From:	Deborah Black
Sent:	Saturday, April 15, 2000 2:12 PM
To:	Steve Ballmer
Cc:	Jim Allchin; Paul Maritz; Eric Rudder; Arne Josefsberg; Dan Neault; Brian Valentine; Bill Gates
Subject:	RE: Windows management

We've completed our analysis of NetIQ, and moved on to look more broadly at other 3rd party solutions including Mission Critical's OnePoint Operations Manager and HP's VantagePoint.

From an operations management *feature* perspective, both OnePoint and VantagePoint look very good. We've installed and evaluated both solutions in a lab setting. ITG uses Mission Critical s/w today to manage servers. It scales well for them, and they are excited about OnePoint. We don't have first hand experience with VantagePoint in a live data center, but ITG has offered to help us evaluate it, and we plan to speak with HP customers who are deploying it in order to understand how well it scales for them.

From a management *infrastructure* perspective, VantagePoint looks like a stronger choice. It is based on WMI, and has the potential of offering us useful infrastructure pieces, which we could leverage across all Windows mgmt solutions. We have begun to discuss a possible relationship with HP around VantagePoint. We don't have anything concrete yet, but are expecting HP to propose some alternatives to us within the next week. I expect they will include both licensing and joint sales ideas.

Take a quick look at these. They are a set of slides we used to brief JimAll on our progress last week, and a summary of the HP discussion to date. Dan Neault has been key in this. We'll send an update to this list after we see what HP proposes.

4.14.2000.ppt (53
KB)

We are scheduled to review our progress on Management with BillG on 4/27 1-4:00, where we'll present our current thinking on mgmt infrastructure, operations mgmt solutions, mgmt services, and the future of SMS. JimAll and I also had some time on 4/25 scheduled to brainstorm on mgmt with you per your previous offer, but it looks like it's gone. I'll check and ensure that you are either at the BillG review, or that we indeed have separate time with you this month if possible.

debbie

-----Original Message-----
From:	Steve Ballmer
Sent:	Friday, April 14, 2000 2:36 PM
To:	Deborah Black; Bill Gates; Brian Valentine
Cc:	Jim Allchin; Paul Maritz; Eric Rudder; Arne Josefsberg; Casey Kiernan; Irena Hudis
Subject:	RE: Windows management

Where do you guys stand on your analysis

-----Original Message-----
From: Deborah Black
Sent: Wednesday, March 15, 2000 5:12 PM
To: Bill Gates; Brian Valentine
Cc: Jim Allchin; Paul Maritz; Eric Rudder; Arne Josefsberg; Steve Ballmer; Casey Kiernan; Irena Hudis
Subject: RE: Windows management

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I agree with Arne's analysis completely. I will definately speak with him.

I am convinced that we need to look an an acquisition to jumpstart our server mgmt solution. It would literally take us years to create a solution as strong as NetIQ's. Our customers are thrilled with NetIQ -- they just want if from us, so that they can count on it being there 3 yrs from now -- and to give them a sense that we are serious about providing a complete enterprise solution. This wouldn't solve our whole problem, but would be a great start.

We're analyzing all of the possibilities and will make a specific recommendation asap - by the end of the month.

debbie

-----Original Message-----
From: Bill Gates
Sent: Wednesday, March 15, 2000 11:32 AM
To: Deborah Black; Brian Valentine
Cc: Jim Allchin; Paul Mantz; Eric Rudder; Arne Josefsberg; Steve Ballmer; Casey Kiernan; Irena Hudis
Subject: FW: Windows management

Arne is very articulate here about the challenge.

I think there is a real question of whether we should just keep getting somewhat better on our own course or if we need to supercharge our efforts with an expensive acquisition.

Getting the acquisition on the same architecture and getting a coherent plan would be hard.

I encourage you to talk more with Arne about his views here. Linux scares me the most!

-----Original Message-----
From: Arne Josefsberg
Sent: Tuesday, March 14, 2000 11:49 PM
To: Steve Ballmer; Bill Gates
Subject: Windows management

We are under attack from Linux in the data center space. While Windows 2000 makes great strides in improving in reliability and scalability, we should expect Linux (and Solaris) to also continue to improve at a rapid pace.
There is one area where we can make an investment to really distinguish Win2000/NGWS) and where competition will have hard time to keep up: in the area of manageability.
The following actions should be taken:
We need to form a windows management division, solely focused on making Win2000/NGWS and all the applications running on it the most manageable platform by far. We should combine all our various efforts in the management space into this. This group needs to be seeded with IT staff that have a core understanding of the enterprise IT management requirements.
We should acquire an event management company while they are still reasonably priced, such as Sentry/NetIQ, Micromuse etc. This should form the core of the management division. It's totally non-credible to ask our enterprise customers to invest millions in Microsoft s/w, and then refer them to a tiny third party to get the management software to manage it all.
We need to better define and implement a consistent hierarchy/taxonomy for NT events and perf counters. These are the lifeblood of managing an NT environment, but anarchy rules today. In our own data center environment our servers generate 25-30M NT events per day. A lot of them make no sense to the operator in the NOC. We need NT events classified in a common taxonomy. We should leverage our extensive relationships with ISVs and groups like DRG to evangelize this taxonomy and ensure the taxonomy is applied by the ISV community. The end result should be that any application running on Win2000/NGWS will conform to this model and the events generated are meaningful and can be sorted, prioritized and acted upon via the event management systems. The analogy here is the work that Microsoft did on a common style guide for Windows applications. Learn to use one Windows application and you can practically use them all. Same approach should be applied to server applications and the events they generate. Learn to manage one and you can manage them all. This will be a huge competitive advantage for NT from the CIO/IT perspective in helping to dramatically driving down both complexity and TCO. There is no way the Linux community could pull this off, they don't have our ISV relationships, our marketing/DRG resources etc.
The SMS work should be integrated into this windows management division.
We should also integrate the MOF (Microsoft Operations Framework) work done in the enterprise group into this division. These are the people that document/define a set of common definitions and best practices/procedures for how to manage an NT environment.

Linux is gaining momentum in the service provider and IT space. We have a huge opportunity to make NT the obvious

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choice for the CIO by making it simplest/easiest platform to manage, helping the CIO to drive down the complexity and cost of managing his/her data center environment. With the huge shortage of IT pro staff in both North America and Europe it's not just a matter of cost today. CIO's just can't find people to manage the complexity of their environments, even if they had the funding.

thanks

      Arne

Management Analysis

4.14.2000

Thumbnail Comparison

	NetIQ	MCS	HP Vantage Point
Description	Performance and application monitoring tool	MS technology specific enterprise management toolset	Heterogeneous ops monitoring. Win2000 WMI & MMC based
Functionality (0-10)	3.9	5.3	6.3
Whistler overlap / code harvest %	70%	80%	85%
Long-term usable / beyond 3 years %	15%	60%	70%
Time to market lead v. make	12-18 months	18-24 months	24-36 months
Asset effort (staff-years)	50-100	75-125	150-200
Build cost at $250K/staff-year ($M)	17.5	25	42.5
Protected IP/patents	at least 3	none known	none known
Technical staff	53	64	100 WMI, 200 Mgmt
Marketing staff	82	108	unknown N/A
Perceived as Enterprise player	partially	partially	#3 v. Tivoli & CA
FY00 Revenues	$38M	$43M	~ < $20M
Projected FY 01 Revenues	$55M	$64M	unknown
Sales Channel/Method	Indirect; MS channel	Direct; tgt MS LORG	Direct, some indirect

Valuation Analysis
How we looked at NetIQ & MCS

- Raw asset/make costs for each of N and M
  - Code asset: Heads * time, true costs of $250K/yr & up based on skill
  - Value for any IP
  - Value for team of skilled persons and management
- Traditional: comparable analysis. Unlikely to justify.
  - Analyze market segmented for risk, unlever for debt, determine fair risk multiple, value at their financial performance
  - Decompose comparables by metrics (e.g. $/per-dev) and scale up
- True value to Msft
  - Raw asset/make costs
  - Value for this product offering stand-alone
  - Increased sales of OS products
    - Sum of impacts (category*% increased sales*revenue)
  - Value of "signal" to the marketplace, outside bounds of OS sales
    - Account influence, accelerated decision-making

MCS/NetIQ Merger Analysis

- Of equals, stock swap, new company name
  - NetIQ Cap $600M, IPO 7/20/99 $16.75, now ~35, ~$38M FY00
  - MCS Cap $550M, IPO 8/5/99 $25.5, now ~33 ~$43M FY00
  - Ganymede private $172M in MCS acquisition, $10M trailing
  - Market cap halved in recent weeks
- Merger May/June: 3/28 HSR early termination, HSR closed, schedule stockholders to vote.
- Walk-away clause per SEC filings, amount unknown
- Either party should be free to entertain better offers (note stockholders vote)
  - Can identify issues with current merger plan
  - Can make a "better" offer
  - Analysts recommending buy/strong buy, 20-30x trailing revenues
- Should not approach NetIQ or MCS unless high confidence (80% +) will act, avoid tortuous interference claims

Valuation Analysis Preliminary Results

- "Valuation" observations for each of MCS & NetIQ based on public reports
  - Focus on product needs "ignored or under-served by ... larger competitors"
  - Have overblown to analysts their relationships with Msft
- Raw asset/make costs and utility for Msft – hard to justify even $100M
  - "Good": NetIQ - 100 syears * 70% usable * $250K = $17.5M
    - 53 technical staff, 3 patents, 12-18 month lead time
  - "Better": MCS - 125 syears * 80% usable * $250K = $25M
    - 64 technical staff, no known patents, 18-24 month lead time
  - "Best": HP VantagePoint (part of OpenView) - 200 syears * 85% usable * $250K = $42.5M
    - $25M HP investment from marketing discussion with HP
    - Est. 50 technical, no known patents, 24-36 month lead time
- Conventional comparable analysis – $100M-300M
  - BDI rough estimate (working on details) $200-$300M for each of NetIQ & MCS
  - HP's previous ~ equiv product earned ~ half the revenues of NetIQ or MCS
- Management offering as isolated business – $1B-$3.25B
  - Revenue stream w/abrupt sunset: Present value of 25% of Win32 Perf. & Networking Perf. Revenue (IDC estimates of market, 5% disc. rate, 5 year period, no residual value) ~ $1B
  - Market: FY 01 MCS + NetIQ rev. ~ $130M (17% of IDC estimates) @ 20x mult = $3.25B
- Incremental 5% of Win2000 Server and Workstation "ballpark" ~ $1B
  - Each of Server and Workstation ~ $2B (rough) * 5% = $100M each
  - $ slope up, life = reinvention time of 2-3 years (but others innovate) ~ 5x $100M each

Engagement with MCS

- Met 4/12 with VP development, CTO, and VP business development
  - Fishing for Microsoft futures, but also realized Msft eventing work overlap
  - MCS offer: if Msft build technology that overlaps with theirs, Msft license theirs to get to market faster (no hint they knew of our internal analysis)
  - Mentioned that CTO will be CTO of merged company
  - Merger expected to close merger within the next month
  - Asked us point blank if we had any plans to build and offer what they market
- Msft messages
  - MCS has already seen high level references to our planned event infrastructure & within a few weeks we expect to give them more details
  - As a matter of fact, customers using Windows 2000 in highly demanding situations are giving us feedback on what they would like us to offer directly
  - We are considering our 3-5 year timeframe product offering and appreciate their invitation to us to have a discussion about licensing
- No follow-up actions except including them in early ISV discussions
  - No plan to pursue business discussions until closure on HP possibilities & clear understanding of Msft future plans

Engagement with HP

- Best technical solution appears to be VantagePoint, other points:
  - Team is in Germany so relocation difficult
  - Less perturbing to ISV marketplace than acquiring MCS or NetIQ or both
  - While valuable technology for HP, strong interest in field collaboration
    - JeffR 3-year go-to-market discussions with Ann Livermore & Tom Ashburn
- In April marketing meetings, HP product mgr (PUM+?) Christoph Pfister expressed interest in bundle, "integration"
- JimAll mail to Duane Zitzner confirming Duane owns VantagePoint: Yes.
- DNeault favorable discussion 4/13 with Pfister on license, engineering support; Pfister list of deal points by end of 4/17 week. Issues touched upon:
  - Msft control over features, future, no restraints on working with other OEMs
  - Msft not offer non-Windows support at outset, but can and can enable others
  - Need engineering support, including on site at Msft
  - Avoided pitching on up-sell, but HP drew own conclusions
- JimAll to send reply to Duane:
  - Make Duane aware of initial discussions with Christoph Pfister about a license
  - If Duane supports, good opportunity for both companies
  - In interests of efficiency, is Christoph the appropriate contact?