddle, President of Interval Research, was elected to Board of Directors. He is also on the Board of Directors of Broderbund Software, NetFrame Systems and Sybase Corporation.
- Borland's \$49.95 Quattro Pro offer extended until May 15, 1994, says "one million users can't be wrong."
- Borland signed an LOI to acquire ReportSmith, a client/server reporting and query tool, for 1.2 million shares of common stock, or approximately \$18 million.
- As of January, WordPerfect will be responsible for selling the WordPerfect/Borland Office. Borland had recorded all of the revenues and paid a royalty to WordPerfect, but will now receive a royalty of 1/3 of the Office revenues from WordPerfect.
- Cash decreased from \$81 million to \$67 million. Borland has \$20 million of short-term borrowings.
- Rob Dickerson, head of database and client-server strategies, resigned.

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SOFTWARE COMPETITION

Top Four Software Companies

Most recent quarter	Microsoft 12/31/93		Novell 10/30/93		Lotus 10/2/93		Borland 12/31/93	
Net revenues	\$ 1,129	100.0%	\$ 309	100.0%	\$ 240 (2) (3)	100.0%	\$ 112 (6)	100.0%
Cost of revenues	185	16.4	68	22.0	47	19.5	29	25.6
Gross profit	944	83.6	241	78.0	193 (4)	80.5	83	74.4
Operating expenses:								
Research and development	149	13.2	51	16.6	33	13.6	15	13.4
Sales and marketing	338	29.9	72	23.2	114	47.9	66	59.3
General and administrative	42	3.7	23	7.4	18	7.3	--	--
Write-off/restructuring	--	--	--	--	--	--	--	--
Total operating expenses	529	46.9	146	47.2	165	68.8	81 (7)	72.7
Operating income	415	36.8	95	30.8	28	11.7	2	1.7
Nonoperating income	22	1.9	9	2.8	1	0.2	--	(0.2)
Income before income taxes	437	38.7	104	33.6	29	11.9	2	1.5
Provision for income taxes	148	13.1	35	11.3	11	4.3	2	1.1
Net income	\$ 289	25.6%	\$ 69	22.3%	\$ 18	7.6%	\$ --	0.4%
Average shares outstanding	304		317		45		27	
EPS	\$ 0.95		\$ 0.22		\$ 0.41		\$ 0.02	

Trailing twelve months	Microsoft		Novell		Lotus		Borland	
Net revenues	\$ 4,108	100.0%	\$ 1,123	100.0%	\$ 949	100.0%	\$ 460	100.0%
Cost of revenues	684	16.7	225	20.0	202	21.3	118	25.5
Gross profit	3,424	83.3	898	80.0	747	78.7	342	74.5
Operating expenses:								
Research and development	537	13.1	165	14.7	128	13.5	61	13.2
Sales and marketing	1,276	31.1	258	23.0	453	47.7	263	57.5
General and administrative	142	3.5	80	7.1	70	7.4	--	--
Write-off/restructuring	--	--	321 (1)	28.5	--	--	--	--
Total operating expenses	1,955	47.6	824	73.4	651	68.6	324	70.7
Operating income	1,469	35.8	74	6.6	96	10.1	18	3.8
Nonoperating income	77	1.9	30	2.7	(19) (5)	(2.0)	1	0.6
Income before income taxes	1,546	37.6	104	9.3	77	8.1	21	4.4
Provision for income taxes	511	12.4	139	12.4	36	3.9	7	1.3
Net income	\$ 1,035	25.2%	\$ (35)	(3.1)%	\$ 41	4.3%	\$ 14	3.2%
Average shares outstanding	304		314		43		28	
EPS	\$ 3.41		\$ (0.11)		\$ 0.93		\$ 0.53	

- (1) Novell's results of operations include a charge of \$321 million related to the acquisitions of USL, Software Transformation, Serius and Fluent. The write-off of purchased research and development and other costs represents a one-time charge against earnings of \$1.00 per share.
- (2) On August 28, 1993, Lotus sold its One Source business, a developer and marketer of CD-ROM information products. No gain or loss was recognized on the sale.
- (3) According to Romtec, a UK market research company, Lotus has doubled its market share in suites in the UK since May 1993. The release of Smartsuite 1.0 contributed to Lotus's market share increasing from 19% to 40% from May 1993 to December 1993.
- (4) Lotus's gross margin increased to 81%, from 77% in the comparable quarter of the prior year, due to manufacturing efficiencies obtained from higher production volumes and the closing of the Puerto Rican manufacturing plant. Material cost reductions and sales of higher margin communication products also contributed to the increase.
- (5) Lotus's trailing twelve months non-operating expense includes a \$20 million write-off in the quarter ended June 30, 1993 in connection with the acquisition of Approach.
- (6) Borland's revenues in the December quarter grew only 7% over the prior year.
- (7) Borland's operating expenses were controlled to only a \$2 million sequential increase.

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SOFTWARE COMPETITION

Top Four Software Companies (Continued)

	Microsoft 12/31/93		Novell 10/30/93		Lotus 10/2/93		Borland 12/31/93	
Current assets:								
Cash and short-term investments	\$ 2,796	62%	\$ 664	49%	\$ 377	46%	\$ 67 (6)	18%
Accounts receivable - net	460	10	332 (1)	25	168	20	81	22
Inventories	131	3	--	--	21	3	10	3
Other	95	3	56	4	31	3	10	3
Total current assets	3,482	78	1,052	78	597	72	168	46
Property, plant and equipment - net	913	20	217	16	124	15	176	48
Capitalized software	--	--	--	--	93	11	--	--
Other assets	91	2	75	6	14	2	21	6
	<u>\$ 4,486</u>	<u>100%</u>	<u>\$ 1,344</u>	<u>100%</u>	<u>\$ 828</u>	<u>100%</u>	<u>\$ 365</u>	<u>100%</u>
Current liabilities	\$ 740	16%	\$ 230	17%	\$ 280	34%	\$ 146	40%
Long-term liabilities	--	--	--	--	78	9	21	6
Other liabilities	--	--	10	1	--	--	--	--
Put Warrants	--	--	107	8	--	--	--	--
Stockholders' equity	3,746	84	997 (2)	74	470 (4)	57	198	54
	<u>\$ 4,486</u>	<u>100%</u>	<u>\$ 1,344</u>	<u>100%</u>	<u>\$ 828</u>	<u>100%</u>	<u>\$ 365</u>	<u>100%</u>

Other data

	Microsoft 1993	Novell 1993	Lotus 1993	Borland 1993
Closing stock price (December 31, 1993)	\$80.63	\$20.75	\$55.00 (5)	\$14.88
Common shares outstanding	304	317	45	27
Market value	\$24,512	\$6,578	\$2,475	\$402
Price/revenues ratio	6.0x	5.9x	2.6x	0.9x
Price/earnings ratio - trailing twelve	23.6x	" (3)	59.1x	28.1x
Price/earnings ratio - future 4 quarters	20.1x	19.4x	26.2x	18.8x
Avg headcount (most recent disclosure)	13,813	3,424	4,350	1,989
Net revenues/employee	\$297,401	\$327,979	\$218,161	\$231,272
Cash per share	\$9.20	\$2.09	\$8.38	\$2.48
Book value per share	\$12.32	\$3.15	\$10.44	\$7.33
Price/book value ratio	6.5x	6.6x	5.3x	2.0x
Growth statistics (over comparable quarter):				
Revenue	20%	19%	16%	7%
Research and development	34%	55%	18%	(21%)
Sales and marketing	7%	21%	11%	(18%)
General and administrative	46%	55%	4%	n/a
Net income	22%	(1%)	(39%)	101%

- (1) Novell's DSO was 106 days at October 30, 1993.
- (2) In the quarter ended October 30, 1993, Novell repurchased 11.1 million common shares. Novell had 317 million shares outstanding as of October 30, 1993.
- (3) Novell's trailing twelve months P/E ratio is negative due to the \$321 million charge related primarily to the acquisition of USL. Excluding the charge, Novell's trailing twelve month net income was \$282 million, or \$.90 per share, up 13% from net income of \$249 million in fiscal 1992.
- (4) In September 1993, Lotus expanded its stock repurchase program by 2.5 million shares. As of October 2, 1993, Lotus had 45 million shares outstanding.
- (5) Lotus's stock price has increased 59%, from \$34 5/8, since June 30, 1993 with the release of new versions of SmartSuite, 1-2-3 for Windows, and Notes.
- (6) In August 1993, Borland was found to be in violation of certain copyrights held by Lotus. A trial to assess damages has been set for October 1994 but the company has appealed. Analysts have estimated the damages to range from \$60 million to \$200 million.
- Not meaningful

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SOFTWARE COMPETITION

Software Company Metrics

	Adobe	Aldus	Autodesk	BMC	Computer Assoc.	Intuit
	11/26/93	10/1/93	10/31/93	9/30/93	12/31/93	9/30/93 (8)
Income statement						
Most recent quarter						
Net revenues	\$87	\$62	\$98	\$68	\$502	\$35
Net income (loss)	16	4 (2)	15	20	81	3
EPS	0.34	0.32	0.60	0.78	0.48	0.26
Trailing twelve months						
Net revenues	\$313	\$195	\$402	\$264	\$1,982	\$121
Net income	57	7 (3)	58	75	298	8
EPS	1.21	0.50	2.34	2.88	1.75	0.76
Net income as a % of net revenues	18%	3%	14%	29%	15%	7%
Balance sheet						
Cash	\$236	\$71 (4)	\$159	\$107	\$289	\$40
Other current assets	68	49	104	63	560	26
Other assets	49	53	119	267	1,477	8
	<u>\$353</u>	<u>\$173</u>	<u>\$382</u>	<u>\$437</u>	<u>\$2,326</u>	<u>\$74</u>
Liabilities	\$74	\$41	\$93	\$156	\$1,229	\$25
Put Warrants	7	0	0	37	0	0
Equity	<u>272</u>	<u>132 (5)</u>	<u>289 (6)</u>	<u>244</u>	<u>1,097 (7)</u>	<u>49</u>
	<u>\$353</u>	<u>\$173</u>	<u>\$382</u>	<u>\$437</u>	<u>\$2,326</u>	<u>\$74</u>
Other data						
Closing stock price (December 31, 1993)	\$22.25	\$27.25	\$45.00	\$48.00	\$40.00	\$42.63
Common shares outstanding (in millions)	46	14	25	26	168	11 (9)
Market value (in millions)	\$1,024	\$382	\$1,125	\$1,248	\$6,720	\$469
Price/revenues ratio	3.3x	2.0x	2.8x	4.7x	3.4x	3.9x
Price/earnings ratio - trailing twelve	18.3x	54.3x	19.2x	16.6x	22.9x	56.0x
Price/earnings ratio - future 4 qtrs.	16.4x	23.9x	16.3x	12.8x	17.6x	42.2x
Avg headcount (most recent disclosure)	794	980	1,419	846	7,300	541
Net revenues/employee	\$394,782	\$199,261	\$283,408	\$311,466	\$271,536	\$224,348
Cash per share	\$5.13	\$5.07	\$6.36	\$4.12	\$1.72	\$3.64
Book value per share	\$5.91	\$9.43	\$11.56	\$9.38	\$6.53	\$4.45
Price/book value ratio	3.8x	2.9x	3.9x	5.1x	6.1x	9.6x
Growth statistics (over comparable quarter):						
Revenue	22%	37%	5%	18%	0%	81%
Research and development	22%	55%	9%	20%	1%	72%
Sales and marketing	29%	24%	6%	41%	(0%)	67%
General and administrative	(6%)	17%	9%	n/a	n/a	n/a
Net income	87% (1)	310%	17%	33%	1%	564%

- (1) Adobe's net income increased 87% over the comparable period of the prior year due to a \$6 million write-off of purchased research and development for the November 1992 quarter. Excluding the charge, net income increased 9%.
- (2) Aldus's results of operations for the quarter ended October 1, 1993 include a \$2.3 million write-off of R&D in connection with the July 1993 acquisition of The Company of Science and Art (CoSA) and a \$1.6 million charge related to a general restructuring of the company's European operations, severance payments and lease terminations in the US and Europe. CoSA was purchased for \$6 million cash, approximately \$1 million in restricted common stock and future contingent consideration. CoSA was a privately held developer of digital-video software tools.
- (3) Aldus's trailing twelve month net income includes a pre-tax charge of \$3 million for the write-off of software development costs in connection with the acquisition of After Hours Software.
- (4) In June 1992, certain Aldus shareholders filed a lawsuit against the company and certain officers alleging violations of securities laws. In November 1993, the company signed a settlement agreement which, if approved, would pay \$.50 to \$1.10 per eligible share. The company estimates that its uninsured liability will not exceed \$2 million.
- (5) For the quarter ended October 1, 1993, Aldus repurchased 40,000 shares for \$.7 million bringing the total to 2.2 million shares for \$39.4 million.
- (6) On January 11, 1994, Autodesk's Board approved the repurchase of up to two million shares of the company's common stock. Since the program's inception in December 1991, three million shares have been repurchased for \$104 million.
- (7) Computer Associates's balance sheet is as of September 30, 1993. For that quarter ended, Computer Associates repurchased 500,000 shares of the company's common stock. The company's Board has authorized the repurchase of an addition 17 million shares.
- (8) On September 1, 1993, Intuit entered into an agreement to merge with ChipSoft, a publisher of income tax preparation software.
- (9) Intuit completed its initial public offering on March 12, 1993 at \$20 per share. The stock closed at \$42 5/8 on December 31, 1993.

Industry

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SOFTWARE COMPETITION

Software Company Metrics (Continued)

	Software				
	Legent	Publishing	Sterling	Symantec	3DO
	9/30/93	9/30/93	9/30/93	9/30/93	9/30/93
Income statement					
Most recent quarter					
Net revenues	\$123	\$15	\$111	\$58	3
Net income (loss)	14 (2)	(34) (4)	(49) (5)	2	(7)
EPS	0.39	(2.80)	(2.75)	0.09	(0.35)
Trailing twelve months					
Net revenues	\$442	\$104	\$412	\$217	\$3 (8)
Net income (loss)	60	(34)	(39)	(10) (7)	(47)
EPS	1.75	(2.78)	(2.24)	(0.40)	(2.46)
Net income (loss) as a % of net revenues	14%	(33%)	(9%)	(5%)	0%
Balance sheet					
Cash	\$146	\$57	\$81	\$55	\$33
Other current assets	225	31	134	61	1
Other assets	253	12	183	30	8
	<u>\$624</u>	<u>\$100</u>	<u>\$398</u>	<u>\$146</u>	<u>\$42</u>
Liabilities	\$224	\$63	\$301	\$75	\$12
Put Warrants	40	0	0	0	0
Equity	360	37	97	71	30 (9)
	<u>\$624</u>	<u>\$100</u>	<u>\$398</u>	<u>\$146</u>	<u>\$42</u>
Other data					
Closing stock price (December 31, 1993)	\$22.63	\$7.75	\$28.38	\$18.25	\$22.00
Common shares outstanding (in millions)	35	12	18	28	20
Market value (in millions)	\$792	\$93	\$511	\$511	\$440
Price/revenues ratio	1.8x	0.9x	1.2x	2.4x	0.0x
Price/earnings ratio - trailing twelve	13.0x	*	*	*	*
Price/earnings ratio - future 4 qtrs.	11.1x	50.8x	12.8x	20.3x	*
					(10)
Avg headcount (most recent disclosure)	1,619	721	2,075	1,049	95
Net revenues/employee	\$273,127	\$144,743	\$198,455	\$206,981	*
Cash per share	\$4.17	\$4.75	\$4.50	\$1.96	\$1.65
Book value per share	\$10.29	\$3.08	\$5.39	\$2.54	\$1.50
Price/book value ratio	2.2x	2.5x	5.3x	7.2x	14.7x
Growth statistics (over comparable quarter):					
Revenue	(48%)	(60%)	5%	19%	100%
Research and development	(9%)	(7%)	3%	(3%)	274%
Sales and marketing	(64%)	(10%)	(11%)	5%	795%
General and administrative	n/a	90%	n/a	(31%)	193%
Net income	1,973% (3)	(309%)	(1,192%)	121%	(229%)

- (1) Subsequent to the September 1993 quarter, Legent acquired Performance Technologies and has signed a letter of intent to acquire Team One Systems.
 - (2) Included in Legent's net income for the quarter ended September 30, 1993 is a \$4 million restructuring charge related to the reorganization of certain distribution and operations areas. The charge reduced EPS by \$.10 per share. In addition, the company acquired Corporate Microsystems and Networx in the September 1993 quarter as well as National DataGuard Technologies in May 1993. The company paid approximately \$18 million for the acquisitions.
 - (3) The growth of Legent's net income was due to certain acquisition related write-offs taken in the September 1992 quarter. The company acquired Goal Systems and Spectrum Concepts during 1992 which resulted in a \$42 million pre-tax charge. Excluding the charge, net income decreased 240%.
 - (4) Software Publishing's net loss for the quarter ended September 30, 1993 includes a \$20 million restructuring charge related to excess facilities and workforce reductions. The company incurred a loss in the quarter exclusive of the restructuring charge. The company attributes the loss to the rapid transition to the Windows platform, increased competition for Windows based applications and declining conditions in the international marketplace.
 - (5) Included in Sterling's net loss for the quarter ended September 30, 1993, is a \$91.3 million charge related to the July 1993 acquisition of Systems Center. Exclusive of the charge, net income increased 159% over the September 1992 quarter.
 - (6) On October 4, 1993, Symantec acquired Fifth Generation Systems. The company develops and markets utilities for the DOS, Windows, OS/2 UNIX, Macintosh and NetWare operating systems.
 - (7) Symantec's net loss for the trailing twelve months was due to charges incurred in obtaining four software companies during the year.
 - (8) Information for 3DO was obtained from the company's prospectus dated March 12, 1993. Due to the lack of available historical data, the trailing twelve months shown covers the 18 month period from April 1, 1992 to September 30, 1993.
 - (9) On November 5, 1993, 3DO announced its intention to file a registration statement for a secondary stock offering of one million shares of its common stock.
 - (10) Analysts are estimating that 3DO will incur net losses of approximately \$.23 to \$.45 per share through December 1994.
- * Not meaningful.

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HARDWARE COMPETITION

HARDWARE COMPETITION

Hardware Company Metrics

	Apple Computer 12/31/93	DEC 1/1/94	Hewlett- Packard 10/31/93 (2)	IBM 9/30/93	AT&T 9/30/93
Income statement					
Most recent quarter					
Net revenues	\$2,469	\$3,254	\$5,687	\$14,743	\$16,662
Net income (loss)	40	(72)	298	(70) (3)	1,073
EPS	0.34	(0.53)	1.18	(12.00)	0.79
Trailing twelve months					
Net revenues	\$8,446	\$13,637	\$20,317	\$62,880	\$66,201
Net income (loss)	(35) (1)	(72)	1,178	(13,859)	(2,527) (4)
EPS	(0.30)	(0.54)	4.65	(24.27)	(1.88)
Net income (loss) as a % of net revenues	(0%)	(1%)	6%	(22%)	(4%)
Balance sheet					
Cash	\$1,123	\$1,147	\$1,644	\$6,174	\$798
Other current assets	3,085	5,152	8,592	34,078	27,395
Other assets	834	4,070	6,500	43,965	31,260
	<u>\$5,042</u>	<u>\$10,369</u>	<u>\$16,736</u>	<u>\$84,217</u>	<u>\$59,453</u>
Liabilities	\$2,989	\$5,539	\$8,225	\$64,114	\$45,055
Equity	<u>2,053</u>	<u>4,830</u>	<u>8,511</u>	<u>20,103</u>	<u>14,398</u>
	<u>\$5,042</u>	<u>\$10,369</u>	<u>\$16,736</u>	<u>\$84,217</u>	<u>\$59,453</u>
Other data					
Closing stock price (December 31, 1993)	\$29.25	\$34.25	\$79.00	\$56.50	\$52.50
Common shares outstanding (in millions)	117	136	254	573	1,355
Market value (in millions)	\$3,422	\$4,658	\$20,066	\$32,375	\$71,138
Price/revenues ratio	0.4x	0.3x	1.0x	0.5x	1.1x
Price/earnings ratio - trailing twelve	*	*	17.0x	*	*
Price/earnings ratio - future 4 qtrs.	15.4x	18.8x	14.8x	27.0x	16.1x
Avg headcount (most recent disclosure)	12,065	104,000	90,800	339,543	312,400
Net revenues/employee	\$700,001	\$131,122	\$223,756	\$185,190	\$211,911
Cash per share	\$9.60	\$8.43	\$6.47	\$10.77	\$0.59
Book value per share	\$17.55	\$35.51	\$33.51	\$35.08	\$10.63
Price/book value ratio	1.7x	1.0x	2.4x	1.6x	4.9x
Growth statistics (over comparable quarter):					
Revenue	23%	(12%)	32%	0%	3%
Research and development	(5%)	(18%)	9%	(20%)	6%
Sales and marketing	(9%)	(23%)	5%	(9%)	3%
General and administrative	n/a	n/a	n/a	n/a	n/a
Net income	(75%)	2%	358%	*	11%

- (1) Included in Apple's trailing twelve month net income is a pre-tax charge of \$321 million, or \$1.63 per share, related to the company's latest restructuring. Apple announced in July 1993 that it was consolidating numerous divisions and establishing a separate software group, Applesoft.
- (2) On January 6, 1994, Hewlett Packard announced its plans to buy a 15% stake in Taligent for approximately \$10 million.
- (3) IBM's net loss for the quarter ended September 30, 1993 was \$70 million, or \$12 per common share, after payment of \$22 million in referred dividends. Results include payments of \$1.1 billion for various employee separation programs which resulted in a decrease in cash to \$6.2 billion.
- (4) In June 1993, AT&T sold its remaining 77% interest in USL to Novell in exchange for a 3% interest in Novell common stock. The pre-tax gain on the sale of \$217 million is included in the trailing twelve month net loss. Also included is a \$287 million restructuring charge related to AT&T's NCR division.
- * Not meaningful.

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HARDWARE COMPETITION

Hardware Company Metrics (Continued)

	Dell		Silicon		
	Compaq 9/30/93	Computer 10/31/93	Intel 12/25/93	Graphics 9/30/93	Sun 12/26/93
Income statement					
Most recent quarter					
Net revenues	\$1,746	\$757	\$2,389	\$302	\$1,131
Net income (loss)	107	10	594	26	44
EPS	1.25	0.26	1.35	0.34	0.46
Trailing twelve months					
Net revenues	\$6,413	\$2,751	\$8,782	\$1,162	\$4,493
Net income (loss)	433	(24)	2,295	107	188
EPS	5.19	(0.61)	5.22	1.44	1.79
Net income (loss) as a % of net revenues	7%	(1%)	26%	9%	4%
Balance sheet					
Cash	\$419	\$266	\$3,136	\$108	\$870
Other current assets	2,566	761	2,666	578	1,219
Other assets	794	93	5,542	365	521
	<u>\$3,779</u>	<u>\$1,120</u>	<u>\$11,344</u>	<u>\$1,051</u>	<u>\$2,610</u>
Liabilities	<u>\$1,381</u>	<u>\$671</u>	<u>\$3,156</u>	<u>\$323</u>	<u>\$1,141</u>
Put Warrants	-	-	688	-	-
Equity	<u>2,398</u>	<u>449</u>	<u>7,500</u>	<u>728</u>	<u>1,469</u> (4)
	<u>\$3,779</u>	<u>\$1,120</u>	<u>\$11,344</u>	<u>\$1,051</u>	<u>\$2,610</u>
Other data					
Closing stock price (December 31, 1993)	\$73.88	\$22.63	\$62.00 (2)	\$24.75 (3)	\$29.13
Common shares outstanding (in millions)	85	40	441	76	95
Market value (in millions)	\$6,279	\$905	\$27,342	\$1,881	\$2,767
Price/revenues ratio	1.0x	0.3x	3.1x	1.6x	0.6x
Price/earnings ratio - trailing twelve	14.2x	*	11.9x	17.1x	16.3x
Price/earnings ratio - future 4 qtrs.	12.2x	13.4x	10.5x	26.6x	12.3x
Avg headcount (most recent disclosure)	9,750	3,810	20,200	3,663	13,050
Net revenues/employee	\$657,697	\$721,922	\$434,751	\$317,156	\$344,292
Cash per share	\$4.93	\$6.65	\$7.11	\$1.42	\$9.16
Book value per share	\$28.21	\$11.23	\$17.01	\$9.58	\$15.46
Price/book value ratio	2.6x	2.0x	3.6x	2.6x	1.9x
Growth statistics (over comparable quarter):					
Revenue	64%	33%	29%	31%	8%
Research and development	4%	20%	22%	30%	1%
Sales and marketing	16%	44%	9%	18%	10%
General and administrative	n/a	55%	n/a	n/a	n/a
Net income	116%	(64%) (1)	39%	97%	82%

(1) Dell's net income decreased 64% over the same period last year despite significant revenue growth due to a decrease in notebook sales and an increase in cost of sales and operating expenses. Dell's results were affected by its recall of notebooks which were discontinued in August 1993. Notebook sales generated only \$5 million in the current quarter versus \$62 million in the comparable quarter a year ago. Dell expects to re-enter the notebook market within the next two quarters.

(2) Intel's stock price dropped \$5 per share immediately following its earnings release due to higher than normal start-up expenses in two new fabs and a mix shift toward lower margin flash memory and systems.

(3) Silicon Graphics's split its stock two-for-one on December 16, 1993.

(4) In June 1993, Sun announced a 10 million share stock buyback program. Since June, the company has repurchased 7.5 million shares.

* Not meaningful

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KEY RELATIONSHIPS

KEY RELATIONSHIPS

	RR		
	Egghead 10/16/93	Merisel 9/30/93 (2)	Donnelley 9/30/93
Income statement			
Most recent quarter			
Net revenues	\$157	\$731	\$1,124
Net income	0	6	69
EPS	0.03	0.20	0.45
Trailing twelve months			
Net revenues	\$759	\$2,822	\$4,287
Net income	3	26	104
EPS	0.18	0.87	0.67
Net income as a % of net revenues	0%	1%	2%
Balance sheet			
Cash	\$15 (1)	\$0	\$13
Other current assets	218	695	1,124
Other assets	23	71	2,434
	<u>\$256</u>	<u>\$766</u>	<u>\$3,571</u>
Liabilities	\$114	\$553	\$1,784
Put Warrants	0	0	0
Equity	<u>142</u>	<u>213</u>	<u>1,787</u>
	<u>\$256</u>	<u>\$766</u>	<u>\$3,571</u>
Other data			
Closing stock price (December 31, 1993)	\$9.00	\$18.38	\$30.13
Common shares outstanding (in millions)	17	30	154
Market value (in millions)	\$153	\$551	\$4,639
Price/revenues ratio	0.2x	0.2x	1.1x
Price/earnings ratio - trailing twelve	51.4x	21.2x	45.0x
Price/earnings ratio - future 4 qtrs.	22.8x	13.5x	16.6x
Avg headcount (most recent disclosure)	2,350	1,695	30,950
Net revenues/employee	\$322,858	\$1,665,358	\$138,527
Cash per share	\$0.88	\$0.00	\$0.08
Book value per share	\$8.35	\$7.10	\$11.60
Price/book value ratio	1.1x	2.6x	2.6x
Growth statistics (over comparable quarter):			
Revenue	12%	32%	8%
Research and development	n/a	n/a	n/a
Sales and marketing	7%	24%	12%
General and administrative	n/a	n/a	n/a
Net income	(33%)	73%	(4%)

(1) Egghead's balance sheet is as of July 24, 1993.

(2) During the quarter ended September 30, 1993, Merisel signed a letter of intent with ComputerLand Corp. to acquire its U.S. franchise and distribution business. The letter of intent provides for a purchase price of between \$80 million and \$110 million, depending on the achievement of certain performance criteria following the acquisition. Current annual revenues for this business are estimated to be approximately \$1 billion.

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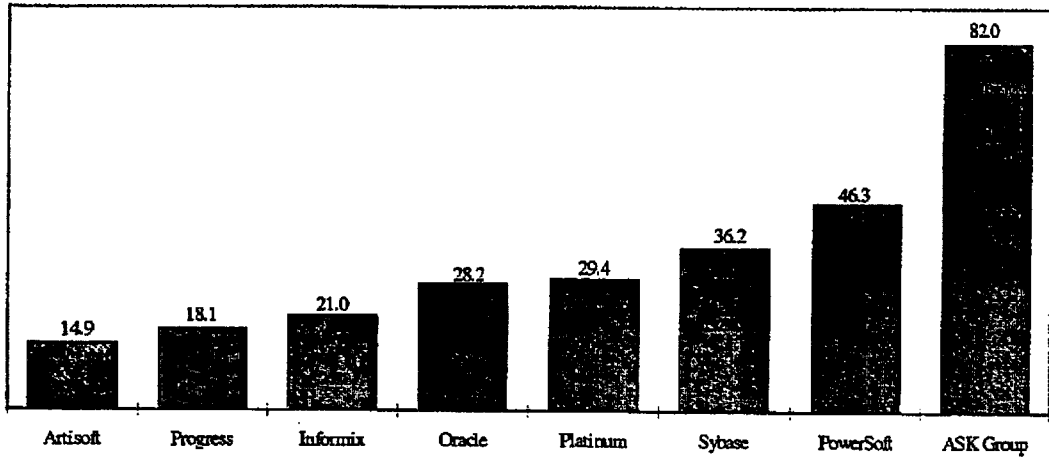
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SUB-INDUSTRY FOCUS GROUP

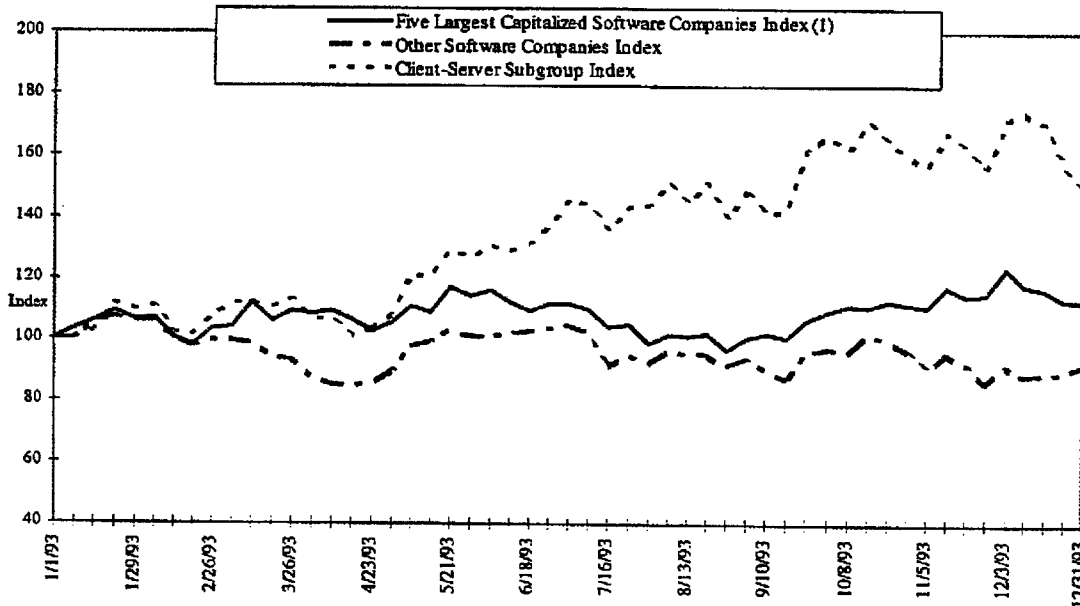
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This quarter's focus group is software companies operating in the client-server market. As can be seen in the chart below, share prices for companies in this index have out-performed other software companies.

Client-Server Software Companies Forward P/E Ratios and One Year Projected EPS Growth Rates



Weighted Share Price Indices for 1993



(1) Includes: Microsoft, Oracle, Computer Associates, Novell, Lotus

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SUB-INDUSTRY FOCUS GROUP

Client Server Metrics

	ASK	Artisoft	Informix	Oracle
	9/30/93	9/30/93	10/3/93	11/30/93
Income statement				
Most recent quarter				
Net revenues	\$84	\$20	\$90	\$452
Net income	(7)	3	15	62
EPS	(0.29)	0.17	0.21	0.21
Trailing twelve months				
Net revenues	\$426	\$83	\$348	\$1,693
Net income	1	9	60	198
EPS	0.04	0.50	0.88	0.77
Net income as a % of net revenues	0%	11%	17%	12%
Balance sheet				
Cash	\$16	\$27	\$121 (1)	\$292
Other current assets	148	26	109	503
Other assets	133	15	52	434
	<u>\$297</u>	<u>\$68</u>	<u>\$282</u>	<u>\$1,229</u>
Liabilities	\$154	\$7	\$111	\$636
Put Warrants	0	0	0	0
Equity	143	61	171 (2)	593 (3)
	<u>\$297</u>	<u>\$68</u>	<u>\$282</u>	<u>\$1,229</u>
Other data				
Closing stock price (December 31, 1993)	\$13.13	\$14.88	\$21.25	\$28.75 (4)
Common shares outstanding (in millions)	23	17	68	296
Market value (in millions)	\$302	\$253	\$1,445	\$8,510
Price/revenues ratio	0.7x	3.1x	4.2x	5.0x
Price/earnings ratio - trailing twelve	304.7x	29.8x	24.0x	37.5x
Price/earnings ratio - future 4 qtrs.	82.0x	14.9x	21.0x	28.2x
Avg headcount (most recent disclosure)	2,297	313	1,283	8,704
Net revenues/employee	\$185,606	\$264,204	\$270,874	\$194,501
Cash per share	\$0.70	\$1.59	\$1.78	\$0.99
Book value per share	\$6.22	\$3.59	\$2.51	\$2.00
Price/book value ratio	2.1x	4.1x	8.5x	14.4x
Growth statistics (over comparable quarter):				
Revenue	0%	(9%)	32%	28%
Research and development	(2%)	(0%)	54%	35%
Sales and marketing	4%	5%	41%	8%
General and administrative	n/a	28%	10%	10%
Net income	11%	(15%)	21%	86%

- (1) In November 1993, Informix signed an agreement with IDK Frontec, a privately-held Swedish corporation, under which Informix will acquire 12% of IDK Frontec for approximately \$2.1 million.
- (2) In May 1993, Informix announced that its Board had authorized a stock repurchase program. Repurchases to date total 290,000 shares for \$6.4 million.
- (3) On October 12, 1993, Oracle announced a two-for-one stock split of the company's common stock. The split was effective November 8, 1993. The company also announced an expansion of its stock repurchase plan to include an additional 2.5 million shares (pre-split). The company has repurchased approximately 2.0 million shares since the program's inception in July 1992.
- (4) Oracle stock has appreciated 102% since its stock split on November 8, 1993.

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SUB-INDUSTRY FOCUS GROUP

Client Server Metrics (Continued)

	Platinum	Powersoft	Progress	Sybase
	9/30/93	12/31/93	(3) 8/31/93	9/30/93
Income statement				
Most recent quarter				
Net revenues	\$16	\$20	\$27	\$113
Net income (loss)	1	3	3	11
EPS	0.11	0.26	0.47	0.43
Trailing twelve months				
Net revenues	\$48	\$51	\$104	\$372
Net income (loss)	(14) (1)	8	12	37
EPS	(1.04)	0.77	1.96	1.46
Net income (loss) as a % of net revenues	(30%)	16%	11%	10%
Balance sheet				
Cash	\$39	\$42	\$60	\$107
Other current assets	20	20	21	114
Other assets	17	4	16	74
	<u>\$76</u>	<u>\$66</u>	<u>\$97</u>	<u>\$295</u>
Liabilities	\$14	\$16	\$32	\$130
Put Warrants	0	0	0	0
Equity	62	50	65	165 (4)
	<u>\$76</u>	<u>\$66</u>	<u>\$97</u>	<u>\$295</u>
Other data				
Closing stock price (December 31, 1993)	\$25.25	\$40.75	\$40.75	\$42.00
Common shares outstanding (in millions)	14 (2)	11	6	26
Market value (in millions)	\$354	\$448	\$245	\$1,092
Price/revenues ratio	7.3x	8.8x	2.4x	2.9x
Price/earnings ratio - trailing twelve	*	53.0x	20.8x	28.8x
Price/earnings ratio - future 4 qrts.	29.4x	46.3x	46.3x	36.2x
Avg headcount (most recent disclosure)	207	106	106	1,348
Net revenues/employee	\$233,303	\$480,868	\$976,849	\$276,100
Cash per share	\$2.79	\$3.82	\$10.00	\$4.12
Book value per share	\$4.43	\$4.55	\$10.83	\$6.35
Price/book value ratio	5.7x	9.0x	3.8x	6.6x
Growth statistics (over comparable quarter):				
Revenue	160%	143%	22%	67%
Research and development	185%	117%	17%	72%
Sales and marketing	162%	138%	31%	69%
General and administrative	119%	139%	n/a	51%
Net income	458%	29%	11%	88%

- (1) Platinum's loss for the trailing twelve months is due to charges of \$21 million incurred in the acquisitions of three software companies in 1993.
- (2) On August 12, 1993, Platinum announced that the company would split its stock three-for-two effective September 2, 1993. Immediately after the split, the company had 13 million shares outstanding.
- (3) During the quarter ended December 31, 1993, Powersoft signed a letter of intent to acquire WATCOM, a leading developer of a SQL database and C/C++ compiler. The price is approximately \$50 million. Powersoft has also entered into \$1.1 million licensing agreement with GTE as well as its agreement with Lotus to develop a PowerBuilding Library for Lotus Notes by the first quarter of 1994.
- (4) On December 1, 1993, Sybase announced its intent to acquire OASIS Group PLC, an international business re-engineering consultant firm. Under the terms of the proposal, Sybase will issue new shares of common stock valued at \$21 million in exchange for all outstanding ordinary shares of OASIS. The acquisition should be completed in early 1994.
- * Not meaningful

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Channel Reporting

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CHANNEL SUMMARY

Results of Operations (in millions)

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$416.5	103 %	\$98.9	120 %	\$147.3	91 %	\$170.3	106 %
Europe FG	323.8	87	50.7	74	99.7	89	173.4	90
ICON FG	60.5	75	16.2	85	24.1	83	20.3	62
Far East FG	53.8	118	14.1	113	20.9	99	18.8	159
OEM	268.3	138	18.9	251	20.6	136	228.8	133
Other	6.1	81	(14.0)	(448)	25.2	130	(5.1)	NM
Worldwide	<u>\$1,129.0</u>	<u>102</u>	<u>\$184.8</u>	<u>96</u>	<u>\$337.8</u>	<u>94</u>	<u>\$606.4</u>	<u>109</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	37 %	37 %	24 %	20 %	35 %	40 %	41 %	40 %
Europe FG	29	34	16	18	31	30	54	52
ICON FG	5	7	27	24	40	36	34	40
Far East FG	5	4	26	27	39	47	35	26
OEM	24	18	7	4	8	8	85	88
Other	1	1	(232)	42	416	260	(84)	(202)
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>16</u>	<u>17</u>	<u>30</u>	<u>32</u>	<u>54</u>	<u>50</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$704.2	103 %	\$163.2	120 %	\$266.1	85 %	\$274.9	117 %
Europe FG	585.3	93	96.9	85	185.5	87	303.0	100
ICON FG	127.0	91	29.6	88	47.4	82	50.0	106
Far East FG	114.1	125	28.0	117	43.7	105	42.4	165
OEM	523.4	140	30.1	194	40.0	134	453.3	138
Other	57.6	467	(4.1)	(79)	65.7	170	(4.0)	NM
Worldwide	<u>\$2,111.6</u>	<u>109</u>	<u>\$343.7</u>	<u>105</u>	<u>\$648.4</u>	<u>93</u>	<u>\$1,119.5</u>	<u>123</u>

	Net Revenue Mix			Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	%	pts Var	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	33 %		35 %	23 %	20 %	38 %	46 %	39 %	34 %
Europe FG	28		33	17	18	32	34	52	48
ICON FG	6		7	23	24	37	42	39	34
Far East FG	5		5	25	26	38	45	37	28
OEM	25		19	6	4	8	8	87	88
Other	3		1	(7)	42	114	313	(7)	(254)
Worldwide	<u>100 %</u>		<u>100 %</u>	<u>16</u>	<u>17</u>	<u>31</u>	<u>36</u>	<u>53</u>	<u>47</u>

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CHANNEL SUMMARY

Net Revenue and Responsibility Margin by Subsidiary (in millions)

Q94-2

	Excluding OEM				Including OEM			
	Net Revenue		Responsibility Margin		Net Revenue		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America								
United States	\$384.7	104.6 %	\$153.9	108.3 %	\$555.7	114.6 %	\$296.8	122.3 %
Canada	31.9	87.1	16.1	85.9	35.5	90.8	19.6	93.1
Other	(0.0)	NM	0.3	NM	0.0	NM	0.0	NM
	<u>416.5</u>	<u>103.1</u>	<u>170.3</u>	<u>105.9</u>	<u>591.1</u>	<u>112.8</u>	<u>316.4</u>	<u>120.0</u>
Europe								
Denmark	6.0	75.1	3.1	61.1	6.4	79.3	3.5	68.0
Finland	2.9	63.1	1.4	46.8	5.3	74.0	3.8	67.1
Norway	4.9	58.9	2.4	42.4	6.3	73.7	3.6	61.3
England	51.7	78.4	23.6	78.4	60.3	85.1	31.4	90.5
Sweden	17.9	88.6	7.5	89.0	19.1	92.9	8.5	98.5
Hungary	2.0	179.7	1.1	236.3	1.9	163.8	1.1	196.1
Russia	0.8	106.2	0.2	NM	1.0	92.8	0.3	153.1
Czechoslovakia	3.1	178.7	2.1	259.2	3.5	182.0	2.4	254.5
Switzerland	20.5	118.1	13.7	136.6	21.2	119.3	14.3	138.5
Germany	93.8	96.2	54.4	107.6	120.8	105.0	80.4	119.8
Poland	1.5	108.8	0.4	72.3	2.2	129.2	1.0	131.2
Austria	9.0	96.4	6.2	110.5	9.3	96.5	6.5	109.8
Netherlands	7.5	87.9	2.5	75.3	9.9	97.3	4.6	96.5
Spain	5.1	68.1	1.8	46.5	6.0	70.3	2.5	52.5
France	65.1	71.8	35.0	65.9	68.0	73.4	37.2	67.9
Italy	21.2	121.1	13.4	143.3	26.1	120.5	18.0	134.9
Belgium	9.1	90.8	5.7	94.0	9.8	95.3	6.3	100.5
Portugal	2.4	72.9	1.1	66.2	2.5	71.0	1.3	63.7
EHQ / Other	(0.8)	(250.3)	(2.2)	NM	(1.6)	(420.1)	(3.8)	NM
	<u>323.8</u>	<u>86.6</u>	<u>173.4</u>	<u>89.7</u>	<u>377.9</u>	<u>92.0</u>	<u>223.0</u>	<u>98.2</u>
ICON								
Caribbean	0.4	65.7	0.0	23.9	0.4	63.7	0.0	21.1
Ecuador	0.7	167.3	0.2	189.7	0.7	167.3	0.2	231.6
Chile	1.4	80.1	0.6	70.6	1.6	87.4	0.7	81.5
Colombia	1.3	103.4	0.7	115.1	1.4	106.3	0.7	121.3
Venezuela	1.0	60.7	0.5	73.0	1.7	87.6	1.0	94.8
Brazil	6.0	89.8	2.4	76.1	7.4	99.9	3.8	98.1
Argentina	2.3	112.2	0.9	165.2	2.3	105.3	0.9	133.5
Mexico	8.1	57.5	4.1	53.8	8.4	58.6	4.4	55.3
Morocco	0.4	58.1	0.1	28.3	0.4	56.5	0.1	27.1
Middle East	1.7	70.5	0.2	29.1	2.2	87.6	0.5	62.7
Turkey	2.2	98.3	0.9	94.1	2.3	97.4	1.0	90.3
South Africa	4.5	90.6	2.0	92.5	4.7	90.4	2.2	92.3
Greece	0.7	71.1	0.2	48.0	0.8	75.0	0.3	58.2
Israel	1.2	136.1	0.5	409.6	1.5	140.7	0.8	263.1
India	0.6	112.8	0.2	112.2	0.7	101.9	0.3	92.7
Thailand	0.7	84.0	0.4	86.6	0.7	78.9	0.4	76.8
Malaysia	0.9	53.3	0.4	51.2	1.2	62.9	0.8	62.6
Singapore	2.6	72.2	1.2	69.7	4.9	88.4	3.4	92.9
New Zealand	4.7	105.0	2.6	112.9	5.0	105.1	2.9	110.9
Australia	19.5	67.3	4.4	38.4	22.0	70.5	6.0	44.0
RHQ/Other	(0.1)	NM	(2.2)	NM	(0.1)	NM	(2.2)	NM
	<u>60.5</u>	<u>75.2</u>	<u>20.3</u>	<u>62.3</u>	<u>70.0</u>	<u>79.7</u>	<u>28.1</u>	<u>70.8</u>
Far East								
PRC	0.9	123.9	0.6	234.8	0.9	123.9	0.6	234.8
Korea	4.4	141.3	2.3	191.0	9.2	101.9	6.8	97.0
Taiwan	2.2	45.0	(0.7)	(33.2)	10.4	72.1	7.3	67.0
Japan	41.9	125.7	14.5	188.9	63.4	136.7	32.9	164.0
Hong Kong	3.3	100.4	1.6	106.7	7.9	145.3	6.1	165.6
RHQ/Other	1.1	NM	0.5	NM	(7.9)	NM	(8.6)	NM
	<u>53.8</u>	<u>118.5</u>	<u>18.8</u>	<u>159.2</u>	<u>84.0</u>	<u>110.4</u>	<u>45.1</u>	<u>110.1</u>
Worldwide								
Other	6.1	81.1	(5.1)	NM	6.1	81.1	(6.1)	NM
Total	<u>\$860.7</u>	<u>94.4</u>	<u>\$377.7</u>	<u>98.5</u>	<u>\$1,129.0</u>	<u>102.1</u>	<u>\$606.4</u>	<u>109.2</u>

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CHANNEL SUMMARY

Net Revenue and Responsibility Margin by Subsidiary (in millions)

FYTD94

	Excluding OEM				Including OEM			
	Net Revenue		Responsibility Margin		Net Revenue		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America								
United States	\$652.8	104.0 %	\$250.2	119.7 %	\$975.7	115.3 %	\$520.0	132.1 %
Canada	51.4	90.6	24.7	94.9	58.1	93.9	30.3	98.3
Other	0.0	NM	0.0	NM	0.0	NM	0.0	NM
	<u>704.2</u>	<u>102.9</u>	<u>274.9</u>	<u>116.9</u>	<u>1,033.8</u>	<u>113.9</u>	<u>550.3</u>	<u>129.7</u>
Europe								
Denmark	10.6	84.7	6.0	77.3	11.3	88.0	6.7	82.8
Finland	4.6	67.2	2.4	53.7	9.3	73.6	6.9	68.5
Norway	9.1	71.3	5.1	60.5	11.5	87.9	7.3	83.5
England	98.1	85.2	46.4	95.2	112.1	89.9	59.2	103.6
Sweden	26.7	86.1	8.7	78.4	29.0	91.7	10.7	93.2
Hungary	3.0	189.6	1.9	358.7	3.0	169.5	1.9	270.7
Russia	1.3	104.0	0.2	NM	1.5	82.8	0.3	120.5
Czechoslovakia	4.3	163.6	3.0	301.2	4.9	161.5	3.5	265.1
Switzerland	38.0	123.2	25.0	143.5	39.2	124.3	26.1	145.3
Germany	177.9	101.7	100.3	114.8	221.6	104.9	142.6	117.1
Poland	2.5	108.3	1.1	151.4	3.6	126.8	2.3	176.0
Austria	16.5	100.1	10.8	110.9	17.3	100.8	11.6	111.3
Netherlands	12.0	81.0	2.2	47.3	16.5	92.0	6.4	84.0
Spain	7.4	75.2	1.8	46.9	8.8	77.4	3.0	57.5
France	110.7	73.7	55.5	66.6	115.4	74.7	59.2	68.2
Italy	43.5	168.3	29.1	234.1	53.6	158.1	38.7	192.4
Belgium	13.2	80.3	6.8	75.4	14.6	86.5	8.1	85.6
Portugal	4.3	88.0	2.1	87.3	4.6	83.5	2.4	79.5
EHQ/Other	1.5	270.8	(5.5)	NM	1.3	194.6	(6.3)	NM
	<u>585.3</u>	<u>92.7</u>	<u>303.0</u>	<u>99.6</u>	<u>679.1</u>	<u>96.3</u>	<u>390.7</u>	<u>104.9</u>
ICON								
Caribbean	1.0	94.8	0.4	170.9	1.0	91.5	0.4	143.3
Ecuador	1.7	220.7	0.9	593.3	1.7	220.7	0.9	826.2
Chile	2.8	89.5	1.2	96.8	3.0	93.3	1.3	102.6
Colombia	3.4	146.2	1.7	180.2	3.6	148.7	1.9	184.6
Venezuela	2.7	104.5	1.6	152.1	3.7	114.8	2.4	138.8
Brazil	11.5	126.1	4.6	171.2	13.6	128.5	6.6	163.1
Argentina	5.3	133.9	2.5	223.7	5.3	126.0	2.5	183.4
Mexico	16.2	73.1	7.7	76.0	16.6	73.3	8.1	75.8
Morocco	0.7	64.6	0.3	72.3	0.7	62.1	0.3	63.9
Middle East	4.5	99.3	1.5	112.2	5.0	106.7	1.9	121.8
Turkey	3.7	99.0	1.7	132.4	3.8	96.5	1.8	120.0
South Africa	8.5	89.7	4.2	109.6	9.1	91.2	4.8	110.1
Greece	1.5	97.8	0.7	135.3	1.6	102.2	0.8	144.9
Israel	3.0	180.8	1.7	544.5	3.8	183.3	2.4	351.4
India	1.1	116.1	0.5	147.2	1.4	105.7	0.8	112.3
Thailand	1.1	73.6	0.5	62.5	1.1	69.0	0.5	54.9
Malaysia	1.8	57.9	0.9	55.0	2.5	69.3	1.5	72.1
Singapore	5.4	83.4	2.7	93.2	9.9	97.0	7.0	105.9
New Zealand	8.7	103.1	4.6	109.3	9.2	102.7	5.0	107.0
Australia	42.2	82.3	13.7	77.1	48.5	87.0	18.5	84.1
RHQ/Other	0.1	NM	(3.7)	NM	0.1	NM	(3.7)	NM
	<u>127.0</u>	<u>91.5</u>	<u>50.0</u>	<u>105.9</u>	<u>145.1</u>	<u>94.9</u>	<u>65.7</u>	<u>108.0</u>
Far East								
PRC	1.6	125.2	0.9	255.6	1.6	125.2	0.9	255.6
Korea	9.9	173.2	5.8	282.2	21.0	123.1	16.5	125.0
Taiwan	8.8	105.6	3.9	125.7	25.9	92.0	20.7	95.3
Japan	85.9	122.2	28.9	147.1	135.0	136.7	73.4	157.4
Hong Kong	6.5	111.5	3.4	129.1	13.3	136.8	10.0	155.2
RHQ/Other	1.5	NM	(0.6)	NM	(0.7)	NM	(2.8)	NM
	<u>114.1</u>	<u>124.8</u>	<u>42.4</u>	<u>163.7</u>	<u>195.9</u>	<u>126.5</u>	<u>118.6</u>	<u>137.5</u>
Worldwide								
Other	57.6	467.2	(4.0)	NM	57.6	467.2	(5.9)	NM
Total	<u>\$1,588.2</u>	<u>101.9</u>	<u>\$666.2</u>	<u>114.7</u>	<u>\$2,111.6</u>	<u>109.2</u>	<u>\$1,119.5</u>	<u>123.0</u>

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CHANNEL SUMMARY

METRICS SUMMARY (ANNUALIZED IN THOUSANDS)

	Finished Goods					OEM
	No. Amer.	Europe	ICON	Far East	Aggregate	
Revenue per Employee						
Actual	\$463	\$545	\$417	\$548	\$492	\$5,657
Plan	411	567	479	450	473	3,920
Q94-1	314	440	480	564	385	5,426
Q93-4	405	508	524	599	460	4,642
Q93-3	345	619	513	467	454	4,342
Q93-2	388	709	588	408	505	3,444
Q93-1	356	617	821	215	457	3,209
People expenses per Employee						
Actual	73	77	80	112	77	101
Plan	75	78	80	107	78	103
Q94-1	71	76	80	98	75	90
Q93-4	77	75	101	78	78	128
Q93-3	68	78	93	66	73	96
Q93-2	69	83	97	61	74	98
Q93-1	66	87	87	59	74	94
Facilities expenses per Employee						
Actual	23	25	30	32	25	15
Plan	25	27	31	34	26	17
Q94-1	21	27	29	31	24	15
Q93-4	21	32	22	33	25	26
Q93-3	18	30	29	30	23	22
Q93-2	18	31	31	21	23	17
Q93-1	18	33	22	19	23	16
Marketing expense % Net revenue						
Actual	13%	12%	9%	12%	12%	0%
Plan	13%	10%	9%	14%	12%	0%
Q94-1	10%	8%	9%	13%	9%	0%
Q93-4	5%	10%	9%	20%	8%	0%
Q93-3	21%	6%	8%	12%	12%	2%
Q93-2	19%	10%	12%	19%	15%	3%
Q93-1	13%	10%	5%	20%	11%	2%

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Headcount Summary

	Q94-2			FY94
	Actual	Plan	Variance	Plan
North America FG	3,558	3,930	372	3,878
Europe FG	2,405	2,676	271	2,743
ICON FG	602	680	78	680
Far East FG	435	473	38	527
OEM	190	199	9	201
Other	297	306	9	306
	<u>7,487</u>	<u>8,264</u>	<u>777</u>	<u>8,335</u>

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CHANNEL SUMMARY

Top Customers (in millions)

Q94-2

	<u>No Amer</u>	<u>Europe</u>	<u>ICON</u>	<u>Far East</u>	<u>OEM</u>	<u>Worldwide</u>
Ingram Micro	\$ 146	\$ 6	\$ 2	\$ --	\$ --	\$ 154
Merisel	99	30	5	--	--	134
Egghead	49	--	--	--	--	49
C2000	--	71	--	--	--	71
IBM	--	--	--	--	14	14
Compaq	--	--	--	--	23	23
Gateway 2000	--	--	--	--	15	15
Soft Bank	--	--	--	12	--	12
Comp USA	--	--	--	--	--	0
Software Spectrum	22	--	--	--	--	22
Macrotron	--	17	--	--	--	17
Other Top Customers	76	76	20	20	205	397
	<u>\$ 392</u>	<u>\$ 200</u>	<u>\$ 27</u>	<u>\$ 32</u>	<u>\$ 257</u>	<u>\$ 907</u>
Percent of Gross Revenue	<u>81%</u>	<u>58%</u>	<u>40%</u>	<u>55%</u>	<u>100%</u>	<u>72%</u>

FYTD94

	<u>No Amer</u>	<u>Europe</u>	<u>ICON</u>	<u>Far East</u>	<u>OEM</u>	<u>Worldwide</u>
Ingram Micro	\$ 235	\$ 11	\$ --	\$ --	\$ --	\$ 246
Merisel	166	57	11	--	--	234
Egghead	72	--	--	--	--	72
C2000	--	129	--	--	--	129
IBM	--	--	--	--	36	36
Compaq	--	--	--	--	43	43
Gateway 2000	--	--	--	--	29	29
Soft Bank	--	--	--	21	--	21
Comp USA	11	--	--	--	--	11
Software Spectrum	32	--	--	--	--	32
Macrotron	--	31	--	--	--	31
Other Top Customers	100	125	37	45	378	686
	<u>\$ 616</u>	<u>\$ 353</u>	<u>\$ 48</u>	<u>\$ 67</u>	<u>\$ 487</u>	<u>\$ 1,571</u>
Percent of Gross Revenue	<u>78%</u>	<u>58%</u>	<u>36%</u>	<u>57%</u>	<u>100%</u>	<u>74%</u>

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Channel Reporting

MS/SA 05009079

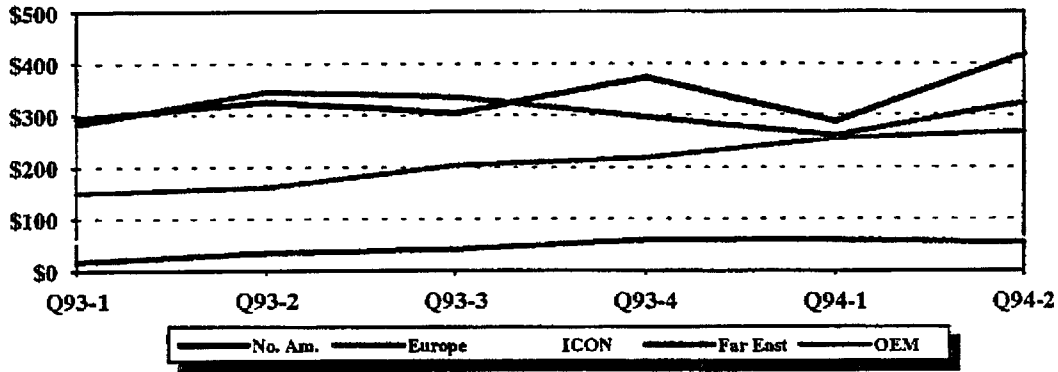
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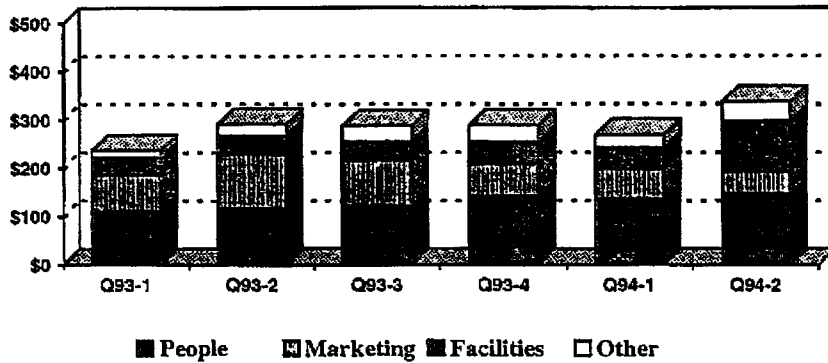
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TREND ANALYSES

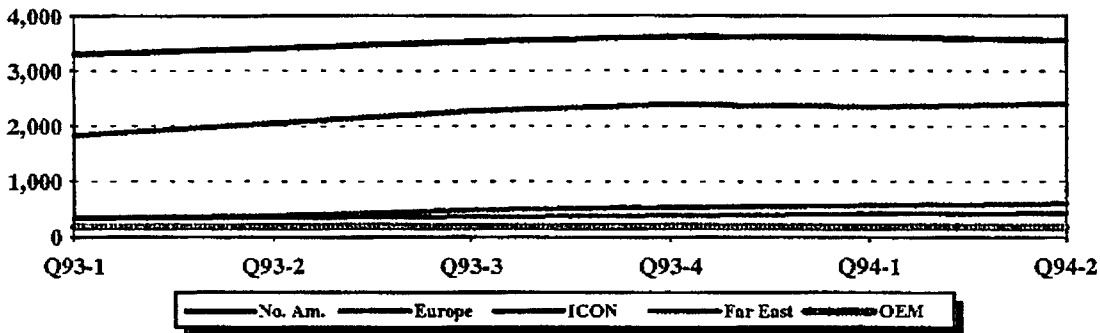
Net Revenue Trend (in millions)



Controllable Expenses (in millions)



Headcount Trend



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NORTH AMERICA FINISHED GOODS

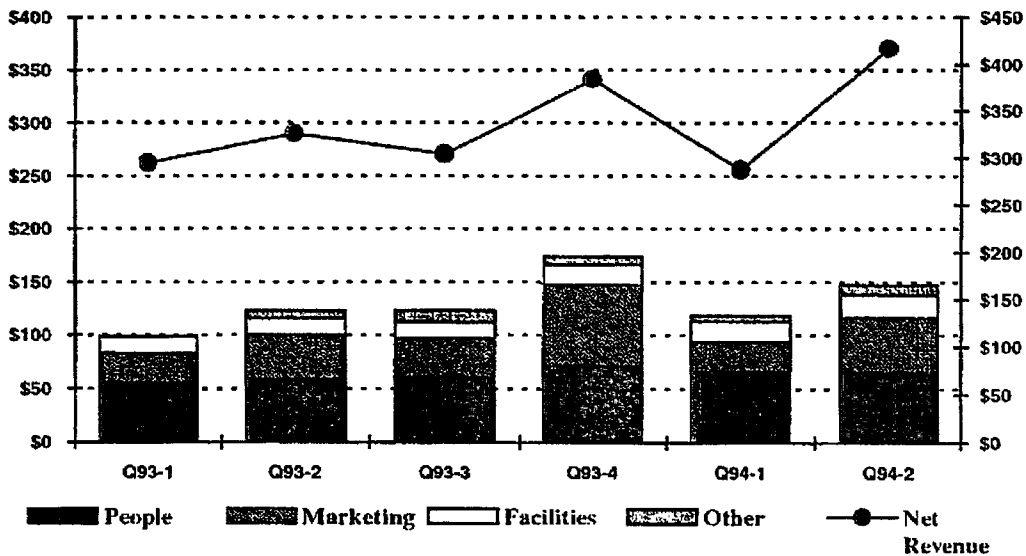
NORTH AMERICA FINISHED GOODS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$416.5	\$404.2	\$12.4	\$704.2	\$684.5	\$19.7
Cost of revenue	98.9	82.3	(16.6)	163.2	136.3	(26.9)
Gross profit	317.6	321.8	(4.2)	541.0	548.3	(7.2)
People expenses	65.3	73.5	8.2	130.9	148.8	17.9
Facilities expenses	20.9	24.1	3.2	40.3	47.1	6.7
Marketing expenses	52.8	54.3	1.5	80.9	98.7	17.8
Other expenses	8.3	9.1	0.8	14.0	18.7	4.7
Controllable expenses	147.3	161.0	13.7	266.1	313.2	47.1
Responsibility margin	170.3	160.8	9.5	274.9	235.1	39.8
Net shared resources	(6.9)	(7.9)	(0.9)	(14.3)	(15.7)	(1.4)
Shared resource margin	\$177.2	\$168.6	\$8.6	\$289.2	\$250.7	\$38.4
Net revenue	100.0 %	100.0 %	- %	100.0 %	100.0 %	- %
Cost of revenue	23.8	20.4	(3.4)	23.2	19.9	(3.3)
Controllable expenses	35.4	39.8	4.5	37.8	45.8	8.0
Responsibility margin	40.9	39.8	1.1	39.0	34.3	4.7
Net shared resources	(1.7)	(1.9)	(0.3)	(2.0)	(2.3)	(0.3)
Shared resource margin	42.6 %	41.7 %	0.8 %	41.1 %	36.6 %	4.4 %

TREND ANALYSES

Net Revenue & Controllable Expenses (in millions)



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Revenue Summary - Q94-2 (revenue in millions, units in thousands)

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$105.1	\$82.5	27%	336.3	265.7	27%	\$313	\$311	1%
MAC Office	16.3	12.5	30%	44.4	34.4	29%	367	364	1%
Excel PU *	15.8	29.8	(47%)	98.2	200.3	(51%)	161	149	8%
Word PU *	38.9	54.7	(29%)	267.6	365.5	(27%)	145	150	(3%)
Graphics PU *	5.4	4.7	15%	34.8	32.1	8%	156	147	6%
Project PU	14.6	11.5	27%	46.2	39.1	18%	317	294	8%
DAD BU New Users **	196.2	195.8	0%	827.4	937.1	(12%)	237	209	13%
WIN Office	38.6	11.1	248%	228.7	58.9	288%	169	188	(10%)
MAC Office	2.4	2.2	8%	12.5	7.9	57%	192	278	(31%)
Excel PU *	2.8	16.6	(83%)	41.8	290.5	(86%)	68	57	19%
Word PU *	24.3	24.3	(0%)	316.8	292.6	8%	77	83	(8%)
Graphics PU *	0.5	0.3	58%	11.3	13.4	(15%)	46	25	86%
Project PU	0.7	0.3	188%	11.5	2.4	380%	64	107	(40%)
DAD BU Existing Users **	69.4	54.8	27%	622.5	665.8	(7%)	111	82	35%
Basic PU	6.7	6.4	4%	45.3	42.4	7%	147	151	(3%)
Database Mgmt (Access) PU *	11.8	7.2	64%	83.9	33.9	147%	141	212	(34%)
Fox Database PU *	6.1	11.3	(46%)	(18.5)	55.2	(134%)	(329)	204	(261%)
Languages PUs	5.6	8.0	(30%)	51.8	46.0	13%	108	174	(38%)
DBDT BU *	30.2	32.9	(8%)	162.5	177.4	(8%)	186	185	0%
Entry PU	30.1	17.0	78%	955.0	473.7	102%	32	36	(12%)
Multimedia Publishing PU	15.7	7.9	98%	264.0	133.8	97%	59	59	0%
Works PU	11.6	10.9	7%	218.1	164.7	32%	53	66	(19%)
Consumer BU	57.5	35.8	61%	1,437.1	772.2	86%	40	46	(14%)
Hardware BU	25.9	28.0	(7%)	445.9	389.2	15%	58	72	(19%)
MS-DOS BU	34.1	13.2	159%	1,968.4	339.6	480%	17	39	(55%)
Windows BU	36.9	15.9	132%	654.3	303.8	115%	56	52	8%
Win NT Family	1.1	18.7	(94%)	11.2	95.8	(88%)	94	195	(52%)
Win NT Adv. Server Family	2.9	5.2	(44%)	4.3	7.9	(46%)	672	655	3%
Win NT Server (SQL/SNA)	5.9	6.1	(4%)	21.5	6.0	261%	275	1,031	(73%)
Other Operating Systems PU	2.7	3.1	(12%)	8.8	12.0	(27%)	308	257	20%
Advanced Systems BU	12.6	33.1	(62%)	45.8	121.7	(62%)	275	272	1%
Workgroup BU *	10.0	9.6	4%	298.0	145.1	105%	33	66	(49%)
Digital Office Systems PUs	0.1	1.8	(95%)	1.2	16.2	(93%)	76	111	(32%)
ACT and APD PUs	2.6	4.2	(38%)	130.3	128.1	2%	20	33	(39%)
Other PUs	0.5	0.3	56%	0.7	2.5	(74%)	730	122	496%
Other	3.2	6.3	(50%)	132.2	146.8	(10%)	24	43	(44%)
Finished goods revenue	475.8	425.4	12%	6,594.0	3,998.7	65%	72	106	(32%)
Other materials	8.0	0.0	NM	0.3	0.0	NM			
Total FG gross revenue	\$483.8	\$425.4	14%	6,594.3	3,998.7	65%			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

Note: Negative unit sales for the Fox PU shown above reflect an adjustment to properly report YTD units for the maintenance agreement with General Electric.

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Revenue Summary - FYTD94 (revenue in millions, units in thousands)

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$155.3	\$130.1	19%	481.7	413.9	16%	\$322	\$314	3%
MAC Office	28.4	22.5	26%	78.0	61.3	27%	364	366	(1%)
Excel PU *	42.2	42.7	(1%)	292.4	296.2	(1%)	144	144	(0%)
Word PU *	70.9	75.5	(6%)	542.2	520.3	4%	131	145	(10%)
Graphics PU *	11.3	10.0	12%	80.5	68.7	17%	140	146	(4%)
Project PU	27.2	24.5	11%	88.2	83.2	6%	308	295	5%
DAD BU New Users **	335.2	305.4	10%	1,563.2	1,443.7	8%	214	212	1%
WIN Office	41.2	15.6	164%	284.2	88.5	221%	145	177	(18%)
MAC Office	3.6	3.9	(9%)	30.8	13.5	128%	116	291	(60%)
Excel PU *	6.9	18.2	(62%)	102.2	314.1	(67%)	67	58	16%
Word PU *	29.1	29.1	(0%)	396.8	353.2	12%	73	83	(11%)
Graphics PU *	1.0	0.6	76%	25.2	19.9	27%	41	29	39%
Project PU	1.5	0.5	198%	24.0	4.9	388%	63	104	(39%)
DAD BU Existing Users **	83.4	68.0	23%	863.1	794.0	9%	97	86	13%
Basic PU	15.2	13.8	10%	124.7	101.9	22%	122	135	(10%)
Database Mgmt (Access) PU *	18.4	16.0	15%	260.0	73.8	252%	71	217	(67%)
Fox Database PU *	13.5	32.0	(58%)	95.6	161.7	(41%)	141	198	(28%)
Languages PUs	12.5	15.6	(19%)	131.7	93.2	41%	95	167	(43%)
DBDT BU *	59.7	77.3	(23%)	612.1	430.6	42%	98	179	(46%)
Entry PU	46.7	28.1	66%	1,345.3	707.4	90%	35	40	(13%)
Multimedia Publishing PU	19.2	10.9	75%	320.8	183.1	75%	60	60	0%
Works PU	20.4	18.3	11%	414.3	287.2	44%	49	64	(23%)
Consumer BU	86.3	57.3	50%	2,080.4	1,177.8	77%	41	49	(15%)
Hardware BU	49.6	54.7	(9%)	851.3	743.5	14%	58	74	(21%)
MS-DOS BU	36.1	23.0	57%	2,053.7	597.0	244%	18	39	(54%)
Windows BU	60.6	26.9	125%	1,121.3	507.6	121%	54	53	2%
Win NT Family	15.4	48.4	(68%)	76.3	249.4	(69%)	202	194	4%
Win NT Adv. Server Family	6.3	11.8	(47%)	9.8	18.1	(46%)	641	652	(2%)
Win NT Server (SQLSNA)	7.3	13.9	(47%)	35.0	16.5	112%	209	842	(75%)
Other Operating Systems PU	6.7	8.5	(21%)	22.9	41.0	(44%)	293	207	42%
Advanced Systems BU	35.7	82.5	(57%)	144.0	324.9	(56%)	248	254	(2%)
Workgroup BU *	19.3	17.0	14%	647.7	279.1	132%	30	61	(51%)
Digital Office Systems PUs	0.3	3.6	(91%)	3.3	32.0	(90%)	96	111	(14%)
ACT and APD PUs	4.4	6.1	(27%)	222.7	179.5	24%	20	34	(41%)
Other PUs	2.1	0.3	572%	7.2	2.5	189%	285	122	133%
Other	6.8	10.0	(32%)	233.3	214.0	9%	29	47	(37%)
Finished goods revenue	772.7	722.1	7%	10,170.1	6,512.3	56%	76	111	(31%)
Other materials	17.1	0.0	NM	0.7	0.0	NM			
Total FG gross revenue	\$789.8	\$722.1	9%	10,170.8	6,512.3	56%			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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Q94-2

Revenue

- Net revenue for the quarter was 103% of plan. Affecting revenue were the successful shipment of Win Office 4.0 in October and the delay in the release of Win Excel 5.0 until very late in the quarter. Win Office exceeded plan by \$50 million and Excel was \$28 million below plan.
- In light of the delay in the release of Excel 5.0 and because Win PowerPoint 4.0 was not scheduled to release until March 1994, Win Office 4.0 was shipped with coupons which can be redeemed for subsequent fulfillment of these version upgrades. A portion of the Office revenue billed upon shipment of the Win Office 4.0 box attributable to the subsequent upgrades was deferred, to be recognized as revenue when the upgrades later ship. The total amount deferred (approximately \$42 million) was computed based on the relative value of the components of the box together with an assumption that all coupons would be redeemed, and represented about 17% of gross revenue billed for Win Office 4.0.
- The release of MS-DOS 6.2 (which was not budgeted) resulted in the MS-DOS Business Unit exceeding plan by 159%. The successful upgraded release of WFW 3.11 caused the Windows product unit revenues to aggregate 131% of plan. Consumer revenues were 61% over plan paced by strong sales of Flight Simulator. Revenue from Advanced Systems business unit was below plan by \$20 million principally from the shortfall in revenue of the standard product of Windows NT.
- At the end of Q94-2, stockouts totaled \$63 million due mostly to Excel 5.0 (\$30 million) and Win Encarta 1994 (\$8 million). The Win Excel stockout was due to the receipt of fulfillment coupons from Win Office 4.0. The Encarta stockout was the result of above plan orders and vendor capacity constraints due in part to relatively complex packaging which is now being simplified.

Cost of Revenue

- Cost of revenue was 23.8% versus plan of 20.4%, a negative variance of \$16.6 million, primarily as a result of the delay in the release of Excel 5.0. Shipping Office in up to three boxes rather than only one increased COGS. For a representative SKU of Win Office, the budgeted product cost varies from approximately \$58 for a one box configuration to approximately \$72 for a three box configuration. As a result, Win Office 4.0 sold with a negative COGS variance.
- As a result of the revenue deferral discussed above, plus COGS accruals for extra boxes, approximately \$48 million of gross profit on Win Office 4.0 was deferred. Recognition will occur in subsequent periods when Win Excel 5.0 and Win PowerPoint 4.0 upgrades ship in exchange for coupons. This deferral and accounting may be noted in the balance sheet where other liabilities increased 69%.
- Royalties were 114% over plan on strong sales of PC Flight Simulator and Word.

Controllable Expenses

- Shared resources margin totaled \$177.2 million, \$8.6 million ahead of plan, as negative variances in gross margin (\$4.2 million) and net shared resources (\$0.9 million) were offset by a positive variance of \$13.7 million in controllable expenses.
- Controllable expenses were lower than plan primarily as a result of positive variances in people expense (\$8.2 million) and facilities expense (\$3.2 million) due to headcount levels below forecast particularly in PSS. Marketing costs were on plan, but did increase 189% sequentially over Q94-1 due to the Win Office 4.0 launch and Home campaigns.

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FYTD94

Revenue

- FYTD94 net revenue was 109% of plan, a positive variance of \$68 million. Revenue growth was driven by the introduction of Win Office 4.0 (\$51 million above plan), strong sales of Windows 3.1 and WFW 3.11 (\$23 million above plan), sales of PC Flight Simulator (\$16 million above plan) to the home market and the release of MS-DOS 6.2 (\$11 million above plan). Significant negative variances to plan were experienced by Excel (\$12 million below plan) due to the delay in the release of Excel 5.0 and Windows NT (\$33 million below plan).
- Gross revenue was 110% of plan, but adjustments to gross revenue totaled \$87 million and exceeded plan by \$49 million principally due to the deferral of revenue from Win Office 4.0. As a result, although gross revenue was \$68 million over plan, net revenue was only \$19.7 million over plan. Rebates were also above plan due to unbudgeted rebates paid on Select revenue.

Cost of Revenue

- Cost of revenue for the quarter was 23.2% of net revenue in comparison with a plan of 20.0%, a negative variance of \$27 million. This is largely the result of the accrual of additional product costs for upgrades to Win Office 4.0 and additional royalties related to Flight Simulator.

Controllable Expenses

- Controllable expenses for the quarter were 85% of plan principally from the delay in hiring headcount. Facilities expenses were 86% of plan principally due to telecommunications and depreciation expense being below plan. YTD marketing expenses were \$80.9 million, \$17.8 million under plan.

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Channel Reporting

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Channels and Discounts (in millions)

	Q94-2			FYTD94		
	Sales	%	Discount	Sales	%	Discount
Resellers						
Distributors	\$ 289	60%	39%	\$ 453	57%	41%
Major Chains	47	10	39	80	10	38
Large Volume Resellers	80	17	33	123	16	36
Total Resellers	416	86	38	656	83	40
VAR's/Solution Providers	9	2	55	17	2	55
Direct	24	5	42	62	8	43
Canada	35	6	36	56	6	36
Gross Revenues	\$ 484	100%	39%	\$ 791	100%	41%

Channels

- Revenue from distributors in the United States in Q94-2 was \$289 million versus a plan of \$194 million. Notably, Ingram Micro purchased \$146 million in the quarter in comparison with plan of \$90 million and Merisel purchased \$99 million compared with a plan of \$72 million.
- Revenue from major chains was \$47 million (67% of plan), consisting of \$49 million of revenue from Egghead offset by a \$3 million credit to CompUSA.
- Revenue from large volume resellers was \$80 million (115% of plan), consisting primarily of revenue from Software Spectrum \$22 million and Corporate Software \$22 million.
- Channel inventory levels for the standard product of Windows NT were high (approximately 10 months of inventory at recent historical sell-through rates), as were MS-DOS for Dummies and certain Consumer products.
- In Q94-2, approximately \$12 million of MS-DOS 6.0 was returned by resellers for credit upon the release of MS-DOS 6.2.

Canada

- Net FG revenue from Canada was \$35 million for the quarter (91% of plan). Responsibility margin was 88% of plan.

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Significant Customers (in millions)

	<u>Q92-4</u>	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
Ingram Micro	\$ 93	\$ 93	\$ 61	\$ 92	\$ 72	\$ 89	\$ 146
Merisel	66	66	56	56	51	67	99
Egghead	52	52	51	46	22	22	49
Software Spectrum	24	24	11	18	14	10	22
Corporate Software	21	21	11	17	10	9	22
Intelligent Electronics	6	6	4	5	2	5	14
Tech Data	--	--	--	--	--	6	12
800 Software	10	10	7	8	8	8	11
Softmart	9	9	6	8	6	6	10
Computerland	10	10	8	6	9	6	6
	<u>\$ 291</u>	<u>\$ 291</u>	<u>\$ 215</u>	<u>\$ 256</u>	<u>\$ 194</u>	<u>\$ 228</u>	<u>\$ 391</u>
Percent of Gross Revenue	<u>75%</u>	<u>75%</u>	<u>75%</u>	<u>77%</u>	<u>73%</u>	<u>74%</u>	<u>81%</u>

- Revenue from the top customers in Q94-2 represented 81% of the gross FG revenue for the United States and Canada.
- Sales to Ingram Micro increased 64% to \$146 million from \$89 million in Q94-1.
- Sales to Egghead increased 123% to \$49 million in Q94-2 from \$22 million in Q94-1.
- Two new customers were added to the significant customers listing, Tech Data and ASAP Software, displacing CompUSA and ComputerLand.

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Channel Reporting

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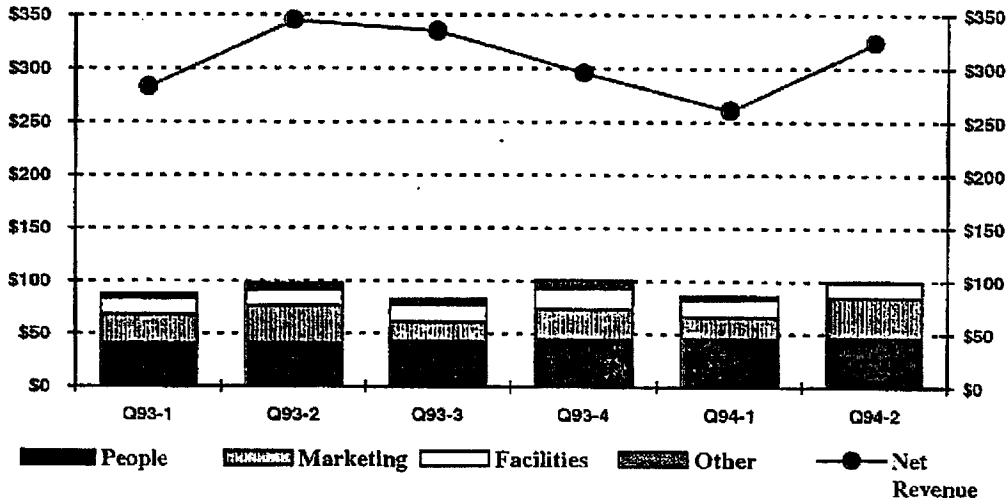
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Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$323.8	\$374.1	(\$50.3)	\$585.3	\$631.1	(\$45.8)
Cost of revenue	50.7	68.6	17.9	96.9	114.0	17.1
Gross profit	273.1	305.5	(32.4)	488.5	517.1	(28.7)
People expenses	45.7	51.7	6.0	90.6	103.1	12.4
Facilities expenses	15.2	17.6	2.5	30.6	34.9	4.3
Marketing expenses	37.7	39.2	1.5	59.1	67.6	8.5
Other expenses	1.1	3.7	2.6	5.1	7.3	2.2
Controllable expenses	99.7	112.3	12.6	185.5	212.9	27.4
Responsibility margin	173.4	193.2	(19.8)	303.0	304.2	(1.2)
Net shared resources	1.1	1.3	0.3	2.4	2.7	0.3
Shared resource margin	\$172.3	\$191.9	(\$19.6)	\$300.6	\$301.6	(\$0.9)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	15.7	18.3	2.7	16.5	18.1	1.5
Controllable expenses	30.8	30.0	(0.8)	31.7	33.7	2.1
Responsibility margin	53.5	51.6	1.9	51.8	48.2	3.6
Net shared resources	0.3	0.4	0.0	0.4	0.4	0.0
Shared resource margin	53.2 %	51.3 %	1.9 %	51.4 %	47.8 %	3.6 %

TREND ANALYSES

Net Revenue & Controllable Expenses (in millions)



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REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

Q94-2

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$122.9	\$77.7	58%	304.5	226.5	34%	\$404	\$343	18%
MAC Office	5.8	5.4	8%	16.0	15.5	3%	362	348	4%
Excel PU *	28.3	38.3	(26%)	116.5	180.2	(35%)	243	212	15%
Word PU *	49.8	55.4	(10%)	266.2	257.5	3%	187	215	(13%)
Graphics PU *	2.0	2.2	(9%)	12.6	8.8	44%	160	252	(36%)
Project PU	6.7	6.2	8%	16.5	16.2	2%	404	382	6%
DAD BU New Users **	215.6	185.2	16%	732.3	704.8	4%	294	263	12%
WIN Office	4.8	11.5	(58%)	45.7	50.7	(10%)	106	227	(53%)
MAC Office	0.5	0.9	(35%)	2.4	4.5	(47%)	230	190	21%
Excel PU *	4.7	13.4	(65%)	96.3	199.3	(52%)	49	67	(27%)
Word PU *	13.9	19.9	(30%)	134.2	180.4	(26%)	104	110	(6%)
Graphics PU *	(0.5)	0.8	(155%)	(4.3)	77.1	(106%)	105	11	888%
Project PU	0.2	0.9	(75%)	2.2	5.7	(62%)	99	154	(36%)
DAD BU Existing Users **	23.8	47.4	(50%)	276.5	517.7	(47%)	86	92	(6%)
Basic PU	5.3	3.9	35%	34.7	29.2	19%	153	135	13%
Database Mgmt (Access) PU *	8.8	17.8	(51%)	61.8	83.2	(26%)	142	214	(34%)
Fox Database PU *	4.4	10.1	(57%)	23.0	43.5	(47%)	189	232	(18%)
Languages PU's	3.9	4.3	(9%)	25.8	25.4	2%	152	170	(10%)
DBDT BU *	22.4	36.1	(38%)	145.3	181.3	(20%)	154	199	(23%)
Entry PU	9.8	5.0	98%	229.9	119.4	93%	43	42	3%
Multimedia Publishing PU	3.1	0.7	326%	57.0	14.8	286%	54	49	10%
Works PU	10.0	13.4	(25%)	150.3	151.7	(1%)	67	88	(24%)
Consumer BU	22.9	19.1	20%	437.3	285.9	53%	52	67	(22%)
Hardware BU	9.7	14.4	(33%)	151.7	213.9	(29%)	64	67	(5%)
MS-DOS BU	7.9	15.2	(48%)	272.9	248.5	10%	29	61	(53%)
Windows BU	20.4	24.4	(16%)	385.2	337.3	14%	53	72	(27%)
Win NT Family	3.2	20.7	(85%)	13.7	81.6	(83%)	235	254	(8%)
Win NT Adv. Server Family	2.5	4.2	(41%)	3.4	5.2	(33%)	726	818	(11%)
Win NT Server (SQL,SNA)	1.1	2.4	(53%)	4.2	2.0	116%	262	1,213	(78%)
Other Operating Systems PU	4.7	1.1	315%	17.2	4.9	254%	271	231	17%
Advanced Systems BU	11.5	28.4	(60%)	38.5	93.6	(59%)	298	304	(2%)
Workgroup BU *	4.1	3.9	6%	71.7	38.0	89%	57	102	(44%)
Digital Office Systems PU's	0.2	0.7	(75%)	1.6	6.7	(76%)	113	107	5%
ACT and APD PU's	0.4	0.6	(43%)	11.1	14.5	(24%)	33	45	(25%)
Other PU's	0.3	0.3	(3%)	0.4	3.3	(89%)	826	98	742%
Other	0.9	1.7	(49%)	13.1	24.6	(47%)	66	69	(4%)
Finished goods revenue	339.1	375.8	(10%)	2,524.5	2,645.6	(5%)	134	142	(5%)
Other materials	3.9	0.0	NM	0.0	0.0	NM			
Total FG gross revenue	\$343.1	\$375.8	(9%)	2,524.5	2,645.6	(5%)			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

FYTD94

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$204.1	\$136.5	50%	493.1	388.2	27%	\$414	\$352	18%
MAC Office	10.2	8.7	17%	26.7	25.1	6%	381	348	9%
Excel PU *	54.1	65.0	(17%)	217.3	295.6	(26%)	249	220	13%
Word PU *	89.3	90.4	(1%)	454.5	409.2	11%	196	221	(11%)
Graphics PU *	4.2	4.0	3%	23.3	15.9	47%	178	254	(30%)
Project PU	13.0	11.8	10%	32.3	30.7	5%	403	384	5%
DAD BU New Users **	<u>374.8</u>	<u>316.5</u>	18%	<u>1,247.3</u>	<u>1,164.7</u>	7%	301	272	11%
WIN Office	9.9	19.0	(48%)	65.1	83.4	(22%)	152	228	(34%)
MAC Office	1.0	1.3	(24%)	4.7	7.0	(33%)	216	191	13%
Excel PU *	9.2	21.9	(58%)	149.0	276.1	(46%)	62	79	(22%)
Word PU *	20.6	31.4	(34%)	187.3	287.5	(35%)	110	109	1%
Graphics PU *	(0.6)	1.5	(143%)	(6.2)	82.6	(107%)	101	18	471%
Project PU	0.4	1.7	(79%)	3.2	11.0	(71%)	114	155	(27%)
DAD BU Existing Users **	<u>40.5</u>	<u>76.8</u>	(47%)	<u>403.1</u>	<u>747.6</u>	(46%)	100	103	(2%)
Basic PU	11.0	7.8	41%	76.0	56.5	35%	145	138	5%
Database Mgmt (Access) PU	18.6	30.9	(40%)	156.1	136.7	14%	119	226	(47%)
Fox Database PU *	11.6	17.9	(35%)	68.6	84.8	(19%)	170	211	(19%)
Languages PU's	7.6	6.7	12%	49.3	40.8	21%	154	165	(7%)
DBDT BU *	<u>48.8</u>	<u>63.4</u>	(23%)	<u>349.9</u>	<u>318.8</u>	10%	139	199	(30%)
Entry PU	12.8	7.9	62%	297.7	188.8	58%	43	42	3%
Multimedia Publishing PU	3.8	1.2	211%	68.7	23.8	188%	55	51	8%
Works PU	17.7	21.7	(18%)	236.6	244.7	(3%)	75	89	(15%)
Consumer BU	<u>34.3</u>	<u>30.8</u>	11%	<u>603.0</u>	<u>457.3</u>	32%	57	67	(16%)
Hardware BU	<u>18.1</u>	<u>25.1</u>	(28%)	<u>277.5</u>	<u>371.2</u>	(25%)	65	67	(3%)
MS-DOS BU	<u>17.1</u>	<u>30.4</u>	(44%)	<u>497.4</u>	<u>483.6</u>	3%	34	63	(45%)
Windows BU	<u>35.4</u>	<u>42.7</u>	(17%)	<u>626.0</u>	<u>583.1</u>	7%	56	73	(23%)
Win NT Family	6.1	27.3	(78%)	24.0	108.5	(78%)	253	252	1%
Win NT Adv. Server Family	3.4	5.4	(38%)	4.7	7.0	(33%)	725	776	(7%)
Win NT Server (SQL,SNA)	1.5	3.8	(60%)	23.0	2.8	709%	67	1,340	(95%)
Other Operating Systems PU	10.2	2.0	409%	45.5	9.0	405%	225	223	1%
Advanced Systems BU	<u>21.2</u>	<u>38.5</u>	(45%)	<u>97.2</u>	<u>127.3</u>	(24%)	218	303	(28%)
Workgroup BU *	<u>7.8</u>	<u>6.9</u>	13%	<u>136.6</u>	<u>67.7</u>	102%	57	102	(44%)
Digital Office Systems PU's	0.5	1.3	(65%)	4.1	12.3	(67%)	113	107	5%
ACT and APD PU's	0.6	1.2	(49%)	16.1	26.2	(38%)	36	44	(18%)
Other PU's	0.5	0.5	3%	1.2	5.7	(79%)	423	87	388%
Other	<u>1.6</u>	<u>3.0</u>	(48%)	<u>21.4</u>	<u>44.3</u>	(52%)	73	67	8%
Finished goods revenue	599.5	634.1	(5%)	4,259.3	4,365.5	(2%)	141	145	(3%)
(Other materials)	6.9	0.0	NM	0.1	0.0	NM			
Total FG gross revenue	<u>\$606.3</u>	<u>\$634.1</u>	(4%)	<u>4,259.4</u>	<u>4,365.5</u>	(2%)			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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Q94-2

Revenue

- Net revenue was 13% lower than plan but was positively affected by actual exchange rates being slightly more favorable than budgeted.
- Desktop Applications were \$7 million higher than plan. Win Office exceeded plan by 43%. MS-DOS and Windows were below plan due to lower than planned unit pricing. Win NT was \$1 million below plan due to less than planned unit sales. The Consumer and Workgroup business units were the only other products exceeding quarterly plan.
- Access and Fox database products were respectively 51% and 57% below plan. The products experienced both volume and unit price shortfalls to plan.
- There was a significant decrease in revenue per license for all products compared to Q93-2, driven by foreign exchange trends, price reductions and product mix differences.
- France had a 31% shortfall to local currency plan, while England and Nordic were 27% and 24% lower than plan, respectively. Italy, Switzerland and Eastern Europe achieved better than expected results compared to plan.

Cost of Revenue

- Cost of revenue was 26% lower than plan. There was a positive variance for product costs for Desktop Applications, due to a favorable sales mix resulting from higher than planned license revenues and lower than planned upgrades. The product cost for all business units approximated plan.

Controllable Expenses

- Controllable expenses were \$13 million lower than plan primarily due to lower than planned hiring and underspending in marketing.
- People expenses in local currencies have increased significantly due to a headcount growth of 648 people since Q93-2. People expense decreased slightly from Q94-1 due to a hiring freeze implementation.
- Marketing costs increased from the prior quarter by \$17 million or 81%. Marketing costs were \$2 million higher than Q93-2. Year-to-date marketing costs were 13% higher than the same period for fiscal 1993.
- Facilities costs increased from Q93-2 due to new facilities in Eastern Europe and additional office facilities in France. Depreciation increased 34% due to fixed asset acquisitions caused by headcount increases. Facilities costs decreased \$4 million from Q93-4 to Q94-2 due in part to the closure of the warehouse in Spain. The warehouse in Germany was closed in Q94-2. The remaining subsidiary warehouses are scheduled to be closed over the next 3 quarters.

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EUROPE FINISHED GOODS

FYTD94

Net Revenue

- Net revenue was 7% lower than plan. Exchange rate trends created a \$29 million positive variance to plan.
- Desktop Applications were \$22 million higher than plan on the strength of Win Office, which exceeded plan by \$58 million. Win Office revenue represented 35% of total gross revenue year-to-date.
- Database & Development Tools Business Unit was 77% of plan principally due to lower than planned pricing of the Access database.
- The Hardware business unit was 72% of plan due to volume shortfalls.
- The Advanced Server business unit was \$17 million below plan due to Windows NT volume shortfalls.
- The Consumer business unit exceeded plan 11%, although unit pricing for the Works product unit was 15% below expectation.
- The Workgroup business unit exceeded plan 13%, but pricing was 44% below planned levels.
- MS-DOS and Windows were lower than plan due to lower unit pricing.
- There was a significant decrease in revenue per license for all products compared to Q93-1, driven by foreign exchange trends, price reductions and product mix differences. Italy, Switzerland and Eastern Europe were the only subsidiaries with above plan local currency net revenues.
- Net revenue in Q94-2 was \$21 million or 6% lower than in Q93-2. In Q93-2, a \$32 million negative revenue adjustment was made to reflect foreign currency and pricing trends. Without the effect of this adjustment, net revenue would have been \$53 million or 15% lower. The combined effect of currency fluctuations had a 15% negative year to date impact on net revenue compared to the Q93-2 period.

Cost of Revenue

- Cost of revenue was 1.5% of net revenue lower than plan. The product costs of Desktop Applications were lower than plan due to a higher than planned mix of license product coupled with lower proportion of upgrade revenue.

Controllable Expenses

- Controllable expenses were 13% lower than plan. People and facility expenses were lower than plan due to implementation of a hiring freeze. Marketing expenses were lower than plan due to expense controls implemented because of the lower revenues.

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EUROPE FINISHED GOODS

Net Revenue by Major Subsidiary (in millions)

	Q94-2		Q94-2 Plan		Net Variance	Operations Variance	Exchange Rate Variance
Germany	\$ 94	29	\$ 98	26	\$ (4)	\$ (9)	\$ 5
France	65	20	91	24	(26)	(28)	2
England	52	16	66	18	(14)	(18)	4
Nordic Region	32	10	41	11	(9)	(10)	1
Italy	21	6	18	5	3	4	(1)
Switzerland	20	6	17	5	3	1	2
Benelux	17	5	19	5	(2)	(3)	1
Austria	9	3	9	2	--	(1)	1
Eastern Europe	8	2	5	1	3	3	--
Spain	5	2	7	2	(2)	(2)	--
Portugal	2	1	3	1	(1)	(1)	--
Redmond	(1)	--	--	--	(1)	(1)	--
	<u>\$ 324</u>	<u>100%</u>	<u>\$ 374</u>	<u>100%</u>	<u>\$ (50)</u>	<u>\$ (65)</u>	<u>\$ 15</u>

- Net revenue was 13% below plan due to volume variances. Favorable foreign exchange trends compared to plan which positively affected net revenue 4%.
- Net revenue in France was 31% lower than planned volume, while the UK was 27% lower.
- Italy's net revenue was 22% over plan, and Eastern Europe exceeded plan by 60%.
- Nordic and Benelux net revenue was respectively 24% and 16% lower than planned volume.

	FYTD94		FYTD Plan		Net Variance	Operations Variance	Exchange Rate Variance
Germany	\$ 178	30	\$ 175	28	\$ 3	\$ (9)	\$ 12
France	111	19	150	24	(39)	(43)	4
England	98	17	115	18	(17)	(23)	6
Nordic Region	51	9	63	10	(12)	(13)	1
Italy	44	8	26	4	18	18	--
Switzerland	38	6	31	5	7	3	4
Benelux	25	4	31	5	(6)	(7)	1
Austria	16	3	16	3	--	(1)	1
Eastern Europe	12	2	9	1	3	3	--
Spain	7	1	10	2	(3)	(3)	--
Portugal	4	1	5	1	(1)	(1)	--
Redmond	1	0	--	--	1	1	--
	<u>\$ 585</u>	<u>100%</u>	<u>\$ 631</u>	<u>100%</u>	<u>\$ (46)</u>	<u>\$ (75)</u>	<u>\$ 29</u>

- Net revenue was 12% lower than volume plan. Favorable currency trends created a 5% positive revenue variance from plan.
- Only Italy, Switzerland and Eastern Europe had above plan volumes.
- Net revenue in France was 29% below local currency plan. Most business units were under plan. Win Office was 6% lower than expectation, primarily due to volume shortfalls.
- The UK was 20% under plan volume. Win Office was \$1 million under plan, primarily resulting due to lower volume shipments.
- Germany was 5% below local currency plan. This was offset by favorable foreign exchange trends. Win Office was 72% higher than plan, but other Desktop Applications products were under plan. Most other significant business units were lower than plan.

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EUROPE FINISHED GOODS

Significant Customers in Major Subsidiaries (in millions)

	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
Germany						
C2000	\$ 24	\$ 35	\$ 33	\$ 27	\$ 28	\$ 25
Merisel	4	15	13	12	16	16
Macrotron	6	9	13	7	12	15
Raab Karcher	--	--	--	--	6	16
England						
C2000	13	18	20	12	15	17
Merisel	11	8	14	10	14	11
Ingram Micro	6	4	8	6	5	6
France						
CEGOS	9	18	7	8	5	10
Softmart	6	11	9	5	5	8
ISTA	6	9	4	5	4	5
Italy						
Ingram	1	1	2	6	4	5
C2000	1	2	2	5	3	4
Nordic region						
C2000	8	16	20	27	4	13
Microsoftware	5	10	14	18	4	4
Scribona AB	3	6	6	6	2	7
Switzerland						
Also ABC	4	5	4	5	5	6
Wyrsh Trading	4	4	4	3	4	6
Merisel	--	1	1	2	3	3
C2000	--	--	--	--	2	4
Benelux						
Ingram	5	7	7	9	4	8
C2000	4	5	6	5	2	5
A-Line	2	1	1	1	--	1
Austria						
C2000	5	6	4	5	4	3
Macrotron	--	--	--	1	2	2
	<u>\$ 127</u>	<u>\$ 191</u>	<u>\$ 192</u>	<u>\$ 185</u>	<u>\$ 153</u>	<u>\$ 200</u>
Percent of Net Revenue	<u>45%</u>	<u>55%</u>	<u>57%</u>	<u>63%</u>	<u>59%</u>	<u>62%</u>

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- The European channel is planned to decrease the number of direct ship customers significantly during the upcoming quarters, to facilitate efficient distribution practices. This should have the effect of increasing sales levels to the remaining individual customers.
- C2000 represented 22% of total net revenues. Ingram and Merisel represented 6% and 9%, respectively.
- The top 10 customers accounted for approximately 59% of total European net revenues.

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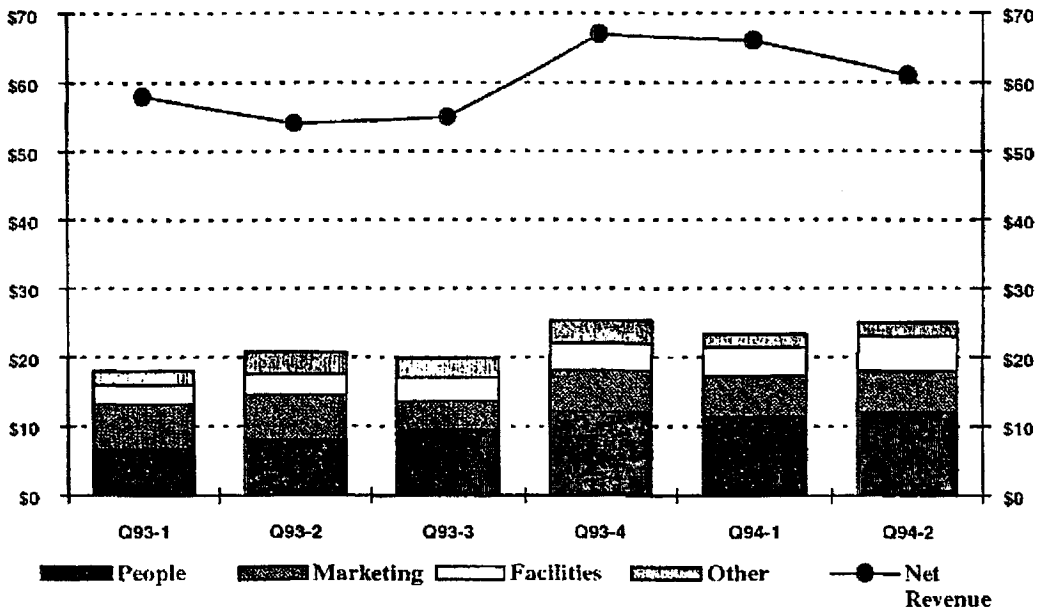
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Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$60.5	\$80.4	(\$19.9)	\$127.0	\$138.8	(\$11.8)
Cost of revenue	16.2	19.0	2.9	29.6	33.5	3.9
Gross profit	44.3	61.4	(17.1)	97.4	105.3	(7.9)
People expenses	11.8	13.5	1.7	23.1	27.1	4.0
Facilities expenses	4.4	5.2	0.7	8.5	10.2	1.7
Marketing expenses	5.7	7.5	1.9	11.6	15.5	3.9
Other expenses	2.2	2.7	0.5	4.2	5.2	1.1
Controllable expenses	24.1	28.8	4.8	47.4	58.1	10.7
Responsibility margin	20.3	32.6	(12.3)	50.0	47.2	2.8
Net shared resources	0.3	0.3	0.0	0.6	0.6	(0.0)
Shared resource margin	\$20.0	\$32.3	(\$12.2)	\$49.4	\$46.7	\$2.7
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	26.7	23.7	(3.1)	23.3	24.1	0.8
Controllable expenses	39.7	35.9	(3.9)	37.3	41.8	4.5
Responsibility margin	33.5	40.5	(7.0)	39.4	34.0	5.4
Net shared resources	0.4	0.4	(0.1)	0.5	0.4	(0.1)
Shared resource margin	33.1 %	40.1 %	(7.0) %	38.9 %	33.6 %	5.3 %

TREND ANALYSIS

Net Revenue & Controllable Expenses (in millions)



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REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

Q94-2

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$19	\$15	24%	73	49	48%	\$257	\$307	(16%)
MAC Office	1	1	(26%)	4	4	7%	225	326	(31%)
Excel PU *	3	7	(62%)	17	39	(57%)	155	178	(13%)
Word PU *	6	8	(20%)	47	49	(3%)	133	163	(18%)
Graphics PU *	0	1	(37%)	2	4	(46%)	189	162	17%
Project PU	1	1	(11%)	3	7	(55%)	423	217	95%
DAD BU New Users **	30	33	(9%)	146	151	(3%)	207	220	(6%)
WIN Office	5	3	57%	35	19	81%	152	175	(13%)
MAC Office	0	0	(27%)	3	2	86%	76	192	(61%)
Excel PU *	0	4	(86%)	7	44	(84%)	68	83	(17%)
Word PU *	2	4	(48%)	34	54	(37%)	69	82	(16%)
Graphics PU *	0	0	(71%)	1	3	(64%)	52	63	(19%)
Project PU	0	1	(82%)	(4)	21	(117%)	(37)	36	(203%)
DAD BU Existing Users **	8	13	(33%)	76	142	(47%)	112	89	26%
Basic PU	1	0	117%	9	4	101%	117	109	8%
Database Mgmt (Access) PU *	1	4	(70%)	18	39	(55%)	76	114	(33%)
Fox Database PU *	2	2	(30%)	10	14	(24%)	150	165	(9%)
Languages PUs	1	1	36%	5	3	46%	146	156	(7%)
DBDT BU *	5	8	(40%)	42	61	(31%)	112	128	(12%)
Entry PU	1	1	54%	49	28	80%	30	35	(14%)
Multimedia Publishing PU	2	0	406%	40	5	771%	40	69	(42%)
Works PU	2	3	(45%)	43	70	(38%)	43	49	(12%)
Consumer BU	5	5	6%	133	102	30%	38	46	(19%)
Hardware BU	2	4	(48%)	44	67	(35%)	48	60	(20%)
MS-DOS BU	3	5	(33%)	135	84	61%	23	54	(58%)
Windows BU	8	8	3%	170	123	39%	49	66	(26%)
Win NT Family	0	2	(95%)	1	11	(89%)	89	195	(54%)
Win NT Adv. Server Family	1	0	456%	2	0	552%	513	601	(15%)
Win NT Server (SQL,SNA)	1	1	2%	2	1	120%	445	958	(54%)
Other Operating Systems PU	0	1	(65%)	3	1	95%	112	625	(82%)
Advanced Systems BU	2	4	(46%)	7	13	(43%)	282	298	(5%)
Workgroup BU *	1	1	(24%)	21	10	103%	52	140	(63%)
Digital Office Systems PUs	0	0	NM	0	0	NM	100	0	NM
ACT and APD PUs	0	0	NM	7	0	NM	19	0	NM
Other PUs	0	2	(99%)	0	24	(100%)	663	86	672%
Other	0	2	(92%)	7	24	(70%)	23	86	(73%)
Finished goods revenue	65	82	(21%)	780	777	0%	84	106	(21%)
Other materials	1	0	NM	0	0	NM			
Total FG gross revenue	\$66	\$82	(20%)	780	777				

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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ICON FINISHED GOODS

REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

FYTD94

	Revenue			Licenses			Revenue per License		
	Actual	Budget	% Var	Actual	Budget	% Var	Actual	Budget	% Var
WIN Office	\$34	\$27	25%	126	88	43%	\$268	\$307	(13%)
MAC Office	2	2	(17%)	7	7	(1%)	275	329	(17%)
Excel PU *	6	11	(45%)	44	60	(28%)	135	177	(23%)
Word PU *	12	12	(0%)	101	75	34%	122	164	(26%)
Graphics PU *	1	1	(35%)	5	8	(30%)	145	157	(7%)
Project PU	3	3	28%	14	12	15%	247	222	11%
DAD BU New Users **	<u>58</u>	<u>56</u>	3%	<u>297</u>	<u>251</u>	18%	196	224	(13%)
WIN Office	9	7	30%	62	37	66%	139	177	(21%)
MAC Office	0	1	(25%)	4	3	34%	107	189	(44%)
Excel PU *	1	6	(73%)	22	66	(66%)	67	83	(20%)
Word PU *	4	7	(35%)	57	81	(29%)	76	82	(8%)
Graphics PU *	0	0	(20%)	3	5	(33%)	77	65	18%
Project PU	0	1	(35%)	9	22	(58%)	39	39	(1%)
DAD BU Existing Users **	<u>15</u>	<u>20</u>	(25%)	<u>158</u>	<u>214</u>	(26%)	98	96	2%
Basic PU	2	1	74%	18	10	81%	116	120	(4%)
Database Mgmt (Access) PU *	3	6	(48%)	42	53	(20%)	79	121	(35%)
Fox Database PU *	4	4	(7%)	24	23	4%	150	168	(11%)
Languages PUs	2	1	81%	11	6	101%	140	155	(10%)
DBDT BU *	<u>11</u>	<u>12</u>	(14%)	<u>95</u>	<u>91</u>	4%	111	135	(18%)
Entry PU	3	2	16%	77	60	29%	33	37	(10%)
Multimedia Publishing PU	2	0	400%	52	6	740%	43	72	(40%)
Works PU	4	5	(32%)	86	111	(23%)	43	50	(13%)
Consumer BU	<u>8</u>	<u>8</u>	4%	<u>215</u>	<u>177</u>	22%	39	46	(14%)
Hardware BU	5	7	(37%)	86	123	(30%)	54	61	(11%)
MS-DOS BU	8	9	(5%)	267	164	63%	31	54	(42%)
Windows BU	17	14	22%	361	215	68%	48	66	(27%)
Win NT Family	2	5	(54%)	12	25	(52%)	175	185	(5%)
Win NT Adv. Server Family	2	0	221%	3	1	218%	584	580	1%
Win NT Server (SQL.SNA)	1	1	(34%)	6	2	233%	153	777	(80%)
Other Operating Systems PU	1	2	(40%)	7	3	140%	145	578	(75%)
Advanced Systems BU	<u>6</u>	<u>8</u>	(31%)	<u>28</u>	<u>31</u>	(9%)	203	268	(24%)
Workgroup BU *	2	3	(22%)	36	21	71%	58	127	(55%)
Digital Office Systems PUs	0	0	NM	0	0	NM	99	0	NM
ACT and APD PUs	0	0	NM	9	0	NM	23	0	NM
Other PUs	0	4	(100%)	0	42	(100%)	663	85	679%
Other	<u>0</u>	<u>4</u>	(93%)	<u>9</u>	<u>42</u>	(78%)	28	85	(67%)
Finished goods revenue	131	142	(8%)	1,551	1,327	17%	84	107	(21%)
Other materials	1	0	NM	0	0	NM	15,147	0	NM
Total FG gross revenue	<u>\$132</u>	<u>\$142</u>	(7%)	<u>1,551</u>	<u>1,327</u>	17%			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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Q94-2

Revenue

- FG gross revenue was 20% below plan while licenses were on plan reflecting continued price erosion, the delivery of Desktop Applications through the Office product, and higher than planned mix of lower revenue per unit products, such as MS-DOS, Windows and Consumer products.
- The Word and Excel negative revenue variances were due to delayed release of these products as well as the shift toward delivery of these products in the Office SKU.
- The Access and MS-DOS negative variances were due in part to overstocks caused by high distributor purchasing in Q94-1 in response to promotional pricing as well as negative publicity about product bugs that have been fixed with maintenance releases (Access 1.1 and MS-DOS 6.2).
- The Hardware negative revenue variance was because the Mouse product that was not competitively priced against the competition and cannot continue to compete as a "premium priced" product. Competition from our OEM mouse (recorded in OEM channel and well over plan) was also a factor.
- The Win NT negative revenue variance was due in part to lack of acceptance for this product on the desktop as well as due to product returns from an overstocked channel.
- The Office (new user) negative revenue per license variance was primarily due to deep discounting in Latin America, particularly in Brazil. The pricing is due both to the delayed release of localized product and in response to pricing actions of Lotus and WordPerfect who have low market share and do not have local sales offices to support (i.e. Lotus Smart Suite offered to OEM's for less than \$100 per unit).
- For the quarter and YTD, respectively, APAC was 72% and 84% of plan, Latin America was 74% and 99% of plan and AIME was 89% and 100% of plan. This trend reflects an unanticipated drop in growth rate for the region as well as effects of the delayed release of Win Word and Win Excel.
- Large negative variances by subsidiary for the quarter were recorded in Australia (\$9.4 million), Mexico (\$6.0 million) and Singapore (\$1.0 million). Australia was under plan due to a 5% devaluation in the Australian dollar, the Office Guarantee deferral, the delayed release of Win Word and Win Excel and overall weakness in all business units. Mexico sales slowed over the uncertainty of NAFTA legislation and even though that has now passed, the outlook is still uncertain through the remainder of the fiscal year.

Cost of Revenue

- Cost of revenue, as a percentage of net revenue, was significantly higher than plan for the quarter because of the revenue deferrals mentioned above (3.3% of revenue) and higher than planned allocations from MD&L (1.6% of revenue). The allocations were over plan primarily because of negative manufacturing variances (incorrect standards) and unplanned costs related to distributed manufacturing.

Controllable Expenses

- The region aggressively managed expenses in Q4-2 because of the below plan net revenue. Despite the termination costs in Australia and the increase in net heads, controllable expenses grew only 3% over the prior quarter (compared to a 2% decrease in gross revenue).
- The positive variance in people expense for the quarter and was due to a headcount freeze in the region (primarily in Mexico and South Africa), termination of heads in Australia, a significant cutback in the number of temporary staff (primarily in Australia) and aggressive management of travel expenses throughout the region. As of December 31, 1993, actual headcount was 602 versus plan of 680 and actual heads of 583 at September 30, 1994. Most of the unhired heads will not be added in FY 94.

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ICON FINISHED GOODS

FYTD94

Revenue

- FG gross revenue was 7% below plan while licenses were 17% over plan reflecting continued price erosion, the delivery of Desktop Applications through the Office product and higher than planned mix of lower revenue per unit products, such as MS-DOS, Windows and Consumer products.
- The Excel negative revenue variance was due to delayed release of Version 5.0 as well as the shift toward delivery of Excel in the Office SKU. In addition, the small differential in price between the Office Competitive Upgrade and Excel promoted a higher percentage of Office sales.
- The Access negative variance was incurred entirely in Q2.
- The Windows NT negative revenue variance was due in part to lack of acceptance for this product on the desktop as well as due to product returns in Q2 from an overstocked channel.
- The Word and Excel (new user) negative revenue per license variances were primarily due to a higher than planned mix of Academic units for this product. There was also a steep decline in the number of full package sales of these two products due to the delayed product release and the pricing of the Office Competitive Upgrade as discussed above.
- The MS-DOS negative revenue per license variance was primarily due to continued promotional pricing, special pricing on large account contracts and zero revenue stock rotation units caused by the unanticipated release of version 6.2.

Cost of Revenue

- Cost of revenue was 23.8% of net revenue in comparison with plan of 24.1%. This positive variance was due to changes in product mix which offset negative manufacturing variances and other unplanned costs.

Controllable Expenses

- Controllable expenses were \$10.7 million under plan, principally as a result of the freeze in headcount for the region. People expenses were \$4.0 million under plan.
- Marketing expenses were \$3.9 million under plan, as funds were conserved for product launches that have been delayed to second-half FY94.

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ICON FINISHED GOODS

Significant Customers in Major Subsidiaries (in millions)

	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
Australia						
Tech Pacific	\$ 4.2	\$ 4.8	\$ 4.8	\$ 8.1	\$ 8.8	\$ 10.1
Merisel	3.4	3.8	6.1	9.0	5.7	5.2
Datacom	--	--	--	--	--	1.7
Mexico						
Ingram-Dicom	2.9	3.9	2.1	4.8	1.4	1.7
Brazil						
Agoal	2.7	4.6	0.4	0.2	0.2	2.8
Compucenter	1.9	1.8	1.7	2.2	2.3	2.2
South Africa						
Workgroup	3.1	2.6	2.0	3.5	3.0	2.9
	<u>\$ 18.2</u>	<u>\$ 21.5</u>	<u>\$ 17.1</u>	<u>\$ 27.8</u>	<u>\$ 21.4</u>	<u>\$ 26.6</u>
Percent of Gross Revenue	<u>32%</u>	<u>40%</u>	<u>31%</u>	<u>41%</u>	<u>32%</u>	<u>40%</u>

- Sales in Q94-2 to the top six distributors increased as a percentage of gross revenue over Q94-1, primarily due to the recovery of Agoal and an increase in market share for Tech Pacific in Australia and New Zealand at the expense of smaller distributors.
- Continued growth in the region is expected to come primarily from smaller distributors in the other ICON countries not represented on this chart where average quarterly sales generally run less than \$1 million per quarter.

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FAR EAST FINISHED GOODS

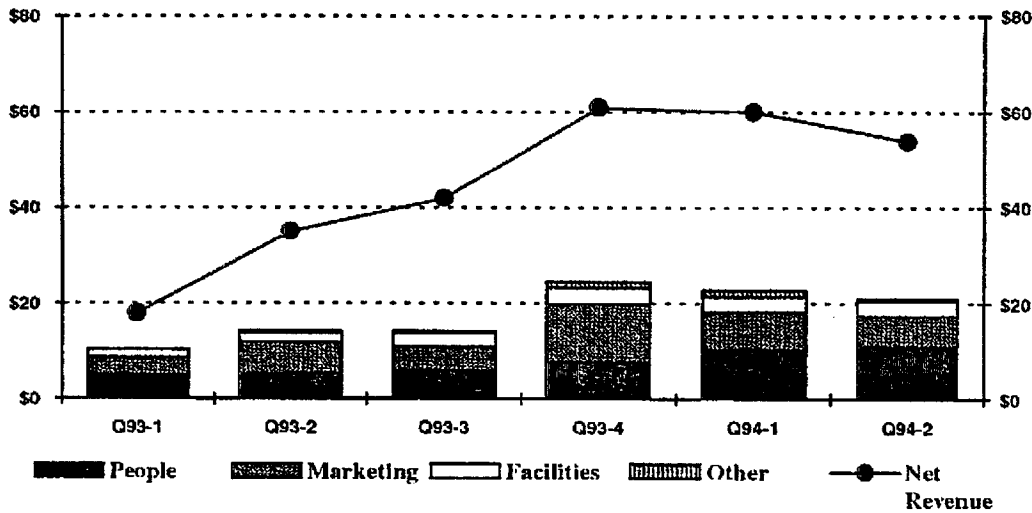
FAR EAST FINISHED GOODS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$53.8	\$45.4	\$8.4	\$114.1	\$91.5	\$22.7
Cost of revenue	14.1	12.4	(1.7)	28.0	24.0	(4.1)
Gross profit	39.7	33.0	6.7	86.1	67.5	18.6
People expenses	11.1	10.7	(0.4)	21.5	20.8	(0.6)
Facilities expenses	3.1	3.4	0.3	6.3	6.9	0.6
Marketing expenses	6.5	6.4	(0.0)	14.3	12.2	(2.1)
Other expenses	0.3	0.7	0.4	1.7	1.7	0.0
Controllable expenses	20.9	21.2	0.3	43.7	41.6	(2.1)
Responsibility margin	18.8	11.8	7.0	42.4	25.7	16.7
Net shared resources	10.1	10.4	0.3	19.4	20.7	1.3
Shared resource margin	\$8.7	\$1.4	\$7.3	\$22.9	\$5.2	\$17.7
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	26.1	27.3	1.2	24.6	26.2	1.7
Controllable expenses	38.9	46.7	7.8	38.3	45.5	7.2
Responsibility margin	34.9	26.0	8.9	37.1	28.1	9.0
Net shared resources	18.8	22.8	4.0	17.0	22.6	5.6
Shared resource margin	16.2 %	3.2 %	13.0 %	20.1 %	5.7 %	14.4 %

TREND ANALYSIS

Net Revenue & Controllable Expenses (in millions)



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FAR EAST FINISHED GOODS

REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

Q94-2

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$13.2	\$7.1	87%	46.3	29.2	59%	\$285	\$243	18%
MAC Office	0.1	0.1	(11%)	0.3	0.4	(16%)	282	264	7%
Excel PU *	7.9	6.8	17%	35.7	58.1	(38%)	222	117	89%
Word PU *	3.8	3.6	6%	32.6	33.9	(4%)	117	107	10%
Graphics PU *	0.3	0.4	(14%)	1.6	2.0	(20%)	191	179	7%
Project PU	0.1	0.2	(38%)	0.4	0.6	(41%)	361	343	5%
DAD BU New Users **	<u>25.5</u>	<u>18.2</u>	40%	<u>116.9</u>	<u>124.2</u>	(6%)	218	146	49%
WIN Office	0.2	0.2	(19%)	1.9	1.0	93%	101	242	(58%)
MAC Office	0.0	0.0	NM	0.0	0.0	0%	0	0	0%
Excel PU *	0.5	1.0	(55%)	3.9	13.6	(72%)	117	73	61%
Word PU *	0.4	0.2	80%	2.4	2.4	(2%)	165	90	83%
Graphics PU *	0.0	0.0	375%	0.2	0.1	41%	224	67	236%
Project PU	0.0	0.0	(81%)	0.0	0.1	(83%)	116	105	10%
DAD BU Existing Users **	<u>1.1</u>	<u>1.5</u>	(27%)	<u>8.3</u>	<u>17.3</u>	(52%)	129	85	52%
Basic PU	2.9	3.2	(8%)	21.1	18.3	15%	138	173	(20%)
Database Mgmt (Access) PU *	6.7	2.0	242%	53.3	15.5	244%	126	127	(1%)
Fox Database PU *	0.7	0.8	(15%)	3.1	4.0	(23%)	218	198	10%
Languages PUs	7.3	5.5	35%	30.0	25.3	18%	245	215	14%
DBDT BU *	<u>17.6</u>	<u>11.4</u>	55%	<u>107.5</u>	<u>63.1</u>	70%	164	180	(9%)
Entry PU	1.7	1.1	62%	43.3	19.7	120%	40	55	(26%)
Multimedia Publishing PU	0.2	0.0	NM	3.9	0.0	NM	53	0	NM
Works PU	0.9	1.1	(18%)	13.7	9.5	44%	66	115	(43%)
Consumer BU	<u>2.8</u>	<u>2.2</u>	31%	<u>60.9</u>	<u>29.2</u>	109%	47	74	(37%)
Hardware BU	0.4	1.7	(74%)	9.2	21.6	(58%)	48	78	(38%)
MS-DOS BU	<u>1.3</u>	<u>0.8</u>	65%	<u>29.8</u>	<u>15.4</u>	93%	43	50	(15%)
Windows BU	4.4	6.0	(27%)	63.9	83.5	(23%)	69	72	(5%)
Win NT Family	0.3	0.8	(59%)	1.6	4.5	(64%)	220	189	16%
Win NT Adv. Server Family	0.7	0.4	66%	0.8	0.4	92%	863	996	(13%)
Win NT Server (SQL,SNA)	0.6	0.4	78%	0.9	0.6	62%	714	648	10%
Other Operating Systems PU	0.4	0.4	7%	2.6	3.7	(30%)	152	100	52%
Advanced Systems BU	<u>2.1</u>	<u>2.0</u>	4%	<u>5.9</u>	<u>9.1</u>	(36%)	352	217	62%
Workgroup BU *	0.4	0.6	(27%)	9.1	5.2	73%	45	105	(58%)
Digital Office Systems PUs	0.0	0.0	(59%)	0.1	0.3	(56%)	76	82	(8%)
ACT and API PUs	0.0	0.0	NM	0.7	0.0	NM	10	0	NM
Other PUs	0.0	1.4	(100%)	0.0	12.4	(100%)	0	110	NM
Other	<u>0.0</u>	<u>1.4</u>	(99%)	<u>0.8</u>	<u>12.7</u>	(94%)	19	110	(82%)
Finished goods revenue	55.6	45.5	22%	412.1	381.3	8%	135	119	13%
Other materials	2.1	0.0	NM	0.0	0.0	NM			
Total FG gross revenue	<u>\$57.7</u>	<u>\$45.5</u>	27%	<u>412.1</u>	<u>381.3</u>	8%			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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FAR EAST FINISHED GOODS

REVENUE SUMMARY (REVENUE IN MILLIONS, UNITS IN THOUSANDS)

FYTD94

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	\$22.2	\$14.4	54%	71.7	48.1	49%	\$310	\$300	3%
MAC Office	0.2	0.2	13%	0.7	0.7	(7%)	322	263	22%
Excel PU *	17.8	14.8	20%	81.7	101.6	(20%)	217	146	49%
Word PU *	9.9	10.9	(8%)	62.9	83.8	(25%)	156	130	22%
Graphics PU *	0.6	0.8	(28%)	2.6	3.8	(32%)	215	203	6%
Project PU	0.5	0.4	28%	1.3	1.1	17%	375	342	9%
DAD BU New Users **	<u>51.2</u>	<u>41.5</u>	23%	<u>220.8</u>	<u>239.1</u>	(8%)	232	173	34%
WIN Office	0.5	0.3	73%	2.9	1.1	153%	165	241	(32%)
MAC Office	0.0	0.0	NM	0.2	0.0	NM	200	0	NM
Excel PU *	0.7	1.1	(41%)	5.1	15.3	(66%)	130	74	77%
Word PU *	4.5	2.5	81%	37.8	23.3	63%	119	107	11%
Graphics PU *	0.1	0.0	330%	0.5	0.2	141%	119	67	79%
Project PU	0.0	0.0	(49%)	0.1	0.2	(53%)	113	105	8%
DAD BU Existing Users **	<u>5.8</u>	<u>3.9</u>	47%	<u>46.7</u>	<u>40.1</u>	16%	124	98	26%
Basic PU	6.3	5.2	21%	49.5	30.6	62%	128	171	(25%)
Database Mgmt (Access) PU *	6.9	2.1	225%	55.4	16.4	238%	125	130	(4%)
Fox Database PU *	2.5	1.4	81%	11.0	7.0	56%	229	197	16%
Languages PUs	11.9	7.3	65%	48.4	33.3	45%	246	218	13%
DBDT BU *	<u>27.7</u>	<u>16.0</u>	73%	<u>164.3</u>	<u>87.4</u>	88%	168	183	(8%)
Entry PU	2.7	1.8	49%	60.4	33.3	81%	45	55	(18%)
Multimedia Publishing PU	0.3	0.0	NM	5.5	0.0	NM	54	0	NM
Works PU	2.6	2.5	4%	27.4	22.6	21%	95	111	(14%)
Consumer BU	<u>5.6</u>	<u>4.3</u>	30%	<u>93.3</u>	<u>55.9</u>	67%	60	77	(22%)
Hardware BU	2.6	4.9	(47%)	33.5	55.2	(39%)	78	89	(13%)
MS-DOS BU	2.8	1.5	89%	67.4	30.4	121%	42	49	(15%)
Windows BU	<u>11.9</u>	<u>13.3</u>	(10%)	<u>135.9</u>	<u>185.3</u>	(27%)	88	72	22%
Win NT Family	0.8	1.0	(22%)	3.9	5.5	(30%)	206	185	11%
Win NT Adv. Server Family	0.8	0.6	39%	1.0	0.6	65%	852	1,013	(16%)
Win NT Server (SQL.SNA)	0.7	0.5	26%	1.1	0.7	60%	604	767	(21%)
Other Operating Systems PU	1.1	0.7	52%	6.1	6.9	(12%)	180	103	74%
Advanced Systems BU	<u>3.4</u>	<u>2.9</u>	18%	<u>12.0</u>	<u>13.8</u>	(13%)	282	209	35%
Workgroup BU *	0.8	0.9	(17%)	16.7	9.1	82%	46	100	(54%)
Digital Office Systems PUs	0.0	0.0	(63%)	0.2	0.5	(65%)	86	82	5%
ACT and APD PUs	0.0	0.0	NM	1.3	0.0	NM	21	0	NM
Other PUs	0.0	2.4	(100%)	0.0	19.2	(100%)	0	124	(100%)
Other	<u>0.0</u>	<u>2.4</u>	(98%)	<u>1.4</u>	<u>19.7</u>	(93%)	28	123	(77%)
Finished goods revenue	111.8	91.7	22%	792.1	736.1	8%	141	125	13%
Other materials	4.7	0.0	NM	0.0	0.0	NM			
Total FG gross revenue	<u>\$116.6</u>	<u>\$91.7</u>	27%	<u>792.1</u>	<u>736.1</u>	8%			

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

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FAR EAST FINISHED GOODS

Q94-2

Revenue

- Far East net revenue was \$8.4 million (18%) above plan. During the past quarter, net revenue in Japan and Korea were \$8.6 million (26%) and \$1.3 million (41%) above plan. Results in Taiwan for Q94-2 were \$2.7 (55%) under plan, although the subsidiary was \$1.1 million above plan FYTD94.
- Far East net revenue was \$18.9 million (54%) higher than in Q93-2. The strong revenue performance compared with both plan and prior year was significant because it happened despite delays in shipment of Japanese Access (shipped in mid-December 1993) and Excel 5.0 (to ship in Q94-3).
- Desktop Applications, led by Office, constituted 48% of gross revenue, compared to a plan share of 43%. Office is now shipping in all Far East countries except Korea. Office revenue was \$6.1 million (87%) above plan, and licenses were 17,000 (59%) above plan, reflecting revenue per license which was 18% above plan despite strong competition from Lotus Smart Suite, which has been localized into Japanese. Office cannibalized sales of Word and Excel, as a competitive upgrade program was launched in Japan in November.
- Database & Development Tools accounted for 32% of Q94-2 gross revenue (versus plan of 25%). The most outstanding performance was from Access, the Japanese version of which shipped in December. Access pricing was essentially at plan, and revenue and licenses were both approximately 240% above plan (Q94-2 Access revenue was \$4.7 million above plan). Lotus Approach was launched in Japan the same day as Access, but at a unit price \$10 lower than Access.
- Windows revenue and licenses were 27% and 23% below plan, reflecting lackluster sales in Japan and Taiwan. There had been a fundamental shift in Window sales to the OEM channel, as the Windows Ready to Run business (credited to the OEM channel) grew significantly during Q94-2.

Cost of Revenue

- During Q94-2, the sales mix of applications was higher than plan. This shift towards lower-cost products (compared with systems products) offset a slight increase in applications product costs as a percent of applications revenue. Total product costs as a percent of net revenue were less than plan for the quarter.

Controllable Expenses

- Controllable expenses were \$300,000 (1%) under plan during Q94-2, and, as a percent of net revenue, were under plan by 7.8 points in Q94-2. Net revenue and controllable expenses with favorable variances to plan produced a responsibility margin \$7.0 million (59%) above plan for the quarter.
- People expenses were \$393,000 above plan during the quarter because of unfavorable foreign exchange rate variances. At the budgeted (instead of actual) exchange rates for Japan, Korea and Taiwan, Q94-2 people expenses would have been \$10.3 million, or \$295,000 below plan. The strength of the Yen had a Q94-2 and YTD positive impact on revenue and a negative impact on reported expenses.
- Facility expenses were below plan primarily because of low expenditures for maintenance and repair and for telecommunications. Another contributing factor was a negotiated reduced rental rate for the Tokyo office, which will result in an annual savings of approximately \$2.0 million, effective Q94-2.
- Marketing expenses were essentially at plan for Q94-2, and \$1.3 million less than in Q94-1, when there was an over-expenditure of approximately \$2.1 million.
- Other expenses were \$400,000 below plan, in part because of several accounting adjustments made during the quarter to reverse erroneous charges during Q94-1.

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FAR EAST FINISHED GOODS

FYTD94

Revenue

- Far East net revenue was \$22.7 million (25%) above plan, and all subsidiaries posted net revenue above plan. Compared with the first half of FY93, FYTD94 revenue was \$61.4 million (117%) higher; the Far East has more than doubled in the past year in terms of net revenue.
- Strong sales of Office in both Q94-1 and Q94-2 helped desktop applications revenue exceed plan by 25%. All locations recorded above-plan Office sales except Korea, which experienced a delay in the release of Hangul Excel 5.0. Japanese Word 5.0 was released in Q94-1, the results of which was evident in Word sales to existing users.
- Sales of Database & Development Tools comprised 25% of Far East revenue. In Japan and Korea, Database & Development Tools revenues were 27% and 25% of sales, respectively. Visual Basic continues to sell strongly, and Visual C++ unit sales and pricing were robust during the first two months of FY94.
- Windows licenses were 27% below plan, while above-plan pricing led to revenue of (only) 10% below plan. The shift of sales to the OEM channel and the slower-than-expected conversion of users from MS-DOS to the Windows environment in Japan are largely accountable for this performance.

Cost of Revenue

- As a percent of net revenue, cost of revenue was 1.6 points below plan. This favorable variance was primarily due to revenue mix, which was weighted more heavily than planned towards applications. The impact of this shift in mix was mitigated to some extent by the strong sales of Database & Development Tools (e.g. Visual Basic, Visual C++ and Fox products), which had a relatively high product cost content.

Controllable Expenses

- Controllable expenses were \$2.1 million (5%) above plan in absolute terms, but were 7.2 points below plan as a percent of net revenues.
- People expenses were \$630,000 above plan because of unfavorable foreign exchange rate variances relative to plan, particularly in the Japanese Yen. If the plan exchange rate were applied to YTD people expenses, the amount would be \$20.1 million, or \$693,000 below plan.
- Facility expenses were 9% below plan because of lower-than-planned costs for telecommunications and for maintenance and repair of facilities and networks.
- Marketing expenses were 17% above plan because of an overspend in Japan in Q94-1. This overspend was related in part to the launch of Japanese Windows 3.1 in Q93-4, and marketing expenditures during Q94-2 were according to plan. Projections for FYE94 indicated that marketing expenses will map closely to plan.
- Other expenses on a FYTD94 basis did not deviate from plan.

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Channel Reporting

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FAR EAST FINISHED GOODS

Significant Customers in Major Subsidiaries (in thousands)

	<u>Q92-4</u>	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
Japan							
Soft Bank	\$ 3,308	\$ 1,109	\$ 7,230	\$ 7,119	\$ 11,554	\$ 9,316	\$ 11,780
Software Japan	2,990	1,388	3,317	3,457	5,087	6,150	6,365
Soft Wing	1,864	885	3,494	3,093	4,500	3,960	4,101
Fujitsu	1,044	1,025	876	1,864	1,389	1,911	2,171
IBM	485	839	1,733	1,528	1,258	1,668	1,799
NEC	1,267	1,249	978	1,211	2,395	2,301	1,361
Canon Sales	1,798	2,078	1,155	2,329	1,724	2,041	1,016
Taiwan							
Eten	315	846	475	926	1,943	2,393	529
Acer Sertek	640	832	806	583	1,276	2,324	563
Korea							
Infotech	486	2,320	594	353	571	2,966	1,850
	<u>\$ 14,197</u>	<u>\$ 12,571</u>	<u>\$ 20,658</u>	<u>\$ 22,463</u>	<u>\$ 31,697</u>	<u>\$ 35,030</u>	<u>\$ 31,535</u>
Percent of Gross Revenue	<u>68%</u>	<u>70%</u>	<u>59%</u>	<u>54%</u>	<u>52%</u>	<u>58%</u>	<u>56%</u>

- Sales to the customers listed above have been within a tight range (as a percent of gross revenues) for the past five quarters. During this period, sales to these entities have constituted between 52% and 59% of Far East gross revenues, which is notably consistent.
- Strong sales to the channel in Taiwan in Q94-1 are reflected in the high sales for Eten and Acer Sertek for that period. Sharply reduced sell-through in Q94-2 is demonstrated by sales to these two distributors equal to 23% of comparable Q94-1 sales.
- In Korea, Infotech is still the predominant Microsoft distributor. Efforts are currently underway to cultivate and diversify distributors in Korea in order to reduce historical dependence on Infotech.
- The traditional distributors in Japan (i.e. Soft Bank, Software Japan and Soft Wing) continue to be Microsoft's most significant customers. Sales to these three distributors increased 59% and 15% from Q93-2 and Q94-1, respectively. Meanwhile, sales to OEMs which maintain unique retail sales systems (i.e. Fujitsu, IBM, NEC and Canon Sales) increased 33% from Q93-2 to Q94-2, and declined 20% from Q94-1 to Q94-2. These trends in Japan suggest that the retail channel there is evolving into a distribution model closer to that found in North American and European markets.

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OEM

OEM

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$268.3	\$194.6	\$73.7	\$523.4	\$374.9	\$148.5
Cost of revenue	18.9	7.5	(11.4)	30.1	15.5	(14.6)
Gross profit	249.4	187.0	62.3	493.3	359.3	133.9
People expenses	4.8	5.1	0.4	9.0	10.3	1.3
Facilities expenses	0.7	0.9	0.1	1.4	1.7	0.3
Marketing expenses	0.6	1.4	0.8	1.1	2.9	1.8
Other expenses	14.4	7.8	(6.7)	28.5	15.0	(13.5)
Controllable expenses	20.6	15.2	(5.4)	40.0	29.9	(10.1)
Responsibility margin	228.8	171.9	56.9	453.3	329.4	123.8
Net shared resources	6.5	9.5	3.0	12.4	19.2	6.8
Shared resource margin	\$222.3	\$162.4	\$59.9	\$440.9	\$310.2	\$130.7
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	7.1	3.9	(3.2)	5.8	4.1	(1.6)
Controllable expenses	7.7	7.8	0.1	7.6	8.0	0.3
Responsibility margin	85.3	88.3	(3.1)	86.6	87.9	(1.3)
Net shared resources	2.4	4.9	2.4	2.4	5.1	2.8
Shared resource margin	82.9 %	83.5 %	(0.6) %	84.2 %	82.8 %	1.5 %

Q94-2

Net Revenue

- Net revenue was 23.8% of corporate net revenue and contributed 40.5% of the consolidated contribution margin. Year-to-date, net revenue was 29% of corporate net revenue and contributed 43.7% of the contribution margin.
- Of the \$74 million positive variance, \$30 million came from strong international performance, \$17 million was generated by the "Big Six" (IBM, Compaq, Gateway 2000, Dell, Packard Bell, AST), \$15 million by other U.S. OEMs, and \$11 million by normally recurring revenue adjustments (GAAP accrual). Year-to-date, all regions had positive variances.

Cost of Revenue

- The negative cost of revenue variance resulted from higher sales volume, manufacture of a more expensive mouse than planned, and from unbudgeted third-party royalty expense.

Controllable Expenses

- As the PC price wars continue to exert margin pressure on the OEMs, MS has identified a number of OEMs that are financially at risk. In addition to the standard allowance for doubtful accounts, billings related to these high-risk companies are reserved for 100%, resulting in \$5 million of the other expenses variance. An allowance for doubtful accounts of \$38 million covers all receivables believed to be of high or moderate collection risk. The remainder of the variance results from B&O tax accruals that are higher than plan due to higher revenues and a higher tax rate than budgeted.

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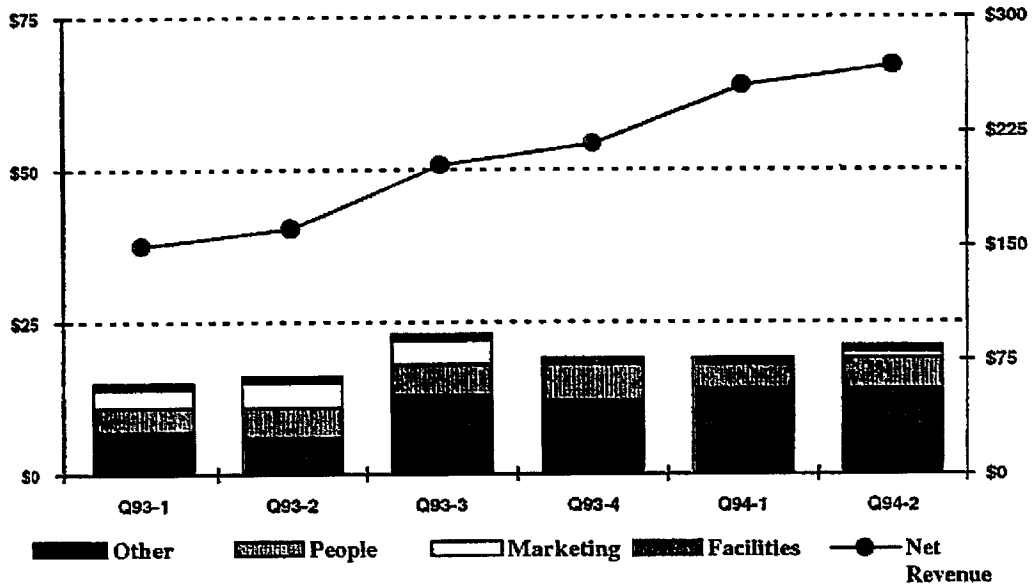
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TREND ANALYSIS

Net Revenue & Controllable Expenses (in millions)



- Gross revenue for FYTD94 grew 79% over the same period last year, almost four times the growth rate of PC shipments.
- Higher unit sales by established OEMs resulting from the PC price wars, higher revenue per PC resulting from Windows, Mouse, and applications licenses, and success in the lower tier "new business" market all contributed to OEM's steady growth over the past two years.
- Other expenses grew because of revenue taxes and bad debt provisions for high risk OEMs.
- OEM has shifted its historical sales model of noninvolvement with customer sales initiatives to working closely with OEMs to develop joint sales and marketing programs, thereby leveraging MS marketing funds. Delay in receipt of invoices from several hardware manufacturers, with which OEM has done joint marketing endeavors, created the positive variance.
- Strict expense policies and close monitoring of expenses reduced employee fringes, travel and entertainment, causing the reduction in people expenses.

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Product Mix (units in thousands, revenue in millions)

Q94-2

	Q94-2			Q94-2 Plan			Variance		
	Units	Revs	\$/Unit	Units	Revs	\$/Unit	Units	Revs	\$/Unit
MS-DOS	5,501	\$ 99	\$ 18	5,635	\$ 94	\$ 17	(134)	\$ 5	\$ 1
Windows	4,561	82	18	3,725	61	16	836	21	2
Advanced Systems	567	14	25	681	15	22	(114)	(1)	3
Hardware	716	14	20	460	6	13	256	8	7
Consumer	1,174	11	9	906	8	9	268	3	1
Desktop	186	10	54	225	11	49	(39)	(1)	5
Other	1,938	27	N/A	408		N/A	1,530	27	N/A
		257			195			62	
Revenue adjustments		11			--			11	
Net Revenue		<u>\$ 268</u>			<u>\$ 195</u>			<u>\$ 73</u>	

- OEMs signed commitments for more than 8 million units of Windows for Workgroups to ship in calendar year 1994.
- Average royalty rates for MS-DOS and Windows were increased slightly due to the add-on charges for MS-DOS 6 with Enhanced Tools and Windows for Workgroups.
- Growth in the consumer channel and increase in the proportion of PCs with CD ROM players contributed to Consumer application sales, primarily Works and Bookshelf. OEM will be an important channel for Microsoft at Home.
- Desktop Applications were under budget due to lower than planned sales by Gateway 2000 and Hewlett Packard. Gateway shipped Works rather than the more expensive desktop applications on many systems. Revenue/unit increased due to the higher proportion of international shipments, which bear higher royalties.
- International mouse sales generated \$4 million of the hardware variance.

Net Revenue (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
North America						
United States	\$149.2	\$117.5	\$31.7	\$283.6	\$218.2	\$65.4
Canada	3.4	2.5	0.9	6.6	5.2	1.4
	<u>152.6</u>	<u>120.0</u>	<u>32.6</u>	<u>290.2</u>	<u>223.4</u>	<u>66.8</u>
International						
Europe	56.0	36.5	19.5	95.0	73.9	21.1
Far East	39.2	30.7	8.5	84.1	63.4	20.7
Asia Pacific	5.5	4.9	0.6	12.0	9.4	2.6
Latin America	2.7	1.6	1.1	3.8	3.1	0.7
AJME	1.3	0.9	0.4	2.3	1.7	0.6
	<u>104.7</u>	<u>74.6</u>	<u>30.1</u>	<u>197.2</u>	<u>151.5</u>	<u>45.7</u>
Revenue adjustments	11.0	--	11.0	36.0	--	36.0
Net worldwide revenue	<u>\$268.3</u>	<u>\$194.6</u>	<u>\$73.7</u>	<u>\$523.4</u>	<u>\$374.9</u>	<u>\$148.5</u>

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- In North America, \$17 million of the variance resulted from strong performances by the "Big Six." A Hewlett Packard payment for Printer System technology and an unbudgeted license with Fountain Technology resulted in an additional \$5 million of the variance.
- Escom, Vobis, and Actebis contributed \$13 million to the European overage due to minimum commitments associated with their applications licenses.
- The Far East's positive variance was driven by NEC and Toshiba.

Significant Customers (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Large Accounts						
Compaq	\$ 22.7	\$ 18.3	\$ 4.4	\$ 43.3	\$ 35.6	\$ 7.7
IBM	14.2	13.3	0.9	36.4	19.4	17.0
Gateway 2000	15.0	14.9	0.1	29.4	28.9	0.5
Dell	12.7	8.0	4.7	23.4	15.3	8.1
AST	11.4	5.8	5.6	18.4	11.2	7.2
Packard Bell	8.6	7.7	0.9	14.5	13.1	1.4
Solution Providers						
Hewlett Packard	6.6	6.5	0.1	11.3	9.2	2.1
DEC	4.5	3.8	0.7	8.4	6.8	1.6
NCR	4.4	3.4	1.0	7.8	6.2	1.6
SCO	2.2	1.7	0.5	10.1	10.3	(0.2)
Other	4.1	3.2	0.9	3.7	0.1	3.6
Named Accounts	16.0	11.5	4.5	28.0	22.4	5.6
New Business Accounts	22.5	19.4	3.1	45.0	40.1	4.9
International Accounts						
NEC	9.3	3.6	5.7	18.8	7.1	11.7
Escom	8.8	1.9	6.9	12.2	3.3	8.9
Toshiba	6.5	1.8	4.7	13.3	2.1	11.2
Vobis	5.7	2.8	2.9	9.9	5.2	4.7
Olivetti	3.2	3.0	0.2	6.2	6.0	0.2
Acer	4.0	2.9	1.1	7.0	5.7	1.3
SNI (Siemens)	2.8	2.4	0.4	5.4	5.5	(0.1)
Other	61.2	56.2	5.0	85.5	116.6	(31.1)
Other Accounts	10.9	2.5	8.4	49.4	4.8	44.6
Gross revenue	257.3	194.6	62.7	487.4	374.9	112.5
Revenue adjustments	11.0	--	11.0	36.0	--	36.0
Net revenue	<u>\$ 268.3</u>	<u>\$ 194.6</u>	<u>\$ 73.7</u>	<u>\$ 523.4</u>	<u>\$ 374.9</u>	<u>\$ 148.5</u>

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- The "Big Six" OEMs (Large Accounts) continued to pick up market share worldwide, while the middle and lower tiers of the PC industry continued to experience margin pressure. Revenues from the Big Six increased 113% from Q93-2 due to volume increases coupled with increase in revenue per PC for several companies. Average revenue per PC for the Big Five (excluding IBM) was \$39, up from \$34 in Q93-2 due to higher MS-DOS royalties and additional licenses for Works and CD titles.

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- IBM is shipping MS-DOS 6 with Enhanced Tools (not IBM's PC-DOS) on its Eduquest, Ambra and PS/1 brands of PC and is shipping Windows on 100% of its Ambra and PS/1 machines.
- Packard Bell continued to dominate the mass merchant channel. They were shipping multimedia machines and will soon introduce a line of notebooks.
- New Business account managers attended CompuExpo, Comdex and various Regional Briefings, signing up approximately \$6 million in new business (based on unit commitments). Microsoft signed an agreement with the Southern California Chinese Computer Association (SCCCA) that offers attractive royalty rates to members of the group in exchange for the group's policing piracy and unbundling issues among their members.
- NEC and Toshiba results created a strong quarter in Japan. In addition to a gross revenue per system increase as they ship more 486 PCs, NEC benefited from the price wars among the other operating systems, including MS-DOS/V. Toshiba has again gained a strong position in the U.S. notebook market.

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PSS

Highlights

- During Q94-2, PSS was awarded two of the most prestigious awards in the microcomputer software support industry; the Information Technology Association of America (ITAA) award and the SSPA STAR Award for Sustained Technical Support. The ITAA award for overall support quality, was based on the Commerce Department's Malcolm Baldrige Award, and was given to the company that best demonstrates excellence in delivering high quality technical support. The SSPA STAR Award for Sustained Technical Support recognized Microsoft's ability to deliver consistent, high quality support for an extended period of time. The award application described key business innovations and service delivery metrics during the 24 months preceding the award application.
- PSS launched the Microsoft Support Network (MSN) for Advanced Systems products in Q94-1, and for the Developer and Personal Operating Systems product clusters in Q94-2. The PR goal was for net neutral coverage, and actual coverage was neutral too positive, exceeding expectations.
- Regular PSS staffing leveled off in Q94-2 relative to the decrease in the PSS staffing level realized through Q94-1. An increase in outsourcing and variable staffing was utilized to address the demand spikes for the new product releases in Q94-2.

Domestic Controllable Expenses (in millions)

	Q94-2		FYTD94	
	Actuals	% of Plan	Actuals	% of Plan
People	\$26.8	91.0	\$52.3	88.7
Facilities	9.3	92.7	17.3	89.8
Other	3.4	118.3	6.5	111.5
Paid Support Offset	(3.4)	106.3	(6.5)	99.3
	<u>\$36.0</u>	<u>92.2</u>	<u>\$69.6</u>	<u>89.9</u>

- Total controllable expenses were 7.8% less than plan for Q94-2 and 10.1% less than plan FYTD. The variance was primarily due to lower than planned hiring, spending per person, and utilizing less expensive outsourcing and variable resources to meet peak demands.
- PSS other was 118.3% of budget in Q94-2 due to higher than planned outsourcing expenses. Paid support offset was 106.3% of plan due to the unplanned revenues in the CompuServ area.

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Domestic PSS Cost Distribution by Channel (in millions)

	Q94-2		FYTD94	
	Actuals	% of Plan	Actuals	% of Plan
USFG	\$29.9	92.4	\$57.4	89.5
US-OEM	3.6	93.6	7.1	92.1
Domestic Channels	\$33.5	92.6	\$64.5	89.8
International	2.5	89.6	5.1	90.3
	<u>\$36.0</u>	<u>92.2</u>	<u>\$69.6</u>	<u>89.9</u>

- The \$2.5 million represented the domestic PSS support costs allocated to the international subs for domestic services provided to them.

Domestic PSS Cost Distribution by Product Unit (in millions)

	Q94-2		FYTD94	
	Actual	% of Plan	Actual	% of Plan
Windows	\$7.5	107.8%	\$14.0	98.8%
Word	5.0	81.2	9.6	78.4
Excel	3.2	73.7	6.2	73.9
Win NT	2.5	66.7	4.8	64.6
DBM	2.4	90.5	4.9	93.4
MS-DOS	2.4	148.3	4.8	146.7
Fox	2.3	95.8	4.7	97.2
Other Operating Sys	1.6	75.8	3.3	77.3
Messaging	1.3	91.6	2.7	97.2
C++	1.2	118.4	2.4	113.7
Works	0.8	117.7	1.7	121.6
Project	0.8	222.4	1.2	174.5
Entry	0.8	99.2	1.3	87.2
Basic	0.6	145.0	1.0	129.8
Graphics	0.3	39.2	0.7	46.4
SET	0.3	73.4	0.5	73.4
Other	0.5	197.8	0.6	99.6
Total	<u>\$33.5</u>	<u>92.5%</u>	<u>\$64.5</u>	<u>89.8%</u>

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- PSS cost of support to the product units was 7.5% lower than planned for Q94-2. This decrease was due to lower than expected call volumes for Windows NT, delayed releases of Word 6.0 and Excel and utilization of outsourcing and variable resources to meet peak demands during product release.
- MS-DOS was over plan due to the unplanned release of Version 6.2, BASIC was over plan due to a support policy change that broadened the scope of BASIC support and as a result call times had increased.

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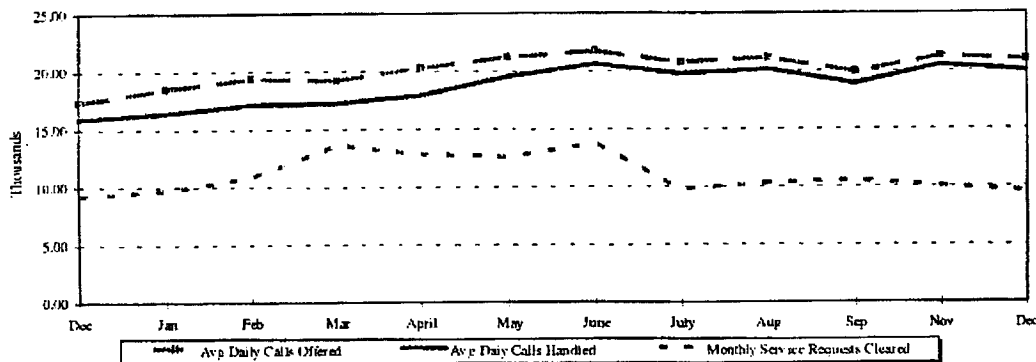
PSS Cost Mix by Product Unit

	Q94-2		FYTD94	
	Actual	% pts Var	Actual	% pts Var
Windows	22.5%	(3.2)	21.7%	(3.2)
Word	15.0	2.1	14.8	2.1
Excel	9.6	2.4	9.7	2.4
Win NT	7.4	2.9	7.4	2.9
DBM	7.3	0.2	7.7	0.2
MS-DOS	7.1	(2.7)	7.5	(2.7)
Fox	6.9	(0.2)	7.2	(0.2)
Other Operating Sys	4.8	1.1	5.2	1.1
Messaging	3.9	0.0	4.2	0.0
C++	3.6	(0.8)	3.7	(0.8)
Works	2.5	(0.5)	2.6	(0.5)
Project	2.4	(1.4)	1.9	(1.4)
Entry	2.3	(0.2)	1.9	(0.2)
Basic	1.7	(0.6)	1.5	(0.6)
Graphics	1.0	1.3	1.1	1.3
SET	0.8	0.0	0.8	0.0
Other	1.2	(0.4)	1.0	(0.4)
Total	100%	0.0	100%	(0.0)

- Windows, Word, Excel, Win-NT, DBM, MS-DOS, Fox contributed 68.9% of all product cost for Q94-2.

Average Daily Calls

PSS Activity



- Note: There was no October phone data for Q94-2. The chart compares November and December data versus Q94-1 data.
- Total average daily calls offered increased 2%, while handled increased 3% over Q94-1 volumes. This increase was due to the release of MS-DOS 6.2, Word 6.0 and WFW 3.11. PSS was able meet its target of handling 95% of calls offered throughout Q94-1 and Q94-2.
- The average monthly service requests cleared remained relatively flat in Q94-2 versus Q94-1 volumes.

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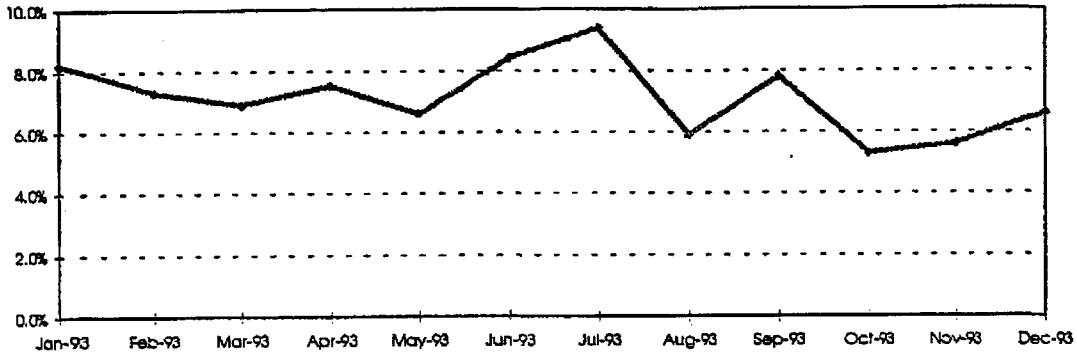
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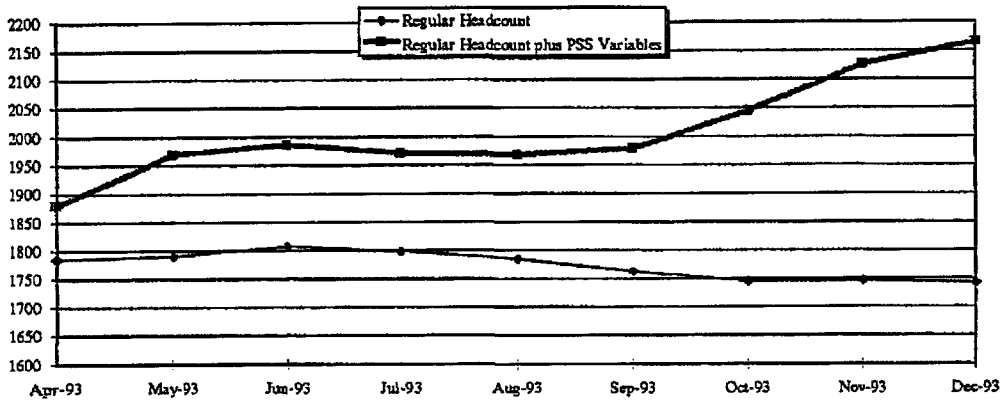
TREND ANALYSIS

Net Domestic PSS Cost as a Percentage of US Net Revenue



- In the chart above, PSS cost is displayed as a percentage of net revenue. For Q94-2, PSS cost as a percentage of US net revenue actual was 6% versus the plan of 7.4%. Q94-2 actual decreased 1.4% from Q94-1. Note: International allocations are not included in PSS Cost

PSS Headcount



- PSS regular FTE headcount remained level during Q94-2. Demand spikes due to product releases were met by utilizing outsourcing and variable employees.

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Product Group Reporting

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WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY SUMMARY

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$487.8	92 %	\$85.2	86 %	\$114.3	101 %	\$288.3	90 %
Database & Dev. Tools	84.9	92	16.4	90	43.7	90	24.8	98
Consumer	97.9	145	22.2	160	31.9	95	43.8	216
Workgroup	26.1	114	2.6	74	15.1	91	8.4	299
Systems	419.3	112	68.9	129	111.6	86	238.8	124
Advanced Technology	3.0	64	0.9	107	12.2	64	(10.0)	NM
Other	10.1	93	(11.4)	(312)	7.5	279	14.0	306
	<u>\$1,129.0</u>	<u>102</u>	<u>\$184.8</u>	<u>96</u>	<u>\$336.1</u>	<u>93</u>	<u>\$608.1</u>	<u>111</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	43 %	48 %	17 %	19 %	23 %	21 %	39 %	60 %
Database & Dev. Tools	8	8	19	20	52	53	29	28
Consumer	9	6	23	21	33	49	45	30
Workgroup	2	2	10	16	58	72	32	12
Systems	37	34	16	14	27	35	57	51
Advanced Technology	0	0	30	18	403	407	(333)	(324)
Other	1	1	(113)	33	74	25	139	42
	<u>100 %</u>	<u>100 %</u>	<u>16</u>	<u>17</u>	<u>30</u>	<u>33</u>	<u>54</u>	<u>50</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$868.7	101 %	\$143.8	92 %	\$200.0	93 %	\$524.8	107 %
Database & Dev. Tools	164.4	93	37.4	109	79.4	85	47.7	98
Consumer	152.2	137	32.9	145	55.7	84	63.6	291
Workgroup	46.1	115	5.3	82	29.1	86	11.7	NM
Systems	811.0	113	123.9	122	211.6	85	475.4	130
Advanced Technology	5.1	73	1.6	128	21.3	57	(17.9)	NM
Other	64.2	337	(1.2)	(19)	36.2	710	29.1	372
	<u>\$2,111.6</u>	<u>109</u>	<u>\$343.7</u>	<u>105</u>	<u>\$633.4</u>	<u>90</u>	<u>\$1,134.5</u>	<u>125</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	41 %	45 %	17 %	18 %	23 %	25 %	60 %	57 %
Database & Dev. Tools	8	9	23	19	48	53	29	28
Consumer	7	6	22	20	37	60	42	20
Workgroup	2	2	11	16	63	84	25	(1)
Systems	38	37	15	14	26	35	59	51
Advanced Technology	0	0	32	18	421	540	(353)	(458)
Other	3	1	(2)	32	56	27	45	41
	<u>100 %</u>	<u>100 %</u>	<u>16</u>	<u>17</u>	<u>30</u>	<u>36</u>	<u>54</u>	<u>47</u>

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WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY SUMMARY

Metrics Summary (Annualized in Thousands)

	Desktop	Database & Dev. Tools	Consumer	Workgroup	Systems	Other	WPG	Adv. Tech.	WPG & A.T.
Net revenue per employee									
Actual	2,320	473	835	263	1,191	112	1,074	35	995
Plan	2,226	433	516	227	951	95	923	41	846
Q94-1	1,801	451	461	212	1,083	528	922	32	869
People expenses per employee									
Actual	79	89	86	73	95	77	86	98	87
Plan	73	75	78	77	93	75	81	104	83
Q94-1	80	87	84	73	91	76	85	92	85
Facilities expenses per employee									
Actual	17	13	14	16	19	14	16	11	16
Plan	17	15	16	15	22	23	19	17	18
Q94-1	17	14	14	16	17	8	15	13	15
Product development expenses per employee									
Actual	26	19	51	16	33	33	30	19	29
Plan	25	26	59	18	44	28	35	37	35
Q94-1	17	14	36	20	21	29	21	9	20
Marketing expense % net revenue									
Actual	12%	15%	8%	11%	5%	7%	9%	10%	9%
Plan	10%	14%	12%	14%	8%	8%	10%	3%	10%
Q94-1	9%	7%	7%	9%	4%	48%	9%	14%	9%

- Consumer revenue per employee was higher than plan due to a positive Q94-2 revenue variance of 45% and business unit headcount remaining below plan.
- Workgroup revenue per employee was 16% above plan and grew 24% from Q94-1 due to continued growth in the overall messaging market and Microsoft's increasing share. Product development per employee was below plan due to timing of expenditures. Expectations are for total spending to approximate budget by the end of FY94.
- People expense per employee for Consumer had a slight unfavorable variance driven by expenses being on plan and headcount below plan. Temporary help and supplies were unfavorable to plan, driving part of the negative variance. Product development per employee was below plan but will ramp up as the year progresses.
- Advanced Technology people expense per employee reflected the unusually high recruitment and relocation costs associated with significantly increased staffing during the fiscal year. Consulting, travel and entertainment, and employee morale expenses were below plan and helped moderate the ratio.
- Product development expense per employee for Systems was below plan due to the localization of Windows NT-J in Japan, and shifts in product release schedules that caused timing changes of code purchases and contractor hiring.
- Database & Development Tools marketing expenses as a percent of net revenue for Q94-1 were significantly offset by registration fees for the Fox Developer's Conference.
- Consumer marketing expense as a percent of revenue was below plan but is expected to increase to the budgeted level by the end of the fiscal year.
- Workgroup marketing expense as a percent of net revenue was below plan, but should increase as the EMS and SFS' ship dates approach (6/94).

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WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY SUMMARY

Headcount Summary

	Q94-2			FY94
	Actual	Plan	Variance	Plan
Word	254	277	23	271
Excel	212	247	35	234
Graphics	67	76	9	77
Project	79	85	6	79
Other Desktop Applications	229	272	43	283
Desktop Applications	841	957	116	944
Applications Programmability	148	151	3	151
Database Mgmt Systems	249	260	11	259
Fox	68	65	(3)	65
DDT Management	53	91	38	93
C++	197	218	21	208
Scientific and Eng Tools	43	65	22	65
Database & Dev Tools	758	850	92	841
Works	166	176	10	173
MM Pubs	120	132	12	143
Entry	132	153	21	153
Other Consumer	51	63	12	78
Consumer	469	524	55	547
Workgroup	397	403	6	399
MS-DOS	28	28	0	28
Windows	328	402	74	402
Advanced Systems	531	625	94	614
Hardware	81	85	4	85
Digital Office Systems	154	170	16	183
Systems Marketing	110	103	(7)	103
Other Systems	136	167	31	188
Systems	1,368	1,580	212	1,603
Advanced Consumer Tech	234	304	70	314
Advanced Product Dev	52	66	14	68
On-Line Services	46	66	20	69
Broad Band Apps	13	19	6	20
Advanced Technology	345	455	110	471
Other WPG	176	220	44	225
International R&D	22	49	27	222
MSU	117	140	23	140
Books	47	50	3	51
Other Product Groups	164	190	26	191
Total Product Groups	4,540	5,228	688	5,443

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Product Group Reporting

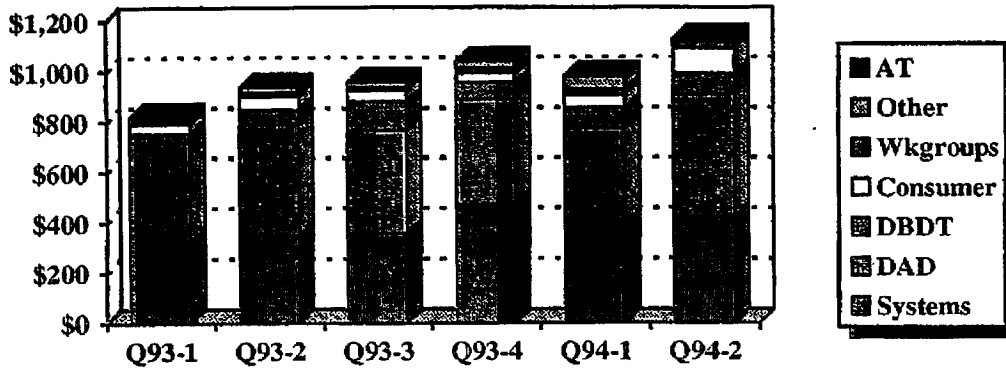
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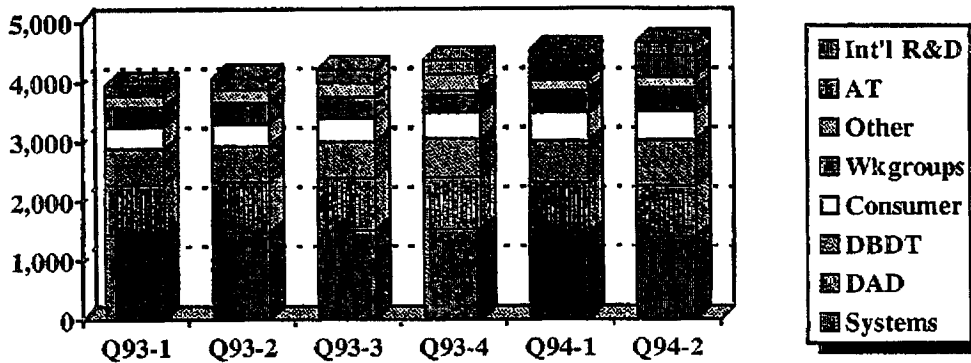
WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY SUMMARY

Net Revenue by Business Unit (in millions)*



*Not restated for business re-organizations

Headcount by Business Unit *



*FY 93 not restated. AT included with systems.

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DESKTOP APPLICATIONS SUMMARY

DESKTOP APPLICATIONS SUMMARY

Key Product Releases

Product	RTM Date		Gross Revenue in Millions *			
	Act/Fcst	Plan	FYTD94			FY94
			Actual	Plan	Variance	Plan
Win Word 6.0 (and Win Office 4.0)	Oct-93	Sep-93	\$394	\$353	\$41	\$736
Mac Word 6.0 (and Mac Office 4.2)	May-94	Mar-94	\$48	\$53	(\$5)	\$133
Win Excel 5.0	Dec-93	Oct-93	\$315	\$298	\$17	\$661
Mac Excel 5.0 (and Mac Office 4.1**)	May-94	Nov-93	\$45	\$47	(\$2)	\$116
Win Project 4.0	Mar-94	Jan-94	\$42	\$38	\$4	\$95
Mac Project 4.0	Sep-94	Apr-94	\$5	\$5	\$0	\$12
Win PowerPoint 4.0 (and Win Office 4.2)	Feb-94	Jan-94	\$71	\$56	\$15	\$126
Mac PowerPoint 4.0	May-94	Feb-94	\$11	\$9	\$2	\$23

* Total all versions sold in FY94. Includes MS Office allocation.

** There will be no Mac Office 4.1 as planned. The current version will ship until version 4.2 is released in June.

- Win Office 4.0 began shipping in November 1993 with Win Word 6.0, Win Excel 4.0 and Win PowerPoint 3.0. The Win Office 4.0 box included coupons which entitle the purchaser to free upgrades of Excel 5.0 and PowerPoint 4.0. English language version users who sent in coupons are now being shipped Excel 5.0 (most localized versions will follow within 30 to 60 days). Win PowerPoint 4.0 free upgrades will be sent out when the new version ships in February. Win Office 4.2 will then be launched with the current versions of all three products (including the Win Word 6.0a maintenance release).
- The Q94-2 Win Excel revenue budget assumed a spike associated with the expected shipment of version 5.0 in October. Since Win Excel 5.0 did not RTM until December, revenues were \$45.5 million below plan for quarter, and \$34.7 million below plan year-to-date. Strong sales of Win Office helped support Win Excel revenue, and resulted in above plan revenue for the year-to-date as shown above. Win Office also helped Win PowerPoint exceed the year-to-date revenue plan.
- Mac Word and Mac Excel are showing revenue shortfalls year-to-date, not due to product launch delays, but to generally weak sales in international markets. Mac revenue was above plan in the North American channel.

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Desktop Applications Key Business Issue: Pricing

- The two primary factors influencing Desktop Applications Division (DAD) revenue was: 1) number of product licenses sold, and 2) revenue per license. The goal is to find the price points which maximize total revenue; prices which allow Microsoft to maintain and increase market share while sustaining profitability. With DAD revenue representing 45% of Microsoft's gross year-to-date revenue, the pricing of DAD products is one of the most critical drivers of overall corporate revenue and profits.
- Over 55% of DAD revenue was derived from international sales. These sales, particularly in Europe, have historically provided very favorable gross margins, and hence profits. During the last year there has been a rationalization of European pricing due to market and governmental pressures. A lowering of local currency pricing, combined with a strengthening dollar has negatively impacted Microsoft's profitability on international products.

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Product Group Reporting

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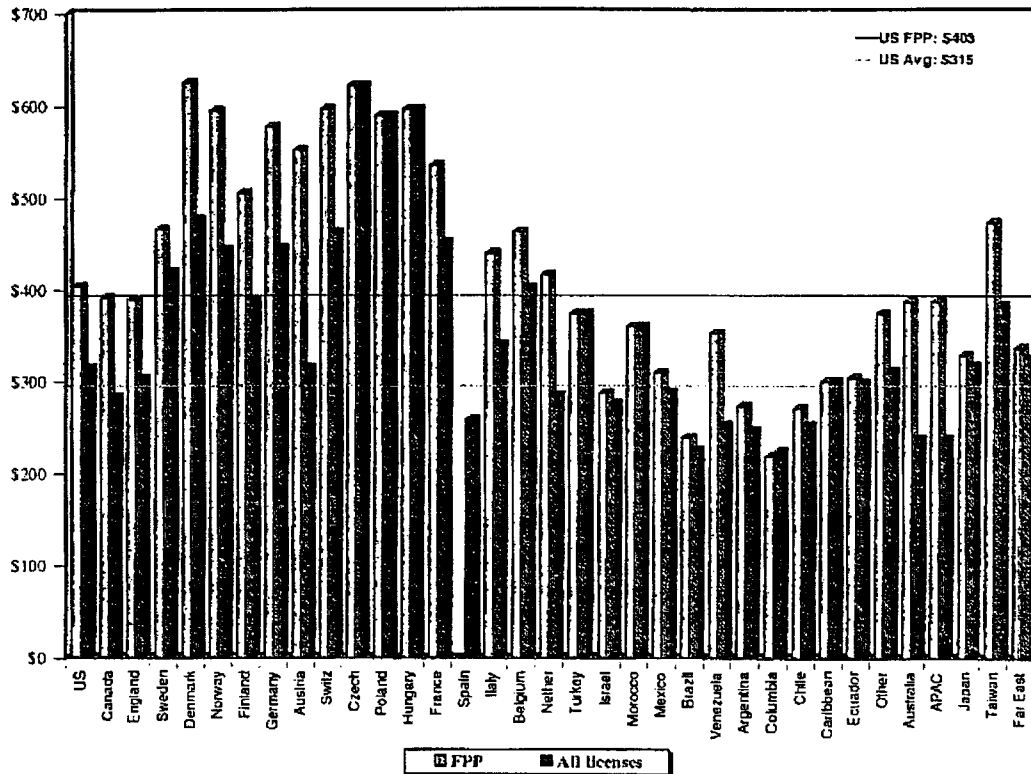
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DESKTOP APPLICATIONS SUMMARY

Win Office - Revenue per "new user" License

Localized Versions - Finished Goods channels - December '93 YTD



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- Many factors influence these figures; product mix (full packaged product versus license) and fluctuating foreign exchange rates among others. Furthermore, "street prices" vary from these prices depending on the location. Market sales channels vary tremendously in their efficiency (markup). The table above includes only one product (Win Office), localized versions only, during one period of time. Also, version upgrades, which are becoming a larger part of the Desktop Applications business are not included. The volume and complexity of data has presented challenges in evaluating these prices worldwide, much less establishing workable guidelines for review and authorization of pricing. A project has been underway to collect and summarize these prices in order to present them in a way that allows for meaningful comparison and evaluation worldwide. The data above is a partial result of that effort.
- The next step is to establish means for rational management of pricing so as to assure optimization of pricing not only in each market, but also *between* markets (gray market and cannibalization transcend country boundaries). This must be done in the context of allowing the subsidiaries to respond to competitive threats and market conditions.

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DESKTOP APPLICATIONS SUMMARY

Results of Operations (in millions)

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Excel PU	\$155.2	74 %	\$28.0	63 %	\$46.1	103 %	\$81.0	67 %
Graphics PU	34.6	96	14.5	170	11.3	97	8.8	56
Project PU	23.0	111	1.6	86	6.6	99	14.8	121
Word PU	275.0	103	41.1	92	50.3	101	183.7	107
	<u>\$487.8</u>	<u>92</u>	<u>\$85.2</u>	<u>86</u>	<u>\$114.3</u>	<u>101</u>	<u>\$288.3</u>	<u>90</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Excel PU	32 %	39 %	18 %	21 %	30 %	21 %	52 %	57 %
Graphics PU	7	7	42	24	33	32	25	44
Project PU	5	4	7	9	29	32	65	59
Word PU	56	50	15	17	18	19	67	64
	<u>100 %</u>	<u>100 %</u>	<u>17</u>	<u>19</u>	<u>23</u>	<u>21</u>	<u>59</u>	<u>60</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Excel PU	\$307.5	91 %	\$51.6	77 %	\$81.2	96 %	\$174.7	94 %
Graphics PU	65.9	104	19.3	147	19.3	86	27.3	99
Project PU	45.3	109	3.3	98	11.6	92	30.3	118
Word PU	450.0	107	69.5	96	87.9	93	292.5	115
	<u>\$868.7</u>	<u>101</u>	<u>\$143.8</u>	<u>92</u>	<u>\$200.0</u>	<u>93</u>	<u>\$524.8</u>	<u>107</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Excel PU	35 %	39 %	17 %	20 %	26 %	25 %	57 %	55 %
Graphics PU	8	7	29	21	29	36	41	44
Project PU	5	5	7	8	26	30	67	62
Word PU	52	49	15	17	20	22	65	60
	<u>100 %</u>	<u>100 %</u>	<u>17</u>	<u>18</u>	<u>23</u>	<u>25</u>	<u>60</u>	<u>57</u>

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DESKTOP APPLICATIONS SUMMARY

Results of Operations (in millions)

Q94-2

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$487.8	\$532.5	(\$44.7)	\$868.7	\$862.3	\$6.3
Cost of revenue	85.2	99.6	14.4	143.8	155.8	12.0
Gross profit	402.6	432.9	(30.3)	724.9	706.5	18.4
People expenses	16.6	17.4	0.8	33.5	35.2	1.8
Facilities expenses	3.6	4.1	0.5	7.2	8.1	0.9
Marketing expenses	58.9	50.9	(7.9)	94.4	91.8	(2.6)
Product development	5.4	5.9	0.6	8.9	11.8	3.0
PSS	21.0	25.2	4.2	40.5	49.3	8.8
Other expenses	4.5	5.5	1.0	7.3	9.1	1.7
Net shared resources	4.4	4.3	(0.1)	8.2	8.8	0.7
Controllable expenses	114.3	113.3	(1.0)	200.0	214.2	14.2
Responsibility margin	\$288.3	\$319.7	(\$31.3)	\$524.8	\$492.3	\$32.5
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	17.5	18.7	1.2	16.6	18.1	1.5
Controllable expenses	23.4	21.3	(2.2)	23.0	24.8	1.8
Responsibility margin	59.1 %	60.0 %	(0.9) %	60.4 %	57.1 %	3.3 %

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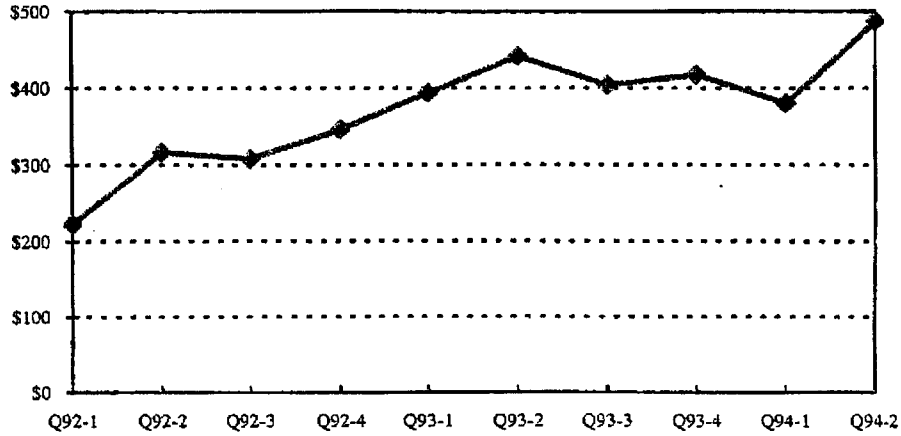
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TREND ANALYSES

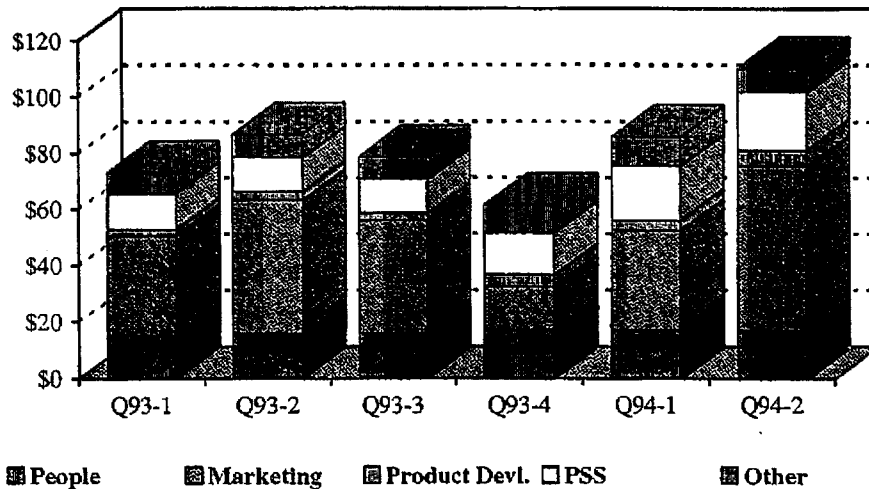
Net Revenue (in millions)



FY92 is stated as reported in FY92 and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

- The revenue trend for Desktop Applications showed a peak in Q93-2, when seasonal sales were strong, and Microsoft was enjoying favorable foreign exchange rates with countries in which our larger subsidiaries do business. Revenue dipped in Q94-1 as planned. Q94-2 revenue reached record levels and exceeded plan due to the shipment of Win Word 6.0 and Win Office 4.0. The expected shipment of Win Excel 5.0, Win PowerPoint 4.0 and Win Project 4.0 in Q94-3 should help DAD achieve the \$524 million plan set for next quarter.

Controllable Expenses (in millions)



* Comments on controllable expenses are addressed in the individual product sections.

FY92 is stated as reported in FY92 and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

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OFFICE

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Highlights

- A reorganization within Desktop Applications resulted in the formation of the Office Business Unit, effective December 1, 1993. Chris Peters was promoted to Vice President and named Office Business Unit manager. The objectives of the new organization include more consolidation of shared code development and further integration of desktop productivity applications. Management profit and loss statements will reflect the new organization in FY95.
- The Office 4.0 launch in New York City on October 19th was very successful, reaching an audience of over 50,000 people. Sales of the new product are breaking all records. Win Office 4.0 shipped with the new Win Word 6.0, and version 4.0 of Excel and 3.0 of PowerPoint. Win Office version 4.2 will ship in late February with the new Win Excel 5.0 and Win PowerPoint 4.0.
- The SRP for MS Office is \$750; MS OfficePro 4.0, \$899. Competitive upgrades of MS Office carry an SRP of \$299, while the SRP for upgrades from Microsoft products is \$259 with a \$40 rebate coupon. In addition, purchasers of MS Office upgrades qualify to trade up to OfficePro with MS Access for \$99. (They pay \$129 for the trade-up and receive a \$30 rebate.)
- Win Office 4.0 topped Lotus SmartSuite in a review in the February 1994 issue of PC/Computing. Favorable reviews were also published by PC Magazine (1/25/94 issue) and InfoWorld (1/10/94 issue).
- The Software Publishers' Association (SPA) began tracking integrated application suites as a distinct market category in May of 1993. The most recent three months of SPA data provide the following market share information for MS Office in North America (three month trailing average):

	Jul.	Aug.	Sep.
Units	77%	83%	76%
Revenue	76%	81%	76%

- Win Office license sales represented 77% of Office application (Word, Excel and PowerPoint) sales in Q94-2. This means on average, three out of four licenses for these products were purchased as part of the Microsoft Office. Product management believes that Microsoft can realize more revenue per desktop by selling the Office versus individual applications.

Competition

- Lotus SmartSuite enjoyed relatively strong sales during the last quarter. Microsoft product managers estimate that Lotus has captured 25% of the suite market during the last six months, up from an estimated 14%. A Notes-based version is scheduled to be released in mid-1994. It will add a Notes client and additional Notes-based content to the suite's current collection of Lotus 1-2-3, Ami Pro, Approach and Freelance Graphics. The release of the Notes suite is expected to ship with Approach version 3.0.
- Borland International and WordPerfect Corp. rolled out Borland Office 2.0 at Comdex in November. It is available through resellers as of January 14, 1994. It consists of WordPerfect 6.0 for Windows, Quattro Pro 5.0 for Windows and Paradox 4.5 for Windows. The SRP is \$595 for the full packaged product, competitive upgrades are \$299 and version upgrades are \$249.

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OFFICE

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Win Office *						
North America FG	\$144.9	\$93.6	\$51.3	\$198.0	\$145.7	\$52.3
Europe FG	128.4	89.2	39.2	214.5	155.6	58.9
ICON FG	24.1	18.4	5.7	42.5	33.7	8.8
Far East FG	13.4	7.3	6.1	22.7	14.6	8.1
WW OEM	0.3	0.0	0.3	0.3	0.0	0.3
Total Win Office	\$311.1	\$208.5	\$102.6	\$478.0	\$349.6	\$128.4
Mac Office						
North America FG	\$18.7	\$14.7	\$4.0	\$32.2	\$26.4	\$5.8
Europe FG	6.4	6.3	0.1	11.2	10.1	1.1
ICON FG	1.1	1.5	(0.4)	2.3	2.8	(0.5)
Far East FG	0.0	0.1	(0.1)	0.3	0.2	0.1
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Office	\$26.2	\$22.6	\$3.6	\$46.0	\$39.5	\$6.5

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Win Office *						
North America FG	\$40.9	\$49.8	\$59.7	\$73.9	\$53.1	\$144.9
Europe FG	26.8	60.0	74.1	74.9	86.1	128.4
ICON FG	7.4	10.8	10.4	15.6	18.4	24.1
Far East FG	0.5	0.7	0.5	2.2	9.3	13.4
WW OEM	0.1	0.0	0.0	0.0	0.1	0.3
Total Win Office	\$75.7	\$121.3	\$144.7	\$166.6	\$167.0	\$311.1
Mac Office						
North America FG	\$11.3	\$15.0	\$12.1	\$18.8	\$13.4	\$18.7
Europe FG	1.1	2.9	3.4	4.8	4.8	6.4
ICON FG	1.4	0.6	0.9	0.8	1.2	1.1
Far East FG	0.1	0.0	0.1	0.1	0.2	0.1
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Office	\$13.9	\$18.5	\$16.5	\$24.5	\$19.6	\$26.3

* Win Office includes MS Office and MS OfficePro.

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EXCEL

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Highlights

- Excel 5.0 for Windows released to manufacturing on December 17, 1993. As of December 31, 1993 approximately 24,000 free upgrade units of Excel 5.0 has been shipped to customers who had purchased Win Office 4.0. A record 339,000 units were also on backorder as of year end.
- Mac Excel 5.0 is not scheduled to be released until May of 1994. Nevertheless, Mac Excel 4.0 dominates the 1993 Macintosh spreadsheet category, and has "no viable contender in sight" according to an October 25 MacWEEK article. Lotus 1-2-3 for the Macintosh has a 6.5% market share while Claris Resolve has 3.3%, according to International Data Corp.
- The Mac Excel 5.0 will include two extra disks which will allow it to run on the Power PC. Licenses of Mac Excel sold after March 1, 1994 will include a "technology guarantee" which will allow users to upgrade to Version 5.0 when it ships.
- According to Dataquest's preliminary estimates for software revenue in calendar 1993, Microsoft Excel 5.0 for Windows is the best selling spreadsheet worldwide independent of the office suites.
- Excel 5.0 for Windows was awarded the highest overall score of 8.7 out of 10 by Software Digest in its December 1993 issue reviewing spreadsheet programs. Version 5.0 also scored highest in both summary categories of Overall Usability and Overall Power.
- Excel 5.0 for Windows was recently named the Editors Pick by Windows Source magazine, and was awarded BYTE magazine's Award for Excellence for 1993.
- French, German, Swedish and Italian Win Excel 5.0 will be released within 30-days of the English language version.

Competition

- Lotus announced Lotus 1-2-3 Release 4 for Windows Multimedia Edition on CD-ROM. It links 1-2-3 Release 4 for Windows with integrated multimedia learning and communication tools. This product is expected to ship first quarter of 1994 at a SRP of \$495. Upgrade from other releases of 1-2-3 or for competitive spreadsheets will be available at \$129.
- In December 1993 Lotus announced a toll-free line and a CompuServe Forum to receive suggestions from customers regarding enhancements to its products.
- Borland claims that the \$49.95 upgrade price offered for Quattro Pro 5.0 for Windows helped them achieve their 500,000 unit goal ahead of schedule. Excel product management estimates that 325,000 of those units were sold in the US.
- On January 6, 1994, after the quarter closed, PC Magazine named Quattro Pro 5.0 for Windows Workgroup Edition - Editor's Choice.

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EXCEL

Results of Operations (In millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$155.2	\$209.7	(\$54.5)	\$307.5	\$336.8	(\$29.4)
Cost of revenue	28.0	44.4	16.4	51.6	66.9	15.3
Gross profit	127.1	165.3	(38.1)	255.9	269.9	(14.0)
People expenses	3.9	4.1	0.2	8.1	8.5	0.4
Facilities expenses	0.8	0.9	0.1	1.7	1.8	0.2
Marketing expenses	25.3	21.3	(4.0)	41.3	38.3	(3.0)
Product development	1.3	1.0	(0.3)	2.2	2.2	(0.1)
PSS	8.0	9.9	1.9	15.6	19.2	3.7
Other expenses	1.6	2.1	0.5	2.8	3.5	0.7
Net shared resources	5.2	5.7	0.5	9.6	11.1	1.5
Controllable expenses	46.1	45.0	(1.1)	81.2	84.6	3.4
Responsibility margin	\$81.0	\$120.3	(\$39.3)	\$174.7	\$185.4	(\$10.6)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	18.1	21.2	3.1	16.8	19.9	3.1
Controllable expenses	29.7	21.5	(8.3)	26.4	25.1	(1.3)
Responsibility margin	52.2 %	57.4 %	(5.2) %	56.8 %	55.0 %	1.8 %

- Excel Business Unit net revenues for Q94-2 were below plan due to the slip of Win Excel 5.0, which caused the \$43 million revenue deferral associated with the Office free upgrade program (see above). Gross revenues were only \$8 million below plan. Strong Win Office sales helped carry Excel revenues, but finished goods channels had budgeted significant version upgrade revenue in the quarter which will not be recognized until Q94-3.
- Win Office sales comprised 73% of the new license sales of Win Excel in Q94-2.
- Product cost of goods as a percent of net revenues were significantly below plan at 12.1%, but above last year's 9.2%. The budget was high this quarter assuming that many free upgrade units would be shipped during the quarter. A \$1 million COGS deferral was booked to help recognize this.
- Operating expenses for Excel were above plan for the quarter due mainly to higher product marketing expenditures. Year to date expenses were below plan due, in part to lower than planned product support costs.
- The negative responsibility margin variance in Q94-2 was due primarily to a revenue shortfall relating to the slip of Win Excel 5.0.

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Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Win Excel *						
North America FG	\$13.5	\$38.9	(\$25.4)	\$37.1	\$48.8	(\$11.7)
Europe FG	31.4	45.9	(14.5)	59.2	77.1	(17.9)
ICON FG	2.4	8.6	(6.2)	6.5	13.2	(6.7)
Far East FG	5.9	6.0	(0.1)	12.4	10.4	2.0
WW OEM	4.4	3.6	0.8	6.7	7.2	(0.5)
Total Win Excel	<u>\$57.5</u>	<u>\$103.0</u>	<u>(\$45.4)</u>	<u>\$121.9</u>	<u>\$156.6</u>	<u>(\$34.8)</u>
Mac Excel *						
North America FG	\$5.7	\$7.5	(\$1.8)	\$14.2	\$12.2	\$2.0
Europe FG	2.7	6.0	(3.3)	5.4	10.0	(4.6)
ICON FG	0.3	1.7	(1.4)	1.0	2.6	(1.6)
Far East FG	2.3	1.7	0.6	5.4	5.4	(0.0)
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Excel	<u>\$11.1</u>	<u>\$16.9</u>	<u>\$0.6</u>	<u>\$26.0</u>	<u>\$30.1</u>	<u>(\$4.1)</u>

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Win Excel *						
North America FG	\$26.7	\$25.5	\$24.6	\$31.0	\$23.0	\$13.5
Europe FG	59.4	64.9	50.4	33.0	27.4	31.4
ICON FG	7.2	5.4	4.5	5.6	4.2	2.4
Far East FG	2.9	9.8	10.1	7.0	6.5	5.9
WW OEM	0.9	1.8	2.8	5.3	2.3	4.4
Total Win Excel	<u>\$97.1</u>	<u>\$107.6</u>	<u>\$92.4</u>	<u>\$81.9</u>	<u>\$63.4</u>	<u>\$57.5</u>
Mac Excel *						
North America FG	\$17.4	\$8.7	\$5.4	\$7.5	\$7.5	\$5.7
Europe FG	7.5	8.6	4.9	3.4	2.7	2.7
ICON FG	1.3	0.9	0.7	0.7	0.6	0.3
Far East FG	1.6	4.1	4.6	3.5	3.0	2.3
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Excel	<u>\$27.8</u>	<u>\$22.3</u>	<u>\$15.6</u>	<u>\$15.1</u>	<u>\$13.9</u>	<u>\$11.1</u>

* Excel does not include MS Office revenue allocation.

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WORD

WORD

Highlights

- Word 6.0 for Windows shipped in October 1993. A free maintenance release, Word 6.0a for Windows, will be available to registered users of Word 6.0 in February. The latest RTM estimate for Mac Word 6.0 is May 1994; an NT (Intel) version is also scheduled for May.
- With the departure of Chris Peters to the Office Business unit, Peter Pathe was promoted to General Manager of the Word Business Unit. Peter was formerly the Director of the Windows Accessories Group, responsible for the True Type Fonts in Windows, the True Type Font Packs, Word Assistant and Microsoft Scenes. Peter has been with Microsoft since 1991.
- In conjunction with the Chicago Legal Tech industry trade show, Microsoft announced that 12 major law firms are making the move to Microsoft Word 6.0 for Windows including: Chadbourne & Parke of New York, Tory DesLauriers & Binnington of Canada and Mallesons Stephens Jacques of Australia.
- This year's Comdex Awards included: Data Based Advisor, Reader's Choice Award, Word for Windows 2.0; COMPUTE Choice award, Word Processor, Word 6.0 for Windows.
- On November 1, 1993, Microsoft announced the Developer's Kit for Word 6.0 for Windows. This kit describes how to use WordBasic to customize the Word interface, automate routine tasks and integrate Word with other applications.

Competition

- Lotus Development's Ami Pro 3.0 for OS/2 was released in December 1993. The product is similar to the Windows version, but without the drawing and charting modules and OLE. It does take advantage of some OS/2 features, but suffers from slow performance according to PC Week.
- WordPerfect 6.0 for Windows Shipped in October 1993. It won PC/Computing's 1993 MVP award for word processing beating Word 6.0 for Windows. This new version occupies 33MB with full installation, 21MB more than version 5.2 according to BYTE magazine. It includes templates and a drawing module from WordPerfect Presentations. WordPerfect plans a maintenance release to fix bugs.
- WordPerfect 6.0 for DOS shipped in June 1993. It has sold two million copies in six months. It includes fax and sound support and has spreadsheet capability in tables.
- WordPerfect 3.0 for the Macintosh is now available. It supports System 7 Pro. The introductory upgrade price of \$59.95 will be extended to March 15, 1994.
- WordPerfect Corporation, in October 1993 filed a complaint in US Federal Court in New York against Microsoft for "most popular" claim for Microsoft Word. Microsoft and WordPerfect settled the matter, Microsoft agreeing to use the term "best selling" rather than "most popular".

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Word

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$275.0	\$266.3	\$8.7	\$450.0	\$420.8	\$29.1
Cost of revenue	41.1	44.8	3.7	69.5	72.4	2.8
Gross profit	234.0	221.5	12.5	380.4	348.4	32.0
People expenses	4.4	4.4	0.1	8.9	9.2	0.3
Facilities expenses	0.9	1.0	0.1	1.8	2.0	0.2
Marketing expenses	25.9	22.6	(3.3)	41.3	40.7	(0.6)
Product development	0.7	0.5	(0.2)	1.5	1.4	(0.2)
PSS	10.6	12.7	2.0	20.6	24.9	4.4
Other expenses	2.2	2.7	0.5	3.4	4.4	0.9
Net shared resources	5.6	6.1	0.5	10.4	12.0	1.6
Controllable expenses	50.3	50.0	(0.3)	87.9	94.6	6.6
Responsibility margin	\$183.7	\$171.4	\$12.2	\$292.5	\$253.9	\$38.6
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	14.9	16.8	1.9	15.5	17.2	1.7
Controllable expenses	18.3	18.8	0.5	19.5	22.5	2.9
Responsibility margin	66.8 %	64.4 %	2.4 %	65.0 %	60.3 %	4.7 %

- Word Business Unit Q94-2 financial performance was above plan in virtually all areas. Revenue was above plan due to very strong sales of Win Office 4.0, particularly in North America and Europe. COGS as a percent of gross revenue was below plan in all channels. Operating expenses were very close to plan in spite of higher than planned marketing expenditures.
- The contribution margin for Q94-2 was 2 percentage points above plan at 44% of net revenue. This was somewhat below Q93-2's 50% margin. The difference was due primarily to higher marketing expenditures associated with the launch of Win Word 6.0 and Office 4.0. Gross margins were virtually unchanged at 85% and most operating expenses were flat from year to year.
- Year-to-date performance was also above plan. Exceptions include marketing and international product support (PSS) costs. International PSS costs were overstated this year due to an allocation rule problem which will be resolved next quarter, lowering year to date costs by an expected \$5 million.

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WORD

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Win Word *						
North America FG	\$54.4	\$65.4	(\$11.0)	\$75.3	\$76.8	(\$1.5)
Europe FG	53.5	59.2	(5.7)	85.6	93.0	(7.4)
ICON FG	7.4	9.0	(1.6)	13.9	13.8	0.1
Far East FG	3.9	3.7	0.2	13.5	13.0	0.5
WW OEM	5.4	5.8	(0.4)	7.9	11.5	(3.6)
Total Win Word	<u>\$124.6</u>	<u>\$143.1</u>	<u>(\$18.5)</u>	<u>\$196.2</u>	<u>\$208.1</u>	<u>(\$11.9)</u>
Mac Word *						
North America FG	\$7.7	\$11.5	(\$3.8)	\$18.9	\$21.4	(\$2.5)
Europe FG	3.6	7.0	(3.4)	7.3	11.6	(4.3)
ICON FG	0.4	1.9	(1.5)	1.2	2.9	(1.7)
Far East FG	0.5	0.1	0.4	1.1	0.3	0.8
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Word	<u>\$12.2</u>	<u>\$20.5</u>	<u>(\$8.3)</u>	<u>\$28.5</u>	<u>\$36.2</u>	<u>(\$7.7)</u>

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Win Word *						
North America FG	\$32.1	\$37.7	\$16.9	\$27.1	\$21.5	\$54.4
Europe FG	60.3	67.3	52.2	38.3	32.0	53.5
ICON FG	7.6	4.8	4.1	5.8	6.7	7.4
Far East FG	1.5	4.7	5.4	5.3	9.6	3.9
WW OEM	0.9	1.8	2.8	6.1	2.6	5.4
Total Win Word	<u>\$102.4</u>	<u>\$116.3</u>	<u>\$81.4</u>	<u>\$82.6</u>	<u>\$72.4</u>	<u>\$124.6</u>
Mac Word *						
North America FG	\$15.2	\$17.9	\$7.0	\$11.0	\$10.1	\$7.7
Europe FG	7.8	7.7	7.0	4.5	3.7	3.6
ICON FG	1.4	0.7	0.9	1.3	0.9	0.4
Far East FG	0.4	0.2	0.8	0.4	0.6	0.5
WW OEM	0.0	0.0	0.1	0.0	0.0	0.0
Total Mac Word	<u>\$24.8</u>	<u>\$26.5</u>	<u>\$15.8</u>	<u>\$17.2</u>	<u>\$15.3</u>	<u>\$12.2</u>

* Word does not include MS Office revenue allocation.

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GRAPHICS

GRAPHICS

Highlights

- The Win PowerPoint 4.0 RTM has been pushed back to mid-February. This new version improves integration and consistency with Excel 5.0 and Word 6.0. Version 4.0 also strives for greater ease of use by automating some of the repetitive work in formatting a presentation.
- Initial feedback in trade publication reviews for Win PowerPoint 4.0 was very encouraging.
- Graphics Business Unit management believes that Win PowerPoint 4.0 will match Freelance in many features, but there are rumors that Lotus may introduce an updated version of Freelance for Windows after PowerPoint ships. There have been indications that Lotus is abandoning their Macintosh applications business.
- In mid-October, PowerPoint launched its first-ever beta program to approximately 2,000 sites including Johnson & Johnson, Kraft Foods, Eli Lilly, Motorola, Arthur Andersen, Exxon, Ford Motor Company and Monsanto. The beta sites were predominately Win Office users and used PowerPoint 4.0 in conjunction with Win Word 6.0 and a beta version of Excel 5.0. Positive feedback from the Win PowerPoint beta sites has included the improved ease of use, customizable toolbars and better integration with Word and Excel. Also praised have been new features such as the auto content wizard, auto layouts and better clip art delivery. On the down side, there have been complaints about performance & speed, larger file sizes, lack of support for Visual Basic for Applications and the lack of multimedia features.
- The release date of the Macintosh version of PowerPoint 4.0 has been pushed back to May, 1994. The schedule has been impacted by projects and development outside of the GBU, such as Graph and OLE.
- The GBU's lease at the Quadras business park in Menlo Park, California is currently being negotiated (lease expires in November 1994). Several other sites are also under consideration.

Competition

- WordPerfect Presentations 2.0 for Windows was released in July 1993. It marked WordPerfect's first entry into the Windows presentation graphics market. This product is recognized for high-end drawing, charting and paint tools. It is the first product to support the TWAIN interface, allowing users to scan images directly into the product.
- Freelance Graphics for Windows Release 2.0 was selected as PC WORLD readers' top choice in the presentation graphics category. Freelance Graphics is noted for its ease of use, support of Lotus Notes and its integration with Lotus' suite for Windows.

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GRAPHICS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$34.6	\$35.9	(\$1.3)	\$65.9	\$63.1	\$2.8
Cost of revenue	14.5	8.6	(6.0)	19.3	13.1	(6.2)
Gross profit	20.1	27.3	(7.3)	46.6	50.0	(3.4)
People expenses	1.7	2.1	0.4	3.5	4.3	0.8
Facilities expenses	0.7	0.7	0.0	1.3	1.4	0.1
Marketing expenses	5.5	4.5	(1.0)	8.4	8.6	0.1
Product development	0.9	1.0	0.0	1.4	2.0	0.6
PSS	1.1	1.7	0.6	2.2	3.3	1.1
Other expenses	0.4	0.4	0.0	0.7	0.7	0.1
Net shared resources	1.0	1.2	0.2	1.9	2.3	0.4
Controllable expenses	11.3	11.6	0.4	19.3	22.5	3.1
Responsibility margin	\$8.8	\$15.7	(\$6.9)	\$27.3	\$27.5	(\$0.2)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	42.0	23.8	(18.1)	29.3	20.8	(8.5)
Controllable expenses	32.5	32.4	(0.2)	29.3	35.6	6.3
Responsibility margin	25.5 %	43.8 %	(18.3) %	41.4 %	43.6 %	(2.2) %

- Graphics Business Unit net revenue was just slightly below plan despite a \$12.6 million revenue deferral associated with the Office free upgrade program. Gross revenue was actually \$12.0 million above plan largely due to strong Win Office sales.
- A \$9.2 million cost of revenue accrual was booked to account for the Office free upgrade program. The accrual will reverse as units are shipped next quarter. Cost of revenue as a percent of gross revenues was significantly below plan due to a mix weighted towards Office units. Win Office sales comprised 91% of the new license sales of Win PowerPoint in Q94-2.
- Operating expenses for the GBU are generally below plan for the quarter and year-to-date, but above last year's levels due mainly to higher product marketing expenditures.
- The negative responsibility margin variance in Q94-2 was due entirely to the accounting adjustment, for the Office free upgrades program and will reverse over the next two quarters.

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GRAPHICS

Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Win PowerPoint *						
North America FG	\$4.1	\$3.3	\$0.8	\$8.3	\$7.0	\$1.3
Europe FG	1.7	2.6	(1.1)	3.2	4.8	(1.6)
ICON FG	0.3	0.7	(0.4)	0.9	1.3	(0.4)
Far East FG	0.3	0.4	(0.1)	0.5	0.8	(0.3)
WW OEM	0.9	0.7	0.2	1.9	1.3	0.6
Total Win PowerPoint	\$7.3	\$7.7	(\$0.4)	\$14.8	\$15.2	(\$0.4)
Mac PowerPoint *						
North America FG	\$2.0	\$1.7	\$0.3	\$4.1	\$3.5	\$0.6
Europe FG	0.3	0.4	(0.1)	0.8	0.7	0.1
ICON FG	0.0	0.1	(0.1)	0.2	0.2	0.0
Far East FG	0.0	0.0	0.0	0.1	0.0	0.1
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac PowerPoint	\$2.3	\$2.2	\$0.1	\$5.2	\$4.4	\$0.8

(Refer to Channel Section for discussion of revenue variances.)

Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Win PowerPoint *						
North America FG	\$7.6	\$4.3	\$4.3	\$5.3	\$4.1	\$4.1
Europe FG	3.3	3.7	2.5	1.9	1.6	1.7
ICON FG	0.9	0.6	0.4	0.6	0.6	0.3
Far East FG	0.2	0.2	0.1	0.2	0.2	0.3
WW OEM	0.5	0.8	1.2	2.6	1.1	0.9
Total Win PowerPoint	\$12.5	\$9.6	\$8.5	\$10.6	\$7.5	\$7.3
Mac PowerPoint *						
North America FG	\$1.0	\$3.9	\$2.8	\$2.3	\$2.2	\$2.0
Europe FG	0.2	0.3	0.5	0.4	0.5	0.3
ICON FG	0.0	0.1	0.1	0.2	0.1	0.0
Far East FG	0.0	0.0	0.0	0.1	0.0	0.0
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac PowerPoint	\$1.2	\$4.3	\$3.4	\$3.0	\$2.8	\$2.3

* PowerPoint does not include MS Office revenue allocation.

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PROJECT

PROJECT

Highlights

- Work continues on Win Project 4.0. Release to manufacturing (RTM) has slid from January to March, 1994. One of the biggest challenges has been integrating Visual Basic for Applications integration. Latest RTM estimate for Mac Project is September, 1994. There are no plans to release a new versions of DOS Project.
- Project product management just completed a long lead press tour to mainstream trade magazines and project management "pundits". The press appears to be showing more interest in project management software in general. The messages of intellisense, workgroup and programmability are being used to help the press see MS Project as a planning tool for a broader market.
- Research is showing that the profile of current Project purchasers has changed over the last 2 years. There are now more users who have never used a product management software package before. Users are now more likely to be in larger companies, and over 80% of them are considered influential end users (IEUs).
- The Project Business Unit's new product, Resource Planning Manager (RPM) completed its Phase 1 development at year end. The first product will be released no earlier than Spring of 1995. There will be 8 developers working on Phase 2.
- Comdex: Microsoft Project 3.0 for Windows won PC World's World Class Award for project management.

Competition

- The project management category has enjoyed tremendous growth during the last two years. This is believed to be due to the increased power of desktop computers, and the improved ease of use of project management software.
- Sales of Mac Project represent only 10% of Project's revenues, but it is considered key to Microsoft Project's success because it is the only core-code, cross platform solution.

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PROJECT

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$23.0	\$20.7	\$2.3	\$45.3	\$41.6	\$3.7
Cost of revenue	1.6	1.8	0.3	3.3	3.4	0.1
Gross profit	21.4	18.8	2.6	42.0	38.2	3.8
People expenses	1.5	1.5	0.0	3.0	3.1	0.1
Facilities expenses	0.3	0.3	0.1	0.4	0.6	0.2
Marketing expenses	2.1	2.5	0.4	3.4	4.3	0.8
Product development	0.3	0.3	(0.1)	0.4	0.5	0.1
PSS	1.3	0.9	(0.4)	2.1	1.8	(0.4)
Other expenses	0.2	0.2	0.0	0.4	0.5	0.1
Net shared resources	0.9	1.0	0.0	1.7	1.9	0.1
Controllable expenses	6.6	6.6	0.0	11.6	12.6	1.0
Responsibility margin	\$14.8	\$12.2	\$2.6	\$30.3	\$25.6	\$4.7
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	6.9	8.9	2.0	7.4	8.2	0.8
Controllable expenses	28.6	32.0	3.4	25.6	30.2	4.6
Responsibility margin	64.5 %	59.1 %	5.4 %	67.0 %	61.6 %	5.4 %

- Project Business Unit revenue for the quarter were above plan, and up slightly from the previous quarter. The Q94-2 budget was fairly conservative due to the expected launch of Win Project 4.0 in January. North America has been the largest market for Win Project. Q94-2 license sales were ahead of plan, and revenue per unit was also higher than planned, due to a mix favoring the \$695 SRP full packaged product. North America was also, by far, the largest market for Mac Project.
- The \$2.6 million favorable revenue variance dropped directly down to the bottom line. Cost of goods sold as a percent of revenue were very close to plan, as were operating expenses. One area of concern is domestic product support which doubled planned levels for the quarter.
- The Project Business Unit's revenue was budgeted to increase to \$35 million next quarter with the expected shipment of Win Project 4.0. Schedule delays could impact the Business Unit's ability to reach this target.

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PROJECT

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Win Project						
North America FG	\$13.4	\$9.4	\$4.0	\$24.2	\$20.7	\$3.5
Europe FG	6.6	6.7	(0.1)	12.7	12.8	(0.1)
ICON FG	1.3	2.1	(0.8)	3.6	3.5	0.1
Far East FG	0.1	0.2	(0.1)	0.5	0.4	0.1
WW OEM	0.3	0.5	(0.2)	0.7	0.9	(0.2)
Total Win Project	\$21.7	\$18.9	\$2.8	\$41.6	\$38.3	\$3.3
Mac Project						
North America FG	\$2.0	\$2.3	(\$0.3)	\$4.5	\$4.3	\$0.2
Europe FG	0.4	0.4	0.0	0.7	0.7	0.0
ICON FG	0.1	0.1	0.0	0.2	0.1	0.1
Far East FG	0.0	0.0	0.0	0.0	0.0	0.0
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Project	\$2.5	\$2.8	(\$0.3)	\$5.4	\$5.1	\$0.3

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Win Project						
North America FG	\$11.3	\$10.8	\$11.6	\$15.7	\$10.8	\$13.4
Europe FG	9.2	8.7	6.9	6.9	6.2	6.6
ICON FG	1.8	1.3	1.4	2.0	2.3	1.3
Far East FG	0.2	0.2	0.1	0.2	0.3	0.1
WW OEM	0.1	0.4	0.4	0.8	0.3	0.3
Total Win Project	\$22.6	\$21.4	\$20.4	\$25.6	\$19.9	\$21.7
Mac Project						
North America FG	\$2.7	\$2.3	\$1.7	\$2.0	\$2.5	\$2.0
Europe FG	0.3	0.4	0.5	0.4	0.3	0.4
ICON FG	0.1	0.1	0.1	0.1	0.1	0.1
Far East FG	0.0	0.0	0.0	0.0	0.0	0.0
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Mac Project	\$3.1	\$2.8	\$2.3	\$2.5	\$2.9	\$2.5

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DATABASE & DEVELOPMENT TOOLS

DATABASE & DEVELOPMENT TOOLS

Key Product Releases

<u>Business Unit/ Product</u>	<u>RTM Date</u>		<u>Gross revenue in millions *</u>			
			<u>FYTD94</u>			<u>FY94</u>
	<u>Act/ Fcst</u>	<u>Plan</u>	<u>Actual</u>	<u>Plan</u>	<u>Variance</u>	<u>Plan</u>
Access 2.0 (and Office Pro allocatio	Feb-94	Dec-93	\$65	\$63	\$2	\$155
SQL Server NT	Sep-93	Sep-93	8	12	(4)	25
Visual C++ 32-Bit Edition	Aug-93	Aug-93	3	6	(3)	14
Visual C++ /J 1.0	Oct-93	Oct-93	4	0	4	n/a **
Visual C++ 2.0	May-94	Jan-94	0	0	0	2
FoxPro 2.5 Mac	Dec-93	Dec-93	0	0	0	6
Fortran PowerStation NT	Oct-93	Oct-93	0	0	0	2
Delta Version Control System	Aug-93	Aug-93	1	1	0	2

* Total all versions sold in FY94. Includes MS Office allocation (Access).

** Visual C++/Japanese version not broken out (included with regular product for budget purposes).

- Access 2.0, originally scheduled for RTM on December 8, 1993, has slipped to the current projected RTM of February 23, 1994.
- Visual C++ 2.0 was pushed back approximately four months, to May 1994, in order to tie in more closely with the Chicago System release.
- FoxPro version 2.6 is scheduled for release on March 1, 1994.
- SQL Server 4.2.1 has a scheduled RTM of late January 1994 with an announcement to follow in February.

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DATABASE & DEVELOPMENT TOOLS

Highlights

- Products from the Database & Development Tools Division accounted for over 40% of Far East FG revenue during the month of December 1993. Access sales in Far East FG were \$6.6 million in December alone, due to the December release of a Japanese version. To date in FY94, Access sales in this channel previously ranged from \$35,000 to \$125,000 per month.
- Also relating to Far East FG, Visual C++ 1.0J (Japanese version) was released to manufacturing on October 14, 1993.
- FoxPro 2.5 for the Macintosh was released to manufacturing on December 8, 1993. Although it is too early to see any sales results, the reaction from the marketplace has been very positive.
- Visual C++ version 1.5 was released to manufacturing on December 1, 1993.
- Fortran PowerStation NT was released to manufacturing on October 27, 1993.

Competition

- On October 20, 1993 Sybase Inc. announced general availability of its System 10 Core products: SQL Server 10 and Backup Server. SQL Server 10, bundled with the Backup Server is available at prices ranging from \$1,995 to \$256,160 depending on hardware platform and number of users supported. SQL Server 10 is scheduled to be available on Microsoft Windows NT and IBM OS/2 in the first half of 1994.
- Relating to the Sybase/Microsoft relationship, negotiations are under way to complete a new deal which would replace the current agreement.
- Borland shipped dBase Compiler 2.0 for DOS in October 1993, which provides 32 bit operating system support. It has a menu-driven user interface and an introductory price of \$199.95 through January 31, 1994. After that, the SRP will be \$495. Users of dBase Compiler 1.0 can upgrade for \$99.95.
- In Borland's release of quarterly results ended September 30, 1993 it was stated that the 500,000 units of Quattro Pro they had hoped to sell by January 15, 1994 had already been sold. This was the result of Borland's special promotional pricing of Quattro Pro 5.0 for \$49.95. This is relevant to the Database & Development Tools division in that it is indicative of the pricing strategy Borland seems willing to adopt to gain market share.
- Powersoft Corporation announced in November it's plan to acquire Watcom Corp. Watcom's technology, particularly their SQL database engine, and engineering talent will be helpful in allowing Powersoft to expand its product line. Currently, PowerBuilder has been receiving very positive attention as a client/server development product with SQL Server "smarts" built in. In the client/server area, PowerBuilder is positioned as a major competitor to Visual Basic.

Divisional Strategy/Business Issues

- A major theme for the next several years will be speaking to developers with a unified voice. With that in mind, an assessment of Microsoft's marketing to developers was completed and factored into the Database & Development Tools division's three year plan. The three year plan also focuses on the needs of client/server development and making sure our tools family delivers the necessary power to developers.
- A unified database architecture code-named DNA (Data Navigation Architecture) and product plan was defined for Microsoft. Product implementation plans are under way.
- An analysis of the developer customer base and the types of applications/solutions developers want to develop for Windows and Windows NT was completed.
- Plans are in place to increase Microsoft's share of the worldwide xBASE market over the next six months. To do this, with the introduction of FoxPro 2.6 in March, there will be only two SKUs, a Standard version, specially priced at \$99 until June 30, 1994 and a Professional version at a \$695 SRP.

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DATABASE & DEVELOPMENT TOOLS

Results of Operations (in millions)

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Database Mgt (Access)	\$39.7	108 %	\$5.5	93 %	\$16.0	86 %	\$18.2	148 %
Fox	12.2	52	2.4	63	10.6	100	(0.8)	(9)
Apps Programmability	15.2	111	3.1	126	5.2	82	6.9	142
C++	15.0	103	4.4	78	9.0	97	1.6	NM
Scientific and Eng. Tools	2.8	79	0.9	192	2.9	84	(1.1)	NM
	<u>\$84.9</u>	<u>92</u>	<u>\$16.4</u>	<u>90</u>	<u>\$43.7</u>	<u>90</u>	<u>\$24.8</u>	<u>98</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Database Mgt (Access)	47 %	40 %	14 %	16 %	40 %	51 %	46 %	33 %
Fox	14	26	20	16	87	45	(7)	39
Apps Programmability	18	15	20	18	34	46	45	36
C++	18	16	29	38	60	64	11	(3)
Scientific and Eng. Tools	3	4	34	14	106	100	(40)	(14)
	<u>100 %</u>	<u>100 %</u>	<u>19</u>	<u>20</u>	<u>52</u>	<u>53</u>	<u>29</u>	<u>28</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Database Mgt (Access)	\$64.8	99 %	\$12.0	120 %	\$28.6	79 %	\$24.3	126 %
Fox	31.1	58	6.1	74	17.4	85	7.6	31
Apps Programmability	33.8	123	7.8	157	10.0	83	16.0	154
C++	28.3	117	9.5	96	17.7	97	1.1	NM
Scientific and Eng. Tools	6.4	108	1.9	220	5.7	83	(1.3)	NM
	<u>\$164.4</u>	<u>93</u>	<u>\$37.4</u>	<u>109</u>	<u>\$79.4</u>	<u>85</u>	<u>\$47.7</u>	<u>98</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Database Mgt (Access)	39 %	37 %	18 %	15 %	44 %	55 %	37 %	30 %
Fox	19	30	20	15	56	38	25	46
Apps Programmability	21	16	23	18	30	44	47	38
C++	17	14	34	41	63	76	4	(17)
Scientific and Eng. Tools	4	3	30	15	90	116	(20)	(30)
	<u>100 %</u>	<u>100 %</u>	<u>23</u>	<u>19</u>	<u>48</u>	<u>53</u>	<u>29</u>	<u>28</u>

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DATABASE & DEVELOPMENT TOOLS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$84.9	\$92.1	(\$7.2)	\$164.4	\$176.5	(\$12.1)
Cost of revenue	16.4	18.3	1.9	37.4	34.1	(3.2)
Gross profit	68.5	73.8	(5.3)	127.1	142.4	(15.3)
People expenses	16.0	16.0	0.1	31.3	32.1	0.7
Facilities expenses	2.3	3.2	0.9	4.8	6.4	1.5
Marketing expenses	12.9	12.8	(0.1)	18.9	23.0	4.1
Product development	3.3	5.6	2.3	5.8	11.3	5.5
PSS	9.6	10.1	0.5	19.0	20.0	1.0
Other expenses	0.7	0.9	0.2	1.4	1.9	0.4
Net shared resources	(1.2)	(0.3)	0.8	(1.9)	(0.8)	1.0
Controllable expenses	43.7	48.4	4.7	79.4	93.8	14.4
Responsibility margin	\$24.8	\$25.4	(\$0.6)	\$47.7	\$48.6	(\$0.9)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	19.3	19.8	0.6	22.7	19.3	(3.4)
Controllable expenses	51.5	52.6	1.1	48.3	53.1	4.9
Responsibility margin	29.2 %	27.6 %	1.6 %	29.0 %	27.5 %	1.5 %

- Net revenue was 92% of plan in Q94-2. Far East FG was the only channel which exceeded plan, primarily attributable to sales of the Japanese versions of Access (released in December), and Visual C++ 1.0J (released in October). Both the Access and C++ Business Units had sales over \$6.5 million in Far East FG. The offsetting negative revenue variance was virtually all attributable to the Fox Business Unit as sales continued to fall below plan by an average of \$3.7 million per month during Q94-2.
- Product cost of revenue as a percentage of gross revenue was at plan of 14% for the division during Q94-2. Total cost of revenue as a percent of gross revenue was 18% versus 19% plan. Lower than planned manufacturing allocations caused the slight variance from plan. Two factors contributed to the lower cost of revenue when compared to last quarter's 22% of gross revenue. The write-off of the Access promotional product lowered margins in Q94-1, and the distribution of Visual C++ on CD is helping to reduce product COGS for this business unit.
- Controllable expenses approximated plan for the quarter with the exception of product development which was under plan in all business units except C++. Registration fees for the Fox Development Conference offset much of Fox marketing expenses in Q94-1. Additionally, general underspending in Q94-1 resulted in the year-to-date variance.
- Responsibility margin approximated plan due to offsetting variances in revenue and expenses.

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Gross Revenue by Channel Results (in millions)

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	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
North America FG	\$35.0	\$37.2	(\$2.2)	\$68.4	\$85.6	(\$17.2)
Europe FG	30.7	38.2	(7.5)	62.2	66.8	(4.6)
ICON FG	5.9	7.9	(2.0)	12.1	12.6	(0.5)
Far East FG	17.7	11.4	6.3	27.8	16.0	11.8
WW OEM	0.4	0.4	0.0	1.4	0.8	0.6
	\$89.7	\$95.0	(\$5.3)	\$171.9	\$181.8	(\$9.9)

(Refer to Channel Section for discussion of revenue variances.)

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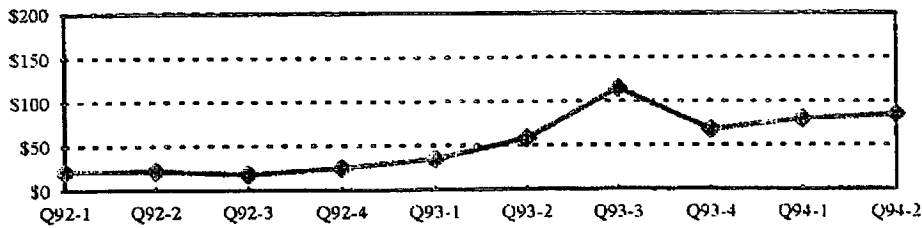
DATABASE & DEVELOPMENT TOOLS

TREND ANALYSES

Gross Revenue by Channel (in millions)

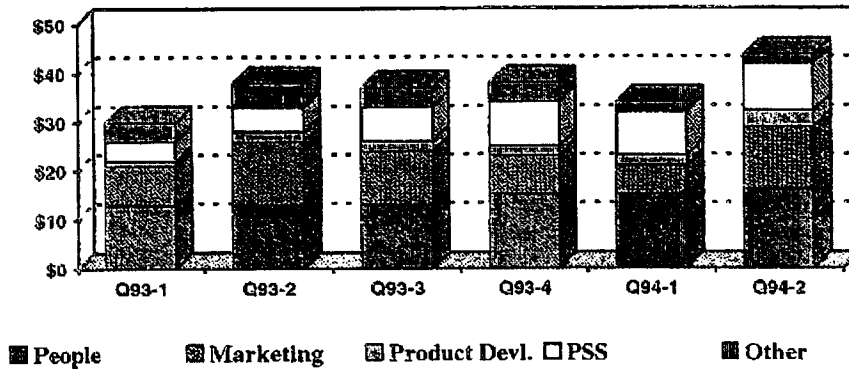
	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
North America FG	\$20.0	\$37.0	\$57.0	\$38.0	\$34.0	\$35.0
Europe FG	9.0	17.0	39.0	20.0	31.0	30.7
ICON FG	2.0	4.0	9.0	5.0	6.0	5.9
Far East FG	3.0	5.0	10.0	9.0	10.0	17.7
WW OEM	1.0	1.0	1.0	1.0	1.0	0.4
	<u>\$35.0</u>	<u>\$64.0</u>	<u>\$116.0</u>	<u>\$73.0</u>	<u>\$82.0</u>	<u>\$89.7</u>

Net Revenue (in millions)



FY92 has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

Controllable Expenses (in millions)



- Marketing expenses in Q93-2 and Q93-3 reflect the launch of Access and continuing promotion of Fox products since the acquisition. Fox marketing expenses in the US were virtually offset by registration fees for the Fox Development Conference, resulting in the relatively low marketing expenditures in Q94-1.
- PSS as a proportion of DDT's overall expenses has grown significantly since the beginning of FY93 due to both the increase in products being offered, and their relatively more technical nature of which the typical desktop user may not be as comfortable with.

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CONSUMER

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Key Product Releases

Business Unit/Product	RTM Date		Gross Revenue in millions *			
			FYTD94		FY94	
	Actual	Plan	Actual	Plan	Variance	Budget
Consumer						
Win Dinosaurs	Jul-93	Jul-93	3.4	0.7	2.7	1.2
Publisher 2.0	Jul-93	Jul-93	19.7	10.8	8.9	19.7
Arcade	Aug-93	Aug-93	3.9	1.2	2.7	2.1
Win Cinemania 1994	Aug-93	Aug-93	2.8	1.0	1.8	1.8
Flight Simulator 5.0	Sep-93	Sep-93	29.2	8.3	20.9	12.8
Win Encarta, 1994	Sep-93	Sep-93	12.3	4.4	7.9	8.2
Win Works 3.0	Oct-93	Oct-93	43.6	30.5	13.1	89.6
Creative Artist	Oct-93	Sep-93	2.7	1.7	1.0	4.0
Mac Encarta, 1994	Feb-94	Nov-93	0.0	0.1	(0.1)	2.5
Fine Artist	Mar-94	Nov-93	0.0	1.7	(1.7)	4.0
Money 3.0	Jan-94	Oct-93	2.7	5.2	(2.5)	10.0
Mac Works 4.0	Mar-94	Feb-94	5.3	4.8	0.5	18.2

Total all versions sold in FY94.

- Win Works 3.0 released to manufacturing on October 30, 1993, at an introductory price of \$89. This was bundled with Money 2.0, and sales for the quarter were strong, particularly in North America. Win Encarta, 1994 reached the channel by the end of October, 1993 at an introductory price of \$99. Revenue for the quarter was almost four times plan, and discussions are being held to move the SRP to \$139 permanently. Similar discussions are being held for MS Publisher and MS Works.
- Creative Writer was released to manufacturing on October 27, 1993, with a large press event in New York which highlighted Microsoft's entry into the children's market as well as the commitment to Home computing. The product was so well received that revenue YTD has surpassed plan, despite being slightly late to market.
- Several additional titles were released this quarter, including: Flight Simulator Paris Scenery, Flight Simulator New York Scenery, Art Gallery (both Win and Mac), Isaac Asimov's Ultimate Robot and Schubert: The Trout Quintet. Many products also released localized versions including: German and French Flight Simulator; French, German and Spanish Publisher; French, French Canadian, German, Australian, Dutch, Danish, Finnish, Norwegian, Italian and Swedish Win Works 3.0.

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Highlights

- The Consumer Division won six awards at the November Comdex show in Las Vegas. These awards included: PC World World Class award, CD-ROM Title for MS Bookshelf; COMPUTE Choice award, Personal Desktop Publishing, for MS Publisher 2.0; PC/Computing MVP, Desktop Publishing, for MS Publisher 2.0; and Home Office Computing's Editors' Pick award, Desktop Publishing, for MS Publisher 2.0.
- The Consumer Division held a press event in New York City on December 7, 1993. The event highlighted Creative Writer and Fine Artist, MS's first two products in the kid's market. Also spotlighted at this event was MS Money 3.0, which was released to manufacturing January 12, 1994. This will be the first home financial product on the market with on-line services for at-home banking.
- Unit sales of Flight Simulator 5.0, which was released to market in September, has nearly eclipsed total unit sales for all previous versions of Flight Simulator. Although this product has been on the market for over ten years, the latest version has so many technical advances, that it is regarded as a virtually new product.

Competition

- Win Works 3.0 was released in a bundle with Money 2.0 with a street price of \$79 (\$69 for upgrades). As a competitive response, Claris Works is offering a \$50 rebate on their Works/Quicken bundle, resulting in an effective street price between \$69 and \$79. MS's domestic market share in the Windows integrated application category climbed back over 70% this quarter. WordPerfect Corp. announced a Windows integrated application that is due to ship in March, 1994 with an SRP of \$149.
- WordPerfect Corp. has formed a new Consumer Products Group which hopes to create, license or acquire a total of approximately 20 products priced between \$29 and \$149. The most immediate threat is in the Kids and integrated application category.
- Comptons' Encyclopedia continues to be bundled on almost 40% of the multi-media PC's offered, while Groliers is bundled on 55%. Groliers is using aggressive pricing strategies, including one contract with Creative Labs at \$2/unit. Microsoft is also pursuing this OEM market and expects to increase share next quarter. Encarta has substantially improved its retail market share since the release of Encarta 1994 in October. Encarta's share of the retail market went from 13% prior to October to over 65% this past quarter.

Divisional Strategy

- There is an explosive growth in home-installed PC's (projected growth of 50% over the next three years) underway, and the Consumer Division is in the process of defining its strategy to penetrate a market relatively new to Microsoft, with the Microsoft Home product line. The Division revenue for the quarter was 78% ahead of the same quarter last year, supporting the assertion that this business is a very fast growing opportunity.

The Division goal is to start calendar 1994 with a simple, straightforward strategy, directing product decisions, investments, technical and marketing decisions. In order to achieve the division goal of 35% compounded annual growth over the next three years, the Consumer Division will be re-organized into six functional categories: Personal Tools, Transactions, Reference/Information, Lifestyle, Entertainment and Kids.

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CONSUMER

Results of Operations (in millions)

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Works PU	\$33.0	93 %	\$4.8	92 %	\$10.2	91 %	\$17.9	96 %
MM Pubs	21.7	237	4.4	203	7.8	76	9.5	NM
Entry PL	43.2	187	13.0	202	13.8	117	16.4	335
	<u>\$97.9</u>	<u>145</u>	<u>\$22.2</u>	<u>160</u>	<u>\$31.9</u>	<u>95</u>	<u>\$43.8</u>	<u>216</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Works PU	34 %	52 %	15 %	15 %	31 %	32 %	54 %	53 %
MM Pubs	22	14	20	24	36	113	44	(36)
Entry PL	44	34	30	28	32	51	38	21
	<u>100 %</u>	<u>100 %</u>	<u>23</u>	<u>21</u>	<u>33</u>	<u>49</u>	<u>45</u>	<u>30</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Works PU	\$60.0	101 %	\$8.4	93 %	\$18.4	85 %	\$33.1	116 %
MM Pubs	27.3	210	5.5	175	14.2	70	7.5	NM
Entry PL	64.9	166	19.0	179	23.1	94	22.9	571
	<u>\$152.2</u>	<u>137</u>	<u>\$32.9</u>	<u>145</u>	<u>\$55.7</u>	<u>84</u>	<u>\$63.6</u>	<u>291</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Works PU	39 %	53 %	14 %	15 %	31 %	37 %	55 %	48 %
MM Pubs	18	12	20	24	52	157	28	(82)
Entry PL	43	35	29	27	36	63	35	10
	<u>100 %</u>	<u>100 %</u>	<u>22</u>	<u>20</u>	<u>37</u>	<u>60</u>	<u>42</u>	<u>20</u>

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CONSUMER

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$97.9	\$67.6	\$30.3	\$152.2	\$111.2	\$41.0
Cost of revenue	22.2	13.9	(8.3)	32.9	22.8	(10.2)
Gross profit	75.7	53.7	22.0	119.3	88.5	30.8
People expenses	10.1	10.3	0.1	20.0	20.4	0.4
Facilities expenses	1.6	2.1	0.5	3.2	4.1	0.9
Marketing expenses	7.4	8.4	1.0	11.2	17.4	6.2
Product development	6.0	7.7	1.7	10.2	15.2	5.0
PSS	2.8	2.9	0.0	5.3	5.5	0.3
Other expenses	2.9	0.8	(2.1)	3.8	1.4	(2.4)
Net shared resources	1.0	1.3	0.3	1.9	2.5	0.6
Controllable expenses	31.9	33.4	1.6	55.7	66.6	10.9
Responsibility margin	\$43.8	\$20.3	\$23.5	\$63.6	\$21.9	\$41.7
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	22.7	20.5	(2.2)	21.6	20.5	(1.2)
Controllable expenses	32.5	49.4	16.9	36.6	59.9	23.3
Responsibility margin	44.8 %	30.0 %	14.7 %	41.8 %	19.6 %	22.1 %

- The Consumer Division had a strong quarter in sales, with North American FG accounting for most of the positive revenue variance, led by strong sales of Flight Simulator and Encarta.
- This quarter, the Multimedia Publishing product unit had a positive responsibility margin against a plan of negative \$3.3M. Year to date the product unit had a positive margin against a plan of negative \$10.6M. This was mainly the result of strong Encarta, Bookshelf and Dinosaur sales.
- Several introductory low prices (Works 3.0, Encarta, 1994, Publisher 2.0) resulted in the number of licenses sold being 55% over plan, while revenue per license was 6% below plan.
- Product development expenses were below plan. Expenses will increase in the next two quarters compared to the budget which was spread evenly over twelve months. Other operating expenses were unfavorable to plan due to a write down of the advanced royalties for Profit, the small business accounting package co-developed with Great Plains Software. Sales of this package were well below plan, and the decision was made to write down the remaining advance royalty.
- Cost of revenues were higher than planned (22.7% versus a plan of 20.5%). This was partially due to higher than planned sales of Flight Simulator and the high royalty associated with this product.

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CONSUMER

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Flight Simulator						
North America FG	\$17.2	\$3.3	\$13.9	\$22.4	\$6.0	\$16.4
Europe FG	4.5	0.9	3.6	5.6	1.3	4.3
ICON FG	0.5	0.2	0.3	0.6	0.4	0.2
Far East FG	0.4	0.5	(0.1)	0.6	0.6	0.0
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
	<u>\$22.6</u>	<u>\$4.9</u>	<u>\$17.7</u>	<u>\$29.2</u>	<u>\$8.3</u>	<u>\$20.9</u>
	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Publisher						
North America FG	\$4.9	\$2.1	\$2.8	\$13.0	\$5.4	\$7.6
Europe FG	3.3	1.6	1.7	4.5	2.8	1.7
ICON FG	0.9	0.3	0.6	1.7	0.8	0.9
Far East FG	0.0	0.0	0.0	0.0	0.0	0.0
WW OEM	0.3	0.9	(0.6)	0.5	1.8	-1.3
	<u>\$9.4</u>	<u>\$4.9</u>	<u>\$4.5</u>	<u>\$19.7</u>	<u>\$10.8</u>	<u>\$8.9</u>
	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Works for Windows						
North America FG	\$8.6	\$6.8	\$1.8	\$12.4	\$11.1	\$1.3
Europe FG	8.2	9.7	(1.5)	13.8	15.6	(1.8)
ICON FG	1.5	2.3	(0.8)	2.9	3.8	(0.9)
Far East FG	0.1	0.0	0.1	0.2	0.0	0.2
WW OEM	7.3	0.0	7.3	14.5	0.0	14.5
	<u>\$25.7</u>	<u>\$18.8</u>	<u>\$6.9</u>	<u>\$43.8</u>	<u>\$30.5</u>	<u>\$13.3</u>

(Refer to Channel Section for discussion of revenue variances.)

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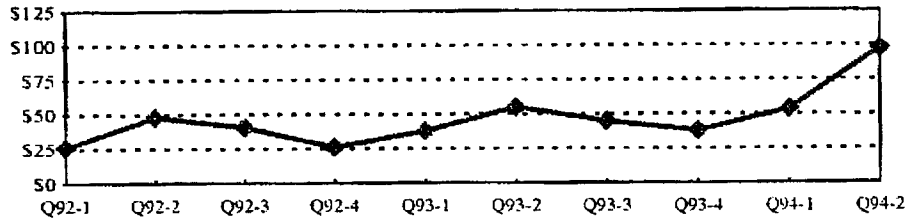
CONSUMER

TREND ANALYSES

Gross Revenue by Channel (in millions)

	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>
PC Flight Simulator						
North America FG	\$0.9	\$1.8	\$1.0	\$0.4	\$5.2	\$17.2
Europe FG	0.3	0.7	0.7	0.3	1.1	4.5
ICON FG	0.1	0.1	0.0	0.0	0.1	0.5
Far East FG	0.0	1.0	0.5	0.3	0.2	0.4
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
	<u>\$1.3</u>	<u>\$3.6</u>	<u>\$2.2</u>	<u>\$1.0</u>	<u>\$6.6</u>	<u>\$22.6</u>
Publisher						
North America FG	\$1.2	\$3.3	\$1.8	\$1.4	\$8.0	\$4.9
Europe FG	0.7	1.1	1.1	0.8	1.3	3.3
ICON FG	0.2	0.3	0.2	0.1	0.8	0.9
Far East FG	0.0	0.0	0.0	0.0	0.0	0.0
WW OEM	0.3	0.5	0.4	0.8	0.2	0.3
	<u>\$2.4</u>	<u>\$5.2</u>	<u>\$3.5</u>	<u>\$3.1</u>	<u>\$10.3</u>	<u>\$9.4</u>
Works for Windows						
North America FG	\$3.7	\$3.9	\$3.9	\$3.9	\$3.8	\$8.6
Europe FG	7.2	10.3	8.9	5.7	5.6	8.2
ICON FG	1.4	1.3	1.1	1.4	1.4	1.5
Far East FG	0.0	0.0	0.0	0.0	0.0	0.1
WW OEM	1.3	3.4	5.4	5.3	7.1	7.3
	<u>\$13.6</u>	<u>\$18.9</u>	<u>\$19.3</u>	<u>\$16.3</u>	<u>\$17.9</u>	<u>\$25.7</u>

Net Revenue (in millions)



FY92 is stated as reported in FY92 and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

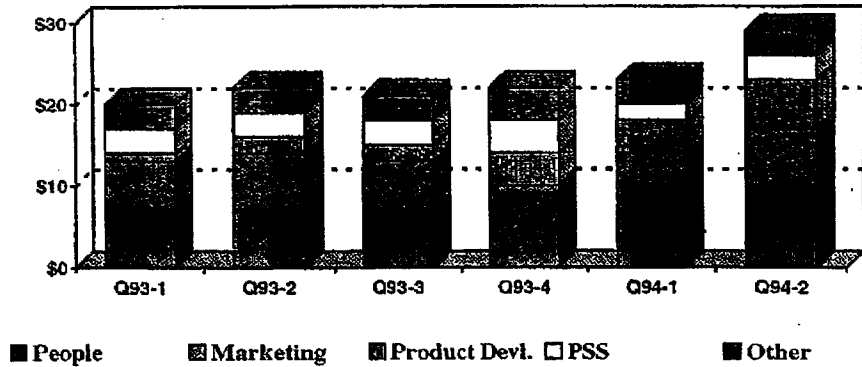
- The Consumer Division had a strong quarter, with net revenue 45% ahead of plan and 80% ahead of last quarter. The Division net revenue was 78% ahead of Q93-2, demonstrating the growth in this division year over year.
- Flight Simulator for DOS was the number one selling product for the Consumer Division this quarter, with Works for Windows, Standard version second. Publisher has exceeded its total FY94 plan. Several other products have also exceeded their FY94 plan, including Encarta, Dinosaurs, Flight Simulator and Arcade.

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CONSUMER

Controllable Expenses (in millions)



- There has been a planned increase in headcount and product development expenses over prior year due to increased production levels, resulting in more titles being shipped at an accelerated pace. As the Consumer Division aggressively develops and ships new products and expands into new markets, marketing expenses will continue to increase. However, these expenses have remained below plan YTD, due to the concentration of key events in December and January (CES, MacWorld, Home launch).

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WORKGROUP

WORKGROUP

Key Product Releases

- Workgroup's major FY94 release is the Enterprise Messaging and Information Server (EMS), which is expected to RTM May 30, 1994. The street date, however, is forecasted as July 1994, so no FY94 revenue impact was budgeted. EMS is expected to be Microsoft's main competitor to Lotus Notes at that time. Current expectations are for EMS to be significantly better than Notes as a messaging platform and to provide bulletin board services and replication at least equal to Notes. The server will be built on Microsoft Windows NT and the client will be built into Chicago.
- Workgroup will also have a new release of the Shared File System (SFS) for smaller users (MS Mail 4.0), with an RTM date late in Q95-1. Schedule+ 2.0, which includes a Mac client, is expected to RTM May 30, 1994, but like EMS will have a Q95-1 street date.

Highlights

- Microsoft shipped version 3.2 of the Microsoft Mail Connection Gateway on November 10, 1993. This upgrade offers several new features, including automated directory synchronization of address lists, full Microsoft Schedule+ meeting request translation, enhanced flexibility & usability and improved network administration. The Mail Connection Gateway enables users to exchange mail, files and address lists between Microsoft Mail for PC Networks and Microsoft Mail for AppleTalk and compatible networks.
- In November, McCaw Cellular Communications Inc.'s Messaging Division introduced MailFlash software, which allows people with alphanumeric pagers to receive electronic mail messages of virtually unlimited length. Initially compatible with Microsoft Mail, MailFlash will be compatible with a variety of other E-Mail systems within the next few months. The SRP for MailFlash is \$79.95.
- On November 22, 1993, Microsoft announced the availability of the beta SDK for MAPI version 1.0, which enables software developers to write messaging and Workgroup applications for the Microsoft Windows and Microsoft Windows NT operating systems, and will be delivered in future versions of these operating systems. The MAPI SDK provides message transport, message store and directory services; no other API currently includes all these key services. More than 80 developers are working to provide a variety of back-end services for MAPI applications. Users will be able to connect to a wide range of services, such as AT&T Easylink, CompuServe, Internet, fax services, LAN-based e-mail (e.g., Microsoft Mail or Novell MHS) and X.400 mail. An additional 70 ISVs have stated their intentions to develop MAPI applications.
- On January 7, 1994, Microsoft and Apple Computer announced the signing of a comprehensive agreement, which focuses on four key areas: access from either platform to the messaging and directory servers provided by either vendor; interpretation between the two vendors' messaging and directory servers; support of Apple Open Collaboration Environment capabilities in principal Macintosh productivity applications from Microsoft, and support for Common Mail Calls on both platforms, resulting in easier cross-platform development for application developers and more choices for end users. Apple and Microsoft will announce specific products, features, capabilities and schedules throughout the course of 1994.
- The January 10, 1994 issue of PC Week reported that testers of the latest version of EMS are bullish about its administration tools, directory services, and the ability to customize and replicate message databases. EMS is being praised as a solid hub for corporate data traffic because of its scalability and tighter integration with existing LAN and host based E-mail systems.
- SPA data for North America indicates that Microsoft's mailbox share rose from 30% in spring of 1993 to over 50% in the fall, due to the launch of Mail 3.2 and Office 4.0 strength. North American revenue share remained flat during this time at approximately 25%. International mailbox share showed a steady climb from 40% to 50% primarily due to the strength of Office, with revenue share remaining flat at 30%. Worldwide, our mailbox share in fall of 1993 is 50% and our revenue share is 27%. Microsoft's worldwide installed base at the end of CY93 approached 4 million, the same as Lotus' recent claim for cc:Mail.

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Competition

- cc:Mail Release 2.0 for Windows scored highest in a comparison of six LAN-based electronic-mail systems (including Microsoft Mail and WordPerfect Office) in the October issue of InfoWorld, was rated the top LAN-based e-mail program in a comparison of LAN-based electronic mail programs in the October issue of Software Digest, and received the 1993 PC World World Class Award in November.
- On November 1, 1993, Wang shipped the first LAN-based E-mail software to integrate both X.400 and X.500 standards in an open client/server environment. This newest version of OPEN/office is able to communicate with cc:Mail, Microsoft Mail, and WordPerfect Office and has a Microsoft Windows-based interface. Licenses are available in 16, 32, 64, 128, 256 & 512 user levels, ranging from \$4,995 to \$46,800.
- Intel Corp. and Da Vinci Systems Corp. in November released the Intel Wireless Modem and Da Vinci Wireless E-mail, respectively. Intel's Wireless Modem comes with software for cc:Mail and Microsoft Mail remote clients and LAN-based servers, along with a client for connecting to the AT&T Mail public mail service. Da Vinci's Wireless E-mail is a wireless version of its remote E-mail client. Both products use RAM Mobile Data Inc.'s Mobidem wireless modem, which transmits data on the RAM Mobile Data packet-radio network.
- On November 22, 1993, IBM announced JustMail/400, a new entry-level, easy-to-use electronic mail system for the AS/400 computer, which provides a simplified subset of the electronic mail, note editing and information filing functions of the widely-used OfficeVision/400, supporting mail exchange between IBM and non-IBM systems, public networks and PC LANs.
- On December 6, 1993, WordPerfect released the WordPerfect Office cc:Mail Gateway, which provides communication between WordPerfect Office 4.0a and cc:Mail. Previously, WordPerfect Office users could only access cc:Mail users via an intermediary protocol such as X.400 or Novell's Message Handling Service (MHS).
- IBM's new FormTalk software will be available for OS/2 in the first quarter of CY94, and on Windows during the second half of 1994. FormTalk, which will cost less than \$150 and be targeted at novice users, comprises designer, filler and routing capabilities.

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WORKGROUP

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$26.1	\$22.9	\$3.2	\$46.1	\$39.9	\$6.2
Cost of revenue	2.6	3.6	0.9	5.3	6.4	1.2
Gross profit	23.4	19.3	4.1	40.8	33.5	7.3
People expenses	7.2	7.7	0.5	14.1	15.9	1.8
Facilities expenses	1.6	1.6	0.0	3.1	3.1	0.0
Marketing expenses	2.8	3.3	0.4	4.6	6.5	1.9
Product development	1.6	1.9	0.3	3.5	4.3	0.8
PSS	1.8	2.0	0.2	3.7	3.9	0.2
Other expenses	0.3	0.3	0.1	0.6	0.6	0.0
Net shared resources	(0.2)	(0.3)	(0.0)	(0.5)	(0.6)	(0.1)
Controllable expenses	15.1	16.5	1.4	29.1	33.7	4.6
Responsibility margin	\$8.4	\$2.8	\$5.6	\$11.7	(\$0.2)	\$12.0
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	10.1	15.7	5.6	11.4	16.1	4.7
Controllable expenses	57.8	72.1	14.3	63.1	84.4	21.3
Responsibility margin	32.1 %	12.2 %	19.8 %	25.5 %	(0.5) %	26.0 %

- Higher revenue, which resulted from stronger than planned sales of virtually all major products, together with lower than budgeted controllable expenses, resulted in positive responsibility margin variances of \$5.6 million for the quarter and \$12.0 million year-to-date.
- The largest Q94-2 and YTD positive spending variances were in people, product development and marketing. The under spending in YTD headcount-related expenses was the result of actual headcount in Q94-1 being 23 heads under plan. Marketing and product development spending levels will increase in the latter half of the year as the SFS (Q95-1) and EMS (July 1994) ship dates approach.

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
North America FG	\$15.7	\$13.0	\$2.7	\$27.5	\$22.2	\$5.2
Europe FG	27.1	23.6	3.6	47.8	41.2	6.6
ICON FG	1.9	2.2	(0.3)	3.5	4.0	(0.5)
Far East FG	0.8	0.8	0.0	1.5	1.4	0.1
WW OEM	0.3	0.4	(0.0)	0.4	0.7	(0.3)
	\$27.1	\$23.6	\$3.6	\$47.8	\$41.2	\$6.6

(Refer to Channel Section for discussion of revenue variances.)

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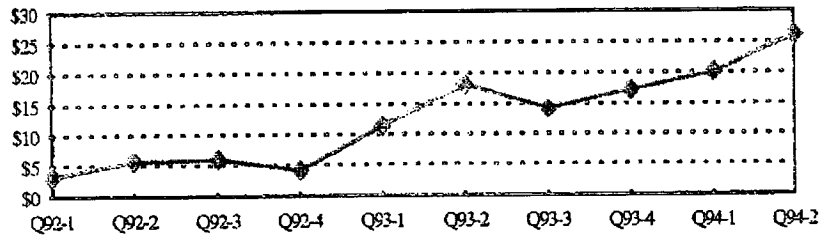
WORKGROUP

TREND ANALYSES

Gross Revenue by Channel (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
North America FG	\$8.0	\$11.5	\$6.8	\$10.3	\$11.8	\$15.7
Europe FG	2.6	5.9	6.2	5.6	6.4	8.4
ICON FG	0.8	1.8	1.3	1.6	1.7	1.9
Far East FG	0.0	0.1	0.1	0.1	0.7	0.8
WW OEM	0.3	0.0	0.1	0.3	0.1	0.3
	<u>\$11.7</u>	<u>\$19.3</u>	<u>\$14.5</u>	<u>\$17.9</u>	<u>\$20.7</u>	<u>\$27.1</u>

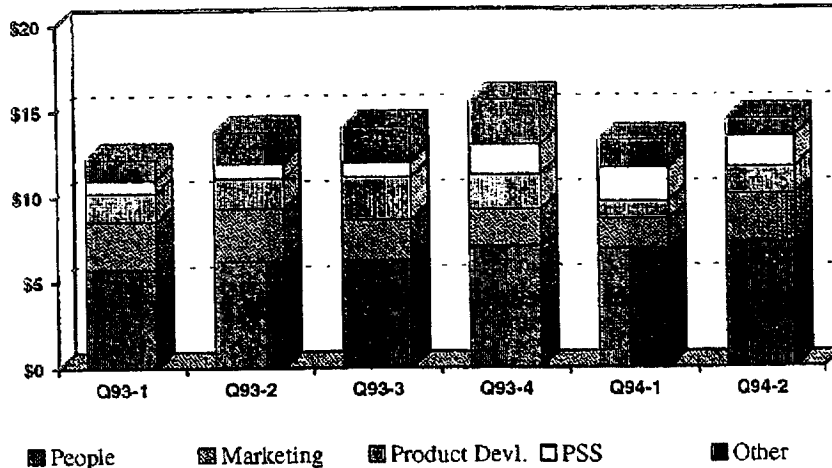
Net Revenue (in millions)



FY92 is stated as reported in FY92 and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

- Workgroup's net revenue per quarter has increased almost 800% over the past 2 1/4 years, from approximately \$3 million in Q92-1 to \$26 million in Q94-2. This is jointly the result of the CSI purchase and the steady growth in market share thereafter.

Controllable Expenses (in millions)



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- Total controllable expenses in Q94-2 were basically flat versus Q94-1.
- Additional product releases in FY93 resulted in growth of PSS expenses. However, PSS usage levels have decreased significantly since Workgroup went to 100% paid support, a trend that is expected to continue.

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SYSTEMS SUMMARY

SYSTEMS SUMMARY

Key Product Releases

<u>Business Unit/Product</u>	<u>RTM Date</u>		<u>Gross revenue in millions</u>			
	<u>Act/Fest</u>	<u>Plan</u>	<u>FYTD94</u>			<u>FY94</u>
			<u>Actual</u>	<u>Plan</u>	<u>Variance</u>	<u>Plan</u>
Advanced Systems						
Windows NT	Jul-93	Jun-93	\$24.5	\$82.6	(\$58.1)	\$169.3
Advanced Server	Jul-93	Jul-93	\$12.3	\$20.0	(\$7.7)	\$55.7
SQL Server for NT	Aug-93	Jul-94	\$8.0	\$16.4	(\$8.4)	\$22.5
MS-DOS						
MS-DOS 6.2 *	Oct-93	Unplanned	\$252.3	\$249.0	\$3.3	\$500.7
Windows						
Windows for Workgroups 3.11	Nov-93	Aug-93	\$24.2	\$26.4	(\$2.2)	\$51.7
Hardware						
Charger OEM Mouse	Sep-93	Nov-93	\$30.8	\$12.7	\$18.1	\$25.1
Ballpoint Mouse 2.0	Jul-93	Jul-93	\$5.4	\$5.8	(\$0.4)	\$11.2
Windows Sound System 2.0	Oct-93	Sep-93	\$4.2	\$6.2	(\$2.0)	\$13.5

* MS-DOS 6.2 was not budgeted. Actual and plan revenues include MS-DOS 6.0.

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SYSTEMS SUMMARY

Results of Operations (in millions)

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
MS-DOS	\$147.0	116 %	\$12.4	237 %	\$19.6	123 %	\$115.0	109 %
Windows	152.4	131	12.9	116	33.4	82	106.2	165
Advanced Systems	40.1	50	8.5	86	41.4	78	(9.8)	(56)
Hardware	52.8	105	34.8	134	9.9	80	8.0	68
Other Systems	27.0	1,605	0.4	34	7.3	97	19.4	NM
	<u>\$419.3</u>	<u>112</u>	<u>\$68.9</u>	<u>129</u>	<u>\$111.6</u>	<u>86</u>	<u>\$238.8</u>	<u>124</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
MS-DOS	35 %	34 %	8 %	4 %	13 %	12 %	78 %	83 %
Windows	36	31	8	10	22	35	70	55
Advanced Systems	10	21	21	12	103	66	(24)	22
Hardware	13	13	66	52	19	25	15	24
Other Systems	6	0	1	69	27	447	72	(416)
	<u>100 %</u>	<u>100 %</u>	<u>16</u>	<u>14</u>	<u>27</u>	<u>35</u>	<u>57</u>	<u>51</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
MS-DOS	\$256.0	103 %	\$17.1	174 %	\$37.8	120 %	\$201.1	97 %
Windows	291.7	137	25.4	124	64.3	83	202.0	176
Advanced Systems	94.2	62	17.4	92	78.7	77	(1.9)	(6)
Hardware	103.9	108	63.2	125	18.0	74	22.7	105
Other Systems	65.3	938	0.9	41	12.9	89	51.5	NM
	<u>\$811.0</u>	<u>113</u>	<u>\$123.9</u>	<u>122</u>	<u>\$211.6</u>	<u>85</u>	<u>\$475.4</u>	<u>130</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
MS-DOS	32 %	35 %	7 %	4 %	15 %	13 %	79 %	83 %
Windows	36	30	9	10	22	36	69	54
Advanced Systems	12	21	19	12	84	67	(2)	21
Hardware	13	13	61	52	17	25	22	22
Other Systems	8	1	1	31	20	208	79	(140)
	<u>100 %</u>	<u>100 %</u>	<u>15</u>	<u>14</u>	<u>26</u>	<u>35</u>	<u>59</u>	<u>51</u>

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SYSTEMS SUMMARY

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$419.3	\$375.5	\$43.8	\$811.0	\$717.1	\$93.9
Cost of revenue	68.9	53.2	(15.7)	123.9	101.9	(22.1)
Gross profit	350.4	322.2	28.1	687.1	615.2	71.8
People expenses	35.9	36.8	0.9	69.0	73.7	4.8
Facilities expenses	6.8	8.6	1.9	13.0	17.2	4.2
Marketing expenses	20.4	30.8	10.4	35.6	53.1	17.5
Product development	9.2	17.5	8.2	16.7	34.2	17.5
PSS	19.5	20.2	0.7	37.7	40.5	2.8
Other expenses	14.8	8.9	(5.9)	29.3	17.3	(12.0)
Net shared resources	5.0	7.0	2.0	10.4	13.4	3.0
Controllable expenses	111.6	129.7	18.2	211.6	249.5	37.8
Responsibility margin	\$238.8	\$192.6	\$46.3	\$475.4	\$365.8	\$109.6
Net revenue	100.0 %	100.0 %	- %	100.0 %	100.0 %	-- %
Cost of revenue	16.4	14.2	(2.3)	15.3	14.2	(1.1)
Controllable expenses	26.6	34.5	7.9	26.1	34.8	8.7
Responsibility margin	57.0 %	51.3 %	5.7 %	58.6 %	51.0 %	7.6 %

- Q94-2 net revenue exceeded plan by 12% or \$44 million. Primary contributing factors for this variance include:
 - Strong MS-DOS, Windows, and Hardware performance in the OEM channel (favorable \$43 million variance) resulting from higher than expected sales of computer systems.
 - Continued strong sales of Windows Products in the NA FG channel (\$21 million above plan).
 - Aggressive sales of MS-DOS upgrades in the North America FG channel (favorable \$21 million variance) stemming from the release of version 6.2.
 - A favorable \$22 million Unspecified Product Billing variance attributed to Systems products.
 - Unfavorable revenue variances in Windows NT and Advanced Server (\$43 million) and the European FG channel for MS-DOS, Windows, and Hardware (\$16 million).
- The negative product cost of revenue variance was driven primarily by the unbudgeted MS-DOS 6.2 release (\$3 million unfavorable) and by MS-DOS and Hardware inventory adjustments (\$3 million and \$7 million unfavorable).
- Marketing spending posted a favorable 34% variance, the result of underspending in both US Marketing (\$7 million) and International Marketing (\$4 million). The decreased marketing spending was consistent across all Systems businesses, with the exception of MS-DOS which incurred unplanned product launch expenses.
- Product Development spending reported a favorable \$8 million variance due to underspending across all segments of the Systems business.
- Bad debt expense included in the other expenses category contributed to the negative variance. OEM accounting has been booking bad debt reserves for high risk accounts.

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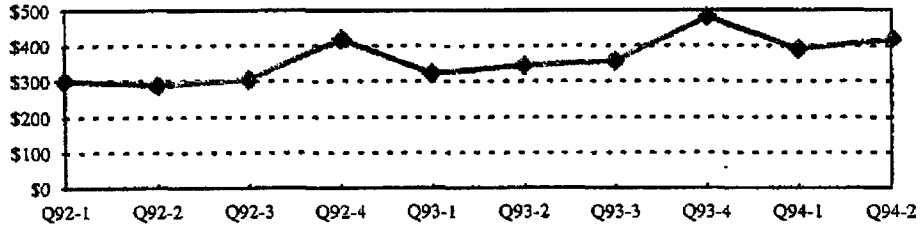
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SYSTEMS SUMMARY

TREND ANALYSES

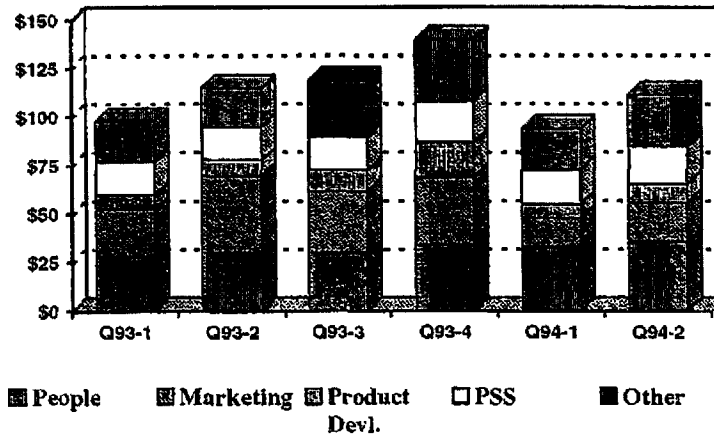
Net Revenue (in millions)



FY92 is stated as reported in FY92 and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

- Systems Q94-2 net revenue grew \$73 million (21% increase) over Q93-2.

Controllable Expenses (in millions)



- People expenses have grown \$6 million over Q93-2, a 20% growth year to year.

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MS-DOS

MS-DOS

Highlights

MS-DOS 6.2 was released on October 19, 1993. The latest release contains ScanDisk, a utility which can find and repair problems on hard disks, and DoubleGuard, which tests data to ensure integrity prior to compressing onto disk. MS-DOS 6.0 users can upgrade to 6.2 by purchasing the Step-Up option, a one disk upgrade, for \$9.95 in retail outlets or for free on CompuServe. A full MS-DOS 6.2 upgrade product offering is also available for pre-MS-DOS 6.0 users at a SRP of \$77.95.

- MS-DOS for Dummies was also introduced with the release of MS-DOS 6.2. The MS-DOS 6.2 software is being packaged with the industry's top-selling computer book, IDG's DOS for Dummies. Microsoft is selling MS-DOS for Dummies into its computer software channel while IDG is selling the bundle into its book channel. The DOS for Dummies packaging is estimated to get MS-DOS into an additional 1,500 to 2,000 retail outlets. The package is being offered at a SRP of \$77.95.
- Based on internal Microsoft estimates, MS-DOS (including IBM's PC-DOS) is expected to ship on 78% of Intel processors in FY94 with Novell DOS shipments estimated at 2-3%. The remaining processors are thought to be shipped with pirated MS-DOS.

Competition

- Novell released Novell DOS 7 in January. Novell DOS 7, an update to DR DOS, is a multitasking version of DOS which includes Personal NetWare, a low-end network operating system positioned to replace NetWare Lite, and DOS Protected Mode Services, an interface which allows device drivers and RAM-resident applications to reside in extended memory. Incompatibilities have been noted in product reviews between Novell DOS 7 and Windows 386 Enhanced Mode. Additionally, Novell DOS 7 does not support Windows for Workgroups 3.11, which is becoming a de facto standard for many OEMs. Novell DOS (including Personal NetWare) is being offered at a retail price of \$99. An upgrade from DR DOS or NetWare Lite can be obtained for \$39.95.

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MS-DOS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$147.0	\$127.0	\$20.0	\$256.0	\$248.3	\$7.6
Cost of revenue	12.4	5.2	(7.2)	17.1	9.8	(7.3)
Gross profit	134.6	121.7	12.9	238.9	238.6	0.3
People expenses	1.1	1.0	(0.1)	2.1	1.9	(0.2)
Facilities expenses	0.1	0.2	0.1	0.2	0.4	0.2
Marketing expenses	3.3	2.6	(0.6)	5.7	5.1	(0.5)
Product development	1.3	1.5	0.2	2.4	2.9	0.5
PSS	3.3	2.5	(0.8)	6.7	5.0	(1.7)
Other expenses	7.2	4.0	(3.2)	13.8	7.8	(6.0)
Net shared resources	3.3	4.1	0.8	6.9	8.2	1.2
Controllable expenses	19.6	15.9	(3.7)	37.8	31.4	(6.4)
Responsibility margin	\$115.0	\$105.9	\$9.2	\$201.1	\$207.2	(\$6.1)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	8.4	4.1	(4.3)	6.7	3.9	(2.7)
Controllable expenses	13.3	12.5	(0.8)	14.8	12.6	(2.1)
Responsibility margin	78.3 %	83.4 %	(5.1) %	78.6 %	83.4 %	(4.9) %

- The 16% positive revenue variance resulted from strong NA FG shipments of MS-DOS 6.2 (\$21 million over plan). This variance is net of 335K NA FG returns of MS-DOS 6.0 upgrade product. MS-DOS OEM revenue continues to be strong, posting a \$8 million increase (9%) over Q94-1, and a \$23 million increase (31%) over Q93-2.
- MS-DOS 6.2 was not planned as part of the FY94 budget process. Thus, the release of the version 6.2 upgrade product is generating negative variances in WW FG Q94-2. Product cost of revenue negative \$3 million, Marketing negative \$1 million, and Product support negative \$1 million.
- An unplanned \$2 million inventory adjustment charge in Q94-2 resulted from the write-off of MS-DOS 6.0 returns in the U.S.
- Bad debt expense, included in the other expenses category, continues to generate negative variances. OEM accounting has been booking bad debt reserves for high-risk accounts.

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MS-DOS

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
MS-DOS New Users						
North America FG	\$ 0.1	\$ 0.0	\$ 0.1	\$ 0.1	\$ 0.0	\$ 0.1
Europe FG	0.2	0.0	0.2	0.3	0.0	0.3
ICON FG	0.2	0.0	0.2	0.5	0.0	0.5
Far East FG	0.4	0.0	0.4	0.9	0.0	0.9
WW OEM	98.3	93.8	4.5	187.2	185.3	1.9
Total MS-DOS New Users	<u>\$ 99.2</u>	<u>\$ 93.8</u>	<u>\$ 5.4</u>	<u>\$ 189.0</u>	<u>\$ 185.3</u>	<u>\$ 3.7</u>
MS-DOS Upgrades						
North America FG	\$ 34.0	\$ 13.2	\$ 20.8	\$ 36.0	\$ 23.0	\$ 13.0
Europe FG	7.7	15.2	(7.5)	16.7	30.4	(13.7)
ICON FG	2.9	4.6	(1.7)	7.8	8.8	(1.0)
Far East FG	1.3	0.8	0.5	2.8	1.5	1.3
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total MS-DOS Upgrades	<u>\$ 45.9</u>	<u>\$ 33.8</u>	<u>\$ 12.1</u>	<u>\$ 63.3</u>	<u>\$ 63.7</u>	<u>\$ (0.4)</u>

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
MS-DOS New Users						
North America FG	\$ 0.5	\$ 0.3	\$ 0.2	\$ 0.0	\$ (0.4)	\$ 0.1
Europe FG	9.2	6.6	3.1	0.5	0.1	0.2
ICON FG	3.9	3.9	2.8	1.1	0.3	0.2
Far East FG	0.6	0.6	0.2	0.4	0.6	0.4
WW OEM	57.2	74.8	79.1	80.1	90.7	98.3
Total MS-DOS New Users	<u>\$ 71.4</u>	<u>\$ 86.2</u>	<u>\$ 85.4</u>	<u>\$ 82.1</u>	<u>\$ 91.3</u>	<u>\$ 99.2</u>
MS-DOS Upgrades						
North America FG	\$ 9.9	\$ 11.2	\$ 51.5	\$ 91.1	\$ 2.5	\$ 34.0
Europe FG	5.6	6.1	10.6	55.5	8.9	7.7
ICON FG	2.0	2.0	3.2	13.2	5.0	2.9
Far East FG	0.2	0.1	0.7	3.5	1.6	1.3
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total MS-DOS Upgrades	<u>\$ 17.7</u>	<u>\$ 19.4</u>	<u>\$ 66.0</u>	<u>\$ 163.3</u>	<u>\$ 18.0</u>	<u>\$ 45.9</u>

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ADVANCED SYSTEMS

ADVANCED SYSTEMS

Highlights

- Digital and IBM agreed to work with Microsoft to ensure Hermes can share information with their respective Polycenter NetView/6000 and NetView 6000 products. Hermes is a server-based suite of tools which performs inventory of hardware and software, installs software on remote systems across a network, and stores client configuration information in an SQL database. Hermes will enable customers to perform centralized management of diverse desktop computing environments. Hermes is an open architecture which key software partners can use to build standards-based system management solutions, and has received broad support across the industry from a variety of vendors.
- The Windows NT Japanese beta was released at the end of September. Windows NT-J is expected to be generally available by the end of the month.
- Microsoft Windows NT Advanced Server received PC Magazine's Technical Excellence Award in the networking software category.
- Daytona, an update to Windows NT 3.1, is being prepared for a Q94-4 release. The goals for Daytona are to minimize size while increasing performance.
- Microsoft's December Professional Developers Conference in Anaheim was attended by more than 5,000 applications developers. More than 250 32-bit applications are available today with several hundred more expected by the spring of 1994. All attendees received the latest developers release of Chicago and Win 32 and a pre-release version of OLE.
- SNA Server for Windows NT was announced in November. SNA Server enables connections of desktop PCs to IBM mainframes and AS/400 systems and allows data residing on these systems to be integrated into client-server applications. SNA Server for Windows is available in 10-user, 64-user, and 250-user configurations for \$995, \$5,995, and \$14,995, respectively.

Competition

- Industry-standard benchmarks have placed Windows NT solutions as price/performance leaders in both the file server and applications server arena.

File Server Benchmark

	<u>System Cost</u>	<u>Quest- Marks*</u>
Windows NT Advanced Server 3.1	\$15,900	227
NetWare 4.01	\$20,273	196

* QuestMark is a benchmark based upon a repetitive set of Excel instructions.
Source: LANQuest Labs, September 1993

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ADVANCED SYSTEMS

Application Server Benchmark

<u>Operating System/Database</u>	<u>Hardware</u>	<u>TPS*</u>	<u>5-year System Cost</u>	<u>S/TPS</u>
Windows NT/SQL Server for NT	Dual Pentium-66	226	\$99,780	\$441
SunOS/Sybase SQL	SPARCServer 690 mp	135	\$372,832	\$2,764
IBM AIX/INFORMIX-OnLine	RS/6000-970	110	\$307,639	\$2,789

* Transaction Processing Council TPC-B transaction per second ratings
Source: Published TPC-B Benchmark Summary, September 1993

- Novell has been working with Oracle to ship OracleWare, which is an integrated solution combining NetWare or UnixWare with the Oracle7 database, Oracle Office, a client-server messaging and scheduling system, and Oracle Glue. Oracle Glue enables connections between server-based data and various front-end tools. Oracle will deliver all product support for the OracleWare product line. The NetWare 3.1.2 edition was shipped to distributors in early December with an SRP of \$3,095 for a 5-user license. The UnixWare-based version will be available in the first quarter of 1994 while the NetWare 4.0-based version will ship in mid-1994.
- Novell announced it is extending the NetWare 4.0 sales promotion through April 1994. Customers who purchase NetWare 4.0 by the end of April will receive any updates which occur prior to July 31, 1994, free of charge.

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ADVANCED SYSTEMS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$40.1	\$80.2	(\$40.1)	\$94.2	\$152.4	(\$58.2)
Cost of revenue	8.5	9.8	1.3	17.4	19.0	1.5
Gross profit	31.6	70.4	(38.8)	76.8	133.4	(56.6)
People expenses	15.3	15.8	0.6	30.0	32.2	2.1
Facilities expenses	3.3	4.2	1.0	6.0	8.4	2.3
Marketing expenses	7.6	11.0	3.4	12.3	18.5	6.3
Product development	3.9	7.1	3.2	7.0	12.9	5.9
PSS	5.5	7.4	1.9	10.8	14.8	4.0
Other expenses	0.9	1.2	0.3	1.9	2.3	0.4
Net shared resources	5.1	6.3	1.2	10.6	12.7	2.1
Controllable expenses	41.4	53.0	11.5	78.7	101.8	23.0
Responsibility margin	(\$9.8)	\$17.4	(\$27.2)	(\$1.9)	\$31.6	(\$33.6)
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	21.1	12.2	(8.9)	18.5	12.5	(6.1)
Controllable expenses	103.3	66.0	(37.2)	83.6	66.8	(16.8)
Responsibility margin	(24.4) %	21.7 %	(46.1) %	(2.1) %	20.8 %	(22.8) %

- The Q94-2 revenue shortfall was the result of negative revenue variances in Windows NT (\$39 million), Advanced Server (\$5 million), and SQL Server for Windows NT (\$1 million) sales. The revenue shortfall was slightly offset by stronger than planned LAN Manager sales (\$3 million positive revenue variance).
- Cost of revenue, as a percent of revenue in Q94-2, exceeded plan due to a \$3.0 million negative variance in royalties which were not planned as part of the FY94 budget process. SQL Server (\$1.7 million) and Xenix (\$0.7 million) account for the majority of the royalties.
- Marketing spending was 31% below plan due to favorable variances in US marketing (\$2 million) and International Marketing (\$1 million). The Advanced Systems marketing direct spending YTD actual is \$2.9 million on a total FY94 budget of \$3.3 million.
- The 45% favorable Product Development variance results from decreased spending on external product development (\$1 million) due to schedule changes and Redmond localization expenses (\$1 million). The localization variance is due to a change in strategy from the FY94 budget where Japan is now paying for the external localization costs associated with the Windows NT-J release.

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ADVANCED SYSTEMS

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Windows NT						
North America FG	\$ 1.1	\$ 18.7	\$ (17.6)	\$ 15.4	\$ 48.4	\$ (33.0)
Europe FG	3.2	20.7	(17.5)	6.1	27.3	(21.2)
ICON FG	0.1	2.1	(2.0)	2.1	4.7	(2.6)
Far East FG	0.3	0.8	(0.5)	0.8	1.0	(0.2)
WW OEM	0.1	1.1	(1.0)	0.1	1.3	(1.2)
Total Windows NT	<u>\$ 4.8</u>	<u>\$ 43.4</u>	<u>\$ (38.6)</u>	<u>\$ 24.5</u>	<u>\$ 82.7</u>	<u>\$ (58.2)</u>
Advanced Server						
North America FG	\$ 2.9	\$ 5.2	\$ (2.3)	\$ 6.3	\$ 11.8	\$ (5.5)
Europe FG	2.5	4.2	(1.7)	3.4	5.4	(2.0)
ICON FG	0.8	0.2	0.6	1.6	0.5	1.1
Far East FG	0.7	0.4	0.3	0.8	0.6	0.2
WW OEM	0.2	1.6	(1.4)	0.2	1.7	(1.5)
Total Advanced Server	<u>\$ 7.1</u>	<u>\$ 11.6</u>	<u>\$ (4.5)</u>	<u>\$ 12.3</u>	<u>\$ 20.0</u>	<u>\$ (7.7)</u>
Lan Manager						
North America FG	\$ 1.3	\$ 3.1	\$ (1.8)	\$ 2.9	\$ 8.5	\$ (5.6)
Europe FG	3.2	1.1	2.1	7.3	2.0	5.3
ICON FG	0.3	0.9	(0.6)	0.8	1.6	(0.8)
Far East FG	0.3	0.4	(0.1)	0.6	0.7	(0.1)
WW OEM	5.9	2.4	3.5	13.6	5.3	8.3
Total Lan Manager	<u>\$ 11.0</u>	<u>\$ 7.9</u>	<u>\$ 3.1</u>	<u>\$ 25.2</u>	<u>\$ 18.1</u>	<u>\$ 7.1</u>

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Windows NT						
North America FG	\$ 0.0	\$ 0.0	\$ 0.0	\$ 0.0	\$ 14.3	\$ 1.1
Europe FG	0.0	0.0	0.0	0.0	2.9	3.2
ICON FG	0.0	0.0	0.0	0.0	2.0	0.1
Far East FG	0.0	0.0	0.0	0.0	0.5	0.3
WW OEM	0.0	0.0	0.0	0.0	0.0	0.1
Total Windows NT	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 19.7</u>	<u>\$ 4.8</u>
Advanced Server						
North America FG	\$ 0.0	\$ 0.0	\$ 0.0	\$ 0.0	\$ 3.4	\$ 2.9
Europe FG	0.0	0.0	0.0	0.0	0.9	2.5
ICON FG	0.0	0.0	0.0	0.0	0.8	0.8
Far East FG	0.0	0.0	0.0	0.0	0.2	0.7
WW OEM	0.0	0.0	0.0	0.0	0.0	0.2
Total Advanced Server	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 0.0</u>	<u>\$ 5.3</u>	<u>\$ 7.1</u>
LAN Manager						
North America FG	\$ 5.2	\$ 4.6	\$ 3.3	\$ 3.7	\$ 1.7	\$ 1.3
Europe FG	5.4	5.9	5.3	4.5	4.1	3.2
ICON FG	0.7	0.1	0.5	0.2	0.5	0.3
Far East FG	0.7	1.1	0.9	0.8	0.3	0.3
WW OEM	5.5	7.8	9.1	7.2	7.8	5.9
Total LAN Manager	<u>\$ 17.5</u>	<u>\$ 19.5</u>	<u>\$ 19.1</u>	<u>\$ 16.4</u>	<u>\$ 14.4</u>	<u>\$ 11.0</u>

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WINDOWS

WINDOWS

Highlights

- Chicago was highlighted at December's Professional Developers Conference. Chicago is a 32-bit operating system with integrated networking which will run in 4MB of memory and support existing MS-DOS and Windows applications. Chicago will update the Windows user interface, increase support for mobile users, and implement Plug and Play functionality, which is a new standard for auto-configuration of hardware adapters and other peripherals. Chicago is scheduled to ship in the first half of FY95.
- Windows for Workgroups 3.11 (WFW) shipped in November. WFW 3.11 includes improved security and interoperability, built-in fax software based on the At Work architecture, and 32-bit extensions which allow it to run up to 30% faster than Windows 3.1. The 32-bit network code will also be used to form Chicago's core networking. WFW 3.11 also includes improved networking compatibility with NetWare and improved remote access services. Gateway 2000, Digital Equipment, Dell, and Zenith Data Systems, along with six other OEMs, have committed to pre-installing wfw 3.11 on all their systems while other OEMs such as Compaq and Hewlett-Packard will offer systems pre-installed with WFW 3.11. WFW 3.11 is being offered at SRPs of \$219.95 for full-packaged product and \$69.95 for an upgrade from Windows 3.1 or Windows for Workgroups 3.1.
- Windows 3.1 received PC World's World Class award for operating system software during Comdex in November.
- The number of life-to-date Windows 3.1 licensed users is estimated at more than 40 million.
- Based upon internal estimates, Windows 3.1 penetration is at 65% of currently shipping Windows-compatible machines. Penetration continues to increase as more and more OEMs ship Windows 3.1 pre-installed on their hardware. More than 4.2 million Windows OEM units were reported in Q94-2 compared to 3.0 million units in Q93-2, a 40% increase.

Competition

- IBM introduced OS/2 for Windows in November. This product allows current Windows users to take advantage of OS/2's multitasking capabilities. IBM also announced its intentions to have OS/2 2.1 and OS/2 for Windows to support the Win32s APIs early in calendar year 1994. A PC Week product review states OS/2 for Windows makes it as easy as possible for Windows users to try out OS/2 at a cheap price, but noted compatibility problems with certain Windows applications and the fact it will not work properly with Windows for Workgroups. OS/2 for Windows is being offered at an introductory price of \$49 until February 10, at which time the price will be raised to \$139. The \$139 price is down from OS/2 2.1 pricing of \$189.
- BIS Strategic Decisions estimates the OS/2 installed base grew to 1.9 million at the end of 1993, up from 1.1 million the prior year. PC/Computing awarded OS/2 with its Most Valuable Product award in the Systems Software Category at Comdex in November.
- Apple plans to offer a DOS/Windows-compatible Macintosh Quadra in the first half of 1994. The personal computer will allow users to run both environments simultaneously with the ability to toggle and cut and paste between the environments.

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WINDOWS

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$152.4	\$116.4	\$36.1	\$291.7	\$213.1	\$78.6
Cost of revenue	12.9	11.1	(1.8)	25.4	20.4	(5.0)
Gross profit	139.6	105.3	34.3	266.4	192.7	73.6
People expenses	7.7	8.7	1.0	14.9	17.3	2.3
Facilities expenses	1.0	1.8	0.8	1.9	3.6	1.7
Marketing expenses	5.3	12.1	6.8	10.5	20.2	9.7
Product development	1.4	3.0	1.6	2.6	6.2	3.6
PSS	9.7	9.4	(0.3)	18.2	18.8	0.6
Other expenses	5.6	3.0	(2.6)	11.0	5.7	(5.3)
Net shared resources	2.5	2.9	0.4	5.1	5.8	0.7
Controllable expenses	33.4	40.9	7.5	64.3	77.7	13.3
Responsibility margin	\$106.2	\$64.4	\$41.8	\$202.0	\$115.1	\$87.0
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	8.4	9.5	1.1	8.7	9.6	0.9
Controllable expenses	21.9	35.1	13.2	22.0	36.4	14.4
Responsibility margin	69.7 %	55.3 %	14.3 %	69.3 %	54.0 %	15.3 %

- Current quarter Windows new license revenue continued to exceed plan in OEM (\$20 million) and North America FG (\$14 million). Q94-2 Windows new license revenue grew \$9 million over Q93-2, an 8% increase. OEM revenues have fueled this growth, with Q94-2 revenues growing 42% over Q93-2.
- Q94-2 product cost of revenue as a percent of net revenue remained slightly below plan with continued savings in the manufacturing and distribution allocation. Total cost of revenue was 8.4% of net revenue as compared to a plan of 9.5%.
- WW marketing spending in Q94-2 was 44% of plan. US Marketing was \$5 million below plan while International Marketing was \$2 million below plan.
- Bad Debt Expense, included in the other expenses line, was \$2 million over plan. OEM Accounting was holding a bad debt reserve for at-risk accounts.

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WINDOWS

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Windows New Users						
North America FG	\$24.5	\$10.1	\$14.4	\$41.4	\$18.6	\$22.8
Europe FG	10.4	13.3	(2.9)	20.1	23.3	(3.2)
ICON FG	6.1	5.3	0.8	12.4	9.4	3.0
Far East FG	2.4	5.4	(3.0)	6.7	11.3	(4.6)
WW OEM	79.3	59.2	20.1	155.3	109.6	45.7
Total Windows New Users	\$122.7	\$93.3	\$29.4	\$235.9	\$172.2	\$63.7
Windows Upgrades						
North America FG	\$5.0	\$2.2	\$2.8	\$8.5	\$3.9	\$4.6
Europe FG	2.6	2.3	0.3	4.7	3.9	0.8
ICON FG	1.1	0.8	0.3	2.6	1.5	1.1
Far East FG	0.4	0.4	0.0	0.9	2.0	(1.1)
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Windows Upgrades	\$9.1	\$5.7	\$3.4	\$16.7	\$11.3	\$5.4
Windows for Workgroups						
North America FG	\$7.5	\$4.5	\$3.0	\$11.3	\$6.7	\$4.6
Europe FG	6.8	8.4	(1.6)	9.5	14.9	(5.4)
ICON FG	1.1	2.1	(1.0)	2.2	3.4	(1.2)
Far East FG	0.1	0.2	(0.1)	0.1	0.4	(0.3)
WW OEM	0.6	0.5	0.1	1.1	1.1	0.0
Total Windows for Workgroups	\$16.1	\$15.7	\$0.4	\$24.2	\$26.5	(\$2.3)

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
Windows New Users						
North America FG	\$16.3	\$21.2	\$22.1	\$32.9	\$16.7	\$24.5
Europe FG	28.3	31.0	20.4	13.6	10.3	10.4
ICON FG	8.5	6.5	6.7	7.8	7.4	6.1
Far East FG	1.1	1.2	1.5	14.6	4.4	2.4
WW OEM	22.2	53.7	65.5	71.4	76.0	79.3
Total Windows New Users	\$76.4	\$113.6	\$116.2	\$140.3	\$114.8	\$122.7
Windows Upgrades						
North America FG	\$2.6	\$2.9	\$1.9	\$6.2	\$3.5	\$5.0
Europe FG	9.9	5.8	3.9	2.8	1.5	2.6
ICON FG	0.9	0.4	0.1	0.2	0.3	1.1
Far East FG	0.0	0.0	0.0	0.4	0.4	0.4
WW OEM	0.0	0.0	0.0	0.0	0.0	0.0
Total Windows Upgrades	\$13.4	\$9.1	\$5.9	\$9.6	\$5.7	\$9.1
Windows for Workgroups						
North America FG	\$0.0	\$24.8	(\$0.8)	(\$4.8)	\$3.8	\$7.5
Europe FG	0.0	6.4	5.6	3.2	2.8	6.8
ICON FG	0.0	2.1	1.1	1.5	1.1	1.1
Far East FG	0.0	0.2	0.0	0.0	0.1	0.1
WW OEM	0.0	0.0	0.2	1.2	0.4	0.6
Total Windows for Wkgroups	\$0.0	\$33.5	\$6.1	\$1.1	\$8.2	\$16.1

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HARDWARE

HARDWARE

Highlights

- On November 1, 1993, Microsoft announced it is joining with Spectron Microsystems to deliver a Windows-based Digital Signal Processor (DSP) software architecture, which will support multifunction audio and communication device capabilities. Microsoft will deliver the host-based software and Spectron will deliver SPOX, its DSP operating system. The Audio product unit plans to make a device driver kit (to develop driver software for unique DSP hardware solutions) available to OEMs in the first half of 1994. Microsoft will also make available the DSP APIs to ISVs and develop products for end users based on the DSP software architecture and SPOX. DSP vendors that support the Microsoft and Spectron relationship include Analog Devices, Inc., Media Vision, Motorola Semiconductor Products, Inc., National Semiconductor Corporation, and Texas Instruments.
- On November 1, 1993, Media Vision announced that it had signed a letter of intent with Spectron Microsystems to license Spectron's SPOX operating system and Microsoft's Windows-based DSP resource manager and DSP Application Programming Interface (API).
- The Microsoft Mouse won PC World's "World Class award for Pointing Devices" at the November 18, 1993 Las Vegas Comdex show.
- As of January 1, 1994, the Hardware business unit (Mouse, Ballpoint, etc.) reports to Patty Stonesifer, VP Consumer Division. The Audio product unit (Windows Sound System) continues to report into the Systems Division.
- Per Tech Scan (Currently Microsoft, Logitech & Microspeed report shipment numbers to Tech Scan), Microsoft Mouse's market share has increased from 49% in July to almost 61% in October, primarily as a result of the fall promotion. Sell through of the price promoted SKUs exploded to 3 times normal sales volume. Hardware and the MSUS organization have jointly decided to continue with the lower street prices permanently. (A full report of the quarter's promotion will be forthcoming in February.)

Competition

- Logitech announced on November 1, 1993, that it had signed a licensing agreement with 3DO, making it the first peripheral licensee for 3DO's new interactive multimedia platform. Under the terms of the agreement, Logitech can manufacture and market a variety of 3DO-compatible peripherals, including mice, trackballs, 3D controllers, and 3D headtrackers. The 3DO Interactive Multiplayer system attaches to a television set and delivers 50 times the graphics animation performance of PCs and video game systems. The 3DO Interactive Multiplayer system plays interactive entertainment, education, and information software, as well as music CDs, photo CDs, and video CDs. Investors in 3DO include Matsushita Electric Industrial Co.; AT&T; Time Warner; Electronic Arts; and Kleiner Perkins Caufield & Byers, a Silicon Valley venture capital firm.
- Logitech introduced their Cyberman game controller at the November 18, 1993 Comdex show. The \$149 SRP (\$89 street price) device is a 2.5D controller that functions like a joy-stick for existing games while providing another axis for game developers. The device also provides for tactile feedback from games.
- Logitech unveiled on November 1, 1993, the new design of its TrackMan desktop mouse for the Macintosh. With a case design that conforms more closely with the human hand than previous versions, TrackMan offers advanced ergonomic styling and precision control.

OEM Competitiveness

- The shift in mouse sales from retail to the lower revenue per unit OEM channel has increased dramatically over the past few years (approx. 65% of Microsoft Mouse unit sales occur in the OEM channel). For this reason, the low cost Microsoft OEM Mouse will be released in January 1994. By the end of FY94-Q3, Hardware will have 300K/units per month capacity in this low cost mouse. The cost competitiveness of these mice has prompted the OEM division to declare calendar year 1994 to be the year of the OEM Mouse. This selling campaign escalates selling focus on the OEM Mouse.

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HARDWARE

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$52.8	\$50.3	\$2.5	\$103.9	\$96.3	\$7.6
Cost of revenue	34.8	25.9	(8.9)	63.2	50.5	(12.7)
Gross profit	18.0	24.3	(6.4)	40.7	45.8	(5.1)
People expenses	2.6	2.5	(0.1)	4.9	5.0	0.1
Facilities expenses	0.3	0.6	0.3	0.6	1.2	0.6
Marketing expenses	3.7	4.0	0.3	6.3	7.2	0.9
Product development	1.5	3.0	1.5	2.6	6.2	3.6
PSS	1.0	0.9	(0.1)	1.8	1.8	(0.0)
Other expenses	0.6	0.8	0.2	1.2	1.5	0.3
Net shared resources	0.2	0.6	0.4	0.6	1.2	0.6
Controllable expenses	9.9	12.4	2.5	18.0	24.2	6.2
Responsibility margin	\$8.0	\$11.9	(\$3.8)	\$22.7	\$21.6	\$1.1
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	- %
Cost of revenue	65.9	51.6	(14.4)	60.8	52.5	(8.4)
Controllable expenses	18.8	24.8	5.9	17.3	25.1	7.8
Responsibility margin	15.2 %	23.6 %	(8.4) %	21.9 %	22.4 %	(0.6) %

- A 5% positive net revenue variance for the quarter and 8% year-to-date were primarily the result of strong OEM Mouse sales, offset by a \$7.0 million inventory adjustment for the quarter, and \$8.5 million inventory adjustment year-to-date, resulted in a responsibility margin that was 32% below plan for the quarter and 5% above plan year-to-date..
- A \$7.0 million charge, taken to reduce obsolete inventory, was the primary reason that Q94-2 COGS were \$8.9 million higher than budget. Hardware is trying to sell out Mouse 1.0 inventory (\$2.5 million adjustment) and Windows Sound System sound board inventory (\$4.5 million adjustment) at severely reduced prices (lower than cost). Margins were lowered to sell these products more aggressively.

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HARDWARE

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
North America FG	\$24.3	\$26.2	(\$1.8)	\$47.7	\$50.8	(\$3.1)
Europe FG	8.9	13.7	(4.8)	18.1	23.8	(5.7)
ICON FG	1.3	3.8	(2.5)	4.5	7.1	(2.6)
Far East FG	(0.8)	1.5	(2.2)	2.5	4.1	(1.6)
WW OEM	21.3	6.6	14.6	35.0	13.2	21.8
	<u>\$55.0</u>	<u>\$51.7</u>	<u>\$3.3</u>	<u>\$107.7</u>	<u>\$98.9</u>	<u>\$8.8</u>

(Refer to Channel Section for discussion of revenue variances.)

Gross Revenue by Channel Trend (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
North America FG	\$30.0	\$29.0	\$14.0	\$25.0	\$23.3	\$24.3
Europe FG	20.0	23.0	10.0	12.0	9.2	8.9
ICON FG	7.0	7.0	5.0	6.0	3.2	1.3
Far East FG	1.0	1.0	1.0	5.0	3.3	(0.8)
WW OEM	7.0	9.0	19.0	13.0	13.7	21.3
	<u>\$65.0</u>	<u>\$69.0</u>	<u>\$49.0</u>	<u>\$61.0</u>	<u>\$52.7</u>	<u>\$55.0</u>

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ADVANCED TECHNOLOGY

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Key Product Releases

Business Unit/Product	RTM Date		Revenue in thousands			
	Actual	Plan	FYTD94		Variance	FY94 Budget
			Actual	Plan		
Advanced Product Dev						
Scenes Sierra Club	18-Aug-93	Jul-93	\$815	\$507	\$308	\$779
Scenes Outer Space	18-Aug-93	Jul-93	869	507	176	779
Scenes Impressionists	18-Aug-93	Jul-93	1103	507	163	779
Word Assistant / Win	15-Nov-93	Oct-93	624	973	-349	2,163
Attache (Office add-on) / Win	15-Mar-94	Oct-93	0	633	-633	1,408
Ink Font Pack / Win	Canceled	Oct-93	0	57	-57	121
Ink Font Pack / Mac	Canceled	Oct-93	0	33	-33	70
Word Assistant / Mac	Apr-94	Jan-94	0	0	0	277
TT Master Set / Win	Mar-94	Jan-94	0	0	0	751
Sizzle (PowerPoint add-on) / Win	Canceled	Jan-94	0	0	0	251
Sizzle (PowerPoint add-on) / Mac	Canceled	Jan-94	0	0	0	101
Attache (Office add-on) / Mac	Jun-94	Feb-94	0	0	0	282

- Microsoft Scenes, a new line of screen saver products announced July 26th, sold more than 100,000 units in its first eight weeks on the market. To date 172,000 units have been sold; the plan for FY94 is 134,000 units. The first three collections available contain photographic images of nature, outer space and art, and include information related to each image provided by experts in the particular field. In addition, users can personalize their workstations through an enclosed offer from Genigraphics Corporation to convert up to three personal photographs into Microsoft Scenes images. SRP is \$29.95 per collection.
- Announced on October 20th, Win Word Assistant is an add-on product to Microsoft Word 6.0 that includes multiple templates and forms, True Type fonts, a font selector with a WYSIWYG (What You See Is What You Get) display, and clip art. In a promotion that ran until 11/30, a free copy of Word Assistant was given away with every three copies of Word Upgrade purchased. Similar add-on products for Office and the Mac environment are being developed. Release dates for these add-on products are dependent on the release of the next version of the product they support.
- Font Pack 2 was bundled with Office, Excel and Word Upgrades in a direct mailing offer dropped the first week of November. The offer is good through the end of January. There was a Mac Line Holiday promotion (good until March) offering a Mac Works/Master Set for the Mac bundle.
- The PowerPoint add-on was canceled upon reexamination of the business case and resources required. Ink Font Pack was postponed due to timing and marketing issues. It will be revisited later in this fiscal year or next.
- The efforts of the other business units within Advanced Technology (Advanced Consumer Technology, Broad Band Applications and On Line Services) are almost exclusively concentrated on exploration of future technologies, opportunities, alliances and industries. This research and development is not expected to yield revenue bearing products in the present fiscal year.

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ADVANCED TECHNOLOGY

Highlights

- Nathan Myrvold, SVP of Advanced Technology was appointed to the National Information Infrastructure Advisory Council.
- Dr. James T. Kajiya, one of the most distinguished researchers in the field of computer graphics has joined Microsoft Research (MSR) to help establish MSR as a prominent research and development organization in 3D graphics and animation.
- Advanced Technology's mission is to develop Microsoft's most forward looking technologies with a focus on the consumer and taking advantage of the impact of digital convergence. Most of these technologies are not expected to become reality until 1995 or later. Key areas of development include:
 - Operating system software for the broadband digital information highway and related client/server reference platform.
 - Leading applications for the broadband digital information highway.
 - A Microsoft branded on-line service for personal computers and other narrowband devices that would ship with Chicago and initially offer product/developer support functions. The range of information is expected to expand to include a broad range of services and information.
 - Software and hardware reference designs for wireless personal companions and other consumer mobile devices.
 - Cryptography.
 - Compression technology.
 - Research into other projects including natural language, voice recognition, advanced interfaces and sophisticated agency.
- On August 4th, it was announced that Microsoft agreed to purchase certain technology, research and product development efforts from Continuum Productions Corp. The core business of Continuum is to create a digital archive and media database, including such media types as video footage, photographic images and sound clips. Approximately 33 continuum staff joined Microsoft on September 1, 1994.

Competition/Related Industry Highlights

- Bell Atlantic and TCI agreed to merge, as did AT&T and McCaw Cellular. There is an impending buyout of Paramount, bidders include Viacom and QVC Network.
- The Apple Wireless Messaging Service delivered by MobileComm was made available to users of the Newton MessagePad. The monthly service fee for this service is expected to range from approximately \$21.00 for standard local coverage to \$83.95 for standard nationwide coverage. The service is enabled by the Newton Messaging Card which sells for approximately \$229.
- TCI provided details on its fiber-optic network, saying it would circle San Francisco Bay within two years.
- October 5th 3DO Co. announced it had teamed up with a unit of US West for an interactive television trial in Omaha, Nebraska, scheduled to reach 100,000 customers by the end of next year. AT&T is a vital investor in 3DO Co.
- Viacom is building a test interactive cable system in Castro Valley, CA.
- Pacific Bell announced their plans to establish a Multimedia Information Network that will reach 1.2 million homes within two years. By the end of the decade Pacific Bell plans to have 60% of their customers on-line.

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ADVANCED TECHNOLOGY

Results of Operations (in millions)

Q94-2

Q94-2

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Advanced Consumer Tech	(\$0.0)	(8) %	\$0.0	17 %	\$7.6	66 %	(\$7.6)	NM %
Advanced Product Dev	3.0	71	0.9	112	3.0	74	(0.9)	NM
On Line Services	0.0	NM	0.0	NM	1.1	45	(1.1)	NM
Broad Band Apps	0.0	NM	0.0	NM	0.5	43	(0.5)	NM
	<u>\$3.0</u>	<u>64</u>	<u>\$0.9</u>	<u>107</u>	<u>\$12.2</u>	<u>64</u>	<u>(\$10.0)</u>	<u>NM</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Advanced Consumer Tech	(1) %	8 %	(26) %	12 %	(24.510) %	2.972 %	24.635 %	(2.884) %
Advanced Product Dev	101	92	29	18	99	95	(28)	(13)
On Line Services	0	0	NM	NM	NM	NM	NM	NM
Broad Band Apps	0	0	NM	NM	NM	NM	NM	NM
	<u>100 %</u>	<u>100 %</u>	<u>30</u>	<u>18</u>	<u>403</u>	<u>407</u>	<u>(333)</u>	<u>(324)</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Advanced Consumer Tech	(\$0.1)	(6) %	\$0.0	(11) %	\$13.5	NM %	(\$13.5)	NM %
Advanced Product Dev	5.1	83	1.6	71	5.3	NM	(1.8)	NM
On Line Services	0.0	NM	0.0	NM	1.9	NM	(1.9)	NM
Broad Band Apps	0.0	NM	0.0	NM	0.7	NM	(0.7)	NM
	<u>\$5.1</u>	<u>73</u>	<u>\$1.6</u>	<u>61</u>	<u>\$21.3</u>	<u>NM</u>	<u>(\$17.9)</u>	<u>NM</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	% pts Var	Actual	Plan	Actual	Plan	Actual	Plan
Advanced Consumer Tech	(1) %	(12)	(44) %	89 %	(26.952) %	(2.875) %	27.096 %	(2.875) %
Advanced Product Dev	101	12	32	81	103	(48)	(34)	(48)
On Line Services	0	0	NM	NM	NM	NM	NM	NM
Broad Band Apps	0	0	NM	NM	NM	NM	NM	NM
	<u>100 %</u>	<u>0</u>	<u>32</u>	<u>82</u>	<u>421</u>	<u>(458)</u>	<u>(353)</u>	<u>(458)</u>

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ADVANCED TECHNOLOGY

Results of Operations (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$3.0	\$4.7	(\$1.7)	\$5.1	\$6.9	(\$1.9)
Cost of revenue	0.9	0.8	(0.1)	1.6	1.3	(0.4)
Gross profit	2.1	3.9	(1.7)	3.4	5.6	(2.2)
People expenses	8.5	11.8	3.3	14.7	22.5	7.8
Facilities expenses	1.0	1.9	0.9	1.9	3.4	1.5
Marketing expenses	0.3	0.2	(0.2)	0.6	0.3	(0.4)
Product development	1.6	4.3	2.6	2.2	9.2	6.9
PSS	0.0	0.0	0.0	0.0	0.0	0.0
Other expenses	0.0	0.1	0.1	0.1	0.1	0.1
Net shared resources	0.8	0.9	0.2	1.8	1.8	(0.0)
Controllable expenses	12.2	19.1	7.0	21.3	37.4	16.0
Responsibility margin	(\$10.0)	(\$15.3)	\$5.2	(\$17.9)	(\$31.7)	\$13.8
Net revenue	100.0 %	100.0 %	-- %	100.0 %	100.0 %	-- %
Cost of revenue	29.5	17.7	(11.8)	32.3	18.4	(13.9)
Controllable expenses	403.3	406.7	3.4	420.8	539.8	119.0
Responsibility margin	(332.9) %	(324.4) %	(8.4) %	(353.1) %	(458.2) %	105.1 %

- The slip of Office Assistant, a result of the delay in release of Office 4.2, contributed to the negative variance in revenues, along with lower than planned sales of Word Assistant and Font Packs.
- Despite the additional headcount brought in to Advanced Technology from Continuum, AT's hiring was below plan, resulting in a positive variance in people expenses.
- The lower than planned headcount and associated development activity resulted in the positive variance in facilities. Depreciation and amortization and the building and grounds distribution were both below plan.
- Product development for Advanced Consumer Technology was below plan by \$1.8 million in Q94-2, and by \$4.4 million YTD. Advanced Technology's exploration into certain new technologies is still at a very early stage. However, as decisions are made and projects take shape, it is expected these investments will occur and the variance will disappear by fiscal year end.

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ADVANCED TECHNOLOGY

Gross Revenue by Channel Results (in millions)

	Q94-2			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
North America FG	\$2.7	\$4.2	(\$1.5)	\$4.6	\$6.1	(\$1.5)
Europe FG	0.4	0.6	(0.3)	0.6	1.2	(0.6)
ICON FG	0.1	0.0	0.1	0.2	0.0	0.2
Far East FG	0.0	0.0	0.0	0.0	0.0	0.0
WW OEM	0.0	0.0	0.0	(0.0)	0.0	(0.0)
	<u>\$3.3</u>	<u>\$4.9</u>	<u>(\$1.6)</u>	<u>\$5.4</u>	<u>\$7.3</u>	<u>(\$1.8)</u>

(Refer to Channel Section for discussion of revenue variances.)

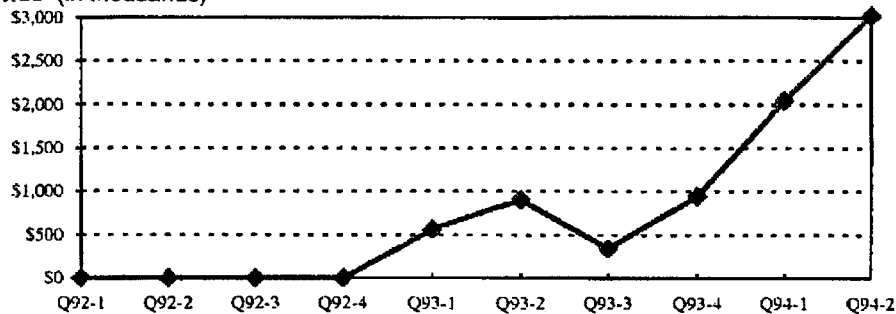
TREND ANALYSES

Gross Revenue by Channel (in millions)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2
North America FG	\$0.6	\$0.9	\$0.3	\$0.9	\$1.9	\$2.7
Europe FG	-	-	-	-	0.2	0.4
ICON FG	-	-	-	-	0.1	0.1
Far East FG	-	-	-	-	0.0	0.0
WW OEM	-	-	-	-	(0.0)	0.0
	<u>\$0.6</u>	<u>\$0.9</u>	<u>\$0.3</u>	<u>\$0.9</u>	<u>\$2.2</u>	<u>\$3.3</u>

(FY 93 revenues from the following products: Font Pack, Multimedia Viewer, MS-DOS Extensions, MM Developers Kit and Modular Windows.)

Net Revenue (in thousands)



FY92 is stated as reported in FY92 (as a part of systems) and has not been restated for product reclassifications which are deemed to be immaterial for the purposes of this graph.

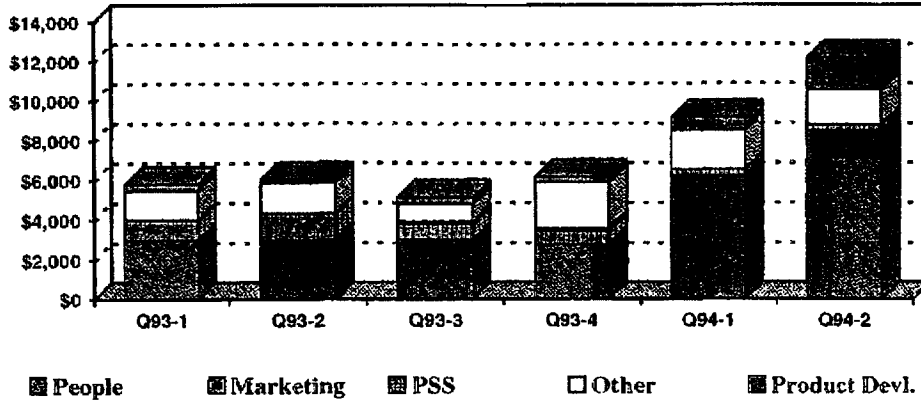
- Sales of the newly released Word Assistant and increased sales of Scenes Impressionists resulted in the revenue growth this quarter over Q94-1.
- The introduction of Microsoft Scenes in Q94-1 more than doubled net revenue over Q93-4 for Advanced Technology.
- There was a drop in North America FG Font Pack sales in Q93-3.

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ADVANCED TECHNOLOGY

Controllable Expenses (in thousands)



- Advanced Technology's headcount has increased 28%, to 345 people from 270 at the end of last quarter, causing headcount related expenses to increase. Headcount excludes AT management and Microsoft Research.

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Operations

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OPERATIONS SUMMARY

Controllable Expenses of Corporate Organizations (in thousands)

	Q94-2		FYTD94	
	Actual	% of Plan	Actual	% of Plan
General & Facility Distributions				
People	\$22,783	82 %	\$44,653	81 %
Facilities	13,389	105	25,450	101
Other	12,131	85	23,938	83
Controllable Expenses	<u>\$48,303</u>	88	<u>\$94,041</u>	86
ITG				
People	\$10,357	89 %	\$20,821	89 %
Facilities	1,903	77	3,485	77
Other	31	207	82	265
Controllable Expenses	<u>\$12,291</u>	87	<u>\$24,388</u>	88
HR & Administration				
People	\$9,516	92 %	\$17,777	86 %
Facilities	1,617	74	3,109	71
Other	214	33	328	25
Controllable Expenses	<u>\$11,347</u>	86	<u>\$21,214</u>	80
Legal				
People	\$3,717	101 %	\$6,726	92 %
Facilities	503	102	953	99
Other	10,446	79	16,862	64
Controllable Expenses	<u>\$14,666</u>	84 %	<u>\$24,541</u>	71
Finance				
People	\$5,955	104 %	\$11,027	92 %
Facilities	1,044	81	2,177	85
Other	2,340	140	4,354	112
Controllable Expenses	<u>\$9,339</u>	107	<u>\$17,558</u>	95
MD&L				
People	\$826	72 %	\$1,525	66 %
Facilities	139	46	261	43
Other	2	100	7	100
Controllable Expenses	<u>\$967</u>	67	<u>\$1,793</u>	62

Headcount Summary

	Q94-2			FY94
	Actual	Plan	Variance	Plan
MD&L	1,450	1,570	120	1,573
ITG	308	326	18	326
Law & Corporate Affairs	140	154	14	155
Finance	260	286	26	288
Human Resources	228	240	12	242
Corporate Services	244	276	32	277
Executive Staff	5	4	(1)	4
Real Estate & Facilities	75	90	15	92
Operations	<u>2,710</u>	<u>2,946</u>	<u>236</u>	<u>2,957</u>

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Operations

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OPERATIONS SUMMARY

General & Facility Distributions

- With no Company holiday party, Q94-2 company events were \$2.3 million below plan. Favorable headcount resulted in positive variances for depreciation (\$1.0 million), beverages and cafeteria (\$722,000) and 401(k) match (\$309,000).
- Below planned hiring kept FYTD94 distributed expenses \$15.5 million below plan. Depreciation and postage and freight were favorable by \$1.7 million and \$1.2 million, respectively. The downturn in hiring and timing of payments, combined to create a positive beverage and cafeteria variance of \$1.6 million. Maintenance costs were under plan by \$1.3 million, mainly for electrical (\$619,000), buildings (\$256,000), security (\$98,000) and telecommunications (\$90,000).

ITG

- People expenses were below plan due to reduced headcount and consulting fees as significant projects (primarily Microsoft On-line Services (MOS)) were ramping up behind budget.
- Below plan facilities expenses were centered in positive variances for telecommunications (\$497,000) and depreciation (\$489,000). Telecommunications was below plan since MS will not see significant telecommunications costs until Q4, and depreciation was below plan primarily due to later than expected purchases of equipment for Sales and Marketing, and Imaging projects.

HR & Administration

- Employee fringes were under plan, consistent with the lower than planned headcount.
- Miscellaneous operating expenses were \$1.1 million below plan primarily due to withholding payment to consultants for the Flexible Benefit Plan until specific conditions were met.

Legal

- Q94-2 budgeted litigation reserves were not considered necessary, resulting in a \$3 million positive settlements variance.
- FYTD94 controllable expenses variance was due to lower than planned litigation and lower than planned third party legal fees.

Finance

- The timing of printing costs for the annual report resulted in a \$675,000 negative variance for "other expenses" for the quarter. In addition, Bain and Company research, consulting for G/L Access Park and District reporting for MS US contributed the \$219,000 Q94-2 negative variance for temporary help and consulting.
- FYTD94 corporate distributions were below plan, resulting in a \$763,000 positive variance in finance. In addition, a lag in hiring created a \$574,000 positive variance for recruiting.

MD&L

- The majority of MD&L's lower than planned spending (\$482,000) was due to the following: contingency (\$238,000), depreciation (\$112,000) and distributions (\$119,000). The favorable contingency and depreciation variances were due to timing.

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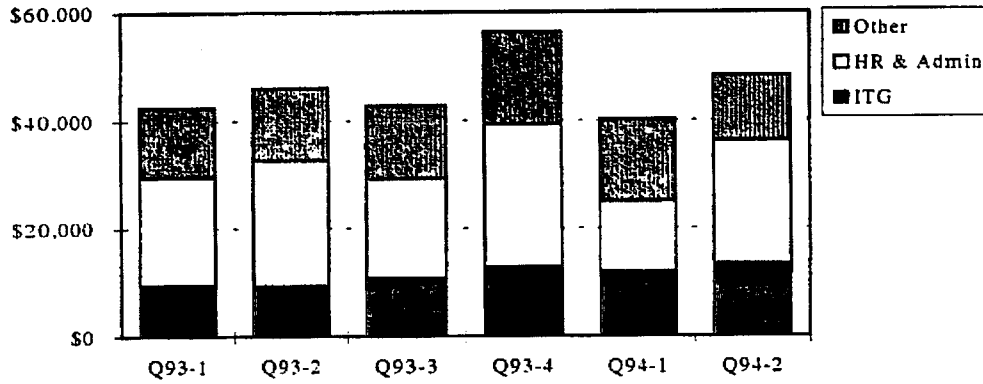
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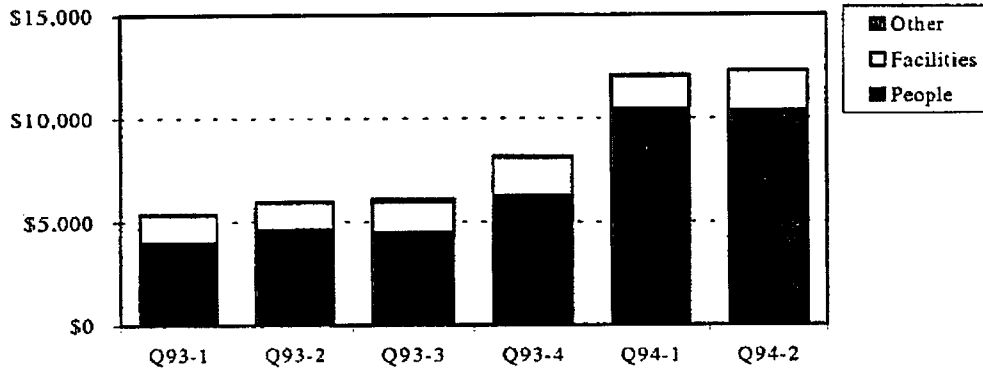
OPERATIONS SUMMARY

TREND ANALYSES - CONTROLLABLE EXPENSES (IN THOUSANDS)

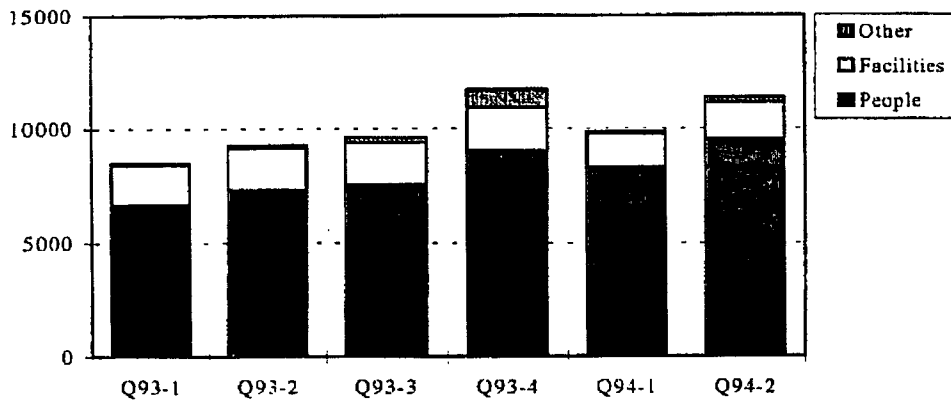
General & Facility Distribution



ITG



HR & Administration



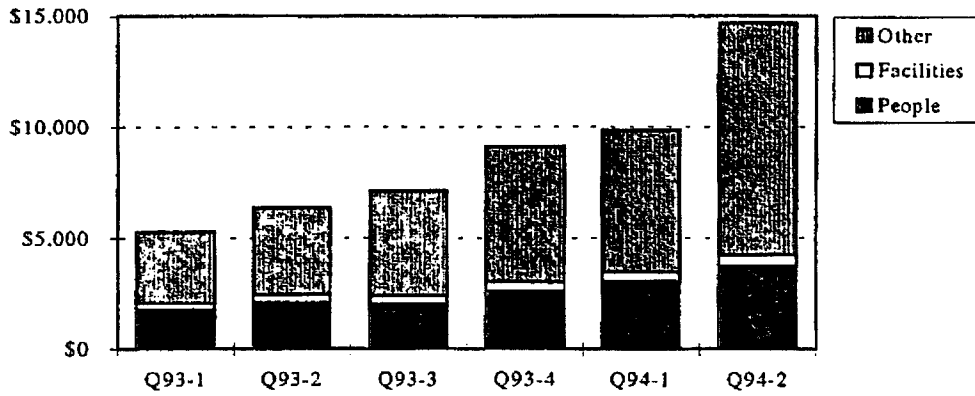
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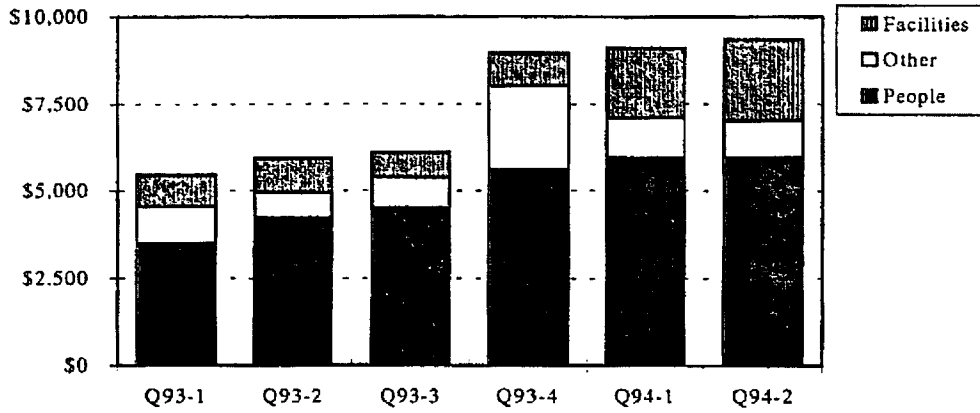
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OPERATIONS SUMMARY

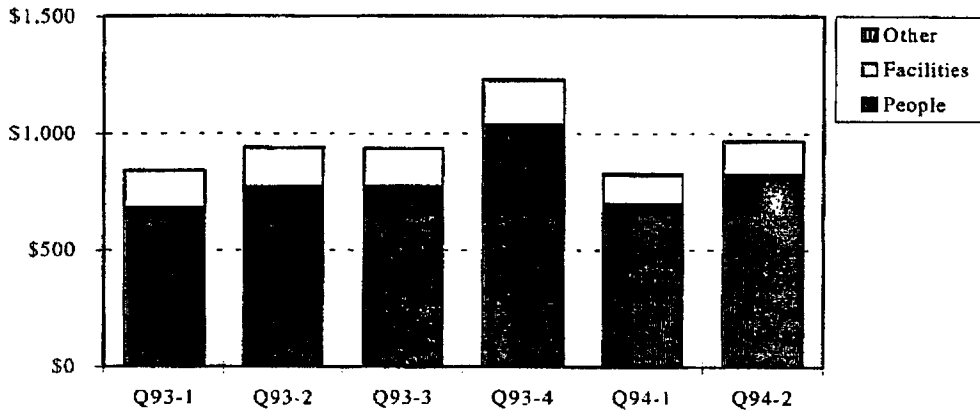
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Finance



MD&L



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FACILITIES

FACILITIES

Worldwide Facility Distribution

Location	December 31, 1993		December 31, 1992	
	Square Feet	% of Total	Square Feet	% of Total
Corporate Campus	1,783,000	34%	1,653,000	37%
Other Domestic	1,594,000	30%	1,343,000	30%
International	1,875,000	36%	1,488,000	33%
	<u>5,252,000</u>	<u>100%</u>	<u>4,484,000</u>	<u>100%</u>

- The worldwide portfolio increased 768,000 square feet (17%) between Q93-2 and Q94-2. YTD expansion has been 382,000 square feet (7%).
- Expansion of domestic facilities in the past 12 months has accounted for 381,000 square feet (50%) of the portfolio's growth, and international expansion has contributed 387,000 square feet (50%) of worldwide growth.
- During the second half of FY94, growth will be limited to the completion of Building 25 (223,000 square feet) and the leasing of several new or expanded offices in the U.S. and internationally. Longer term growth will be focused on Corporate Campus and a proposed new facility in Dublin for WPG.

Domestic Facilities

- The supply of office space on and in the vicinity of Campus remains very constrained. As a result, additional groups will move off Campus in early FY95.
- Growth during the remainder of FY94 will be concentrated at the Corporate Campus (Building 25 will add 223,000 square feet in Q94-4), several expanded field sites, and additional leased space in the Redmond area. One of the field sites is actually a Latin American regional headquarters in Miami.
- FY94 and FY95 will have relatively few leases expiring, measured in square footage. However, in FY96, leases comprising 428,000 square feet will expire. This expiration schedule is currently under study to take advantage of perceived real estate market cycles and to reduce long term occupancy costs.
- Stage 1 of a Campus and local area occupancy plan was completed during Q94-2; this report evaluated projected demand for and supply of space in the local area and on Campus. Stage 2 of this plan will be completed soon, and will make recommendations regarding the quantity and timing of new construction on Campus and/or Redmond West.
- Redmond West land use approvals will be completed during Q94-3.

International Facilities

- Slower growth rates and reallocation of resources in Europe are presenting opportunities to optimize the use of both office and warehouse space. The realization of efficiencies in distribution and logistics will allow Microsoft to achieve net reductions of warehouse space in Europe in the future. Also currently under consideration is the disposition of unused office space in France.
- Growth in all international regions was nil during Q94-2. There will be several moves/expansions of sales offices during Q94-3 and Q94-4, although increases in office space will not be as dramatic as in the past 12 months.
- After further review, approval was granted to proceed with the construction of a build-to-suit office facility in Dublin, Ireland, to accommodate WPG- Ireland personnel. This 70,000 square foot facility will have a value of approximately \$13.0 million, and construction will begin late in FY94. A decision on purchase or lease is contingent on a pending ruling by Irish tax authorities on the tax treatment of the facility.

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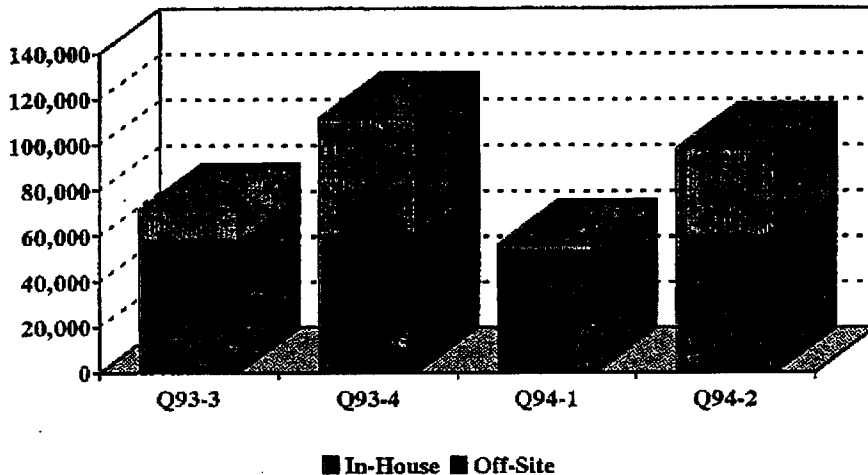
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MANUFACTURING, DISTRIBUTION, & LOGISTICS

MANUFACTURING, DISTRIBUTION, & LOGISTICS

Domestic Focused Factory - Component Pieces (in millions)



- Outsourcing continues to be an integral part of the manufacturing solution to increasing demand. In Q94-2 domestic products were built at 10 sites, including Puerto Rico. Five sites distributed products directly to customers. Planning for Chicago release is well underway; we are projecting that product will be manufactured at 15 sites.
- The domestic focused factory (DFF) set a new weekly production record. In October, over 935,000 units of product were manufactured in-house and offsite combined. DFF also set a new daily shipment record in December, shipping over \$24 million of product.
- Puerto Rico is now operating at full capacity, working seven days per week, 24 hours per day most of the time.
- DFF outsourced 39% of its production demand; this was significantly higher than the prior quarter. The higher outsourcing was the direct result of increased demand.
- Manufacturing continued efforts to achieve ISO 9002 certification at Canyon Park and Puerto Rico. Registration audits are scheduled for April in Puerto Rico and will be conducted at Canyon Park during June 1994.

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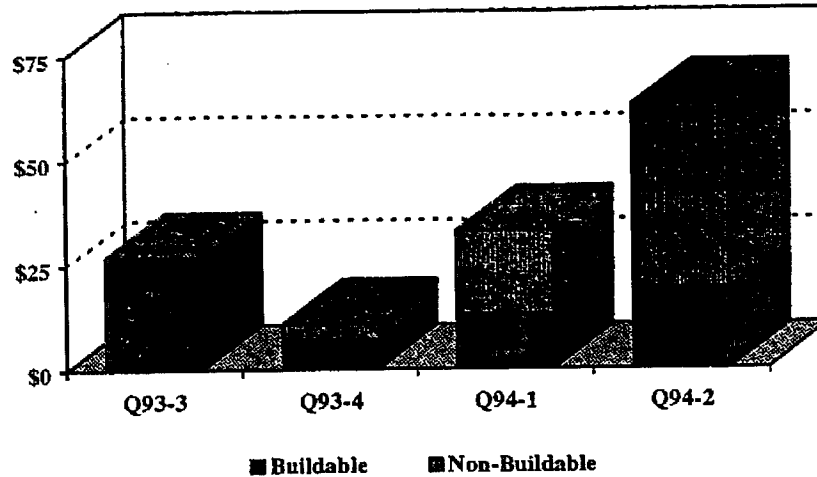
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Domestic Focused Factory - Backlog (in millions)



- Domestic backlog increased to a record \$63 million which was 91% higher than the prior quarter. Applications represented \$56 million while systems accounted for \$7 million.
- Buildable backlog for the quarter was \$19 million and non-buildable backlog was \$44 million. Excel 5.0 accounted for the majority of the non-buildable while MS DOS, Office and Encarta accounted for most of buildable backlog which resulted from higher than anticipated demand.
- Buildable backlog occurs when customer demand exceeds forecast or when the plant fails to build to forecasted demand. Non-buildable backlog occurs when orders are placed for products that have not been released to manufacturing.

International Focused Factory

- International Focused Factory (IFF) continues to build a strategic partnership with RR Donnelley & Sons (RRD) to single source all of IFF's worldwide outsource requirements.
- RRD in Singapore continues to expand its product offering. Until recently, only MS DOS and Windows were manufactured. Word was added this quarter and Excel, PowerPoint, Access and Office are expected to be added during Q94-3.
- IFF outsourced duplication and assembly of all MS DOS and Windows products, primarily to RRD (Preston, WA). The change will free up capacity to build other products in-house.
- IFF is assisting Japan (through RR Donnelley & Sons) to reduce product cost of goods sold. Access was manufactured this quarter with favorable results. Japan is preparing to expand manufacturing with RRD to further reduce cost of goods sold.
- RRD is organizing a production facility in Australia to support the Australian and New Zealand markets. Manufacturing is expected to begin in Q94-4.
- IFF is determining how best to reduce time to market and increase product availability in Brazil and Mexico while containing costs.

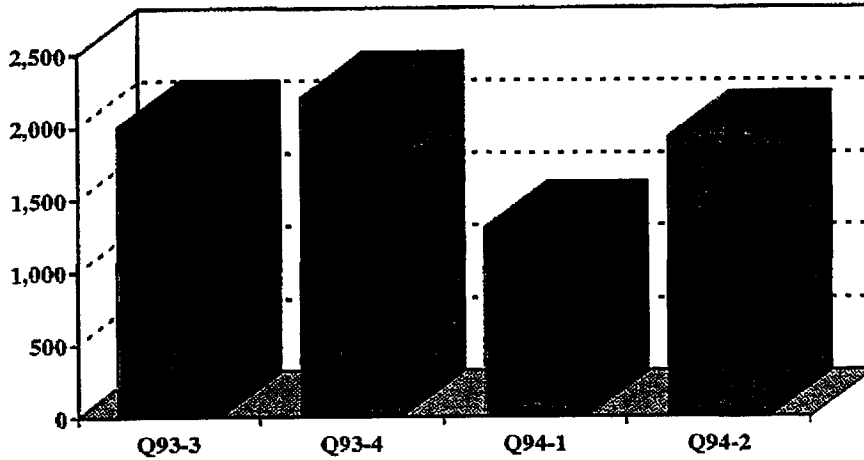
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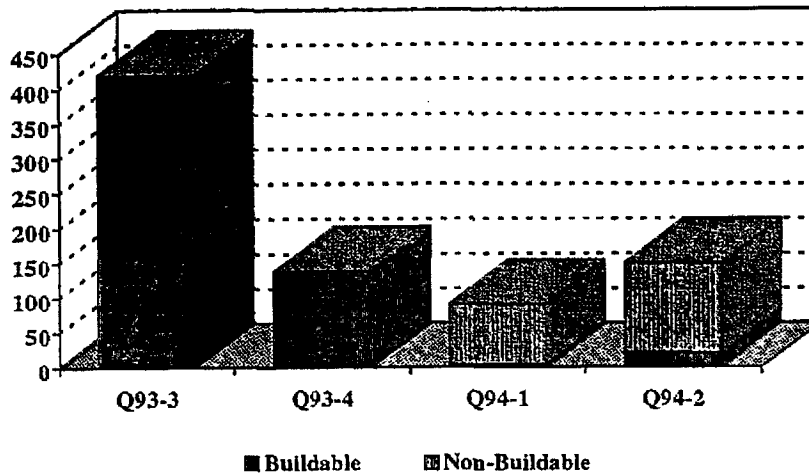
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MS Ireland - Units Produced (in thousands)



- Microsoft Ireland, which provides the majority of packaged products sold by our European subsidiaries, measures production by packages built. Ireland produced 1.9 million units in Q94-2, 46% higher than the 1.3 million units produced last quarter. Q93-2 volumes were higher due to Office and Word 6.0.

MS Ireland - Backlog Units (in thousands)



- Ireland's manufacturing demand is created by orders from European subsidiaries. While the backlog definition is consistent with that used domestically, backlog is tracked in units rather than dollars. Backlog increased as demand for product was greater than anticipated.

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MANUFACTURING, DISTRIBUTION, & LOGISTICS

Headcount

	Q94-2			FY94
	Actual	Plan	Variance	Plan
Campus North	585	619	34	621
Ireland	407	418	11	418
IFF	239	264	25	264
Puerto Rico	160	204	44	204
Procurement/Mgmt	59	65	6	66
MD&L	1,450	1,570	120	1,573

- The favorable variance to plan relates primarily to production associates. Ireland's favorable variance relates to delayed hiring for the consolidation of European Warehouses.

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INVESTOR RELATIONS / STOCK ACTIVITY

INVESTOR RELATIONS / STOCK ACTIVITY

FY94 Earnings Release

- On January 19, 1994, financial results for Q94-2 were released. Earnings per share were \$0.95 for the quarter. Selected analysts' earnings projections for the upcoming quarters, updated as of January 6, 1994, are summarized in the table below.

Selected Earnings per Share Estimates, FY94 - FY95

Analyst	Q94-2E	Q94-2A	Q94-3	Q94-4	FY94	FY95
Alex. Brown	0.92	\$0.95	\$1.00	\$0.99	\$3.73	4.50
Cowen & Co.	0.92	0.95	1.02	1.04	3.80	4.40
Dean Witter	0.92	0.95	0.97	1.01	3.75	4.50
Goldman, Sachs	0.91	0.95	1.00	0.96	3.70	4.45
Lehman Brothers	0.92	0.95	1.01	1.00	3.75	4.65
Merrill Lynch	0.92	0.95	0.98	-	3.70	4.60
Montgomery	0.90	0.95	1.01	1.00	3.75	4.60
Morgan Stanley	0.94	0.95	1.03	0.94	3.70	4.45
Paine Webber	0.93	0.95	1.03	1.02	3.80	4.70
Piper Jaffray	0.92	0.95	1.02	1.07	3.83	4.30
Salomon Brothers	1.02	0.95	0.99	1.06	3.77	4.75
UBS Securities	0.94	0.95	1.05	1.00	3.80	4.50
Mean -- all analysts	<u>0.92</u>	<u>\$0.95</u>	<u>\$1.01</u>	<u>\$1.00</u>	<u>\$3.73</u>	<u>\$4.50</u>

Ownership of Microsoft Stock

- As of December 31, 1993, Microsoft officers and directors held 44% of outstanding Microsoft stock, a decrease from the 45% held as of September 30, 1993.

Stock Ownership Profile, Q94-1

	Number of Shares	% of Total
Officers, directors and 5% shareholders		
William H. Gates	76,962,044	27%
Paul Allen	30,499,040	11
Steve Ballmer	14,976,382	5
	<u>122,437,466</u>	<u>43%</u>
Other officers and directors	2,754,713	1
Total officers and directors	<u>125,192,179</u>	<u>44</u>
Other holders (float)	<u>159,514,683</u>	<u>56</u>
Total shares outstanding	<u><u>284,706,862</u></u>	<u><u>100%</u></u>

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INVESTOR RELATIONS / STOCK ACTIVITY

Institutional Shareholders

- The 20 largest institutional owners of Microsoft stock held 15.6% of outstanding shares at September 30, 1993 (the latest date for which information is available). These same institutions held 11.1% of outstanding shares the prior year. There are more than 140 institutions that hold more than 100,000 shares of MSFT.

Twenty Largest Institutional Shareholders

Institution	December 31, 1993		December 31, 1992		Change (000)
	Shares Held (000)	Percent of Total Outstanding	Shares Held (000)	Percent of Total Outstanding	
Equitable Companies, Inc.*	8,222	2.9	9	0.0	8,213
Provident Investment Counsel	3,982	1.4	3,418	1.2	564
IDS Financial Corp.	2,887	1.0	3,057	1.1	(170)
Fidelity Management	2,835	1.0	3,616	1.3	(781)
Jennison Associates Capital	2,778	0.9	2,590	0.9	188
Kemper Finl Services	2,282	0.8	1,908	0.7	374
RCM Capital Management	2,214	0.8	967	0.3	1,247
College Retire Equities	2,050	0.7	2,344	0.8	(294)
Smith Barney Shearson	1,781	0.6	28	0.0	1,753
Wellington Management Company	1,717	0.6	384	0.1	1,333
California PER	1,474	0.5	1,473	0.5	1
Scudder Stevens & Clark	1,410	0.5	1,328	0.5	82
NW Bank of Minnesota N.A.	1,396	0.5	457	0.2	939
Morgan JP & Co	1,374	0.5	2,035	0.7	(661)
State Street Resr & Mgmt	1,370	0.5	1,328	0.5	42
Northern Trust Corporation	1,260	0.4	907	0.3	353
Wells Fargo Inst.	1,240	0.4	2,123	0.8	(883)
Massachusetts Finl Svcs	1,228	0.4	1,625	0.6	(397)
Hellman Jordan Management Co.	1,217	0.4	809	0.3	408
Stein Roe & Farnham	1,119	0.4	722	0.3	397
	<u>43,836</u>	15.3	<u>31,128</u>	11.1	<u>12,708</u>

*Note: This is a name change from Alliance Capital

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INVESTOR RELATIONS / STOCK ACTIVITY

Microsoft Market Capitalization

- Based on market values as of January 20, 1994, total market capitalization for Microsoft equals \$26.2 billion.

Largest Public Companies (in billions)

<u>Rank</u>	<u>Company</u>	<u>Market Capitalization</u>
1	General Electric	\$91.4
2	Exxon	80.7
3	American Telephone & Telegraph	74.1
4	Wal Mart Stores	58.0
5	Coca Cola	54.1
6	Phillip Morris	49.6
7	General Motors	43.2
8	Merck	41.5
9	Procter & Gamble	39.4
10	Shell Transport & Trading	36.0
11	DuPont	35.8
12	IBM	33.3
13	GTE	32.4
14	Pepsico	31.6
15	Ford Motor	31.6
16	Mobil	31.5
17	Bristol-Myers Squibb	29.9
18	Chevron	29.3
19	Johnson & Johnson	28.5
20	Intel Corporation	27.7
21	Motorola	27.5
22	Bellsouth	27.4
23	American Internat Group	27.3
24	Amoco	26.8
25	Microsoft Corporation	26.2

Q94-1 Stock Market Activity Summary

Market Performance Comparison

	<u>Microsoft Prices</u>	<u>S & P 500</u>	<u>Industrial Index</u>
Quarter High	86 1/2	471.28	806.15
Quarter Low	79 1/4	461.44	774.91
Quarter Close	80 5/8	466.44	805.84
Previous Quarter Close	80	461.78	782.81
Change	1%	1%	3%

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Short Interest of Microsoft Shares

	<u>Short Position</u>	<u>Days to Cover</u>
September 15, 1993	2,252,502	1
December 15, 1993	3,166,148	2

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HUMAN RESOURCES

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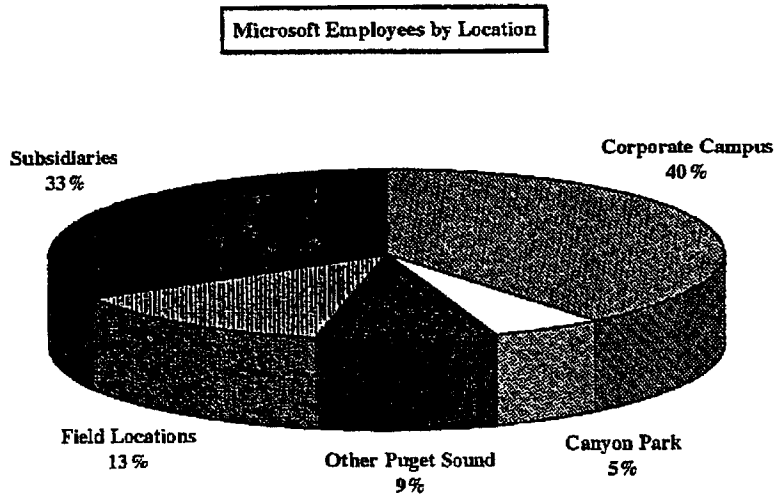
Q94-2 Headcount

	Actual		Plan		Variance	
	Headcount	Mix	Headcount	Mix	Headcount	%
Sales & Support	7,487	50%	8,264	50%	777	5%
Product Group	4,195	29%	4,773	29%	578	4%
Advanced Technology	345	3%	455	3%	110	1%
Operations Group	2,710	18%	2,946	18%	236	1%
	<u>14,737</u>	<u>100%</u>	<u>16,438</u>	<u>100%</u>	<u>1,701</u>	<u>10%</u>

Worldwide actual headcount was 90% of planned headcount at the end of Q94-2.

Worldwide Headcount by Location

- The following chart shows the distribution of total Microsoft employees by location. Approximately 54% of total employees are employed in the Puget Sound area.



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HUMAN RESOURCES

Profile of Domestic Employees

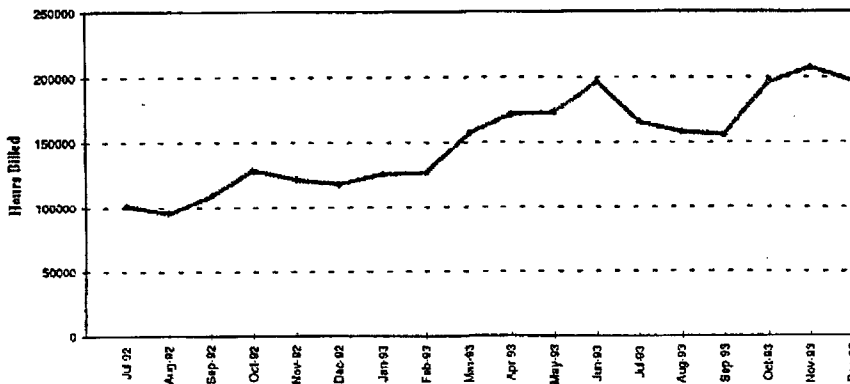
U.S. Employee Statistics

	<u>No. of Employees</u>	<u>Mix</u>
Sex:		
Female	3,540	36%
Male	6,296	64%
Ethnicity:		
White	8,420	86%
Asian Pacific/Islander	834	8%
African American	262	3%
Hispanic	231	2%
American Indian/Alaska Native	51	< 1%
Other	38	< 1%
Age:		
Under 20	38	< 1%
20 - 29	3,511	36%
30 - 39	4,699	48%
40 and Over	1,588	16%
Average Age:	32.3 years	
Average Tenure:		
Domestic	3.1 years	
Subsidiaries	2.4 years	
Worldwide Average	2.8 years	

- The table above summarizes Microsoft's U.S. employee demographics with respect to age, tenure and affirmative action metrics. These statistics have remained relatively constant, with the average age of domestic employees slowly starting to increase.

Temporary Employees

Temporary Employee Hours Billed



July 1, 1992 - December 31, 1993

- Use of temporary employees at Microsoft increased during Q94-2. The average cost per hour for temporary employees has increased from \$15 to \$21 due to the increased number of temporary employees being used in more technical (higher paying) positions. Year to date expenses for temporary help employees are \$1.9 million less than budget (\$19.2M v \$21.1M).

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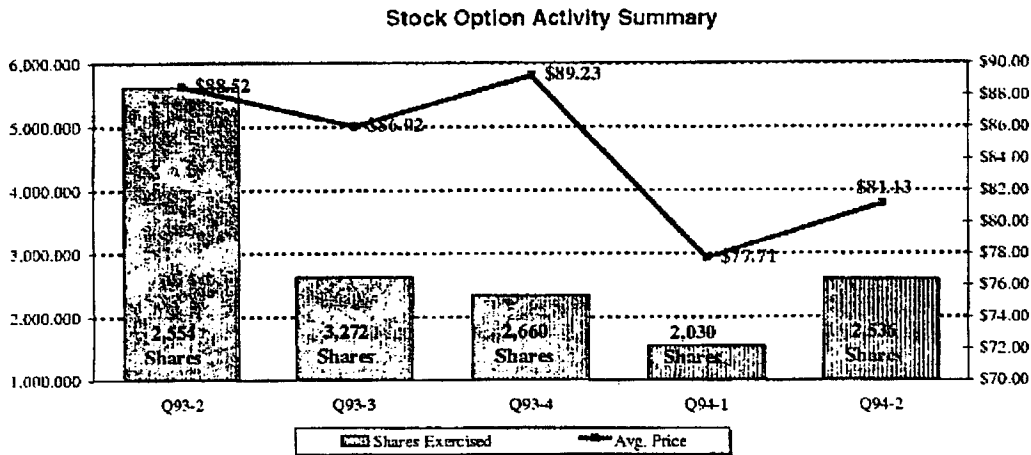
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HUMAN RESOURCES

Stock Administration



- In Q94-2, a total of 2,593,745 shares were exercised, a 68% increase over the previous quarter. Q94-2 also showed a 25% increase in employee exercise transactions (2,536 optionees) over the previous quarter and comparable to the same period in FY93. Factors attributing to these increases were the upward trend in the average stock price throughout the quarter, and employees taking advantage of the favorable tax rates prior to 1994. The statutory withholding rate for Non Qualified stock option exercises will increase from 20% to 28% with the option to withhold at 31%, 36%, and 39.6% in 1994.

ESPP Administration

Domestic Issuance 12/31/93

- The sixth period of the 1991 Employee Stock Purchase Plan ended on December 31, 1993. On that day the closing price of Microsoft common stock was \$80.625, as compared to the closing price of \$87.125 at the beginning of the period (7/1/93). ESPP shares were purchased at \$68.53 per share.

A total of 217,804 shares were issued to domestic employees for the period ending December 31, 1993. This is a 19% increase from the 183,034 shares issued for the previous period ending June 30, 1993. The participation rate for domestic employees increased by approximately 4% from 7,022 employees in the previous period to 7,284 employees for the period ending December 31, 1993.

The seventh offering of the 1991 Employee Stock Purchase Plan began on January 3, 1994 with a closing FMV of \$80.125.

The International issuance summary will be reported next quarter.

New Enrollment 12/31/93

- A total of 10,491 employees (domestic and international) are currently enrolled in the ESPP period ending December 31, 1993. Total enrollment has increased 11% (9,406) from the previous period ended June 30, 1993.

Grant Administration

On Hire Options

- A total of 157 stock option grants were processed totaling 292,120 shares for Q94-2. A total of 334 stock option grants were processed totaling 529,205 shares during Q94-2 that were dated in prior quarters.

Operations

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HUMAN RESOURCES

Severance Plan Vesting Acceleration

Type	# of Employees	Acceleration	# of Shares Accelerated
RIF	8	12 weeks	1,670
RIF	32	6 months	25,950
RPP	8	12 weeks	4,282
Total	48		31,902

- The above table is a summary of the option shares accelerated during Q94-2 and are in accordance with the Severance Plan. (RIF-Reduction in Force; RPP-Refused Performance Plan).

Vesting Accelerations Not Covered Under Severance Plan or Stock Option Plan

Type	# of Employees	Acceleration	# of Shares Accelerated
RIF Australia	17	6 months	6,793
RIF Canada	1	6 months	188
Negotiated Resignations	8	12 weeks	4,282
Total	26		11,263

- This table summarizes vesting accelerations which are results of international severance packages and domestic Negotiated Resignations that are not covered under the Severance Plan or Stock Option Plan and require Board Approval.

Reduction in Workforce

- While worldwide total headcount is expected to grow during the current fiscal year, Microsoft continues to aggressively seek efficiencies in its operations. As a result of these efforts to realign the workforce with the current and future business objectives, Microsoft now provides severance packages to employees whose positions have been eliminated due to restructuring of various organizations and who have not been able to secure another position within the company. During Q94-2, a total of 53 employees were terminated as a result of a reduction in workforce. All of those employees received the standard severance package.

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HUMAN RESOURCES

401(k) Savings Plus Plan

401(k) Investment Portfolio

Investment Option	Dec. 31, 1993	%	Dec. 31, 1992	%
Retirement Money Market Fund	\$ 16,776,148	11	\$ 14,432,522	13
Intermediate Bond Fund	\$ 14,653,433	10	\$ 10,914,219	10
US. Equity Index Fund	\$ 20,685,386	14	\$ 16,240,119	15
Growth Company Fund	\$ 11,638,961	8	\$ 5,052,734	5
Magellan Fund	\$ 19,931,777	14	\$ 8,021,122	7
Overseas Fund	\$ 5,292,656	4	\$ 1,597,921	2
Microsoft Stock Fund	\$ 57,716,107	39	\$ 53,422,326	48
	\$ 146,694,468	100	\$ 109,680,963	100

- The fair market value of Microsoft's 401(k) Savings Plus Plan was \$146.7 million at December 31, 1993. This represents a 34% increase from December 31, 1992. The Microsoft Stock Fund continues to represent the majority of the Plan's assets at 39% of total assets. Seventy seven percent of eligible employees participate in the Savings Plus Plan at an average contribution rate of 7%.

Flexible Benefits Program: First Time Enrollment

- Microsoft's new flexible benefits plan "Choice" was rolled out via on-line enrollment to approximately 10,000 eligible domestic employees during Q94-2. The objectives of the new benefits structure were: 1) to introduce a vehicle to control rising benefits costs over time; 2) to increase employee understanding of and accountability for their benefit elections, and; 3) to provide a program that would meet the needs of our diverse workforce while allowing employees the flexibility and freedom to design a benefits package to fit their individual needs. Enrollment results are typical of a first year enrollment in a flexible benefit plan.

Summary of select program elections:

Medical Options	% Participation	Dental Options:	% Participation
New Core Plan	1%	New Core Plan	4%
Current Standard Plan	13%	Current Plan	96%
New Standard Plan	1%		
Current Preferred Plan	74%	Long Term Disability Options:	
New Preferred Plan	3%	New 40% Benefit	3%
Current Group Health	8%	New 50% Benefit	2%
		Current Plan	95%
Stay Fit Option:			
Columbia Health Club	3% *		
PRO Club	39%		
Stay Fit Credits	55%		
No Election	3%		

* 3% participation in Columbia Health Club represents participation by 50% of actual MD&L headcount.

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INFORMATION TECHNOLOGY (IT)

INFORMATION TECHNOLOGY (IT)

IT Application Development & Maintenance

Key Product Releases:

Business Unit/Product	Beta or Production Date	
	Plan	Current Status
Finance & Manufacturing/Distribution Projects:		
APOC commission agent conversion	May-94	May-94
Astro-Online Purchase Orders 1.0	N/A	N/A
BWB 2.0	Mar-94	Mar-94
Canada EDI pilot	Apr-94	Apr-94
EDI	Mar-94	Mar-94
EForm	Jan-94	Production
EOC 1.0 Customer Conversion Begins	Apr-94	Mar-94
EOC 1.0 Software Enabled	Mar-94	Mar-94
EOC Design Complete	Oct-93	Released
Far East commission agent conversion	TBD	TBD
Mac Pac 7.0	Aug-93	Production
MacPac EC/EDI integration	Mar-94	Mar-94
MOLP - Redmond ICON	Dec-93	Jan-94
MPRU version 2.0	Apr-94	Apr-94
MS License 1.0 - Forecasting	Nov-93	Feb-94
MS License 2.0 - Business Services	Mar-94	TBD
NGBS - SAP Conference Room Pilot	Apr-94	Apr-94
OE Imaging (Chameleon)	Nov-93	Released
Platinum	Nov-93	Production
Redmond ICON MacPac 7.1 CID upgrade	Mar-94	Mar-94
UPI 1.0	Aug-93	Production
Human Resource Projects:		
ERS	Jul-93	Production
Flex Benefits 1.0	Oct-93	Production
HR Vantage 1.0	Oct-93	Production
People 1.0-Position Reporting	Jul-94	Jul-94
People 1.0-WW Reporting DB	Jan-94	Jan-94
Internal IT Projects:		
Desktop VTC	Nov-93	Jun-94
Email/Vmail Integration 1.0**	Mar-94	May-94
EMS MS Mail 4.0*	Dec-93	Sep-94
Hermes 1.0	Dec-93	Released
ISDN Rollout	Nov-93	Production
Legacy Outsource	Jan-94	Mar-94
PC Telephone 1.0**	Jan-94	Apr-94
Rhino(TCP) 1.0*	Jan-94	Apr-94
SIAM	Nov-93	Production
Win NT Migration	July-Dec-93	Production
PSS Projects:		
MOS MSC 1.0	N/A	Aug-94
PSS Delta 1.5 Int'l	Dec-93	Released
PSS Delta 1.5 US	9/1/93	Production
PSS WB 2.0 Full Convergence	May-94	Jul-94
Sales & Marketing Projects:		
AFS (Account Forecasting System)	Oct-94	Oct-94
CMS 1.0 (AMS/MBS Enhancements)	Nov-93	Production
CMS 1.1 (Sales Out)	Jun-94	Jul-94
EDI 1.0 Inventory Reporting	Oct-93	Production
IMS (Internal Market Share)	Oct-94	Oct-94
ISWB 1.0	Jan-94	Released
ISWB 1.5 Amplitude	Jan-94	Mar-94
Marketing Exp 1.0	May-94	May-94
MS Manager 1.0	Jul-93	Production
MS Sales 1.0	Jan-94	May-94
MS Sales 1.0 Interim (WWS Clean up)	Nov-93	Production
WAM 1.0	Apr-94	Mar-94

*Delayed due to later than anticipated code development by MS product groups.
 **Delayed due to unanticipated vendor delays.

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INFORMATION TECHNOLOGY (IT)

External Costs for Major Applications:

<u>Project</u>	<u>Fiscal Year</u>	<u>Fiscal YTD</u>	<u>Costs</u>	<u>Status</u>
		<u>Budget</u>		
ISWB		\$899	\$764	Forecast within budget
PSS Workbench		499	190	Forecast within budget
LRS		810*	525	Forecast within budget
MS Sales		842	155	Forecast within budget
NGBS		1,756	190	Forecast within budget
BWB		540**	225	Forecast within budget
WAM		562	285	Forecast within budget

*Funding subsequently increased to \$1,437 to encompass OEM business services.

** Funding subsequently increased to \$607 to encompass further enhancements.

- The above figures represent the introduction of project level reporting within Information Technology. Currently, only the external costs for a project such as contract developers, program manager, and product managers are able to be tracked as a time tracking system has not been installed for internal use. During Q3, various time tracking systems will be evaluated for internal use and one beta tested. It is anticipated that during Q4 all newly initiated development projects will be managed via a time tracking system.
- The applications in development reported above are all in various phases of completion, and utilize different mixes of internal and external resources. Thus, their reported external costs may represent a very small or very significant portion of total development costs. However, all the above projects are forecast to be completed within their appropriate external budgets.

Significant development achievements during Q2 include:

- Continued to refine development framework to implement common worldwide approach.
- Completed Concorde (European Operations Center) design and consolidated the German warehouse.
- Merged the significant systems of MS Canada into MS U.S.
- Reevaluated NGBS (Next Generation Business Systems) vendor which resulted in the selection of SAP as current "Strawman" for conference room pilot of enterprise-wide Finance and MD&L system.
- During the quarter, IT released the following significant new applications (in beta or production) to its customers:
 - Finance and Manufacturing
 - EOC (Concorde) design.
 - MS EForm
 - Human Resources
 - HR Vantage 1.0
 - Flex Benefits 1.0
 - Internal Projects
 - ISDN Rollout
 - PSS
 - Delta 1.5 International (CITS)
 - Sales and Marketing
 - EDI 1.0 (Inventory Reporting)
 - CMS 1.0 (Channel Measurement System - AMS/MBS Enhancements in phase 1.0)
 - ISWB 1.0 (Inside Sales Workbench - Kenai)

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INFORMATION TECHNOLOGY (IT)

Applications currently supported

<u>Client</u>	<u>Applications</u>	<u>% of Total</u>
Corporate Services	14	7 %
Finance	40	20
Human Resources	17	8
Information Technology	12	6
Law & Corporate Affairs	7	3
Microsoft Consulting	4	2
Mfg & Distribution	23	12
Microsoft Press	2	1
Product Service & Support	14	7
Sales & Marketing	<u>67</u>	<u>34</u>
	200	100%

- Approximately 24 applications are supported outside of IT.

IT Infrastructure

- Migrated 819 servers worldwide from OS/2 to NT.
 - Implemented new NT domain structure.
 - Surpassed OS/2 to NT server conversion goal of 90% by converting 92% of servers to NT by December 31st. 200 of IT's 1,094 servers remain on Xenix as mail servers.
- Implemented several new formal network security policies to further secure MS information and technology.
- Implemented first phase (external costs) of a project tracking and reporting system.
- Developed standard business case analysis process to evaluate proposed projects within IT Steering Committees.
- Completed the development of a telecommunications tracking and auditing tool.
 - Preliminary indications suggest significant telecommunication credits due to improper billing.
- Outsource European legacy systems to Andersen Consulting.
 - Continued to evaluate legacy outsource proposal for Redmond legacy systems.

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RECONCILIATION OF CHANNEL AND PRODUCT P&LS TO RESULTS OF OPERATIONS P&L

Q94-2

	Channel				Product Group			
	Actual	% Net Rev	Plan	% Net Rev	Actual	% Net Rev	Plan	% Net Rev
Net revenue	\$1,129	100.0 %	\$1,106	100.0 %	\$1,129	100.0 %	\$1,106	100.0 %
Cost of revenue	185	16.4	193	17.5	185	16.4	193	17.5
Gross profit	944	83.6	913	82.5	944	83.6	913	82.5
Controllable expenses								
People	147	13.0	164	14.8	101	9.0	109	9.8
Facilities	47	4.1	54	4.9	18	1.6	24	2.2
Marketing	103	9.2	110	10.0	103	9.2	107	9.7
Development	3	0.3	4	0.4	30	2.7	46	4.2
Other	38	3.4	22	2.0	28	2.5	17	1.5
PSS	NA	NA	NA	NA	55	4.9	60	5.5
Total controllable expenses	338	29.9	354	32.0	336	29.8	363	32.8
Responsibility margin	606	53.7	559	50.6	608	53.9	550	49.7
Corporate allocations								
Executive	0	0.0	0	0.0	0	0.0	0	0.0
Corporate F&A	34	3.0	38	3.4	34	3.0	38	3.4
Legal	15	1.3	17	1.6	15	1.3	17	1.6
R&D	129	11.4	165	14.9	NA	NA	NA	NA
S&M non-specific *	NA	NA	NA	NA	131	11.6	155	14.0
Other	13	1.2	4	0.4	13	1.2	4	0.4
Total corporate allocations	191	16.9	224	20.2	193	17.1	215	19.4
Total expenses	529	46.9	578	52.2	529	46.9	578	52.2
Contribution margin	\$415	36.8 %	\$335	30.3 %	\$415	36.8 %	\$335	30.3 %

FYTD94

	Actual		Plan		Actual		Plan	
	Actual	% Net Rev	Plan	% Net Rev	Actual	% Net Rev	Plan	% Net Rev
Net revenue	\$2,112	100.0 %	\$1,933	100.0 %	\$2,112	100.0 %	\$1,933	100.0 %
Cost of revenue	344	16.3	328	17.0	344	16.3	328	17.0
Gross profit	1,768	83.7	1,605	83.0	1,768	83.7	1,605	83.0
Controllable expenses								
People	290	13.7	328	17.0	197	9.3	217	11.2
Facilities	92	4.3	106	5.5	35	1.7	48	2.5
Marketing	191	9.0	201	10.4	191	9.1	194	10.0
Development	6	0.3	8	0.4	53	2.5	92	4.8
Other	70	3.3	43	2.2	50	2.4	31	1.6
PSS	0	0.0	0	0.0	106	5.0	119	6.2
Total controllable expenses	649	30.7	687	35.5	633	30.0	700	36.2
Responsibility margin	1,119	53.0	918	47.5	1,135	53.7	905	46.8
Corporate allocations								
Executive	1	0.0	1	0.0	1	0.0	1	0.0
Corporate F&A	65	3.1	76	4.0	65	3.1	76	4.0
Legal	25	1.2	35	1.8	25	1.2	35	1.8
R&D	253	12.0	328	17.0	NA	NA	NA	NA
S&M non-specific *	NA	NA	NA	NA	269	12.8	315	16.3
Other	17	0.8	8	0.4	17	0.8	8	0.4
Total corporate allocations	361	17.1	448	23.2	377	17.8	434	22.5
Total expenses	1,010	47.8	1,134	58.7	1,010	47.8	1,134	58.7
Contribution margin	\$758	35.9 %	\$470	24.3 %	\$758	35.9 %	\$470	24.3 %

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SUPPLEMENTAL INFORMATION

SUPPLEMENTAL INFORMATION

ABBREVIATIONS, ACRONYMS AND TERMS

ABC	Activity Based Costing
ABU	Analysis Business Unit
ACE	Advanced Computing Environment
ACIS	IBM academic pricing program using bundles
AED	Authorized Education Dealer
AI	Artificial Intelligence
AIME	Africa, India & Middle East
APAC	Asia Pacific: Australia, New Zealand, Singapore, Malaysia, Thailand, SE Asia
Apps	Applications
BBS	Bulletin Board System
BIDI	Bidirectional
CN	Campus North
CP	Component Piece
CPU	Central Processing Unit
CSA	Client Server Applications
CSI	Consumer Software, Inc.
DABU	Data Access Business Unit
DAD	Desktop Applications Division
DBCS	Double Type Character Set
DBMS	Database Management Systems
DDT	Database and Development Tools
DK	Dorling Kindersley
DLL	Dynamic Load Library
DOEM	Domestic Original Equipment Manufacturer
Domestic	Redmond, Campus North, Puerto Rico and Workgroup Canada
DOS	Disk Operating System
DSO	Days Sales Outstanding
EBU	Entry Business Unit
ECU	European Currency Unit
EPS	Earnings Per Share
ERISA	Employee Retirement Income Security Act
ESPP	Employee Stock Purchase Plan
EU	Equivalent Units
F&A	Finance and Administrative
FG	Finished Goods
FX	Foreign Exchange
GAAP	Generally Accepted Accounting Principles
G&A	General and Administration
GBU	Graphics Business Unit
GLVR	Government Large Volume Reseller
GUI	Graphical User Interface
GULP	Global Update License Pack
ICON	Intercontinental: Latin America, AIME and APAC regions
IFF	International Focus Factory
IFG	International Finished Goods
IOEM	International Original Equipment Manufacturer
IPG	International Product Group
IPO	Initial Public Offering
IPR	Intellectual Property Rights
ISV	Independent Software Vendor
ITG	Information Technology Group
JIT	Just-In-Time Manufacturing
LCA	Law & Corporate Affairs
LM2	Lan Man 2.0

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SUPPLEMENTAL INFORMATION

Lng Languages
LOI Letter of Intent
LTD Life to Date
LVR Large Volume Reseller
Mac Macintosh
MCS Microsoft Consulting Services
MCD Master Copy Disk
MD&L Manufacturing, Distribution & Logistics
MET Management Expense Tracking
MLP Microsoft License Pak
MS Microsoft
MSJ Microsoft Systems Journal
MSU Microsoft University
NQSO Nonqualified Stock Option
OBU Office Business Unit
ODBC Open Database Connectivity
OEM Original Equipment Manufacturer
OS Operating System
OOS Other Operating Systems
PC Personal Computer
PPB Prepaid Balance
PSS Product Support Services
R&D Research and Development
RM Raw Materials
ROW Rest of World: Far East and ICON channels
S&M Sales and Marketing
SCO Santa Cruz Operation
SDK Software Developer's Kit
SEC Securities and Exchange Commission
SKU Stock Keeping Unit (part number)
SMSD Sales, Marketing and Service Division
SPAG Systems, Peripherals and Accessories Group (hardware)
SRP Suggested Retail Price
Sys Systems
TCN Third Country National
UPB Unspecified Product Billing
Upg Upgrade
USSMD United States Sales, Marketing and Distribution
Var Variance
VEBA Voluntary Employees' Beneficiary Assn.
VGA Video Graphics Array
VPP Volume Purchase Program
WCM World Class Manufacturing
WGA Workgroup Applications
WGC Microsoft Workgroup Canada
Win Windows
Wks Works
WOG Worldwide Operations Group
WPG Worldwide Products Group
WRK Workgroup
WWS Worldwide Sales
WSSG Worldwide Sales & Support Group
WW Worldwide
XLA Extended License Agreement
XLL Excel Load Library

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CREDIT RATING DEFINITIONS

Investment Grade

- AAA Capacity to pay interest and principal extremely strong.
- AA Capacity to pay interest and principal very strong.
- A Capacity to pay interest and principal strong.
- BBB Capacity to pay interest and principal adequate.
- MS Rated This category consists of securities which may not carry a published rating but for which MS Treasury has conducted credit research and assigned an implied investment grade rating. An example is City of Redmond LID bond anticipation notes.

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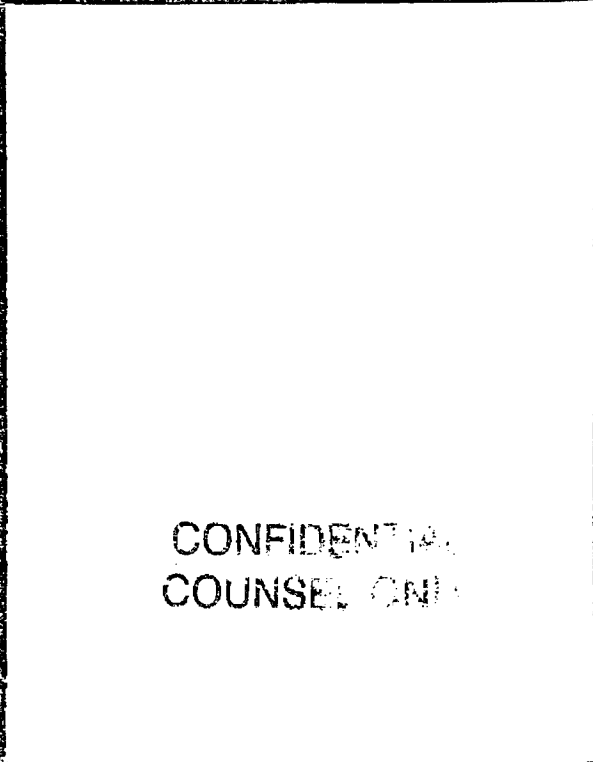
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