

PRISM 2002 FY03 Discussion Guide

Windows Client Breakout
Rogers Weed

Afternoon

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Windows Client Day 3 Agenda

Planning Assumptions (30 minutes)

- Business overview
 - Key challenges
 - Customer satisfaction
 - Feedback from the field
- Product roadmap

FY03 Strategies (2.5 hours)

- Segment situation
- Themes and initiatives
- Strategies per segment (EPG, SMB, consumer, OEM)
- Revenue review and targets

Prioritization/Summary (30 minutes)

Key Challenges

Business

- PC sales declining
- Pro mix gains are not a given, especially in SORG
- Sustaining launch excitement
- SA value
- Linux share flat but gaining mindshare, particularly in gov't and education
- Piracy flat to increasing

Customers

- Support IPU higher than expected, some challenges at launch
- Resistance to Activation
- Security concern on the desktop and server

Partners

- Ecosystem quality and profitability
- OEMs obscuring the Windows Experience

Customer Satisfaction and Feedback

Feedback		Top Issues/Needs								
	FY02 H1 data except as noted	Cost				Customer Sat (launch + 3 mos.)***				
		IPU*	MPI	Cost/Min**	CPI	Cost per Unit Sold	Support		Product	
						% Vsat	% Dissat	% Vsat	% Dissat	
PSS	Win 98	0.20	64	\$1.21	\$77	\$15	68%	11%	53%	8%
	Win ME	0.17	99	\$1.21	\$119	\$20	66%	12%	36%	19%
	Win 2K Pro	0.25	143	\$1.89	\$270	\$67	76%	6%	42%	15%
	Win XP	0.22	78	\$1.21	\$91	\$20	58%	18%	37%	18%
		* XP projected ** Win9X cost data reflects current PSS costs. *** Win98 data reflects last 6 months								
	US Call Centers									
	OEM (WinXP)	<ul style="list-style-type: none"> • Dell: Seeing 50% of expected volume. • HP: Seeing 25% of expected volume. • Gateway: Decline in calls; 10% improvement in solve rate. 								
Windows	Crash Data	<ul style="list-style-type: none"> • Approx. 850,000 crashes per day reported via OCA/WER • IE generates 13% of calls. 44% are MS-non IE, 33% 3rd-party, 9% misc. 								

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Feedback from the Field

Feedback	Top Issues/Needs	Actions/Comment
SMG & MCS	Product <ul style="list-style-type: none"> • Security deficiencies have damaged our reputation, hindered our sales productivity, and created barriers to sales. • Our efforts to increase customer satisfaction are ineffective, fragmented and we lack a customer-centered culture. • Licensing instability and lack of customer lead time for the change has created adversarial relationships with customers. XP PUR for auto-update capabilities is a potential issue for LORGs and PR. • Desktop OS Deployment across a large organization is still very time consuming exercise and one in which it takes folks with 10-20K desktops at least 12 months to do at very high costs. 	<ul style="list-style-type: none"> • February security push underway. CERT to audit and advise. • Dev focus to mine and address crash data. • Product group undertaking community engagement. • Documented how to disable auto update. No PUR change needed. See microsoft.com/windowsxp/faq/faq/updates/updates/updates/default.asp • Windows PMG and US SMG are aggregating info and tools to facilitate XP deployments. Will get even better with Longhorn.
	Marketing <ul style="list-style-type: none"> • Marginal cross-product marketing integration (e.g. Windows & Office). • Lack of XP-only killer applications (business, consumer). • Lack of an integrated set of product offerings and coordinated strategy to increase home penetration. • Internationalization of online resources (catalog, update, activation) • Need greater investment in International Windows evangelism. • Need a step-up SKU from Home to Pro. 	<ul style="list-style-type: none"> • Working w Office PMG to deliver XP Desktop initiative in FY03. • Developing integrated Windows consumer product strategy. • Exploring localization effort of online resources. • Proposing to resource regional Windows evangelists in FY03. • Investigating limited-time Open step-up SKU for SORGs.
	PC Ecosystem <ul style="list-style-type: none"> • XP launch great big for ecosystem, but not sustainable. • Microsoft-led ecosystem improvement programs compete with Intel Inside. • Greater alignment needed between OEM and retail policies and programs. 	<ul style="list-style-type: none"> • Use Tablet, Mira, Freestyle, Corona, & MSNB to sustain excitement. • New Intel relationship team of six reporting directly to BrianV. • Introducing Windows Catalog to all tier-1 subs (13 localizations).
	Public Relations <ul style="list-style-type: none"> • Very bad perception of security in our products & processes in the press. • Negative PR and customer distrust over XP service integration (passport, activation, registration). • Confusion on licensing 6.0, activation and registration. • PR weapon blunted by 9/11 tragedy. 	<ul style="list-style-type: none"> • February security push, Trustworthy Computing Initiative. • Considering a 'security day' at the end of our push to talk more about what we have done and to share tools and learnings with the industry. • SPI consent degree changes address service integration.
	Competition <ul style="list-style-type: none"> • Linux on desktop a challenge where Windows viewed as overly complex / costly - easy port when moving apps from LINUX to Intel - growth in developing countries in gov, edu and SMB (India, China, Taiwan, France, Germany, Brazil). • Sun is using customer dissatisfaction & licensing changes as a lever for Star Office on Linux - going after the DMR channel with a focus on Insight and CDW. 	<ul style="list-style-type: none"> • TCO content/evidence on Linux due from PMG in May 02. • PMG investigating Linux-competitive TS client for legacy PCs. • PMG to brief analysts/press when the TCO analysis is completed.

Client Roadmap

	FY 02				FY 03				FY 04				FY 05				FY 06			
Fiscal Year	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	CY 02				CY 03				CY 04				CY 05							
Calendar Year	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Windows Client	▲ Windows XP								▲ Windows "Longhorn"											
	▲ SP 1								Aligned with Office.NET											
	▲ Tablet PC								▲ Tablet PC "v2"											
	▲ eHome "Freestyle"								▲ eHome "Slalom"											
Other Releases	▲ IE 6.0				▲ Windows Media "Corona"															
Embedded	▲ Windows XP Embedded																			
	▲ Windows CE Talisker																			
	▲ Mira								▲ Windows CE Maccallan											

Windows XP Service Pack 1

Includes

- QFE rollup
- Consent Decree updates
- Updates to enable new PC scenarios
 - Tablet PC, Freestyle, and Mira
- Common Language Runtime as a separate install
- Top security fixes
- Other changes that 1) make the schedule, 2) do not affect compatibility or 3) change the default user interface

Schedule

- Target RTM is August
- Dependent on results of Security month
- .NET Server will ship separately and later

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FY03 Strategies (2.5 hours)

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- Strategies per segment (EPG, SMB, consumer, OEM)
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Prioritization/Summary (30 minutes)

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Segment Situation

Enterprise

- Pro mix on new PCs in FY02 ~70%, up from ~50% in FY01. 1% incremental=\$10MM (Finance)
- ~35% of enterprise desktops in US are still running Win9x (Oct01 Business Desktop OS Tracker)
 - 13% of new LORG desktops and 39% of new LORG laptops are running Win9x (new=w/in 6mos)
- WinXP knowledge jumped from Oct to Dec in US, but still 50% of LORGs know nothing/very little (Dec01 WinXP BP/DIU)
- Linux continues to gain mindshare, though penetration remains flat in US (Oct01 Business Desktop OS Tracker)
- Dissatisfaction with Licensing 6.0 & annuity rollout; unclear SA value (MYR feedback)

Medium Enterprise

- Pro mix on new PCs in FY02 ~55%, up from ~40% in FY01. 1% incremental=\$7MM (Finance)
- ~60% of medium enterprise desktops in US are still running Win9x (Oct01 Business Desktop OS Tracker)
- Need to drive evaluation - 70% are either planning to evaluate or have no plans to evaluate (Oct01 Biz DT OS Tracker)
- Knowledge of WinXP has tripled to 16% from Oct to Dec in US, but 63% still know nothing/very little (Dec01 BP/DIU)

SORG

- OEM Pro mix @ 33% of SORG PC ships; 1% incremental=\$5m (Finance)
- 25-30m XP capable SORG PCs; 1% upgrade = \$40m
- Low knowledge and intent to evaluate Windows XP in SORG - 55% of US SORGs claim to "know nothing" about Windows XP. 66% have no plans to evaluate (Dec01 WinXP Business Purchase/Deployment Intent Update)
- SORGs rapidly adopting networks (incl wireless) - 7% to 12% of SORGs plan on adopting a LAN. Larger markets planning on Wireless LAN: 2% US, 8% UK, 18% in Germany, France 7%. (AMI Research)
- Application compatibility a big issue for SORGs - 25% consider compatibility a barrier to XP adoption. (Oct01 Tracker)

Consumer

- WW Home PC penetration = 16% (Yellowbook)
- 39M PCs shipped into Home WW in FY02, -9% Y/Y growth (Finance)
- Average WW Home PC lifecycle extending to 4-4.5 years (Internal)
- WW WinXP awareness among technology-engaged end users 60-80% in major subs (Windows XP Global Ad Tracking Study)
- 5% of capable IB WW has upgraded to WinXP (Finance)

OEM

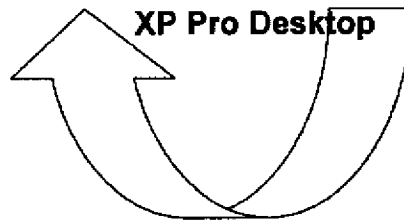
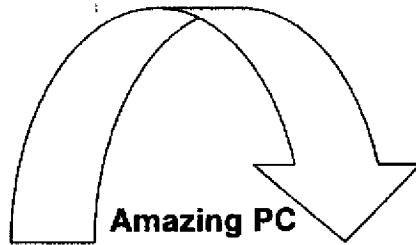
- PC growth -6% in FY02
- FY02 Pro Mix 22% to 31% to contribute \$387M in revenue
- Lack of SORG PCs with XP Pro at retail

FY03 Top-level Themes

- **Pro Mix! Pro Mix! Pro Mix!**
 - Include Windows XP Pro in licensing push
 - 100% Pro on notebooks across all segments
 - Drive Pro adoption in SORG by arming and orchestrating partners
 - Stretch goal – 100% Windows XP Pro on new business PCs
 - Drive Pro mix at retail
- Accelerate deployments by removing blockers, promoting business value
- Increase mainstream adoption by growing the enthusiast base and stimulating PC Excitement with new product launches
- Demonstrate clear customer value versus Linux on desktop, focus on a plan for higher education and government
- PMG to invest in understanding emerging geographies with a focus on Brazil, Russia, India, and PRC

Making It Happen -- Two Key Initiatives

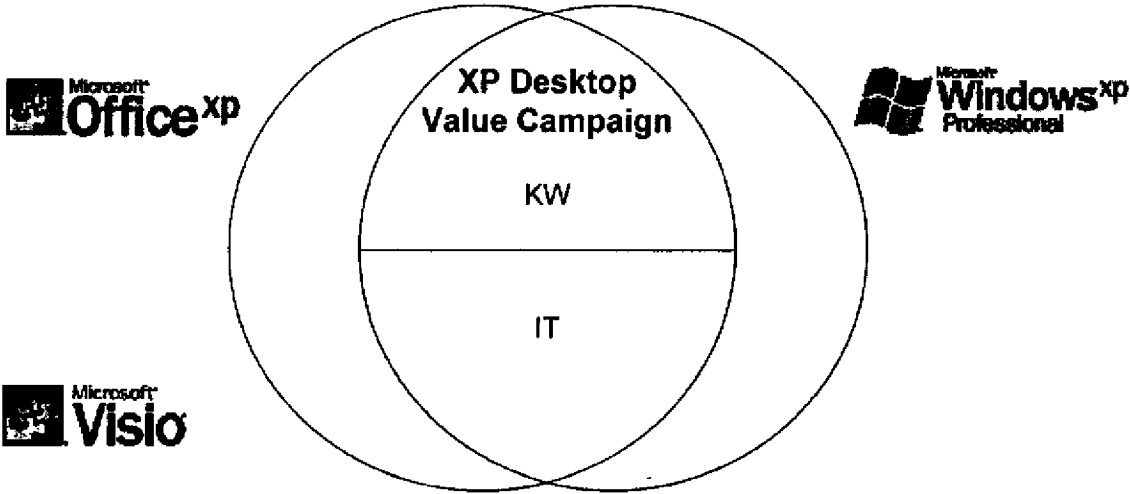
- Generate excitement
- Scenario focused
- Umbrella for several important launches
- May be only for large subs



- Office and Windows
- Communicate value
- Remove obstacles
- Licensing adjustments
- Every sub should participate

XP Desktop Value Campaign – Tenets

- Joint initiative around Windows XP Pro, Office XP & Visio 2002
- New messaging on shared value & productivity scenarios
- Segment & audience specific execution



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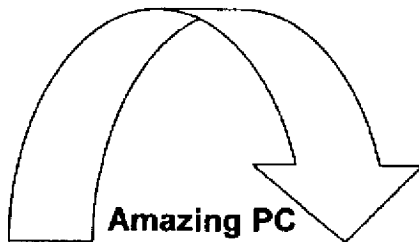
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Enterprise and Medium Enterprise

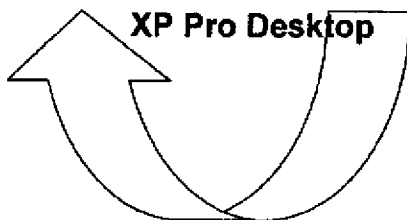
Goals/Opportunity

- Accelerate adoption of new experiences – WinXP Pro=Mobility
- Achieve 100% XP Pro penetration on notebooks
 - FY03 business notebook ship growth ~12% vs 3% for all PCs
- Sell 1 million Tablet PCs = 11% of ultra-portables
- Continue growth of volume licensing into ME segment
- Accelerate deployments - 50% of licenses deployed in Enterprise to increase cust satisfaction, enable upsell, and improve renewal rate
- Demonstrate/communicate more cust value than Linux+StarOffice



Amazing PC: Establish XP Pro as the Mobile Platform

- Use Tablet PC launch to highlight XP Pro platform benefits for both tablets and notebooks
- Drive demand for Windows XP Pro from OEMs in Enterprise/ME
- Increase Win XP Pro + Office XP value understanding and attach



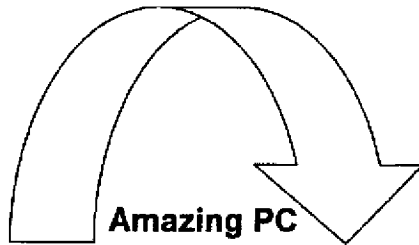
XP Pro Desktop: Drive Deployments

- Training & tools to enable rapid deployment; Better together with MS server technologies
- "Deployment Portal" on TechNet; Channel deployment training
- Partner deployment certification & lead mining/referral
- Continue ME volume licensing penetration w/ XP Desktop Biz Value
- Windows XP Pro and Office XP tools and programs

Small Business

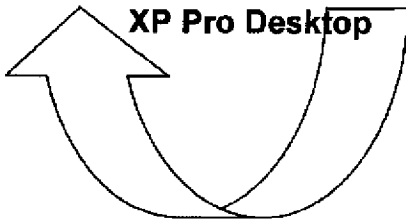
Goals/Opportunity

- Accelerate XP Pro adoption
- FG \$261m ⇒ \$445m (71%)
- COEM \$1,038m ⇒ \$1,097m (6%)
- 25-30m XP-capable PCs; 1% upgrade=\$40m
- 7-12% of SBs adding a LAN this year
 - WLAN: US 2% UK 8% Ger 18% France 7%
- >30% of SBs have laptops



Amazing PC: Networking, Mobility, & Communications

- Create excitement and demand for Windows XP with end-to-end solutions around Networking, Mobility, & Communications
- Drive simple networking (Win XP LAN) solutions into Low SORG
- Wireless adds sizzle, better XP-specific value
- Provide channel with tools and materials to sell XP LAN solutions



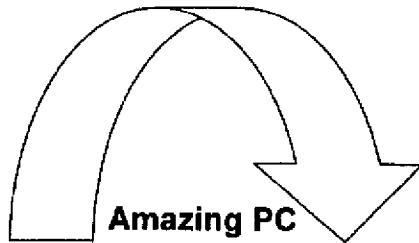
XP Desktop: Go Pro

- Increase demand for XP Desktop as default business platform
- Identify top SB applications and drive towards Win XP compatibility
- Reinforce Pro message around security and reliability
- Investigating additional license option, terms for volume licensing

Consumer

Goals/Opportunity

- WW Home PC Shipments:
 - Finance goal FY03: 39m units, 0% growth Y/Y
 - Our stretch goal FY03: 40m units, 3% growth Y/Y
 - 1m increase = \$23m
- WW FPP Home:
 - Finance goal FY03: 2.5m units, -22% growth Y/Y
 - Our stretch goal FY03: 2.7m units, -14% growth Y/Y
 - 200k unit increase = \$31m

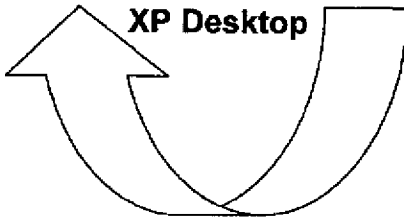


Amazing PC: Leverage Key Experiences

- Photography and music are low-hanging fruit
 - PC HHs with digital devices; non-PC HHs w/ cameras and music
 - Extend promotions to non-PC partners/retailers
- Maintain/grow excitement by leveraging Mira, Freestyle, WMP8
- MSN8 launch integration – better together campaigns focusing on key experiences (e.g. dig photos, music)

XP Desktop: Trial, Upgrade, Upsell

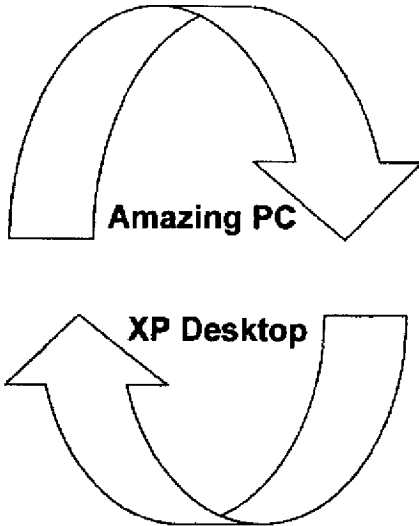
- Drive broad trial (PMG investigating eval solution)
- Retail upgrade - focus on performance, reliability, and security
- Retail upsell – focus Pro messaging on “work from home” (#1 pc activity in US); also leverage Mira for Pro upsell
- Invest in “community”, MS or 3rd party, to grow enthusiast base - help and support, gaming, photography, etc.



OEM

Goals:

Grow PC shipments <ul style="list-style-type: none"> • Forecast +3% to 117M units • Each 1% extra growth = \$88M 	XP Pro on new business PCs <ul style="list-style-type: none"> • Forecast 46% to 57% of business PCs • Each 1% growth = \$28M (\$43M all ships)
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Consistent Messages	<i>XP Pro = Business</i>		<i>Home = Digital Media</i>
Amazing PC			
Focused Product Scenarios	Mobility	Networking Mobility Comms.	Photos Music
<i>Excitement</i>	<ul style="list-style-type: none"> • Tablet • Pro Notebook 	<ul style="list-style-type: none"> • Wireless LAN • Pro Notebook 	<ul style="list-style-type: none"> • Freestyle • Mira
XP Desktop			
Core Initiatives	Deployments	Pro Desktop Value	Trial Pro Upsell
Target Segments	LORG/ME	SORG	Consumer

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Revenue Review and Targets

(Adj. Gross Rev - USD \$M)

	FY01	FY02	Y/Yr Growth	FY03	Y/Yr Growth
Commercial					
Product (revenue view)					
Windows Pro	1,752	2,415	37.8%	2,981	23.4%
Windows Home	0	398	n/a	537	34.8%
Windows Sx	1,340	408	-80.7%	63	-84.5%
Other OS/Academic	134	122	-9.3%	114	-6.2%
Total	2,926	3,344	14.3%	3,695	10.5%
Customer Segment					
EPG	1,165	1,343	15.3%	1,443	7.6%
Small-Medium Business	1,241	1,439	16.0%	1,767	22.7%
Consumer	327	386	18.2%	310	-19.7%
Academic/Other	194	175	-9.5%	175	-0.3%
Total	2,926	3,344	14.3%	3,695	10.5%
Geography					
United States	1,164	1,388	19.3%	1,526	9.9%
Rest of Americas	297	270	-9.0%	307	13.4%
Americas	1,461	1,659	13.5%	1,833	10.5%
Japan	195	232	18.8%	255	10.0%
Asia-Pacific	282	271	-3.9%	310	14.6%
Asia-Pacific and Japan	477	503	5.3%	565	12.5%
EMEA	988	1,182	19.7%	1,297	9.7%
Total	2,926	3,344	14.3%	3,695	10.5%
Royalty OEM					
Windows Pro	1,907	2,547	33.6%	3,249	27.5%
Windows Home	0	1,832	n/a	2,795	52.6%
Windows Sx	3,381	1,388	-58.7%	244	-82.4%
Other OS	17	15	-6.5%	8	-50.0%
Total	5,285	5,783	9.4%	6,297	8.9%
Total Windows Desktop	8,212	9,127	11.1%	9,982	9.5%
By Pricing Level					
FPP	473	507	7.2%	398	-21.6%
Open	184	308	67.9%	557	80.7%
Select	320	363	13.6%	373	2.5%
Open & Select	504	672	33.4%	929	38.4%
Enterprise Agreement	854	1,012	18.6%	1,160	14.7%
Academic/Other	127	115	-9.5%	111	-3.4%
Commercial OEM	969	1,038	7.1%	1,097	5.7%
Royalty OEM	5,285	5,783	9.4%	6,297	8.9%
Total	8,212	9,127	11.1%	9,982	9.5%

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FY02

- Revenue of \$9.1B up 11%.
- PC Shipments down 6% - \$1.2B lost revenue
- Piracy up to 18%, up from 17%
- OEM/COEM Pro mix 31%, 46% of business PCs
- FPP Pro mix 35%, up from 15%
- FPP revenue up 7%
- Licensing up 24% - Pro migration and sales efforts

FY03

- Revenue \$10.0B, up 9%
 - Royalty OEM revenue \$6.3B, up 9%
 - Commercial OEM revenue \$1.1B, up 6%
 - Finished Goods revenue \$2.6B, up 13%
- PC shipments grow 3%
- OEM/COEM Pro Mix:
 - 39% of all PC shipments
 - 57% of business PC shipments
- Piracy flat at 18%
- EPG revenue up 7% - lower allocation of Platform EA going forward
- Small-Medium Business up 23%
 - Extension of EA to MORG
 - Carry-over from FY02 annuity push
 - Flat COEM PC Shipments
- Consumer revenue down 20% following Windows XP launch
- Higher growth rates in emerging regions

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Growth Opportunities

(At) Gross Rev - USD \$M

	FY02	FY03	Yr/Yr Growth	FY01	Yr/Yr Growth	FY05	Yr/Yr Growth
Commercial							
Product (revenue view)							
Windows Pro	2,415	2,981	23.4%	3,424	14.9%	4,358	27.3%
Windows Home	398	537	34.8%	547	1.9%	621	13.5%
Windows 9x	409	63	-84.5%	0	-100.0%	0	n/a
Other OS/Academic	122	114	-6.2%	114	-0.1%	117	2.8%
Total	3,344	3,695	10.5%	4,085	10.6%	5,097	24.8%
Customer Segment							
EPG	1,343	1,443	7.5%	1,492	3.4%	1,496	0.4%
Small-Medium Business	1,439	1,767	22.7%	2,142	21.2%	2,777	29.7%
Consumer	385	310	-19.7%	270	-12.6%	622	130.3%
Academic/Other	175	175	-0.3%	181	3.5%	199	9.9%
Total	3,344	3,695	10.5%	4,085	10.6%	5,097	24.8%
Geography							
United States	1,388	1,526	9.9%	1,683	10.3%	2,110	25.4%
Rest of Americas	270	307	13.4%	347	13.2%	428	23.3%
Americas	1,659	1,833	10.5%	2,030	10.6%	2,538	25.0%
Japan	232	255	10.0%	278	9.0%	352	26.6%
Asia-Pacific	271	310	14.6%	351	13.2%	433	23.3%
Asia-Pacific and Japan	503	565	12.5%	629	11.3%	785	24.8%
EMEA	1,182	1,297	9.7%	1,426	9.9%	1,774	24.4%
Total	3,344	3,696	10.5%	4,085	10.6%	5,097	24.8%
Royalty OEM							
Windows Pro	2,547	3,249	27.5%	3,713	14.3%	4,502	21.2%
Windows Home	1,832	2,795	52.6%	3,003	7.4%	2,790	-7.1%
Windows 9x	1,388	244	-82.4%	0	-100.0%	0	n/a
Other OS	16	8	-50.0%	4	-50.0%	2	-50.0%
Total	5,783	6,297	8.9%	6,720	6.7%	7,294	8.5%
Total Windows Desktop	9,127	9,992	9.5%	10,805	8.1%	12,391	14.7%
By Pricing Level							
FPP	507	398	-21.6%	341	-14.1%	834	144.1%
Open	308	557	80.7%	819	47.1%	1,026	25.2%
Select	363	373	2.5%	418	11.6%	459	10.4%
Open & Select	672	929	38.4%	1,235	32.9%	1,465	20.2%
Enterprise Agreement	1,012	1,180	14.7%	1,223	5.4%	1,264	2.5%
Academic/Other	115	111	-3.4%	112	1.6%	116	3.7%
Commercial OEM	1,038	1,097	5.7%	1,173	6.9%	1,408	20.0%
Royalty OEM	5,783	6,297	8.9%	6,720	6.7%	7,294	8.5%
Total	9,127	9,992	9.5%	10,805	8.1%	12,391	14.7%

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