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PLAINTIFF'S EXHIBIT 2010 Comes v. Microsoft

Productivity Applications Mission, FY95-97
DRAFT, 2/2/94

Executive Summary

Microsoft has gained the lead in productivity applications with superior products, early exploitation of Windows and the Macintosh, leadership in the office suite category, and the missteps of DOS leaders Lotus and WordPerfect. Both, however, have rebounded from these early errors and are now shipping competitive products. Lotus is particularly strong thanks to their creation of SmartSuite through acquisition and their competitive advantage in workgroup applications with Lotus Notes. Borland and WordPerfect are trying to catch up with Borland Office 2.0. Our applications compare favorably today and have considerable momentum and market share — 70+% of the suite category and ~50% share of Windows word processing, spreadsheet, presentation graphics, and project management — but the market increasingly views the alternatives as near-substitutes. This, plus increasing price competitition threaten to permanently damage the business.

Our mission is to develop the most successful desktop productivity tools in the world, marketed both as suites and standalone applications. Our market share goal is 80% for office suites and 60% for apps, including spreadsheet, word processing, presentation graphics, database, and project management. Achieving these goals hinges on our ability to sustain product development momentum, leverage other Microsoft assets (e.g. pss), and create innovative marketing approaches to increase differentiation vis-à-vis Lotus and Borland/WordPerfect. At the same time, we have aggressive internal goals for reducing costs, particularly cost of goods sold, documentation and localization costs, and increasing development and marketing efficiency.

$2.8B is a reasonable revenue target for FY1997. The market for productivity applications is maturing, but growth will not come to a screeching halt, and the annuity opportunity from our installed base will continue to increase. Even with moderate growth in major markets, narrowing of the uplift between European and North American prices, and price deterioration due to competition and mix changes, we can continue to grow this business.

Outlined below is a high-level view of the market today, the competition, and the product and marketing strategies needed to continue to grow the business profitably.

Business Model

Steve's FY95 business planning memo projected Desktop Applications Division to be $1.8B in FY97 based on 2.3M competitive/version upgrades @ $100, 3M Office competitive/version upgrades @ $150, 2M standalone products at $200, and 2.4M new Office @ $300.

Forecasting 3 years out is an inexact science. There are enough variables in this analysis for pages of scenarios. Summarized below for your consideration is an alternative $2.8B FY97 view of the Desktop Applications Division based on reasonable assumptions about market growth, pricing pressures, changes in the license mix, changes in market share, and our ability to upgrade our installed base. The following takes a trend-line approach based on the existing business, accelerating current changes in license mix and downward trends in price. It is reasonable, if not a bit conservative. Relative to Steve's projection, it is more conservative on price (average revenue per license of Office $247 versus $300, single app version upgrade revenue of $73 versus $100). On the other hand, the combination of more aggressive category growth and higher upgrade percentage contributes to the $1B difference.

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Desktop Applications FY97 Projection

Units in Thousands, Revenue in Millions

	FY94 Forecast			FY97 Projected					
	Licenses	$/unit	Revenue	Licenses	Growth	$/unit	Growth	Revenue	Growth
Office New Users	2,580	$ 355	$ 915	5,045	96%	$ 247	-30%	$ 1,246	36%
Other Apps* New Users	6,264	$ 158	$ 989	5,916	-6%	$ 143	-9%	$ 848	-14%
Office Existing Users	543	$ 139	$ 75	2,349	333%	$ 109	-22%	$ 256	239%
Other Apps* Existing Users	2,372	$ 89	$ 210	6,600	178%	$ 73	-17%	$ 483	130%
Total DAD Revenue			$ 2,190					$ 2,832	29%

* *Word, Excel, PowerPoint, Project*

Category Growth

Desktop Applications Categories: Growth Projections

Licenses in Thousands

	FY92	FY93		FY94		FY95		FY96		FY97	
	Licenses	Licenses	Growth %	Licenses	Growth %	Licenses	Growth %	Licenses	Growth %	Licenses	Growth %
Windows											
Suites	325	1,581	387%	2,797	77%	3,916	40%	5,287	35%	6,873	30%
Other Apps*	6,589	13,277	101%	22,384	69%	26,881	20%	30,256	13%	33,608	11%
Macintosh											
Suites	108	187	74%	202	8%	212	5%	223	5%	234	5%
Other Apps*	1,702	2,009	18%	1,586	-21%	1,675	5%	1,758	5%	1,846	5%
Total Units	8,291	15,285	184%	23,979	57%	28,535	19%	32,013	12%	35,454	11%

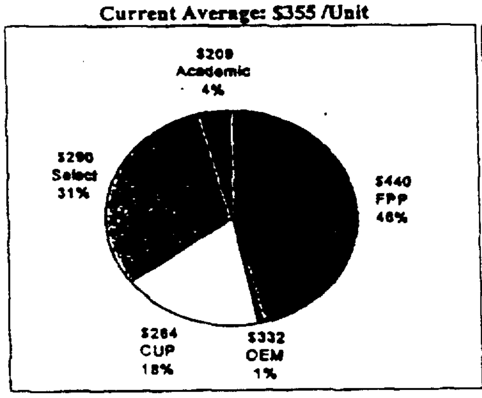
* *Word Processing, Spreadsheets, Presentation Graphics and Project Management. Includes Suite licenses in categories*

DISCUSSION:

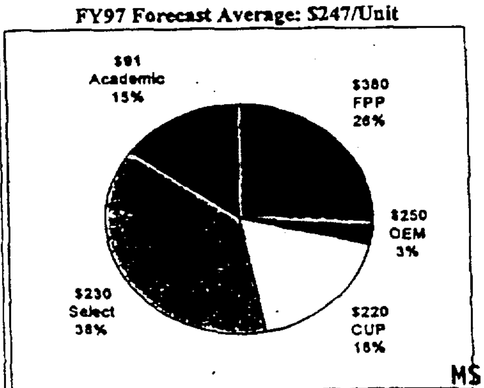
- Actual data from SPA. Estimates based on IDC forecasts.
- FY94-97 new user growth slows due to market saturation. We need a far greater understanding of this trend.
- Analysis assumes new user units decline from 74% of our business in FY92 to 55%. This is close to Steve's *New/Existing user mix.*
- Suite licenses are included in the "Other Apps" line. Their growth accounts for overall industry growth as individual application sales slow dramatically.
- Assumes the high-end Mac business resumes moderate growth with the Power Macintosh.

New-user Office License Mix and Revenue per Unit

Current Average: $355 /Unit



FY97 Forecast Average: $247/Unit



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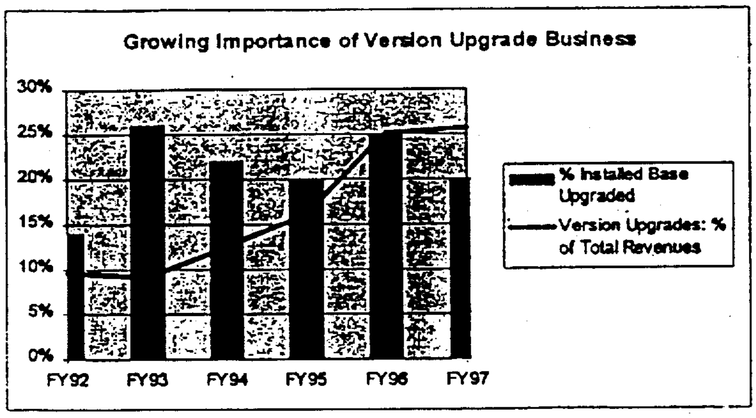
- We project the average price per Win Office license to decline about 30% over three years to $247. This is slightly faster than with the 10% drop ($393 to $340) from FY92-94.

Discussion:

- Revenue per unit declines as international prices settle to a 1.1 uplift, we respond to competitive price pressure overall, and lower priced SKUs (OEM, Academic, and Select) figure larger in the mix.
- FPP ($440 to $380) and CUP($284 to $220) revenue per unit declines on competitive pressure and increase in license mix.
- Forecast assumes Office reaches 70% of Word and Excel units by FY97.
- Office Academic and Select mix rise dramatically due to new Office academic SKU and continued emphasis on Select business in corporate accounts.
- Academic single app mix drops as users move to Office.
- OEM app mix rises (conservatively) as competitive pressure in this channel continues, especially outside the US.

Version Upgrade Business



ASSUMPTIONS:

- **Version upgrades increase to a larger percentage of total mix due to growing installed base relative to new users. If 20% of our installed base upgrades for $73 in FY97, the VUP business is $793M. The comparable business will be $285M in FY94.**
- **Version upgrade rates vary based on major and minor releases. Overall, the rate is assumed to decline due to increasing frequency of updates and because the aggregate number just seemed to be getting too big. Also, a larger % of the cumulative number becomes user of older versions who are expected to be less likely to upgrade.**
- **A one-percent increase in the annual upgrade rate is worth about $31M in FY97 (all Desktop Applications Division products, worldwide).**

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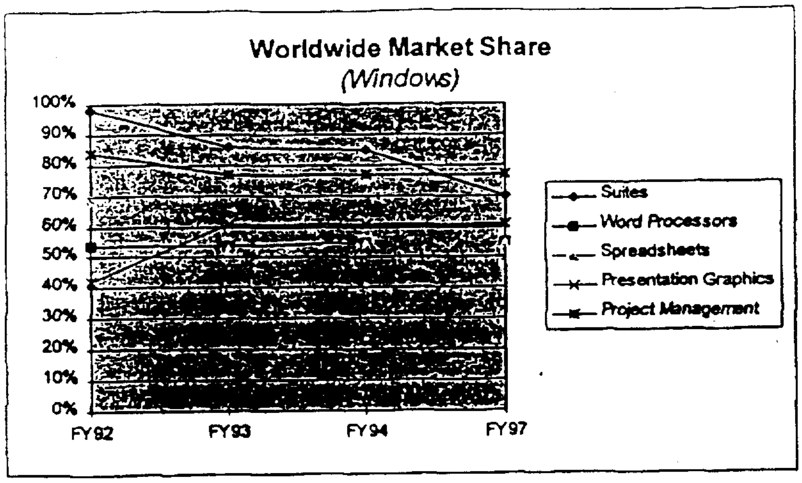
Market Share



Discussion:

- Office share trends down over the period due to improved Lotus product and marketing focus. This also assumes that Notes momentum hurts our share position, and there is some downside risk that share could drop below 70% level if we can't stem the tide.
- Worldwide standalone applications share stabilize at 55%.
- *Net effect on desktop apps share is still positive because of market shift to office suites where we have higher absolute share.*
- Although difficult, significant growth potential exists through market share growth.

OTHER BUSINESS ISSUES

Falling prices over the next 3 years require us to reduce costs in order to maintain or at least slow margin deterioration. COGS and headcount issues are briefly discussed below. PSS costs still need to be addressed. Above all, we need to build a complete model for productivity applications profitability for the next 3 years to better understand the changing business model.

Although the average price per license has fallen about 25% over the last 2 years (all licenses, worldwide–$191 to $142), product COGS as a percent of revenue has remained flat for the Desktop Applications Division.

COGS as a % of Gross Revenue

	FY92	*FY93*	*FY94 (YTD)*
North America	11.2%	10.4%	9.6%
Europe	8.6%	8.3%	8.1%
ICON (ROW)	11.5%	13.0%	12.6%
Far East			17.1%
OEM	5.3%	1.2%	0.8%
Total	9.9%	9.6%	9.5%

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Clearly, several factors are at work that need to be modelled more rigorously. At least in the US, however, product costs for Win Office (shown below) and other applications have remained flat such that growth in low-

- cogs license revenue has basically offset declining prices. COGS in general needs more attention. The COGS of CD-Office 3.0 is included to highlight the potential of rapid acceptance of CD Rom distribution.

Domestic Win Office COGS

	Win Office 3.0	Win Office 4.0	Win Office 4.2	Office CD ROM 3.0
Media	$15.88	$14.12	$22.95	$3.57
Documenation	$28.74	$23.81	$16.84	$0.00
Other	$4.33	$4.92	$4.92	$2.45
TOTAL	$48.96	$42.85	$44.71	$6.02

Headcount

Desktop Applications Division
Headcount by Function

	Actual						Budget									
	Jun-92		Jun-93		Dec-93		Dec-93		Jun-94		Jun-95		Jun-96		Jun-97	
Function																
Management	18	3%	21	3%	20	3%	35	5%	35	5%	37	5%	39	6%	38	6%
Program Mgmt	69	11%	95	13%	107	16%	107	15%	104	15%	120	18%	120	17%	120	17%
Development *	164	26%	209	29%	181	27%	198	28%	200	29%	200	29%	210	30%	220	31%
Test	137	22%	140	19%	143	21%	148	21%	148	21%	148	22%	150	22%	150	21%
User Ed	178	28%	184	26%	137	20%	157	22%	135	19%	110	16%	110	16%	110	16%
Marketing	65	10%	71	10%	83	12%	74	10%	72	10%	65	10%	65	9%	65	9%
Subtotal	629	100%	720	100%	671	100%	719	100%	694	100%	680	100%	694	100%	704	100%
Growth			*14%*		*-7%*						*-2%*		*2%*		*1%*	
Ireland			106		92		100		91		85		80		80	
Japan					109		109		109		100		90		90	
Buffer							27		47		0		0		0	
Grand Total	629		826		872		955		941		865		864		874	

Discussion:

- Overall, headcount for the Desktop Applications Division is projected to be nearly flat to over the next 3 years. We will experience a nearly 10% decrease in actual headcount in FY94 (ex Ireland and Japan) due to reductions in eser education and localization heads and will close the fiscal year at about 660 heads. Ireland and MSKK will be a total of about 30 heads below plan for a grand total of about about 100 heads below plan.
- Future declines in other functions will be matched by modest increases in development capacity and program management (esp. FY95). Testing is assumed to flatten due to improved efficiency.
- UE will decline as a percent of the overall headcount mix due to shrinking documentation size, increased outsourcing, and improved process. This analysis assumes flat UE headcount from FY94 forward (actuals).
- Marketing is assumed to decline by about 10% from FY93-FY95 and then flatten.

Competitive Situation

Lotus. Lotus is a formidable competitor. Thanks to accelerating momentum behind Notes (including a growing list of third parties adding value to it), Windows SmartSuite, OS/2 SmartSuite, improving financials and company image, 20 million customers, high product awareness, broad distribution, and an alliance with IBM that is increasingly having an impact on corporate purchase decisions, Lotus is on the upswing. Lotus will continue to push Notes as a computing platform and will integrate their apps more tightly using Lotus Basic, Application Field Exchange, and OLE. Notes, plus the little work they've done with AFE and Version Manager, has positioned them as the leader in workgroup computing and SmartSuite as the leading workgroup application. Microsoft must effectively challenge Notes with EMS and later with Cairo. We must provide better workgroup features in our productivity applications, including support for Notes as a back-end, to break this perceived advantage.

WordPerfect. The time has never been better to seize WordPerfect's traditional franchise. New CEO Ad Reitveld has announced plans to diversify the business, with word processing expected to contribute only a third of revenues by FY97, while he is aggressively shrinking the company to achieve greater profitability. They launched the final release of its flagship DOS product and have backed-off from their free support policy, historically their most valuable asset. Their challenge is to quickly become competitive in the suite market through their alliance with Borland while growing their workgroup and consumer businesses.

Borland. The price renegade in the industry, Borland recently announced the success of its Quattro Pro promotion — one million new users — and quarterly earnings of .02 per share. The company, leaner through layoffs, has been nimble in introducing features that keep a semblance of parity with ours. The Borland bundle, which is priced at parity with Office, has not garnered serious interest in the market.

Claris. Works is pressuring our premium standalone apps business and challenging the value proposition of our suites. Claris is strong and well positioned. Its revenues grew 48% to $154m in FY93, and its awareness more than doubled to 17%. On the Mac, where Works is frequently bundled, the integrated category is growing faster than the total Mac software market.

Product Strategy

The 3-year strategy for productivity applications is based on the following principles:

- **Focus on Office first, but continue category innovation.** The suite category is the fastest growing in the business and is an area of competitive advantage for Microsoft, especially versus historically single-product competitors like Borland and WordPerfect. Increasingly, many of the traits that define a great application are becoming common to all of the productivity applications. As with Office 4.0, future areas of focus will include ease of use (IntelliSense features, improved discoverability), user interface consistency, interoperability between the applications, and programmability. We recently created the Office Business Unit to drive this effort. Individual product releases will be synchronized beginning with Office '95, making it easier to share code and designs and much easier to market and sell.

  At the same time, we cannot afford to lose the best of breed battle. It is crucial to the perception of Office, and even the most aggressive scenario for Office cannibalization implies that the standalone application businesses are among the largest in the company.

- **Add value to Office.** We will continue to add value in the form of additional product breadth and value-added data and services. MOM was a good example of leveraged value-added in Office 4.0. REN will be our primary focus in Office '95. The image editor, possibly RPM, and other add-ons/servers are candidates for Office '95 and beyond.

- **Exploit systems releases (and rest of Microsoft).** Microsoft's ability to set industry direction is a key asset for the company and the productivity applications mission. We will time apps releases with systems releases and ensure Microsoft applications uniquely exploit these releases for customer advantage. We will take a similar approach to leveraging other parts of Microsoft, including workgroup applications, Advanced Development and Research, the Consumer Division, and others. An added benefit of release synchronization across divisions is that it facilitates technical cooperation and synergy.

  This plan assumes that Windows (moving to Win-32) and Macintosh remain the dominant platforms in the next 3 years. Other than moving our products to RISC platforms running NT and to the PowerPC Macintosh, no new platforms or operating systems are planned. OS/2 success, even to the point where it becomes the relevant second platform in cross-platform, is a risk in this plan.

- **Build long-term product differentiation.** Although we have benefited from the last releases of the applications, competitors have proven they can neutralize many feature advantages, particularly the user-oriented "auto" type features. We must continue to innovate and invest in sustainable technology advantages. Visual Basic for Applications, PivotTables, Word's AutoFormatter, OLE 2.0 support, and the applications infrastructure effort are examples of features that can differentiate for longer periods of time. We will need to reduce the number of "small" features to achieve this goal.

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- 12/24 is an approach to scheduling releases that allows for major architectural releases every 24 months and competitive releases every 12. Since architectural changes take longer and frequent releases are inefficient and hard on the team, the majority of the development resource will work on the 24 month release. In between, however, up to 25% of the team will develop low-cost, high-visibility releases designed to win reviews, respond to competition, and create upgrade revenue. The goal will be to create much of the value of these releases through add-ons, OLE Servers, and through VBA code rather than changing the core .exe.

- **Best desktop applications for use in a workgroup.** We must build support for workgroup scenarios into all of the applications. They will be designed to support multiple back-ends, including Lotus Notes and others. It is our goal to have better workgroup application support than Lotus.

- **Be the best platform for business solutions.** Productivity applications are increasingly being used as part of company-wide solutions, including solutions that automate important business processes. Getting design wins for these solutions is an important source of business, but more importantly makes the tools the de facto choice for general productivity use and very difficult to dislodge. We will invest more in the use of technologies (e.g. VBA, OLE 2.0, OLE controls and forms, MAPI, etc.) that make our applications great components of customer solutions. The 12/24 development approach recognizes that supporting these technologies often takes longer.

- **Office Friendly.** We will license pieces of the Office UI (and, in the future, Office code) to complementary ISVs and eventually SPs to build an extended family of applications with a common look, feel, and behavior.

- **Organization usability.** Software administration — installation, tracking, updating, supporting — is far too costly for our customers. We took some steps with the integrated Setup and un-install features of Office 4.0, but we have a long way to go to dramatically reduce customer administration costs.

- **Expand into new geographies.** Productivity application market growth will be highest in new geographies, including the Far East, Eastern Europe, and ROW. Development groups will take greater responsibility for Far East development to bring the delta down to 60 days and increase the Far East product content. Deltas for all languages will be reduced to less than 90 days, while improvements in localizability, development of third-party localization partners, and reduction in word count will reduce localization time and cost.

- **New products.** Ren, an integrated PIM and mail client, and Resource Planning Manager (RPM), a non-CPM based planning tool, are two new products scheduled to ship in 1995. Ren will and RPM might be included in Office. They will also be sold standalone. Both have potential to add significant value to the product line and add upside revenue potential to the plan.

- **Increase development efficiency**, including efficiency of code development, user assistance development, and localization. There are redundant development efforts within the mission and across the company. Our goal is to double our use of shared code to 40% by 1996. This plus investments in new tools and processes are needed to address the difficulty and time required to debug and ship these large applications. We will also reduce the number of print-based and on-line words by at least 50% by 1995. This plus increased use of outsourcing and process improvements will address the user-assistance and localization goals.

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Release Plan

We've scheduled two significant releases of Office and its components over the next 3 years, as outlined below.

"Office 94 1/2"

We are considering some tactical activity in 1994 to combat Lotus' growing ability to leverage their Notes success into SmartSuite business. Key features would be support for Application Field Exchange and the ability to save documents into a Notes database. At press time we have not determined whether this is a ".01" release of Office timed for Spring Comdex or an add-in.

Office '95 (March 1995)

Themes
- Exploit Chicago, EMS, Notes, Ren
- Meet competitive workgroup challenge
- Leveraged category features — every feature demoable

Design Goals
- 32 bit version for Chicago and NT
- Potentially 16 bit version for Chicago, Win 3.1, OS/2
- NT, RISC, MAC OS, and PowerPC; "top 10" (possibly other) Int'l versions
- 25% of development effort (done in parallel with Office '96)

Competitive Advantages
- Leadership application of the Chicago generation
- Best support for workgroup scenarios
- Best integration, consistency, programmability

Office '96 (March 1996)

Themes
- Discoverability and ease of use
- Memphis synergy
- Significant category innovation
- Improved performance (operation, file I/O, memory footprint)
- Programmability and customization

Design Goals
- 32 bit only, targeted for Memphis.
- All NT platforms
- Mac (68020 + PPC, Sys 7+ only)
- Office infrastructure 1.0 (shared across applications)
- 75% of development effort

Competitive Analysis of Release
- Sustained leadership in programmability, ease-of-use
- Best support for systems services and other technologies
- Other innovative responses to customer requirements

Marketing Strategy

The core marketing challenge for the next 3 years is to differentiate our products as product features become less sustainable sources of differentiation. This is not to say we will stop trying–marketing our products in traditional ways to traditional customers is the foundation for future marketing efforts. However, we need to adapt to changes in the market, building new marketing assets that are less tied to individual products or versions, reach new customer segments, and exploit new technologies to fight commoditization, gain market share, fight price erosion, and grow the business. Following below are key new strategies, focusing on new customer targets and programs to develop them, positioning and communication challenges, and other promising new marketing initiatives.

Customer Initiatives

- **Large accounts** will remain an important segment, although our message will evolve to be more solutions-oriented. Productivity applications will increasingly be used as components in business solutions. Consistent with our product strategy, we need to develop the infrastructure (SPs), tools, and programs to promote our products as a development platform and get these design wins. They are an important source of revenue, are difficult to reverse once obtained, and will drive definition of company-wide productivity standards.

- **Gain share in small organizations (smorgs).** WordPerfect and Lotus outperform us among organizations with fewer than 100 employees. This segment represents about 25% of the desktops in North America and is growing faster than the market overall. The initial focus will be to raise Office and individual application awareness among smorg influencers with business press advertising, increasing visibility and availability of the product in retail environments, and identifying SPs who develop solutions within targeted segments. Longer term, we must learn to reach the business and industry peers (the most important smorg influentials since most smorgs don't employ computer professionals in a number of targeted industries (accounting, legal, real estate, and insurance).

- **Build an annuity business from our installed base.** We must learn how to generate more revenue from our installed base on a regular basis by upgrading a higher percentage of them, moving more to Office or selling additional apps, or selling them add-ons, data, or service. Building this business profitably, including tools and techniques to reduce the cost of upgrades, will be a challenge. Historically, relatively little attention has gone into understanding the needs of this segment, developing unique product for them, and marketing to them. Yet, in FY97 each 1% increase in upgrade rate is worth about $31M. Additionally, there are over 3 million OEM Works users that we can potentially upsell to Office applications or all of Office. Competitive users will remain an important part of this effort, particularly in upgrading them from a competitive applications to Office Professional.

  Building this business will require better marketing and additional investments in end-user affinity programs such as Microsoft Plus. Various ideas for personal maintenance, subscription, etc. also warrant exploration. We also will need to investigate product strategies (12/24 is a start) that capture the imagination of the installed base and encourage them to upgrade on a regular basis.

- **Solution Providers.** Beginning with Office 4 we are positioning Office as a development platform. Further evolution of the products will make this a stronger message, generating increased opportunity to develop and leverage the SP channel to sell productivity applications to all customer types. Solution providers with content expertise or expertise in key vertical areas can make our products indispensable components of solutions that may be far more compelling than new features. We have the dual challenge of meeting their needs for development platforms and supporting their requirements as remarketers. The solution provider channel will also generate additional demand for special pricing and packaging. Embedded license (runtime) pricing is in demand today and will need to be resolved. We also need to develop a model for reselling individual application components. Over time, we need to define a layer of application functionality that is available to all developers in say the Windows SDK or C Compiler, one that is available to Office Friendly (non-competitive) and proprietary to our applications.

Positioning and Communication

Past positioning strategies have emphasize around the best-of-breed features of individual products, and more recently, features of Microsoft Office. This continue, but our should change:

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- **Define and own the suite category.** In the same way that Lotus defined spreadsheets and WordPerfect defined word processing, Microsoft is the only credible company that can now define and own the suite category. We have a unique opportunity with Office because the suite category is still largely undefined in the minds of most consumers. There must be a high synergy and convergence between key messages for the standalone products and Office to maximize the effectiveness of marketing spending.

- ***Lead with Office, especially Office Pro; balance with standalone applications.*** We have established Office as the required applications platform for many users and will continue to emphasize it. We have to understand how to balance this with standalone applications that may help us in specific user segments and channels, create opportunities for Office upgrades, and redress share loss against competitors' standalone products.

- **Exploit long-term leadership.** Although we have won the majority of product reviews in recent years and have dominant market share, we have not declared victory effectively. Higher awareness of our long-term success would contribute to the perception that Microsoft is the preferred brand and safe purchase.

- **Effectively address the broader market.** Increasingly, growth is coming from customers who are more difficult to reach through traditional techniques. Our traditional IEU-driven influence model still applies, but we will need to identify new approaches to reach these less involved users. The awareness of Microsoft applications is alarmingly low today.

- **Use new approaches to positioning** that go beyond product features. IntelliSense and OfficeLinks are attempts to brand features in a non-version-specific way. Branding Microsoft Office implies establishing a higher level meaning for Microsoft Office to create a long-term asset. We also need to build a marketing asset from our product support advantage. This means communicating our cost and quality advantage, but also developing new programs based on CD distribution, Microsoft On-Line, and special programs such as the Microsoft Support Network. Finally, we have the opportunity to communicate our hardcore commitment to rapidly exploit Microsoft Systems as well as other initiatives throughout the company.

- **Define the new generation of applications.** Coming advances in systems technology must be related to advantages for business usage and tasks and made our unique advantage. Just as we led the definition of GUI applications and to a lesser extent Usability in the past, critical future opportunities exist to lead the definition of Chicago applications, Memphis applications, productivity applications as a development platform, as tools for business process automation, applications for small organizations, for vertical markets, and others. Inherent in our strategy is bigger investments in major technological advances. We need to do a better job of selling these advances, not just as technologies for technically-proficient users, but as solutions to real business problems. Lotus has done a brilliant job positioning Notes as the solution for business process re-engineering.

- **Position Microsoft Office as the "front office" for "back office" workgroup solutions.** Despite Lotus significant lead with Notes and SmartSuite, opportunity exists to define real advantages for productivity applications in workgroup scenarios. Using a better back office (EMS), better programmability, and richer support for key workgroup scenarios while also embracing Notes in our applications, we must make Office the client side of workgroup solutions.

Pricing Strategy

We should seek to maintain our current strategy of pricing leadership, commanding a small price premium over the #2 player, Lotus. As the market leader, inability to maintain this premium should be taken as our failure across a broad front: product development, marketing, and our value-add strategy. As discussed above, avoiding commoditization and maintaining both share and reasonable price levels is the overriding objective of this plan.

We will add more functionality and bundle more bits to slow price erosion and strain competitors development capability. Ren in Office '95 is a good example. It is critical to this strategy that we create a strong sense of value for these additional components.

At the same time, although we should seek to avoid escalating a price war that would have long-term, negative effects for all players, we cannot allow competitive initiatives to gain share through specific channels such as large accounts or OEM (the threat today). We should use our financial strength to respond aggressively to these situations.

Other Marketing Strategies

There are a number of other marketing strategies underway or worthy of consideration that cut across customer types:

- **Retail Distribution.** We need to grow distribution of Office, Office Professional (in N. America anyway) and the individual applications. We are losing in the retail channel (superstore and mail-order reseller may be better) to Lotus and WordPerfect.

- **OEM.** Our OEM focus should be on tactical response to competitors, as is underway in Europe today, or to take advantage of unique channels (e.g. Gateway). Our primary thrust in this channel should be consumer products or to work with them to advance new technologies.

- **CD Unlock.** The expected rapid growth of CD ROM drives creates new distribution and packaging opportunities. We will be able to offer CDs with encrypted versions of our products that allow customers to try before buying. Purchase will be the acting of calling an 800 number to unlock and then install desired products off the CD. AliBaba is the codename for internally-developed software to enable this approach. CD unlock will be a useful tool to promote trial as a CD with Microsoft applications could today be given away by a reseller or included in an OEM machine

  CD Unlock may also change the model for purchasing software. Rather than buying Excel all at once, the customer could pay less to purchase core functionality and never buy Solver or buy it later. Another alternative is to let users purchase add-ons or third-party products from the CD a la carte.

- **Leveraging Microsoft On-line** represents an opportunity to deliver cool add-ons, vertical solutions, data, special support, documentation, easy upgrades, on-line registration, as well as design special features in the products to utilize other services. We can dramatically expand the use of on-line services to a much less technical audience by making sign-up, connection, browsing, and downloading virtually automatic from within our applications.

- **Packaging/specialized solutions.** We need to constantly evaluate the current Office/Office Pro configuration as well as others that could help differentiate Office in different segments. Versions with different workgroup components and value-added, for example, may be necessary to combat the forthcoming version of SmartSuite that includes a Notes client. The smorg marketplace sees little need for PowerPoint and Mail, gravitating instead toward products like Publisher and Access. They would prefer a "build your own" Office wherein they choose an applications to go along with Word and Excel. A related idea is to offer a family of vertical add-on packs for Office. Independent of whether there's a large standalone add-on business, they would add to the perceived value of Office and help us target Office at specialized segments.

- **Office Friendly (final name tbd).** This is a key initiative designed to broaden the scope and visibility of Microsoft Office and to create an industry-wide Office standard for companion products. We are encouraging ISVs to adopt certain Office UI conventions and over time, components and technologies (e.g. Setup, VBA, Text Control, OLE servers). They will also be given the opportunity to co-market with us and place an "Office Friendly" mark on their boxes.

SUMMARY

Key Success Factors

- Leverage Microsoft assets - leadership, systems and research, partners, installed base
- Add value to Office
- Listen to our customers
- Innovate in product development and marketing
- Lead definition of new categories, marketing, and business models
- Building annuity business. Learning how upgrade rates.
- Execute efficiently and effectively. Manage costs.
- Protect our franchise in large organizations
- Provide relevant long-term differentiation

Issues/Risks/Threats

- Price erosion (including volume discounts, concurrent use, category dilution)
- Lotus creates a long-term technology and marketing advantage by linking Notes and SmartSuite
- Lotus /IBM relationship
- OS/2 success; Macintosh decline.
- WordPerfect converts its huge and loyal installed base
- Borland/WordPerfect build momentum for a suite
- Continued decline in productivity application penetration on the Macintosh. ClarisWorks success.
- We fail to communicate a leadership message or leverage our leadership position
- Fail to identify and gain leadership share in emerging growth markets and segments
- Fail to define and dominate key categories