

Author: Robert Olstad at SERVER1
Date: 8/21/97 12:51 PM
Priority: Normal
TO: Laura F. Lee at Orchid
Subject: RE: Re[2]: Aspire 5 Titles

----- Message Contents -----

Rob,

I had a good trip but unfortunately it was a quick one. Other than the limo to/from the airport we didn't venture more than 3 blocks from our hotel! I didn't see Mike while I was there but did see Ronald at the S.F. airport, he was on the same flight we were.

Thank you for your comments below. They provided me with some concrete examples I could use to demonstrate to our product group your concerns about our OEM business model for consumer applications. They agreed, as I do, that many of your arguments are valid. After talking with them though, I believe our current business model also has validity and that this is one of those cases where one of us isn't right and the other wrong, but instead we are just looking at two different sides of the same coin.

Below are some summary comments addressing your concerns. Let's talk further over the next few days.

* I plan to continue addressing replication costs by working with our product group to minimize the requirements. For this bundle, I hope to be able to make all manuals and frontliners optional components. In your example then, the first product would cost \$1.25 and each additional product \$.99 because of the combined MPI card. The only big piece remaining is the \$.37 for "assembly" and I'm not sure what that's for. I assume this is the cost of Stream's "service", but if so, wouldn't there also be an assembly cost associated with our competitors products? Regardless, I'm sure our costs are higher because our requirements are higher, but this is a big improvement over what you are paying today which I believe is \$1.70+/title.

* Today, we have a similar business model to our competition for many of our "Standard" titles. These titles are usually priced under \$5 and many are in the \$1-\$2 range. These include titles such as Money, Kids Plus!, Arcade, Fury3, Space Simulator, Creative Writer, Dinosaurs, Wine Guide, and many more. The idea here is to get marketshare, drive upgrades, or maximize a product's life and revenue stream. On the other hand, we have a different business model for our "Premium" titles. These titles are usually >\$5 and include Works, Publisher, Picture it!, DreamWorks, Deadly Tide, Flight Simulator, Bookshelf, Encarta, and others. Our goal here is to get marketshare and drive upgrades but still command a more reasonable royalty.

* Selling SW through OEMs at \$1-\$2, even with future upgrade revenue (which is usually limited), is not a sustainable business model for ISVs. You mentioned how extremely profitable it is for ISVs to offer titles at \$1-\$2, but the truth is our consumer apps business is not profitable today (CONFIDENTIAL), even at our higher ASPs. We are taking a very long-term approach, so unlike many of our competitors, years from now we will still be producing very high quality titles.

* Like our retail pricing, the OEM ASP for consumer apps has decreased over time. I have been in OEM almost 3 years and have regularly seen our pricing drop. Usually this was done to better our competitive position or reflect the decreases in retail pricing as you described.

* I am still investigating what we can offer for the \$999 PC. Would be great if we could get Works or Works/Money on it. May need

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some more info from you on quantity, which retailers, etc.

I just got your VM message. 9:00am on Tuesday is good, talk to you then!

Thanks,
Bob

> -----Original Message-----

> From: Robert Olstad [SMTP:rolstad@smtplink.acer.com]

> Sent: Tuesday, April 22, 1997 7:46 AM

> To: Bob Chapman; rolstad@smtplink.acer.com

> Subject: Re[2]: Aspire 5 Titles

>

> Hi Bob:

>

> Hope your are having a wonderful time meeting with the folks at Acer
> in

> "Beautiful" Taipei. We'll at least the weather should be decent.

> Culver's actually out there as well. I am providing you a somewhat

> lengthy e-mail summarizing my thoughts and comments for your

> information

> and which I would like to use as a basis for a future discussion.

>

> The material costs I outlined to you reflect the new MPI card format.

>

> Here is the cost outline for Works/Money:

>

> CD \$.53

> COA \$.18

> MPI Card \$.08

> Frontliner \$.28 (I would like to delete this for each
> product if possible to save costs)

> CD Sleeve \$.04

> Assembly \$.37

> Export Lbl \$.05

> -----

> Total \$1.53

>

> We always negotiate with Stream and also bid out to other replicators

> on

> the Micorsoft items so the above costs from Stream are competitive.

>

> The cost for ANY non-MS product is currently:

>

> CD \$.53

> CD Sleeve \$.05

> -----

> Total \$.58

>

> So, in the case of Works/Money, the MS title is almost \$.95 higher

> (uncompetitive) right from the get-go not to mention the 1/4 person I

> need to allocate to manage the on-going MS consumer Apps logistics.

> Again, we must view and recognize all costs (Royalty, COGS, Logistics)

>

> associated with each title and burden the product line accordingly.

>

> The material cost is only one issue and by the way I thank you for

> your

> help so far in helping us drive down some of these costs. Here are

> some

> others:

>

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> MS Royalty vs. MS Street Price:

> -----

> Based on my recent research, our current value pack bundle has a
> confirmed street price/value of \$99.99 while the proposed bundle has a
>
> street price/value of \$104.99.

>
> The other is just royalty cost:

>
> Current Acer Current (Source Acer Royalty =
> \$9

> MS Consumer Street All, COMPUSA Fremont, CA)
> Prices

> -----

> Works \$39.99 After \$10 Mfgs Rebate
> Money \$0
> Encarta \$39.99 After \$10 Mfgs Rebate
> Trip Planner \$24.99 After \$15 Mfgs Rebate

> -----

> Total \$104.99

> -----

> Current Acer Current (Source COMPUSA,
> Consumer Value Street Best Buy, Dallas)
> Pack Prices Fry's, Fremont).

> -----

> Works \$39.95 After \$10 Rebate, CompUSA, Fremont
> Money \$0
> 3D Movie Maker \$39.95 No rebate, Fry's, Fremont
> Magic School \$29.95 No rebate, Best Buy, Dallas

> -----

> Total \$99.99

> -----

> Currently, MS is pricing their OEM titles (s/w royalties) at around
> 10%
> of street price and in the case of Works alone 20% of street. I would
>
> like to see this at 5% of street or less as well as compensation for
> the
> higher MS material costs. In the past, MS consumer titles used to
> carry
> a premium in retail and warranted paying a royalty premium. Also, the
>
> ASP for these titles used to be very high so the consumer, in buying a
>
> system with these titles, would associate more value to the system
> purchase. Now, MS has crashed its ASP's on its consumer Apps through
> pricing and promotional actions as a result of heavy competition in
> the
> retail channel so that now, a MS title costs just as much as any
> competing title in that category. As a result, the consumer value
> proposition as it relates to systems bundled with MS software (or
> quite
> frankly any s/w) has diminished. MS is appropriately focused on
> maintaining OEM revenue/unit and ASP's/unit on consumer apps but this
> is
> totally opposite to the realities that happened during the last two
> years of MS price competition and down ward price trends in the retail
>
> channel. I believe that MS needs to adjust its OEM pricing strategy
> to
> be more in alignment with how the retail market has settled out.

> -----

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> Again, we talked about this topic two months ago where we also did a
> small whiteboard session together in my office outlining how
> extremely
> profitable the MS OEM consumer application business is even at
> royalties
> that approach what other vendors EASILY offer for these types of
> titles
> in these categories (I.E. no higher than \$1.5 royalty). We spoke
> earlier on in the year about MS OEM pricing strategy and you mentioned
>
> that the product group is getting more realistic on their royalties.
> I
> would really like to see MS work with us on royalties and of course
> material costs, we can in return help promote your strategic titles
> and
> MS follow on business via s/w upgrades (i.e. Works 98, ect..). This
> how
> we both win.
>
> When we chose the value pack, 3D Movie Maker was the hot MS title that
>
> Bill Gates himself demonstrated at 1996 Winhec Conference as the
> compelling MS direct 3D game. MS normally prices their little kids
> games at \$29 and normal games (monster trucks, hellbender, ect...) at
> \$39. Electronic Arts, and most other games companies also price their
>
> game titles typically at the \$39 price as well. The value pack deal
> we
> did last year was within reason at the time but quite frankly, our
> total
> s/w budget for Aspire 5 is even less now. There's just not a lot of
> \$'s
> to play with here. As you know, our S/W strategy has been to furthur
> reduce the number of titles to increase customer service, to make our
> systems more cost competitive and consequently more affordable. We
> are
> positioning our systems to address both the value concious and price
> sensitive consumer segment with a unique differentiated product. We
> continue to maintain solid relationships with our retailers and are
> building new relationships as well (yes even CompUSA) so Acer's
> business
> prospects as well as an Acer/MS partnership look very promising and
> mutually beneficial.
>
> What I need your help on is communicating the some of above issues as
> well as our stratgy to the product groups as well as some of the
> parameters and business realities in which we must operate within. As
>
> it stands right now, I believe it would probably be best to focus on
> the
> core bundle I mentioned above and see how we can fit these strategic
> titles into the line-up.
>
> Best Regards,
>
>
>
> Robert Olstad
> 4/22/97
>
> We can work on this via email this week or talk on Monday when I
> return

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> to the office. Here are some of my initial comments:
 > * I think we can continue to improve the material costs by moving
 > to an MPI card (incl. a single COA, EULA, Reg Card) for the whole
 > bundle. Besides this, you would have only the CDs and frontliners for
 >
 > each product. I can talk to the product and operations groups about
 > not
 > requiring frontliners as well. I would also suggest getting price
 > quotes from other ARs to make sure Stream is being competitive.
 > * Your cost for Works only would not be any less than the
 > Works/Money (full version) combo.
 > * In order for me to put together the type of deal we've discussed
 > (low bundle pricing, recoupmnt of Office PPB, etc.), I need you guys
 > to
 > ship at the least Encarta, Works, Money, and Trip Planner. Also, you
 > shouldn't assume that shipping less titles than we proposed will
 > dramatically reduce the bundle royalty. Those 6 titles (above 4 +
 > Plus!
 > for Kids + Bookshelf) were all strategic to MS and the \$20 we proposed
 >
 > was aggressively discounted because you were shipping them all. My
 > thinking is not shipping Plus! for Kids doesn't save you any \$\$
 > (except
 > COGS), and not shipping Bookshelf maybe will save you \$1-\$2.
 > * On the low-cost PC (\$999), I would like to see Works/Money but
 > not sure how low on royalty we could go. I need to talk with some
 > people about this but my guess is we wouldn't get anywhere close to
 > \$1,
 > but probably better than the \$8 you pay today. I'm sure some
 > precedent
 > has already been set here but I'm not sure what that is.

> > -----Original Message-----

> > From: Robert Olstad [SMTP:rolstad@smtplink.acer.com]
 > > Sent: Monday, April 21, 1997 7:15 AM
 > > To: Bob Chapman
 > > Subject: Aspire 5 Titles

> >
 > > Hi Bob, I have been looking at our Aspire 5 s/w line up and
 > > would
 > > like
 > > to talk to you. The high material costs are painful as well
 > > and
 > > are
 > > limiting the flesibility. I will not be able to afford the
 > > line
 > > up
 > > you presented to me last month so I would like to talk to you
 > > about an
 > > alternate more scaled back line up:
 > > *
 > > MS Works Productivity Category
 > > MS Money Personal Finance Category
 > > Could delete this to save royalty as we
 > > can get Quicken SE for Free. Yes, Quicken
 > > is
 > > crippled but it nonetheless would fulfil
 > > our Home Finance Category. My understanding
 > > is that MS Money is kinda a free title
 > > anyway.
 > > We
 > > would be open to continuing to carry Home

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> > Banking
> > Edition if there is any royalty for the full
> > edition
> > Material Costs (Works/Money)= \$1.53
> Including
> > CD
> > MS Encarta Fulfill Reference Category
> > Material Costs = \$1.34 (Can we delete the
> > Frontliner \$.28).
> > These three would be the core MS line up for the Aspire.
> > Depending on
> > the royalty and material costs, we may be able to "fit" in MS
> > Trip
> > Planner => Home/Hobby Category.
> > White PC I would like to keep it the same same
> > (Word/Bookshelf).
> > We also plan to have a \$999 type low cost PC. At this time, we
> > plan
> > only to have utilities, Win 95, maybe a Works only type
> > products.
> > For example, like a Works for \$1 royalty only for this low/low
> > end
> > product.
> > As we need to finalize the line up soon, please give me a call
> > to
> > discuss.
> > Regards,
> > Robert Olstad

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; Mon, 28 Apr 97 18:26:24 pst

Return-Path: <bobche@MICROSOFT.COM>

Received: by INET-02-IMC with Internet Mail Service (5.0.1458.14)

id <J5AR6VYN>; Mon, 28 Apr 1997 18:09:32 -0700

Message-ID: <D6135F3835AAD011ACAC00805F145D173122A3@RED-73-MSG.dns.microsoft.com>

From: Bob Chapman <bobche@MICROSOFT.COM>

To: Robert Olstad <rolstad@smtpink.acer.com>

Subject: RE: Re[2]: Aspire 5 Titles

Date: Mon, 28 Apr 1997 18:12:04 -0700

X-Priority: 3

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