BUSINESS PLAN
FOR FY92
MICROSOFT EUROPE

By Bernard Vergnes
Vice President, Europe
Redmond, Washington
May 28th, 1991

"The only constant is change"

—Heraclitus, 400 B.C.

1. INTRODUCTION

The last months of the 80's were spent celebrating "Europe's Horn of Plenty". However, a year of trading with a highly undervalued Yen and Dollar, the war in the Gulf and the worldwide (US) economic dislocation are inviting most analysts to revise their predictions downwards. From 3.3% in 1989 and 2.9% in 1990, European economic growth is expected to be only 2.2% in 1991. Inflation is creeping up slightly and unemployment has started to rise again.

Nevertheless, Europe 1993 will happen and in less than 80 weeks the United Market will be born. The Commission in Brussels is frantically working out the numerous Directives that will make this a reality, but we already know that much will be left for after the magic date of January, 1993. For one thing, VAT harmonization will not happen before 1996 at the earliest.

Our success in Europe this past year seems to negate this somewhat gloomy look at the future. It is clear that our segment of the computer industry is still enjoying reasonable growth, although with an economy developing more slowly we can expect customers to become more selective in their choices, more conservative in their decisions. Increased focus on competitiveness, customer relationships, and efficiency is needed more than ever. At the last shareholders meeting of IBM, John F. Akers outlined a market philosophy that we should take as our own vision for Microsoft in Europe:

> "The only thing that should exceed the strength of our products is the strength of our ability to market and support them. That strength must be reflected and reinforced by excellence in our customer relationships. Excellence means we are so in tune with our customers' needs that we not only read their requests, we can almost read their minds and we never rest in our obsession to satisfy and delight them. Our objective is total customer satisfaction. And total customer satisfaction must be reached by combining the best technology with the best services."

This proposed plan for FY92 is our attempt to extend the excellence of Microsoft in Europe to reach this level of customer satisfaction and achieve greater success.

2. FISCAL YEAR 1991 PERFORMANCE

We estimate that **Retail Revenues** (including networking and services) will end up close to $710M at FY91 exchange rates. This will represent more than 90% dollar growth over last year, or some 75% in local currency when we eliminate the dollar exchange effect. The budget will be beaten by more than 30%.

OEM Revenues will also beat budget by almost 11%, with sales of $60M and a 20% year-to-year growth rate.

With the exception of Spain, every subsidiary is planning to beat their **Operating Income** budget by a wide margin. In spite of the investments made in NBU, Consulting and PSS, we will remain very close to FY90's achievement and return more than 22% local operating income.

X 166792
CONFIDENTIAL

Retail Revenue ($000) (#1)

Territory	FY87 Actual	% Growth 88/87	FY88 Actual	% Growth 89/88	FY89 Actual	% Growth 90/89	FY90 Actual	% Growth 91/90	FY91 Forecast	FY91 Budget	% Fore/ Budget	CAGR 87-91F
UK	$8,256	127.0%	$18,744	37.5%	$25,764	64.1%	$42,289	72.3%	$72,868	$62,639	16.3%	72.4%
Nordic	$5,749	141.0%	$13,857	44.6%	$20,044	82.8%	$36,642	70.9%	$62,628	$51,886	20.7%	81.7%
German/Aust (#2)	$25,735	71.1%	$44,031	53.3%	$67,521	47.9%	$99,881	93.7%	$193,452	$132,773	45.7%	70.3%
Switzerland							$15,532	49.3%	$23,194	$20,808	11.5%	N/M
France	$24,988	76.7%	$44,150	67.5%	$73,936	57.7%	$116,581	68.3%	$196,158	$143,311	36.9%	67.4%
Iberica (#3)			$1,412	138.0%	$3,360	92.5%	$6,468	72.2%	$11,137	$10,366	7.4%	99.1%
Benelux	$4,497	90.9%	$8,583	61.0%	$13,820	30.4%	$18,015	71.8%	$30,942	$24,084	28.5%	62.0%
Italy	$3,502	86.3%	$6,526	66.7%	$10,877	82.0%	$19,798	52.8%	$30,257	$26,881	12.6%	71.4%
Europe Total	$72,727	88.8%	$137,303	56.8%	$215,322	65.0%	$355,206	74.7%	$620,636	$472,747	31.3%	70.9%

OEM Revenue ($000)

Territory	FY87 Actual	% Growth 88/87	FY88 Actual	% Growth 89/88	FY89 Actual	% Growth 90/89	FY90 Actual	% Growth 91/90	FY91 Forecast	FY91 Budget	% Fore/ Budget	CAGR 87-91F
UK	$2,746	99.8%	$5,486	49.6%	$8,205	3.3%	$8,473	15.2%	$9,760	$7,480	30.5%	37.3%
Nordic	$1,290	124.4%	$2,895	44.9%	$4,195	34.1%	$5,627	65.0%	$9,287	$6,860	35.4%	63.8%
German/Aust (#2)	$3,794	97.0%	$7,476	27.9%	$9,565	74.2%	$16,660	15.8%	$19,300	$19,067	1.2%	50.2%
Switzerland							$13	0.0%	$13	$0	N/M	N/M
France	$4,489	14.3%	$5,132	36.1%	$6,985	(12.0%)	$6,147	(42.5%)	$3,533	$4,127	(14.4%)	(5.8%)
Iberica (#4)			$1	N/M	$225	63.1%	$367	(67.3%)	$120	$547	(78.1%)	(27.0%)
Benelux	$1,422	113.1%	$3,030	(8.6%)	$2,770	(35.3%)	$1,793	172.9%	$4,893	$3,060	59.9%	36.2%
Italy	$2,666	289.5%	$10,383	1.6%	$10,550	3.3%	$10,900	18.2%	$12,887	$12,887	0.0%	48.3%
Europe Total	$16,407	109.7%	$34,403	23.5%	$42,495	17.6%	$49,980	19.6%	$59,793	$54,028	10.7%	38.2%

#1: All revenues calculated using FY92 exchange rates. Revenues include networking and services but exclude OEM commissions.
#2: Germany's CAGRs include revenue for Switzerland.
#3: Iberica's retail revenue CAGR is for FY88-FY91F only.
#4: Iberica's OEM CAGR is for FY89-FY91F only.

X 166793
CONFIDENTIAL

2

Operating Income ($000) (#1)

Territory	FY87 Actual	% Growth 88/87	FY88 Actual	% Growth 89/88	FY89 Actual	% Growth 90/89	FY90 Actual	% Growth 91/90	FY91 Forecast	FY91 Budget	% Fore/ Budget	CAGR 87-91F
UK (#2)	($667)	N/M	$1,274	24.4%	$1,584	451.4%	$8,734	17.9%	$10,295	$4,455	131.1%	100.7%
Nordic	$182	771.0%	$1,583	(53.6%)	$734	927.4%	$7,541	57.2%	$11,858	$4,687	153.0%	184.2%
German/Aust (#3)	$2,824	277.0%	$10,646	47.1%	$15,663	51.0%	$23,653	110.8%	$49,867	$24,179	106.2%	111.4%
Switzerland							$5,515	17.7%	$6,492	$3,319	95.6%	N/M
France	$3,264	137.3%	$7,745	85.9%	$14,395	101.9%	$29,065	91.7%	$55,728	$26,614	109.4%	103.3%
Iberica			$28	629.4%	$205	64.4%	$337	(143.9%)	($148)	$140	(205.5%)	N/M
Benelux	$489	(33.1%)	$328	245.2%	$1,131	109.6%	$2,370	118.9%	$5,187	$2,340	121.6%	80.4%
Italy	$161	284.3%	$618	72.2%	$1,065	211.0%	$3,312	5.9%	$3,508	$2,220	58.0%	116.1%
Europe Total (#4)	$6,253	255.4%	$22,222	56.5%	$34,777	131.6%	$80,527	77.3%	$142,787	$67,956	110.1%	118.6%

Operating Income (% of Retail Revenue)

Territory	FY87 Actual	Diff 88/87	FY88 Actual	Diff 89/88	FY89 Actual	Diff 90/89	FY90 Actual	Diff 91/90	FY91 Forecast	FY91 Budget	Diff Fore/ Budget
UK	(8.1%)	14.9%	6.8%	(0.6%)	6.1%	14.5%	20.7%	(6.5%)	14.1%	7.1%	7.0%
Nordic	3.2%	8.3%	11.4%	(7.8%)	3.7%	16.9%	20.6%	(1.6%)	18.9%	9.0%	9.9%
German/Aust	11.0%	13.2%	24.2%	(1.0%)	23.2%	0.5%	23.7%	2.1%	25.8%	18.2%	7.6%
Switzerland							35.5%	(7.5%)	28.0%	16.0%	12.0%
France	13.1%	4.5%	17.5%	1.9%	19.5%	5.5%	24.9%	3.5%	28.4%	18.6%	9.8%
Iberica			2.0%	4.1%	6.1%	(0.9%)	5.2%	(6.5%)	(1.3%)	1.4%	(2.7%)
Benelux	10.9%	(7.1%)	3.8%	4.4%	8.2%	5.0%	13.2%	3.6%	16.8%	9.7%	7.0%
Italy	4.6%	4.9%	9.5%	0.3%	9.8%	6.9%	16.7%	(5.1%)	11.6%	8.3%	3.3%
Europe Total (#4)	8.6%	7.6%	16.2%	0.0%	16.2%	6.5%	22.7%	0.3%	23.0%	14.4%	8.6%

#1: All operating incomes calculated using FY92 exchange rates; excludes OEM commissions but includes OEM related expenses.
#2: UK's CAGR is for FY88-FY91F only.
#3: Germany's CAGR includes operating income for Switzerland.
#4: For comparison purposes, this excludes expenses of the European Headquarters.

3

3. MARKET OVERVIEW

I can only reiterate what I said in last year's Business Plan: good data is hard to come by. Coherence between analysts, and sometimes within one single company, does not yet exist. Only trends and order of magnitude can be derived from the many reports produced by Dataquest, IDC, Inteco and the SPA.

It is clear, however, that this last year was not a good one for most computer manufacturers. In Europe, both local manufacturers (such as Olivetti, Philips, and Bull) and US companies (such as Digital Equipment) announced significant staff reductions along with, in most cases, financial results ranging from poor to disastrous. As a result, competition has clearly intensified, reducing margins and forcing manufacturers and the distribution channel into a continual search for productivity. With some 26% white collar workers and less than 4% of all households equipped with a PC, the market is not yet saturated but is certainly showing signs of maturity.

Hardware

Dataquest estimates that just over 6 million units of Intel based personal computers were sold into all market segments in FY91. This corresponded to a growth of nearly 12% over FY90. It is expected that next year's growth will be 11%.

CPU Sales Data by Country (#1)

	Intel CPUs (000s Units) (#2)								
Country	FY89	% Growth 90/89	FY90	% Growth 91/90	FY91	% Growth 92/91	FY92	% Growth 93/92	FY93
U.K.	768.7	24.1%	954.1	9.3%	1,043.0	8.4%	1,130.2	6.9%	1,208.2
Nordic Countries	468.6	20.8%	566.1	12.1%	634.7	10.2%	699.7	7.8%	754.2
West Germany	844.6	17.3%	990.7	17.8%	1,167.3	18.5%	1,383.0	14.1%	1,578.1
Switzerland	154.8	19.8%	185.4	11.7%	207.1	7.5%	222.7	4.6%	232.9
France	727.0	19.2%	866.4	12.0%	970.2	11.2%	1,078.5	9.9%	1,184.9
Spain	357.7	25.4%	448.7	14.5%	514.0	11.1%	571.0	8.7%	620.8
Benelux	553.0	7.3%	593.3	8.5%	643.5	6.4%	684.6	4.1%	712.4
Italy	472.8	17.4%	555.2	7.2%	595.3	7.9%	642.2	5.8%	679.7
Others	177.1	28.4%	227.5	10.5%	251.3	10.0%	276.5	8.7%	300.5
Europe Total	4,524.1	19.1%	5,387.2	11.9%	6,026.1	11.0%	6,688.3	8.7%	7271.5

	Non-PC Compatible CPUs (000s Units) (#3)								
Country	FY89	% Growth 90/89	FY90	% Growth 91/90	FY91	% Growth 92/91	FY92	% Growth 93/92	FY93
U.K.	64.4	58.7%	102.1	24.5%	127.2	11.4%	141.7	7.0%	151.6
Nordic Countries	48.3	26.8%	61.3	16.1%	71.3	10.1%	79.0	7.5%	85.0
West Germany	57.1	24.4%	71.1	17.1%	83.2	4.2%	86.7	12.0%	97.1
Switzerland	25.8	39.5%	36.0	16.9%	42.1	10.0%	46.3	7.0%	49.6
France	86.0	23.6%	106.2	22.0%	129.6	12.6%	146.0	9.5%	159.8
Spain	15.3	43.1%	21.9	15.1%	25.2	8.3%	27.3	10.4%	30.2
Benelux	39.9	1.6%	40.5	10.7%	44.9	10.9%	49.8	2.4%	51.0
Italy	24.5	21.1%	29.6	6.8%	31.6	4.3%	33.0	3.8%	34.2
Others	11.0	49.5%	16.5	13.1%	18.6	0.8%	18.8	6.4%	20.0
Europe Total	372.6	30.3%	485.6	18.2%	574.1	9.5%	628.4	7.9%	678.2

#1: Source: Dataquest shipments data, Dec. 1990. Fiscal year information is calculated based on an average of calendar year data.
#2: Intel data includes both business and home CPUs.
#3: Non-PC compatible data (predominantly Motorola 68xxx based machines) includes business CPUs only.

In the professional market, Intel has continued to dominate with more than 91% of all personal computers sold in FY91. The share of 386+ based machines has further increased and now represents more than 42% of the market

X 166795
CONFIDENTIAL

(including 386+ laptops). This share could approach 60% next fiscal year and would represent more than 4 million units of Windows capable machines.

European Processor Sales Data (#1)

	CPUs (% of Total)								
CPU	FY89	Diff 90/89	FY90	Diff 91/90	FY91	Diff 92/91	FY92	Diff 93/92	FY93
8086/88	33.2%	(13.0%)	20.2%	(11.1%)	9.2%	(6.0%)	3.2%	(2.3%)	0.8%
286	38.9%	(2.2%)	36.7%	(7.7%)	28.9%	(11.1%)	17.8%	(9.4%)	8.4%
386	12.8%	11.5%	24.3%	14.5%	38.9%	12.3%	51.2%	4.8%	56.0%
486	0.8%	0.3%	8.3%	0.7%	1.0%	1.8%	2.7%	3.7%	6.5%
Laptops	7.4%	2.8%	10.2%	3.2%	13.4%	3.1%	16.5%	3.3%	19.8%
Intel Total	92.4%	(0.7%)	91.7%	(0.4%)	91.3%	0.1%	91.4%	0.1%	91.5%
Non-PC <$2K (#2)	2.0%	0.4%	2.4%	0.3%	2.7%	(0.1%)	2.6%	0.0%	2.6%
Non-PC >$2K (#2)	5.6%	0.3%	5.9%	0.1%	6.0%	0.0%	6.0%	0.0%	5.9%
Non-PC Total	7.6%	0.7%	8.3%	0.4%	8.7%	(0.1%)	8.6%	(0.1%)	8.5%
Europe CPU Total	100.0%		100.0%		100.0%		100.0%		100.0%

#1: Source: Dataquest shipments data, Dec. 1990. Fiscal year information is calculated based on an average of calendar year data. Intel data includes both business and home CPUs. Non-PC compatible data includes only business machines.

#2: Predominantly Motorola 68xxx based machines.

One of the significant events in the hardware market this last year was the strengthening of low-end offerings with major products introduced by IBM (PS/1) and Apple (Classic). This, in addition to the success of some of the low-end clones (like VOBIS) and the increased acceptance in some markets (especially Germany) of Far East products, has driven prices down and rejuvenated the home market. At roughly 20% share, the home market has been growing faster than the professional market and now represents nearly 30% of all machine sales in Germany (this country representing about 25% of the total European home market, well ahead of the UK at 22% and France at no more than 15%). The major manufacturers represent just under 60% of the business segment this year, slightly less than last year, another sign of the success of low price machines in this part of the market. IBM, Zenith, Tandon, Amstrad, and Olivetti were the losers in terms of market share, with mostly Compaq, Apple, and the "unnamed many" increasing their presence.

CPU Vendor Market Share

Business Shipments (#1)

Company	CY89 Market Share	CY90 Market Share	% Diff	1989 Rank
IBM	20.1%	17.6%	(2.5%)	1
Compaq	5.9%	7.2%	1.3%	3
Apple	5.8%	6.7%	0.9%	4
Olivetti	6.8%	6.5%	(0.3%)	2
Commodore	4.2%	4.3%	0.1%	6
Zenith/Bull	4.8%	3.6%	(1.2%)	5
Toshiba	3.0%	3.6%	0.6%	9
Tandon	3.9%	3.4%	(0.5%)	7
Amstrad	3.0%	2.6%	(0.4%)	8
Philips	2.4%	2.5%	0.1%	11
Others	40.1%	42.0%	1.9%	
Total Share	100.0%	100.0%		
Total Units	4,795.7	5,821.5		

#1: Source: Dataquest vendor data, February 1991.

X 166796
CONFIDENTIAL

Software

According to Inteco, European PC users spent some $4.75 billion for third party software in 1990. 58% of this was spent on personal productivity applications, 24% on commercial (vertical) applications, 12% on operating environments and 6% on tools. This represents an average spending of $833 per new personal computer. Assuming average margins of 18% for distributors and 30% for dealers, this corresponds to an average manufacturer's revenue of $478 per new PC. Furthermore, with retail sales of $550M and an estimated $100M of OEM revenues generated by European distributed machines, we can fairly estimate that Microsoft represented more than 25% of the European microcomputer software market during this last year.

Inteco expects this market to keep growing at a compound annual rate of 20% over the next four years. According to the SPA, the current growth is much higher, at least for the American companies that are part of the census. One could believe that these companies' growth is higher than the market average, especially due to the "Microsoft effect" given that our growth has been even higher than the SPA average in every single country.

Software Market Growth (#1)

Territory	# of Firms Reporting	CY90/89 Unit Growth	CY90/89 $ Rev Growth	CY90/89 MS $ Rev Growth
UK	20	34.5%	39.0%	84.5%
Nordic	19	46.0%	54.7%	123.6%
German/Aust	18	39.1%	67.3%	100.2%
Switzerland	N/A	N/A	N/A	N/A
France	16	37.7%	66.2%	122.0%
Iberica	15	104.0%	197.5%	90.7%
Benelux	16	22.8%	48.7%	110.5%
Italy	15	63.5%	70.1%	119.5%
Europe Total		39.8%	58.9%	116.0%

#1: Source: SPA market data for firms tracked in both CY89 and CY90.
Revenue data includes effects of changes in exchange rates.

The fight against piracy has been very visible during the last twelve months. Major actions taken in several countries have resulted in numerous corporations openly deciding to enforce the legal use of software. The Brussels EEC Directive has further provided publicity to the significance of licensing software. As a result, we estimate that "software penetration" has grown by 25% from 0.55 software units per machine in CY89 to 0.69 in CY90.

Software Penetration (#1)
Units per Intel CPU

Territory	CY89	CY90	% Change
UK	0.78	0.95	21.5%
Nordic	0.68	0.87	28.0%
German/Aust	0.73	0.91	24.2%
Switzerland	N/A	N/A	N/A
France	0.57	0.69	21.7%
Iberica (#2)	0.19	0.33	75.7%
Benelux	0.52	0.58	11.7%
Italy	0.25	0.40	58.6%
Other	0.27	0.38	39.0%
Europe Total	0.55	0.69	25.5%

#1: Source: Dataquest and SPA market data for business and home CPUs; assumes SPA data includes 75% of the market.
#2: Includes CPU data for Spain only.

X 166797
CONFIDENTIAL

While this is impressive, the absolute number of licensed software units per machine, even if only approximate, remains very low and justifies the continuation of the fight against piracy.

4. FISCAL YEAR 1992 PLAN

Fiscal Year 1992 will be a year of transition towards FY93 and Europe 1993, dates for which we have set several ambitious goals.

- First, we will support and service our customers at a level of quality equivalent to what is currently provided in the USA. This translates in this plan into major hiring in the PSS and Operations areas.
- Second, we will converge both our T&C's and our prices across Europe to achieve mark-ups in FY92 of no more than 40% for English products and 80% for localized products. The FY93 objectives are 15 to 30% for English products and 40 to 60% for localized products. This translates in this plan into selected price decreases and a reduction of most distributor and dealer discounts by at least one percentage point.

Average Budgeted Price Changes
By Subsidiary

Territory	FY92F Price Change
UK	3.0%
Nordic	7.0%
Germany/Austria	12.0%
Switzerland	10.0%
France	3.4%
Iberica (#1)	25.0%
Benelux	3.1%
Italy	7.0%

#1: This price change was implemented in FY91.

To achieve these pricing objectives while maintaining adequate levels of profitability, we are forecasting significant increases in the productivity of the sales and marketing teams.

Further investments will be made during FY92 to confirm our presence in the Network market and to develop the European consulting practice. After opening in the UK and Italy in FY91, we will expand our MS Consulting invesment to include Germany and France in FY92. Our geographic expansion will also continue with new country offices being opened in Austria and Finland, and numerous new offices within existing countries: Manchester, Geneva, Lyon, Marseille, Toulouse, Strasbourg, Lille, Nantes...

It is important to note that several components of the economic equation are planned to be modified in FY92. Dollar exchange rates, local prices, and distribution discounts are all pieces of the complex puzzle that we must manage. This will be a significant challenge for us.

The budgeted price reductions have been planned on the basis of a dollar that was some 15% cheaper than the one currently budgeted: As a result, the budgeted mark-ups nearly all meet the objectives set for FY93. If the dollar

X 166798
CONFIDENTIAL

keeps rising (and we understand that we might have to face another 8% increase by the close of the budgeting process), many of the budgeted price decreases would not be put into effect.

Less controllable is the effect of the dollar exchange rate on the Microsoft bottom line. It is interesting to calculate that if the FY91 average exchange rate had been the one planned for FY92, our $710M revenue would have been $620M and our fully burdened operating income margin would have been 2% lower (a net "loss" of $60M). Additionally, if our prices in FY91 had been 10% lower, total revenues would have shrunk further to $558M and fully burdened operating income would have been decreased by 7% (a net "loss" of $115M). This must be kept in mind when comparing the FY92 budget with our FY91 achievements.

Retail Revenue

Net retail revenue (including networking and services) will total $929M, a 49.6% growth versus the FY91 forecast. This is a challenging growth projection but we believe it is achievable. While hardware growth will only be 11%, the 386/486 segment will grow at 48%. We also expect that the software market will keep growing at a faster rate than the overall CPU market, probably at 35% to 40%, due to a) the success of our anti-piracy action and b) the advent of the GUI platform, which typically generates more units of software per machine.

Additionally, a number of new products (or new releases) will strengthen our competitive position. In particular, the DOS 5 Upgrade is expected to represent a one-time sales boost of approximately 700K units contributing by themselves nearly 6 percentage points of the growth. On the Lan Manager side, the budgeted increase in this activity will contribute more than 4 percentage points to the FY92 growth.

Retail Revenue ($000) (#1)

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	% Growth vs. Fore
UK	$62,639	$72,868	$110,901	52.2%
Nordic	$51,886	$62,628	$98,574	57.4%
German/Aust	$132,773	$193,452	$318,876	64.8%
Switzerland	$20,808	$23,194	$31,288	34.9%
France	$143,311	$196,158	$252,482	28.7%
Iberica	$10,366	$11,137	$19,880	78.5%
Benelux	$24,084	$30,942	$51,574	66.7%
Italy	$26,881	$30,257	$45,183	49.3%
Europe Total	$472,747	$620,636	$928,758	49.6%

#1: All revenues calculated using FY92 exchange rates. Revenues include networking and services but exclude OEM commissions.

OEM Revenue

OEM revenue will total $58.6M, a decrease of 2.0% versus the FY91 forecast. This is not a complete representation of reality but reflects the fact that several European manufacturers are now under American or Japanese control and their OEM revenues are being accounted elsewhere (Philips, Zenith...). The OEM activities of coordinating manufacturers' development, insuring design wins for our platforms, and promoting Packaged DOS need to be strengthened and the OEM staff will be increased from 24 to 33 persons.

X 166799
CONFIDENTIAL

OEM Revenue ($000)

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	% Growth vs. Fore
UK	7,480	9,760	10,000	2.5%
Nordic	6,860	9,287	5,500	(40.8%)
German/Aust	19,067	19,300	21,000	8.8%
Switzerland	0	13	0	N/M
France	4,127	3,533	4,000	13.2%
Iberica	547	120	153	27.5%
Benelux	3,060	4,893	3,647	(25.5%)
Italy	12,887	12,887	14,300	11.0%
Europe Total	54,028	59,793	58,600	(2.0%)

Cost of Goods

Cost of Goods will average 59.9% of retail sales during FY92. This is 7.6% more than the forecasted COGs for FY91. This difference is due to the combined effect of price decreases and discount modifications being budgeted and the higher dollar rates being used. On a weighted average basis, the budget exchange rates being used are 13.7% higher than the FY91 average exchange rate and 4.8% higher than the FY91 budgeted rates.

COGs %

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	Diff vs. Fore	% Curr Chge (#1)
UK	59.7%	53.9%	61.5%	7.6%	1.0%
Nordic	59.1%	53.3%	63.5%	10.2%	5.2%
German/Aust	52.1%	52.6%	56.7%	4.2%	5.3%
Switzerland	55.5%	50.0%	61.2%	11.1%	3.6%
France	53.9%	49.3%	58.9%	9.6%	5.3%
Iberica	56.2%	60.9%	71.7%	10.9%	4.1%
Benelux	57.4%	56.9%	61.0%	4.1%	6.7%
Italy	61.8%	57.9%	68.5%	10.7%	6.9%
Europe Total	55.5%	52.3%	59.9%	7.6%	4.8%

#1: % currency change based on year to year budget rates. Europe Total calculated using a revenue based weighted average.

It should be noted, however, that this notion of COGs is an artificial one that does not fairly represent Corporate COGs. This value could also be impacted further by higher exchange rates or higher transfer prices, both of which are being discussed.

Operating Expenses

Operating expenses will be 28.1% of retail sales. This is 2.9% higher than FY91 forecast but 2.8% lower than FY91 budget.

X 166800
CONFIDENTIAL

Operating Expense % (#1)

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	Diff vs. Fore
UK	33.2%	32.0%	33.4%	1.4%
Nordic	31.9%	27.8%	28.1%	0.3%
German/Aust	29.7%	21.7%	25.2%	3.6%
Switzerland	28.6%	22.0%	27.1%	5.1%
France	27.5%	22.3%	24.3%	2.0%
Iberica	42.4%	40.4%	40.3%	(0.2%)
Benelux	32.9%	26.4%	29.0%	2.6%
Italy	30.0%	30.5%	29.5%	(1.0%)
Europe Total (#2)	30.9%	25.2%	28.1%	2.9%

#1: Includes OEM related expenses.
#2: Europe Total includes expenses of the European Headquarters.

At 8.4%, marketing expenses as a percent of retail sales are being budgeted slightly higher than the 7.8% forecasted for FY91, but much lower than the 9.9% that was budgeted last year. Throughout Europe, marketing expenses will total in excess of $77.5M. Operating expenses without marketing reflect the investment being made in support and services, as well as the investment being planned in education and training. They are planned to represent 19.7% of retail sales.

Operating Expense % (without Marketing) (#1)

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	Diff vs. Fore
UK	21.6%	21.6%	24.3%	2.7%
Nordic	20.9%	18.7%	19.5%	0.8%
German/Aust	20.7%	14.7%	17.7%	2.9%
Switzerland	18.4%	12.8%	17.6%	4.8%
France	18.4%	15.6%	16.6%	0.9%
Iberica	31.2%	29.2%	30.8%	1.5%
Benelux	23.2%	18.4%	20.4%	2.0%
Italy	19.3%	20.4%	20.0%	(0.4%)
Europe Total (#2)	21.0%	17.4%	19.7%	2.4%

#1: Includes OEM related expenses.
#2: Europe Total includes expenses of the European Headquarters.

Operating Income

Operating income will be 12.0% of Retail Sales. This is 10.5% lower than FY91 forecast and 1.6% lower than FY91 budget. These differences are mostly due to the decline in gross profit.

X 166801
CONFIDENTIAL

Retail Operating Income % (#1)

Territory	FY91 Budget	FY91 Forecast	FY92 Plan	Diff vs. Fore
UK	7.1%	14.1%	5.1%	(9.0%)
Nordic	9.0%	18.9%	8.4%	(10.5%)
German/Aust	18.2%	25.8%	18.0%	(7.7%)
Switzerland	16.0%	28.0%	11.7%	(16.3%)
France	18.6%	28.4%	16.8%	(11.6%)
Iberica	1.4%	(1.3%)	(12.0%)	(10.7%)
Benelux	9.7%	16.8%	10.0%	(6.8%)
Italy	8.3%	11.6%	1.9%	(9.7%)
Europe Total (#2)	13.6%	22.5%	12.0%	(10.5%)

#1: Excludes OEM commissions but includes OEM related expenses.
#2: Europe Total includes expenses of the European Headquarters.

People

We plan to end FY92 with 1,694 people in the European field operation. This corresponds to 49.8% growth over FY91 forecast and continues the challenge of finding, hiring, integrating, and training some 50 new persons each month.

Year End Headcount by Territory

Territory	FY91 Fore	% Growth 92/91	FY92 Plan	% Growth 93/92	FY93 Fore	% Growth 94/93	FY94 Fore
UK	167	43.7%	240	27.9%	307	23.1%	378
Nordic	125	41.6%	177	39.0%	246	19.1%	293
German/Aust	341	50.1%	512	47.3%	754	21.5%	916
Switzerland	18	88.9%	34	47.1%	50	42.0%	71
France	270	47.8%	399	22.6%	489	13.3%	554
Iberica	39	56.4%	61	41.0%	86	34.9%	116
Benelux	70	58.6%	111	24.3%	138	23.2%	170
Italy	83	36.1%	113	22.1%	138	28.3%	177
EHQ	18	161.1%	47	29.8%	61	29.5%	79
Europe Total	1,131	49.8%	1,694	33.9%	2,269	21.4%	2,754

Apart from Consulting and NBU where we are still in investment mode, the highest departmental growth, as one would expect, will be in PSS. This is the only "traditional" department we will grow faster than revenues. The relatively high increase in F&A is due in part to the strengthening of the "operations" side in order to supply better service to our customers, but it mostly reflects the addition or extension of the MIS groups. Sales and Marketing are contained at a lower growth than revenues, denoting the increase in productivity expected. However, in some countries we might be faced with Large Account Sales teams that will be understaffed. We need to be prepared to react and approve extra heads if sales in that area exceed budget.

X 166802
CONFIDENTIAL

Year End Headcount by Function

Function	FY91 Fore	% Growth 92/91	FY92 Plan	% Growth 93/92	FY93 Fore	% Growth 94/93	FY94 Fore	FY92 % of Total
Retail	241	35.7%	327	28.7%	421	18.3%	498	19.3%
Marketing	164	40.9%	231	24.2%	287	17.4%	337	13.6%
OEM	24	37.5%	33	21.2%	40	17.5%	47	1.9%
NBU	60	56.7%	94	59.6%	150	30.7%	196	5.5%
PSS	292	61.3%	471	39.3%	656	20.6%	791	27.8%
F & A	247	47.4%	364	31.3%	478	18.2%	565	21.5%
Warehouse	61	26.2%	77	27.3%	98	23.5%	121	4.5%
Consulting/MSU	24	108.3%	50	56.0%	78	53.8%	120	3.0%
EHQ	18	161.1%	47	29.8%	61	29.5%	79	2.8%
Europe Total	1,131	49.8%	1,694	33.9%	2,269	21.4%	2,754	100.0%
Retail Revenue Growth (#1)		49.6%		36.1%		30.0%		

#1: All revenues calculated using FY92 budget rates.

Productivity

Global productivity for Sales and Marketing (Sales + Marketing + NBU heads) will grow during FY92 by 6.7% to $1,424K per "marketing" head.

Revenue/Retail & Marketing Head (#1)

Territory	FY91 Forecast	FY92 Plan	% Growth vs. Fore
UK	$1,056	$1,109	5.0%
Nordic	$1,204	$1,388	15.3%
German/Aust	$1,433	$1,678	17.1%
Switzerland	$1,784	$1,360	(23.8%)
France	$1,816	$1,706	(6.1%)
Iberica	$619	$828	33.9%
Benelux	$998	$1,121	12.3%
Italy	$776	$904	16.5%
Europe Total	$1,335	$1,424	6.7%

#1: Based on year end retail, marketing, and NBU headcount. All revenues calculated using FY92 exchange rates; excludes OEM commissions.

Revenue per CPU and Market Share

Revenue per PC will continue to increase significantly in almost every subsidiary in FY92, with a 34.9% increase planned for Europe as a whole. On the Macintosh, many subsidiaries are forecasting a decrease in $/Mac in

X 166803
CONFIDENTIAL

FY91, largely due to the introduction of the low cost Classic machines. However with the exceptions of Germany and Iberica, this situation will be reversed in FY92, with solid increases budgeted in most subsidiaries.

Revenue per CPU (#1)

	$/PC					$/Mac				
Territory	FY90	% Growth 91/90	FY91	% Growth 92/91	FY92	FY90	% Growth 91/90	FY91	% Growth 92/91	FY92
UK	$44	9.1%	$48	50.0%	$72	$112	(2.7%)	$109	12.8%	$123
Nordic	$57	56.1%	$89	43.8%	$128	$85	12.9%	$96	41.7%	$136
German/Aust	$67	55.2%	$104	40.4%	$146	$116	(10.3%)	$104	(37.5%)	$65
Switzerland	$93	21.9%	$114	38.2%	$157	$74	(40.1%)	$44	93.2%	$86
France	$122	30.3%	$159	17.0%	$186	$167	(27.5%)	$121	0.8%	$122
Iberica (#2)	$13	59.9%	$21	14.0%	$24	$19	13.3%	$22	(1.3%)	$22
Benelux	$30	63.3%	$49	59.2%	$78	$106	(18.9%)	$86	16.3%	$100
Italy	$32	46.9%	$47	31.9%	$62	$55	(32.7%)	$37	32.4%	$49
Europe (#3)	$60	41.0%	$84	34.9%	$114	$112	(17.0%)	$93	6.3%	$99

#1: All revenues based on FY92 budget exchange rates; excludes update revenue.
#2: Includes Spain only.
#3: Weighted average based on CPU shipments per country.

Market shares in the various countries follow a similar trend. With PC products, the FY91 to FY93 trend is generally very positive across Europe. Macintosh market share projections are more mixed with some countries forecasting modest share declines. This reflects both the increase in Classic sales and our high market shares in some categories where competition is increasing.

Category Share by Country (#1)

	Total PC WP Share			Total PC SS Share			Total PC Integ Share		
Territory	FY91	FY92	FY93	FY91	FY92	FY93	FY91	FY92	FY93
UK	25%	29%	32%	20%	27%	35%	30%	38%	39%
Nordic	18%	24%	36%	43%	44%	49%	49%	39%	44%
Germany (#2)	60%	56%	56%	50%	52%	57%	32%	37%	41%
Switzerland	46%	50%	51%	40%	42%	47%	24%	38%	40%
France	71%	73%	74%	56%	55%	54%	75%	65%	61%
Iberica	18%	21%	N/A	19%	22%	N/A	41%	42%	N/A
Benelux	22%	28%	33%	20%	27%	36%	57%	63%	61%
Italy	49%	52%	52%	30%	38%	41%	43%	61%	68%

	Total Mac WP Share			Total Mac SS Share			Total Mac Integ Share		
Territory	FY91	FY92	FY93	FY91	FY92	FY93	FY91	FY92	FY93
UK	85%	87%	83%	79%	80%	78%	90%	94%	86%
Nordic	33%	30%	30%	72%	75%	77%	20%	25%	28%
Germany (#2)	52%	55%	55%	86%	81%	70%	18%	33%	37%
Switzerland	46%	48%	49%	82%	83%	81%	50%	52%	51%
France	73%	68%	67%	91%	82%	78%	59%	53%	53%
Iberica	17%	17%	N/A	54%	52%	N/A	N/A	N/A	N/A
Benelux	74%	71%	76%	81%	84%	86%	81%	82%	83%
Italy	53%	56%	58%	81%	80%	81%	64%	59%	62%

#1: Based on data from subsidiary business plans. Includes all Microsoft products in the category.
#2: Does not include Austria.

X 166804
CONFIDENTIAL

Territory	Mouse FY91	Mouse FY92	Mouse FY93	Networks FY91	Networks FY92	Networks FY93
UK	27%	31%	34%	20%	22%	42%
Nordic	58%	54%	50%	30%	35%	38%
Germany (#2)	38%	40%	42%	14%	24%	33%
Switzerland	33%	33%	32%	3%	12%	20%
France	56%	63%	67%	38%	40%	40%
Iberica	42%	45%	N/A	18%	19%	N/A
Benelux	64%	65%	67%	13%	20%	24%
Italy	28%	27%	27%	21%	26%	31%

#2: Does not include Austria.

European Market Shares (#1) (#2)

	FY91	Diff FY92/91	FY92	Diff FY93/92	FY93 (#3)
WP-PC					
Microsoft	43.4%	2.6%	46.0%	4.1%	50.1%
WordPerfect	27.9%	-0.3%	27.6%	-3.0%	24.6%
IBM	9.6%	-1.8%	7.8%	-0.8%	7.0%
Lotus	2.5%	2.1%	4.6%	0.6%	5.2%
All Others	16.6%	-2.6%	13.9%	-0.9%	13.0%
Total	100.0%		100.0%		100.0%
WP-Mac					
Microsoft	59.8%	-3.4%	56.4%	0.8%	57.2%
Claris	32.8%	-5.9%	26.9%	0.8%	27.7%
All Others	7.3%	9.3%	16.6%	-1.5%	15.1%
Total	100.0%		100.0%		100.0%
SS-PC					
Microsoft	38.4%	4.5%	42.8%	5.8%	48.6%
Lotus	42.3%	-2.4%	39.9%	-5.0%	34.9%
Borland	8.6%	2.2%	10.8%	0.5%	11.3%
All Others	10.7%	-4.3%	6.5%	-1.3%	5.2%
Total	100.0%		100.0%		100.0%
SS-Mac					
Microsoft	83.5%	-3.2%	80.2%	-2.4%	77.8%
Informix	8.8%	-2.5%	6.3%	-0.9%	5.4%
All Others	7.7%	5.7%	13.4%	3.3%	16.8%
Total	100.0%		100.0%		100.0%
Integ-PC					
Microsoft	45.0%	1.3%	46.3%	2.9%	49.2%
Lotus	26.3%	3.2%	29.5%	-0.8%	28.6%
All Others	28.7%	-4.5%	24.2%	-2.0%	22.1%
Total	100.0%		100.0%		100.0%
Integ-Mac					
Microsoft	50.0%	-0.9%	49.1%	0.9%	50.0%
Ragtime	35.8%	2.2%	38.0%	-2.3%	35.7%
All Others	14.2%	-1.3%	12.8%	1.4%	14.2%
Total	100.0%		100.0%		100.0%

#1: Rollup of sub forecasts; includes all of a company's products in the category.
#2: "Other" is often large because not all products were listed explicitly by each sub.
#3: Does not include any data for Iberica.

X 166805
CONFIDENTIAL

European Market Shares (cont) (#1) (#2)

	FY91	Diff FY92/91	FY92	Diff FY93/92	FY93 (#3)
Mice					
Microsoft	38.5%	2.7%	41.1%	2.3%	43.4%
Logitec	36.2%	-3.0%	33.1%	0.0%	33.1%
All Others	25.4%	0.4%	25.7%	-2.3%	23.5%
Total	100.0%		100.0%		100.0%
Networks					
Microsoft	23.2%	3.7%	26.9%	8.4%	35.2%
Novell	55.8%	0.6%	56.4%	-6.5%	49.9%
All Others	21.1%	-4.3%	16.8%	-1.9%	14.9%
Total	100.0%		100.0%		100.0%

#1: Rollup of sub forecasts; includes all of a company's products in the category.
#2: "Other" is often large because not all products were listed explicitly by each sub.
#3: Does not include any data for Iberica.

5. EUROPEAN ORGANIZATION AND EUROPEAN HEADQUARTERS

When the European Headquarters was founded 24 months ago, Microsoft was active in Europe in seven offices, staffed by just over 400 persons with retail revenues in FY89 of just over $200M. Over the last two years we have grown tremendously. During FY92, we will be operating out of 15 national subsidiaries, total staff will pass 1,600 persons (a factor of 4 when compared with FY89) and retail revenues will probably pass the $1,000M mark (a factor of 5 when compared with FY89).

At the same time the markets in which we operate have become more complex. Our product offering is more extended: we have entered new, much more technical and demanding markets (NBU) and are contemplating new areas of development (Mail, Database). We have also raised the level of quality expected from our services, both internal and external. We have set challenging goals for PSS and Operations and have added Consulting and MSU to our service offering.

All this has been done without modifying the structure of our European operation, defined in May 1989. As a result, most management time is spent on operational issues and not enough reserved to strategic thinking. With Jeremy Butler's departure, it is time to reflect on the current organization and propose a model for the next two years and beyond. The proposed evolution outlined below calls for a restructuring of field operations into three regions and an extension of the European Headquarters functions.

European Regional Organization

Once the decision to create regions in Europe was taken, the possible options were multiple: 3 to 5 regions, internal or external hires as Directors, field or EHQ based ...or some combination of the above! After multiple consultations, we have decided to create three regions, to fill the Regional Director positions internally from Microsoft in Europe, and to locate them in the field, thus easing the transition and strengthening their role as "Operational Directors". All three Directors will report to the Vice President, Europe. Starting July 1, 1991 the European structure will be as follows:

X 166806
CONFIDENTIAL

- Northern Europe: Nordic and the UK
  6 countries in FY92
  $210M Retail Revenues
  $15.5M OEM Revenues
  417 staff
  Regional Director: Rolf Skoglund, Stockholm

- Central Europe: Germany, Switzerland, Austria, and Eastern Europe
  3 countries ... plus numerous distributors in FY92
  $350M Retail revenues
  $21M OEM Revenues
  546 staff
  Regional Director: Christian Wedell, Munich

- Southern Europe: France, Benelux, Italy, Spain, and Portugal
  6 countries in FY92
  $370M Retail Revenues
  $22M OEM Revenues
  684 staff
  Regional Director: Michel Lacombe, Paris

The objective of this regionalization is to improve efficiency and add value to the structure. A large segment of the Vice President, Europe's authority will be delegated down to the Regional Directors for immediate action. They will see to the proper staffing, training and development of the General Managers and direct reports, own a vision of the long-term growth and real profitability of their subsidiaries, and make sure that there are multi-year strategies in place. They will approve most subsidiary administrative policies within the constraints of Corporate policy, and in concert with the Business Units and IPG, they will drive the product planning and localization decision process. Their local staff will be limited to an executive assistant and an admin, but the EHQ resources will be available to them. The Regional Directors will remain in the field. They will also remain the legal representative of their current subsidiary but will totally delegate the day to day management to a new General Management staff.

Together with this new European structure, we will also evolve the structure of the largest subsidiaries. The current Sales and Marketing Managers, Mats Wennberg in Sweden, Jochen Haink in Germany, and Jean-Philippe Courtois in France, will be promoted to the new position of General Manager of Sales and Marketing. Additionally, the recognition of the importance given to all forms of "services" will be highlighted by the creation in these subsidiaries of "Business Operations" management positions. Business Operations will include the management of F&A and PSS and will thus supervise all Microsoft service functions, both internal and external (including HR, Facilities, MIS, and Warehouse). The mission for these groups is to ensure the excellence of all services provided by Microsoft. These management positions, only justified at the Director or General Manager level, will also offer career paths to non Sales/Marketing executives. Three such positions are being created:

- Director of Business Operations, TBH, in Stockholm reporting to Rolf Skoglund, Regional Director;

- General Manager of Business Operations, TBH, in Munich reporting to Christian Wedell, Regional Director;

- General Manager of Business Operations, Jean-François Heitz, in Paris reporting to Michel Lacombe, Regional Director.

Each Regional Director will then have two direct reports responsible for the day-to-day subsidiary management in his country of origin: a General Manager of Sales & Marketing and a General Manager (or Director) of Business Operations.

European Headquarters

The European Headquarters (EHQ), in its unchanged charter, will continue to supervise European operations, to coordinate the activities of the subsidiaries in the field, and to supply guidance, coaching and foster cross communication between the operational groups. More than in the past, the EHQ will need to focus on strategic reflection and act as a source of input from the field for the corporate business units and organizations.

During FY92, the two existing functional groups of the EHQ (Systems Marketing and Channel Development) will be further developed and a new group (F&A) will be formed. The EHQ staff will grow to 47 people, and in November 1991, we will move to a new office space in La Défense. See Appendix A for a complete EHQ organization chart.

Systems Marketing Group:

The European Systems Marketing Group is organized into two product units (network products and desktop operating systems) and two service functions (developer programs and marketing services including PR).

Efficient and consistent policy definition, negotiation and implementation for all of Europe is the primary focus of the product groups. We will continue to develop the business model that combines each countries' local overall responsibility for Microsoft's systems business into a tightly synchronized international organization. The European Systems Marketing Group represents Microsoft's European corporate interest in this process.

The two marketing services groups operate across product lines. They offer services to and in coordination with the European subsidiaries. We apply the following restrictive criteria to the centralization of services at Microsoft Europe:

- Obvious value add from central service; example: PR coordination.
- No value add from local duplication at higher cost; example: market research.
- No cost justification on a country-by-country basis; example: specialized ISV evangelists.

Monthly (in some cases bi-monthly) meetings of the subsidiary business unit and marketing managers have been established as business management bodies. They follow the CMM model. Their regularity and focus allow us to take full advantage of the subsidiaries' marketing expertise for the implementation of European marketing programs. The meetings also drive the presentation of consolidated European positions on systems product and marketing strategies to the Systems Division in the US.

The Network Business Units have already established multiple, sophisticated reseller channels for LAN Manager and client server applications during their first year of operation. They have also built systems selling expertise inside Microsoft. The eventual integration of the NBUs into the subsidiaries' mainstream organizations offers considerable benefits to the local corporate accounts and channel sales teams. We plan to coordinate this organizational evolution with the Country Managers and the European Channel Development group.

Desktop Operating Systems: The budgeted increase in Windows penetration on eligible machines by 12 points to 44% can only be achieved if the subsidiaries capture the full potential of additional Windows sales behind the release of new Windows applications (Lotus, WordPerfect, ...) and successful reference selling. We will provide optimal support for the programs that are designed to grow Windows retail sales during the remainder of the Windows 3.0 product life cycle: seminar programs, Windows Resource Kit, Windows World events, etc. A very tight localization schedule (30 - 90 days delta) for all localized versions of Windows 3.1 is crucial in order to achieve the projected 40% increase in monthly sales with the new release.

The key to success with DOS 5 is to build sales and momentum fast. The DOS 5 Upgrade is a new product category with unique marketing, distribution, and support requirements. The countries have forecast widely diverging DOS 5 Upgrade penetration rates in the FY92 budgets. It is our goal at the European level to help them achieve consistently high performance in this area. We will conduct monthly, at the beginning, and then quarterly DOS 5 business reviews in order to identify the causes of performance differences and to highlight additional business opportunities.

We will monitor DOS 5 sales on new PCs sold in Europe in the second half of FY92 when PC manufacturers can be expected to have all localized versions in their channels. PR will play a crucial role to establish that users and PC dealers should only accept DOS 5 when they purchase new PCs. DOS 5 Upgrade sales have been budgeted to reach 3.5% of the European installed base by the end of FY92.

Network Products: The European Network Business Units' budgets are much more ambitious than the US budget for FY92. The subsidiaries continue to pursue the market share growth path of the initial International Network Business Plan. The European FY92 budgets are based on the assumption that new product versions and functionality enhancements will become available for LAN Manager 2.x as currently scheduled. They also rely on the release of a Microsoft OS/2 Packaged Product for PC manufacturers. Microsoft's European marketing strategy for network products must encompass both the current OS/2 based products and future Win-32 based network services in order to maintain credibility and continuity. The eventual shift to Win-32 based products must emerge as a gradual transition as these new products are being released.

Microsoft Europe will concentrate its network marketing efforts on client server solution selling as well as on the launch of VAR, systems integrator and consultant programs. New services and training programs will be driven by the European group. One initial market research project in the first half of FY92 will be designed to identify success stories and failures for Microsoft's network business.

European ISV Program: A new group of seven Microsoft ISV evangelists is the central element of the European ISV program. They will form a closely knit team that conducts specialized developers workshops, SDK alpha and beta programs, in addition to the on-going Developers Conference Series and a new formalized Microsoft Developers Program. This new European ISV program acknowledges that the availability of powerful applications is the most important factor for the success of an operating system. We will build the European team and its developer services throughout the year. European Windows developers will ultimately receive a similar level of support to that which is available from Microsoft in the US. The centralized European group has also been chartered to support local ISV programs in each country and to generate the developer feedback that will allow PSS to offer better developer services.

Public Relations: The greatest PR challenge is to portray a positive image of Microsoft's attitude and track record for openness, credibility and partnership in the PC industry. It is equally important to create a high-tech image for Microsoft Windows against the IBM / Unix coalition who position DOS and Windows as non-professional toys.

<u>Channel Development Group:</u>

FY91 saw the start-up of the European Channel Development Group still in its infancy. The mission of the group is to address pan-European issues concerning our customers, distributors, and dealers and to try to improve communication between the subs and between Europe and Corporate. While initial headcount needs have been assessed, the first few group members hired, and the mission statement for the group written and circulated, FY92 will be the year when we first fully staff the group and are able to pro-actively put strategies, structures and systems in place to vault Microsoft well past $1 billion in revenues in Europe as well as help cement fruitful partnerships between ourselves and our customers.

The three key goals of the group for FY92 are:

- We plan to reach clear agreement on our relationship to the channel and the implications it has for corporate account selling. We will continue to monitor the effect the consolidation of the channel and Europe 1993 have on the structure of our relationship with the channel. We will continue to harmonize the SRP's and channel terms and conditions across Europe. We will formulate terms for large volume and pan-European (or worldwide) deals for corporate accounts that both use the channel as our delivery mechanism (where we own the account) and which the channel can offer to accounts on their own.

- We will use closer partnering with the channel to get reporting mechanisms in place and help improve our distribution operations. We will do a detailed profiling of the channel in FY92 to determine who will be the winners and losers in this changing environment. Accurate data on sell-through and large account sales are a prerequisite for sophisticated sales expansion programs and performance measurement. We also need to examine ways to increase the sophistication of our sales order and delivery system to both reduce our costs and our dealers' costs, as well as assure better delivery in countries like Switzerland and Belgium.

- We will build a structure for large account selling which integrates the many elements Microsoft offers (products, consulting, training, and support) and reflects the international nature of our operations. In addition to putting in place a structure for large volume sales, we need to fix firmly the framework for offering and responding to requests for pan-European and worldwide treatment. In addition, we need to migrate our selling ability forward as we move away from being a vendor of packaged product software towards a vendor which sells an integrated platform of office automation software, networking, and services.

<u>OEM:</u>

The European OEM business is managed out of Redmond by Jeff Lum. The challenge for this group next year will be to maintain motivation and generate new business in a market where most European OEM's are fighting for survival. On-going and new challenges will be faced: converting DRI OEMs, ensuring RISC design-wins towards OS/2 3.0, closing Multimedia and Pen Windows OEM deals, and hopefully exceeding budget for FY92.

<u>Microsoft Consulting:</u>

Gordon Ross, who directs this group in Europe, is located in our UK subsidiary and is a dotted line report to the Vice President, Europe. The challenge for Consulting in FY92 is to achieve the necessary market recognition to generate the required revenue. A higher market profile will also help in recruitment which is likely to continue to be difficult given the quality standard that has been established with the first recruits to Consulting. Consolidation of our presence in Germany, the UK, and through CORIS in Italy, and the establishment of a consulting capability in France, are all key goals. Servicing opportunities in other countries from this base will be a priority. FY92 should be the year that Microsoft becomes recognized in Europe as a provider of quality consulting services which deliver real and lasting client value through exploiting the potential of the personal computing platform.

<u>Finance & Administration:</u>

With the growth we have experienced and the level of demand imposed on the subsidiaries, it became clear during FY91 that some level of centralized "consultancy" and help was needed in the Finance and Operations areas. The creation of an F&A group at the EHQ will fulfill this need. The Finance side will be primarily oriented towards analysis and guidance of the field operations. The HR group will focus on developing the right methodology to help and guide subsidiaries in their hiring and training tasks. An Operations person will be responsible for all pan-European issues relating to logistics, product creation and supply, and cost of goods. The MIS Manager will coordinate the development of the MIS functions in each sub, determine pan-European needs, in particular in the area of database management, and put in place the necessary actions to provide solutions. This group, expected to be staffed by nine persons, will be managed by a Director of Finance & Administration, Europe, who will be a dotted line report to the Vice President, Europe.

Legal:

The Legal Group at the EHQ will grow from the current two people to five by the end of FY92. This will allow for better follow up on day-to-day legal activity and provide improved legal consultancy support to the subsidiaries. Of course, we will continue our anti-piracy efforts along with our involvement in the BSA.

PSS:

The challenge for PSS in FY92 will be to better meet the support demand in each country and to make PSS a great place to work and enhance one's career. European PSS management, based in Redmond and reporting dotted line to the EHQ, has three major goals: (1) to participate in an International PSS customer satisfaction survey to measure customer satisfaction in each country; (2) to coordinate the implementation of support tools and technologies enhancing the productivity of the support engineers; and (3) to ensure that the training demands for European PSS are well met, both at the technical as well as management level.

6. CONCLUSION

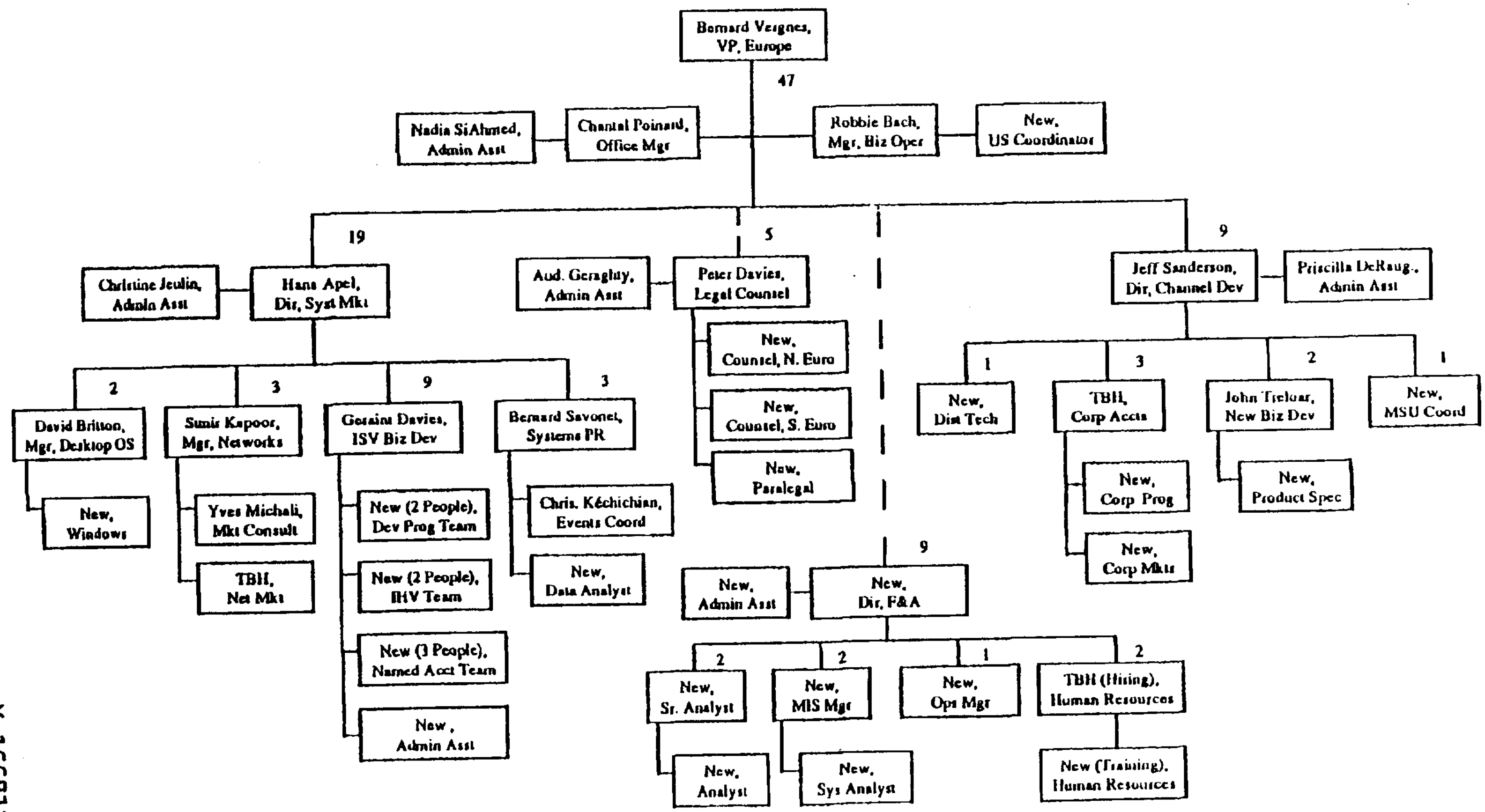
With direct subsidiaries in 15 European countries, Microsoft will be well prepared in FY92 for the Europe 1993 challenge. The proposed structure will strengthen our organization and further facilitate cooperation and communication between countries. Nevertheless, we will face multiple challenges:

- Our competitors will enter the market with new Windows products that will force us to defend entrenched positions and hopefully further develop our successes.
- Our final actions in the pricing area still need to be determined. Our budget calls for an aggressive reduction of our prices by more than 10%. We might not be obliged to carry out all of these changes, but there is also a remote chance that we might need to do more based on the competitive situation.
- Our image and our relationship to our customers, partners and the industry as a whole need to regain a level of "serenity" that has been lacking lately. Fighting arrogance and supplying the best quality products and services are part of the corporate mission.
- All employees and their managers need to feel at ease in the new structure and be ready to exceed their own expectations and skills. With our past growth record and with more growth ahead of us, too often people feel over-stretched and unable to give their best. Better training (quite often just taking the time for it) and still more communication should help everyone.

The rewards will be great. The proposed plans are challenging but realistic and achievable. Based on past experience, I know that we can count on everyone's complete energy and commitment. There are good reasons to be confident that in FY92 Microsoft Europe will become the second software company in the world to achieve more than $1 billion in sales in the micro computer industry.

X 166811
CONFIDENTIAL

Appendix A
EHQ Organization



X 166812
CONFIDENTIAL