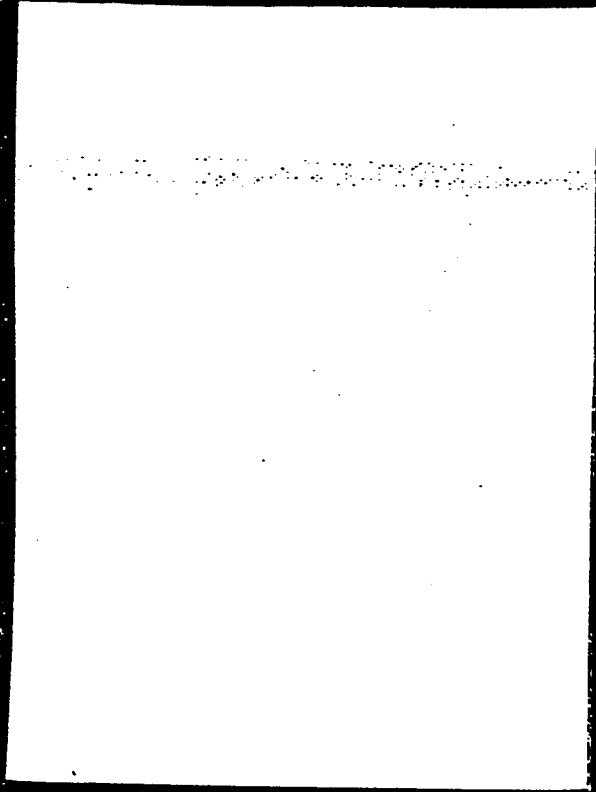


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BOARD OF DIRECTORS' REPORT

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This report was prepared with Win Word 6.0. All tables were created in Win Excel 5.0 and either embedded in the document or linked to master spreadsheets. Additionally, most of the channel and product group tables were generated via automation from the general ledger. Each of these automated tables is made accurate in its calculations by using data at a lower level than the rounded amounts shown in this report. These lower level amounts are used to calculate variances and are then rounded and displayed in this report. Therefore, individual amounts are rounded perfectly but totals and variances may not foot precisely. All other tables have individual numbers that may be rounded. While these individual numbers may not be precisely to supporting schedules, they will foot exactly as shown in this report.

Note: Revenue is "net" revenue unless otherwise stated. Gross revenue is net of returns.

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INCOME STATEMENT & KEY RATIOS
(IN MILLIONS)

Q94-3

	Actual		Plan		Variance	
	\$	%	\$	%	\$	%
Net revenue	\$1,244	100.0 %	\$1,091	100.0 %	\$153	14 %
Cost of revenue	208	16.7	186	17.1	(22)	(12)
Gross profit	1,036	83.3	905	82.9	131	15
People expense	269	21.6	298	27.3	29	10
Facilities expense	114	9.1	95	8.7	(18)	(19)
Marketing expense	96	7.7	90	8.3	(5)	(6)
Other expenses	198	15.9	69	6.3	(130)	(189)
Total expenses	676	54.3	552	50.6	(124)	(23)
Contribution margin	360	28.9	352	32.3	8	2
Nonoperating income	22	1.8	26	2.4	(5)	(18)
Income taxes	126	10.2	129	11.8	3	2
Net income	\$256	20.6 %	\$250	22.9 %	\$6	3
Net income (excl. Stac)	\$336	27.0 %	\$250	22.9 %	\$86	34

FYTD94

	Actual		Plan		Variance	
	\$	%	\$	%	\$	%
Net revenue	\$3,356	100.0 %	\$3,024	100.0 %	\$332	11 %
Cost of revenue	552	16.4	515	17.0	(37)	(7)
Gross profit	2,804	83.6	2,509	83.0	295	12
People expense	805	24.0	904	29.9	99	11
Facilities expense	274	8.2	279	9.2	5	2
Marketing expense	286	8.5	287	9.5	1	0
Other expenses	320	6.0	216	7.2	(104)	(48)
Total expenses	1,686	50.2	1,687	55.8	1	0
Contribution margin	1,118	33.4	822	27.2	296	36
Nonoperating income	64	1.9	69	2.3	(6)	(7)
Income taxes	398	11.9	302	10.0	(96)	(32)
Net income	\$784	23.4 %	\$589	19.5 %	\$194	33
Net income (excl. Stac)	\$864	25.7 %	\$589	19.5 %	\$275	47

Metrics Summary (dollars annualized in thousands)

	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2	Q94-3
Net revenue per employee	\$275	\$299	\$287	\$294	\$271	\$308	\$337
People expense per employee	69	68	66	71	73	74	73
Facilities expense per employee	23	23	23	26	21	23	31
Marketing expense % net revenue	10%	12%	10%	7%	9%	9%	8%
R&D expense % net revenue	13%	12%	12%	13%	14%	13%	12%
PSS Expense % net revenue	5%	4%	4%	5%	5%	5%	5%

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MICROSOFT & COMPETITOR HIGHLIGHTS

Microsoft

- Announced and initiated a reorganization to realign business. The three new key organizational elements are Product Division, Customer Units and Operations.
- Promotions: Bill Neukom (SVP), Deborah Willingham (VP), Rolf Skoglund (VP) and Michel Lacombe (VP).
- Key releases were Win Office 4.2, Win PowerPoint 4.0, and Japanese versions of Win NT servers and server applications. Win Excel 5.0 released in late December, with significant revenue impact to Q94-3.
- Strong sales of Windows; users exceeded 50 million.
- Strong sales in OEM (revenue 58% over plan), Far East (FG revenue 57% over plan) and Europe (FG revenue exceeded plan for the first time FYTD94, by 9%).
- Stac jury determination of \$120 million was charged against earnings (other expenses). Operationally, product rework to remove DoubleSpace caused only minimal disruptions.
- Headcount increased by only 36 to 14,773 in Q94-3 (11% below plan) resulting in significant positive variances in controllable expenses.
- Q94-3 EPS was \$0.84, or \$1.11 before Stac charge (an increase of 39% over Q93-3).

Novell

- Agreed to purchase WordPerfect for stock valued at \$1.4 billion (at the time of announcement) and Borland's Quattro Pro spreadsheet for \$145 million in cash.
- Hired Hewlett-Packard VP Robert J. Frankenberg as president and CEO.
- Released Novell DOS 7.0 in January.
- Sold Sun Microsystems a fully-paid license for Unix system technology for \$82 million.

Lotus

- Announced joint venture with AT&T to create a telecommunications and computer network based on Notes. Lotus shares jumped up \$5.75 following the announcement to close at \$85.50.
- Shipped Lotus Notes Pager Gateway for SkyTel, a wireless messaging system.
- Cut Improv price from \$495 to \$125 and positioned it as an add-on for spreadsheets or databases.
- Halted development of Desktop applications for Mac and Power PC.
- In its proxy, Lotus asked shareholders to approve a doubling of authorized shares. Three directors will not stand for reelection (Lawrence Graev, Ajdo Papone and Chester Siuda).

WordPerfect

- Laid off 1,025 employees, leaving about 4,900 workers worldwide.
- Announced Main Street, a new consumer line of software. Also announced an agreement with Intuit that will give purchasers of WordPerfect Works for Windows a free copy of Quicken.
- Announced an around-the-clock paid support program for its word processing customers.
- Shipped WordPerfect 3.0 for Power Mac and WordPerfect 5.1 for DOS, but announced suspension of further DOS upgrades.

Borland

- Announced organizational restructuring, including reduction of U.S. workforce by 200 people (14%).
- Keith Maib, a partner in Price Waterhouse business turnaround services group, named COO.
- Channel inventory remains at high levels.
- Shipped 2nd beta version of dBase for Windows program.

Comparative Cash Flow & Balance Sheet

COMPARATIVE CASH FLOW & BALANCE SHEET

Cash Flow Summary
(in millions)

	Q94-2	Q94-3	Change
Cash and short-term investments, beginning of quarter	\$2,532	\$2,796	\$264
Cash flow:			
Net income	289	256	(33)
Depreciation and other non-cash items	59	167	108
Cash from operations	348	423	75
Common stock issued	45	103	58
Common stock repurchased	(92)	(147)	(55)
Stock option income tax benefits	43	45	2
Cash used in financing	(4)	1	5
Additions to property, plant, and equipment	(63)	(69)	(6)
Other	(15)	(13)	2
Cash used for investments	(78)	(82)	(4)
Effect of exchange rates on cash	(2)	5	7
Net change in cash & short-term investments	264	347	83
Cash and short-term investments, end of quarter	\$2,796	\$3,143	\$347

Balance Sheet
(in millions)

	Dec. 31, 1993		Mar. 31, 1994		Change	
Assets						
Current assets:						
Cash and short-term investments	\$2,796	62%	\$3,143	64%	\$347	12%
Accounts receivable - net	460	10	522	11	62	13
Inventories:						
Raw materials -	54	1	56	1	2	4
Finished goods	76	2	75	2	(1)	(1)
Total inventories	130	3	131	3	(1)	0
Other	96	3	116	1	20	21
Total current assets	3,482	78	3,912	79	430	12
Property, plant, and equipment - net:						
Land	144	3	160	3	16	11
Buildings	374	8	383	8	9	2
Leasehold improvements	70	2	69	1	(1)	(1)
Furniture & equipment	92	2	96	2	4	4
Computer equipment	233	5	210	4	(23)	(10)
Total property, plant, and equipment - net	913	20	918	19	5	1
Other assets	91	2	96	2	5	5
Total assets	\$4,486	100%	\$4,926	100%	\$440	10
Liabilities and Stockholders' Equity						
Current liabilities:						
Accounts payable	\$ 242	5%	\$ 296	6%	\$ 54	22
Accrued compensation	99	2	71	1	(28)	(28)
Income taxes payable	211	5	219	4	8	4
Litigation accrual	0	0	120	2	120	NM
Other	188	4	208	4	20	11
Total current liabilities	740	16	914	17	174	24
Stockholders' equity:						
Common stock and paid-in capital	1,232	28	1,373	29	141	11
Retained earnings	2,514	56	2,639	54	125	5
Total stockholders' equity	3,746	84	4,012	83	266	7
Total liabilities and stockholders' equity	\$4,486	100%	\$4,926	100%	\$440	10

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Microsoft Results

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Q94-3 TOP PRODUCT SALES FLASH

Q94-3 TOP PRODUCT SALES FLASH
(Gross revenue in millions, licenses in thousands)

Finished Good Top Products:	Gross Revenue			Licenses		
	Actual	Plan	% Plan	Actual	Plan	% Plan
Win Office, New Users	\$216	\$145	149 %	721	491	147 %
Win Excel, New Users	95	74	128	529	433	122
Win Office Pro, New Users	58	36	162	139	88	159
Win Word, New Users	52	76	69	342	449	76
Win Office, Existing Users	42	19	219	214	93	229
Win Excel, Existing Users	39	28	137	792	413	192
Windows, New Users	36	26	140	516	376	137
Access	24	42	57	173	245	71
Mouse Hardware Only	24	17	140	466	295	158
Win Word, Existing Users	23	22	107	237	223	106
Win Project	22	32	67	66	118	56
Mac Office, New Users	20	20	98	60	58	104
Win Works	18	17	104	271	204	133
WFW, New Users	16	7	232	324	77	420
WFW, Existing Users	14	6	252	348	101	345
Win Visual C++	14	13	109	79	71	112
Win Encarta	13	2	739	189	11	1791
Win Powerpoint	11	11	103	321	273	118
Win Visual Basic Pro	10	5	185	44	23	190
Windows, Existing Users	8	4	237	199	84	237
Windows NT Advanced Server	8	13	62	12	15	77
Total	<u>\$765</u>	<u>\$616</u>	124			

OEM Top Products:	Gross Revenue			Licenses		
	Actual	Plan	% Plan	Actual	Plan	% Plan
MS-DOS	\$137	\$99	138 %	7,069	5,934	119 %
Windows	108	69	156	5,901	4,022	147
Mouse	18	6	319	1,277	489	261
OS/2	13	8	170	516	506	102
Works	10	6	164	1,032	581	178
Total	<u>\$286</u>	<u>\$188</u>	152			

Note: Gross revenue is shown since adjustments to revenue are not made at the product family level.

Highlights:

- The top 20 products above represented 79% of total FG gross revenue. Top products represented 89% of total OEM gross revenue.
- Gross revenue from Win Office, new users, was 149% of plan due to the release of the upgrade version of localized product in Europe and continued strong sales of suite products in North America.
- The localized version of Win Word 6.0 was released in Europe. Sales of Win Word 6.0, existing users, approximated plan. Gross revenue from new users was less than plan due to the shift in sales to suite products.
- Gross revenue from Win Excel, new and existing users, exceeded plan. The English version of Win Excel released in December, causing strong Q94-3 revenue sell-in. The release of the Japanese version of Win Excel 5.0 and European localized versions also positively influenced the quarter.
- Access 2.0, originally scheduled for RTM during Q94-2, slipped to an actual RTM of April 7, 1994. Access was only 57% of plan gross revenue for Q94-3.

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FYTD94 TOP PRODUCT SALES FLASH

(Gross revenue in millions, licenses in thousands)

Finished Good Top Products:	Gross Revenue			Licenses		
	Actual	Plan	% Plan	Actual	Plan	% Plan
Win Office, New Users	\$554	\$401	138 %	1,738	1,306	133 %
Win Excel, New Users	195	184	106	1,045	1,045	100
Win Word, New Users	189	217	87	1,147	1,242	92
Win Office Pro, New Users	134	88	152	294	211	139
Windows, New Users	114	82	139	1,713	1,191	144
Win Office, Existing Users	89	51	175	442	245	180
Access	70	94	75	457	510	90
Win Word, Existing Users	70	75	92	714	784	91
Mouse Hardware Only	69	51	134	1,285	877	147
Win Project	62	70	89	191	262	73
Mac Office, New Users	61	53	114	173	149	116
Win Excel, Existing Users	49	66	74	907	979	93
Win Works	47	48	98	742	611	121
MS-DOS	36	89	41	1,069	1,791	60
Win Visual C++	33	32	102	177	172	103
Win Visual Basic Pro	32	17	183	175	85	207
DOS Flight Simulator	29	11	275	909	331	275
WFW, Existing Users	28	19	146	629	341	185
Mac Word, New Users	28	42	67	261	302	86
WFW, New Users	27	20	131	462	226	204
Mac Excel, New Users	27	39	69	161	250	64
Total	\$1,941	\$1,748	111			

OEM Top Products:	Gross Revenue			Licenses		
	Actual	Plan	% Plan	Actual	Plan	% Plan
MS-DOS	\$327	\$285	115 %	16,668	16,759	99 %
Windows	265	179	148	14,885	8,063	185
Mouse	47	17	279	3,093	1,366	226
OS/2	26	20	131	1,249	1,257	99
Works	26	17	158	2,604	1,595	163
Total	\$691	\$517	134			

Note: Gross revenue is shown since adjustments to revenue are not made at the product family level.

Highlights:

- The top 20 products listed above represented 74% of total FG gross revenue. The OEM top products represented about 83% of the OEM gross revenue.
- Gross revenue from Win Office exceeded plan by 38% due to the increasing market for suite products.
- Lower PC prices, increased penetration of naked systems, and a growing consumer market were factors contributing to the strong FYTD94 OEM results.
- Gross revenue from Win NT was \$27 million, representing 22% of plan. The shortfall was due to several factors: long sales cycle of Win NT, the lack of 32 bit applications and an overestimate of the market demand for this product.
- Consumer gross revenue exceeded plan due to the expanding home PC market. PC Flight Simulator was 275% of plan, Win Encarta was 412% of plan, and Win Publisher was 166% of plan.

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FY94 KEY PRODUCTS RELEASE SCHEDULE

FY94 KEY PRODUCTS RELEASE SCHEDULE

Business Unit / Product:	RTM Date		Gross Revenue (in millions)*			
	Actual	Plan	FYTD94			FY94
			Actual	Plan	Variance	Plan
Desktop Applications:						
Win Word 6.0 (and Win Office 4.0)	Oct-93	Sep-93	\$618	\$546	\$72	\$736
Win Excel 5.0	Dec-93	Oct-93	\$593	\$491	\$102	\$661
Win PowerPoint 4.0 (and Win Office 4.2)	Feb-94	Jan-94	\$120	\$90	\$30	\$126
Win Project	Apr-94	Jan-94	\$65	\$72	(\$7)	\$95
Mac Word 6.0 (and Win Office 4.2)	Jul-94	Mar-94	\$67	\$80	(\$13)	\$133
Mac Excel 5.0	May-94	Nov-93	\$65	\$84	(\$19)	\$116
Mac PowerPoint 4.0	Jun-94	Feb-94	\$15	\$16	(\$0)	\$23
Mac Project	Oct-94	Apr-94	\$8	\$7	\$0	\$12
Database & Development Tools:						
Access 2.0 (and OfficePro allocation)	Apr-94	Dec-93	\$101	\$114	(\$13)	\$155
Visual C++ 1.5	Dec-93	N/A	\$33	\$32	\$1	\$42
Win FoxPro 2.6	Mar-94	N/A	\$27	\$41	(\$14)	\$53
Systems:						
MS-DOS 6.2	Oct-93	N/A	\$405	\$374	\$31	\$501
Windows for Workgroups 3.11	Nov-93	Aug-93	\$62	\$39	\$23	\$52
Windows NT Advanced Server	Jul-93	Jun-93	\$21	\$36	(\$15)	\$56
Windows NT	Jul-93	Jul-93	\$27	\$123	(\$96)	\$169
SQL Server for NT	Aug-93	Jul-93	\$15	\$18	(\$3)	\$23
Charger OEM Mouse	Sep-93	Nov-93	\$50	\$19	\$31	\$25
Defender OEM Mouse	Mar-94	Mar-94	(combined w/ Charger OEM Mouse)			
Ballpoint Mouse 2.0	Jul-93	Jul-93	\$7	\$9	(\$2)	\$11
Windows Sound System 2.0	Oct-93	Jul-93	\$6	\$9	(\$3)	\$14
Consumer:						
Publisher 2.0	Jul-93	Jul-93	\$25	\$15	\$10	\$20
Flight Simulator 5.0	Sep-93	Sep-93	\$31	\$12	\$19	\$13
Win Encarta, 1994	Sep-93	Sep-93	\$28	\$6	\$22	\$8
Win Works 3.0	Oct-93	Oct-93	\$70	\$63	\$7	\$90
Money 3.0	Jan-94	Oct-93	\$6	\$8	(\$2)	\$10

* Total of all versions sold in FY94. Includes MS Office allocation.

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SUMMARY

Results of Operations
(IN MILLIONS)

Q94-3

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$375.2	96 %	\$287.7	92 %	\$150.9	92 %	\$61.9	61 %
Europe FG	391.4	109	321.8	109	225.8	118	130.8	104
ICON FG	68.0	92	51.7	92	26.7	93	7.0	46
Far East FG	88.2	158	70.2	174	48.7	253	26.8	NM
OEM	322.9	158	307.0	157	286.6	159	202.3	216
Other	(1.7)	(23)	(1.6)	(39)	(70.7)	NM	(68.2)	(429)
Worldwide	<u>\$1,244.1</u>	<u>114</u>	<u>\$1,036.7</u>	<u>115</u>	<u>\$667.9</u>	<u>117</u>	<u>\$360.5</u>	<u>102</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	30 %	36 %	77 %	80 %	40 %	42 %	16 %	26 %
Europe FG	31	33	82	83	58	53	33	35
ICON FG	5	7	76	76	39	39	10	21
Far East FG	7	5	80	72	55	34	30	(0)
OEM	26	19	95	96	89	88	63	46
Other	(0)	1	95	57	NM	(162)	NM	214
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>83</u>	<u>83</u>	<u>54</u>	<u>52</u>	<u>29</u>	<u>32</u>

FYTD94

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America FG	\$1,079.4	100 %	\$828.7	96 %	\$425.8	107 %	\$240.3	105 %
Europe FG	976.8	99	810.2	100	528.8	107	327.8	104
ICON FG	195.0	92	149.1	92	76.7	101	33.7	91
Far East FG	202.4	137	156.3	145	91.0	203	34.5	NM
OEM	846.3	146	800.3	144	739.9	145	519.8	199
Other	55.8	283	60.0	527	(69.2)	NM	(37.3)	374
Worldwide	<u>\$3,355.7</u>	<u>111</u>	<u>\$2,804.6</u>	<u>112</u>	<u>\$1,793.0</u>	<u>121</u>	<u>\$1,118.8</u>	<u>136</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
North America FG	32 %	36 %	77 %	80 %	39 %	37 %	22 %	21 %
Europe FG	29	33	83	82	54	50	34	32
ICON FG	6	7	76	76	39	36	17	17
Far East FG	6	5	77	73	45	30	17	(8)
OEM	25	19	95	96	87	88	61	45
Other	2	1	107	58	(124)	(210)	(67)	(51)
Worldwide	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>53</u>	<u>49</u>	<u>33</u>	<u>27</u>

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SUMMARY

FINISHED GOODS TOP PRODUCT SALES FLASH
GROSS REVENUE (IN MILLIONS)

Q94-3

	North America		Europe		ICON		Far East		Worldwide	
	Actual	% Plan	Actual	% Plan	Actual	% Plan	Actual	% Plan	Actual	% Plan
Win Office, New Users	288.3	181 %	391.6	123 %	516.8	114 %	319.5	263 %	5216.2	168 %
Win Excel, New Users	36.6	137	34.9	98	5.7	121	18.2	253	95.4	128
Win Office Pro, New Users	8.5	31	45.7	568	3.5	525	0.3	NM	58.0	162
Win Word, New Users	9.4	30	34.3	95	4.1	93	4.3	103	52.3	69
Win Office, Existing Users	21.3	458	16.1	150	1.7	50	2.4	1,329	41.5	219
Win Excel, Existing Users	20.9	206	15.6	111	2.1	88	0.1	8	38.7	137
Windows, New Users	19.4	355	9.7	98	4.1	78	2.8	54	35.9	140
Access	8.1	41	8.6	49	0.8	34	6.8	256	24.4	57
Macintosh Hardware Only	14.7	165	6.9	84	1.3	315	1.2	212	24.1	140
Win Word, Existing Users	6.3	91	15.1	125	0.8	31	1.0	1,013	23.3	107
Win Project	11.8	57	7.8	82	1.8	98	0.3	171	21.7	67
Mac Office, New Users	12.9	92	6.3	124	0.6	50	0.2	232	20.0	98
Win Works	3.5	70	12.2	134	2.1	142	0.0	3	17.9	104
WFW, New Users	7.0	987	6.7	169	2.1	131	0.0	6	15.8	232
WFW, Existing Users	3.7	190	9.6	300	1.1	214	0.0	76	14.5	252
Win Visual C++	6.1	81	3.1	134	0.4	103	4.9	163	14.4	109
Win Encore	11.2	708	1.2	777	0.9	1,157	0.1	NM	13.4	739
Win Powerpoint	9.0	138	1.9	61	0.4	29	0.2	72	11.5	103
Win Visual Basic Pro	3.9	137	3.1	185	0.6	727	2.4	321	9.9	185
Windows, Existing Users	5.2	577	2.2	145	0.6	70	0.4	151	8.4	237
Windows NT Advanced Server	3.8	62	2.3	40	0.6	179	1.5	161	8.2	62
Mac Excel, New Users	2.3	28	1.4	35	0.2	34	4.1	132	8.0	50
Win FoxPro	3.8	75	2.1	37	0.9	254	0.3	110	7.1	62
Mac Word, New Users	3.5	56	2.4	51	0.3	36	0.7	664	6.9	58
MS-DOS	(1.2)	(14)	5.7	59	0.1	3	0.2	6	4.8	19
Win Publisher	2.3	160	1.5	106	0.5	241	0.0	NM	4.4	141
DOS Works	1.1	60	1.5	60	0.4	68	1.0	102	3.9	68
Win Office Pro, Existing Users	0.0	0	3.5	349	0.0	0	0.0	NM	3.5	96
DOS FoxPro	1.2	36	1.1	50	0.4	22	0.2	47	2.8	37
Windows NT	(2.3)	(11)	1.4	10	0.0	1	2.3	253	1.4	4
Total	<u>\$322.4</u>		<u>\$355.3</u>		<u>\$55.0</u>		<u>\$75.5</u>		<u>\$208.2</u>	

Highlights:

- North American gross revenue from the top 30 products represented 81% of total gross revenue for the region. Win Excel 5.0 was launched in December 1993, with strong sell-in during Q94-3. Sales of Win Office continued to exceed plan in Q94-3. Gross revenue from Win Office Professional was substantially behind plan due in part to the delay in the release of Access 2.0. In Q94-3, customer returns of MS-DOS 6.0, for version upgrade, and Windows NT, for stock balancing, exceeded sales. Both Windows and WfW achieved sales significantly above plan. This was due to the plan being based on a lower level of sales for Windows and WfW in anticipation of the release of Chicago.
- For Europe, gross revenue from the top 30 products represented 87% of total gross revenue. Localized versions of Win Word 6.0 were released in Q94-3, resulting in significant sell-in for the stand-alone product and the Office suite. Localized versions of Win Excel 5.0 were shipped late in Q94-2. Sales of this product remained strong through Q94-3.
- ICON gross revenue from the top 30 products represented 80% of total gross revenue for the region. Gross revenue from Win Office, new users, was stronger than planned; however, this variance was offset by lower gross revenue from existing users.
- Far East gross revenue from the top 30 products represented 84% of total gross revenue for the region. The Japanese version of Win Excel shipped in Q94-3, resulting in gross revenue from new users of this product being 253% of plan. Win Office, new users, gross revenue was 263% of plan. An Office sales campaign which commenced in Q94-2 was extended through the end of Q94-3.

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SUMMARY

FINISHED GOODS TOP PRODUCT SALES FLASH
GROSS REVENUE (IN MILLIONS)

FYTD94

	North America		Europe		ICON		Far East		Worldwide	
	Actual	S.Plan	Actual	S.Plan	Actual	S.Plan	Actual	S.Plan	Actual	S.Plan
Win Office, New Users	\$228.5	161 %	\$238.8	122 %	\$45.5	112 %	\$41.7	191 %	\$354.5	138 %
Win Excel, New Users	69.7	115	84.6	98	18.8	81	30.0	181	195.1	186
Win Word, New Users	60.4	72	101.1	96	14.0	108	13.3	90	188.9	87
Win Office Pro, New Users	23.7	37	99.7	439	10.5	597	0.4	NM	134.2	152
Windows, New Users	38.2	289	28.7	90	15.8	111	11.3	73	114.1	139
Win Office, Existing Users	57.1	438	22.4	81	6.4	67	2.9	433	88.7	175
Access	34.7	78	37.9	61	3.8	44	13.7	286	70.1	75
Win Word, Existing Users	28.8	96	31.3	89	4.2	54	5.3	207	69.5	92
Microsoft Hardware Only	44.8	159	18.7	88	3.5	322	2.8	205	69.0	134
Win Project	35.3	85	20.4	91	5.3	99	0.8	133	61.7	89
Mac Office, New Users	41.2	115	16.6	121	2.6	73	0.5	166	60.9	114
Win Excel, Existing Users	22.5	94	22.5	70	3.2	46	0.5	19	48.8	74
Win Works	15.8	98	25.9	105	4.9	94	0.2	13	66.9	98
MS-DOS	13.1	42	16.9	42	4.5	35	1.3	38	34.0	41
Win Visual C++	13.5	86	7.9	123	1.3	118	9.9	113	32.6	102
Win Visual Basic Pro	14.1	170	10.5	192	2.2	405	2.9	164	31.6	183
DCS Flight Simulator	28.0	277	7.6	449	0.9	174	0.9	70	29.2	275
WFW, Existing Users	11.5	135	14.6	142	1.9	133	0.1	85	28.2	146
Mac Word, New Users	17.3	89	7.9	61	1.3	43	1.6	454	28.0	67
WFW, New Users	11.1	495	11.8	92	3.7	85	0.1	9	26.7	131
Mac Excel, New Users	11.1	65	5.2	30	1.1	40	9.2	109	26.6	89
Win FontPro	11.5	49	10.7	68	2.9	333	1.4	176	26.4	84
Windows NT	13.1	19	7.4	18	2.2	30	3.1	159	25.8	22
Win Encarta	21.0	385	2.3	551	2.0	436	0.2	NM	25.5	412
Win Publisher	15.2	221	6.0	143	2.2	212	0.1	NM	23.4	194
Win Powerpoint	16.6	133	4.7	59	1.2	49	0.8	71	23.2	93
Windows NT Advanced Server	10.1	56	5.7	50	2.2	262	2.3	152	20.3	64
Windows, Existing Users	10.7	336	6.3	121	2.9	128	0.2	7	20.1	155
DCS Works	4.0	88	5.6	76	1.2	63	3.4	99	14.1	76
DCS FontPro	4.5	32	7.6	67	1.8	35	1.3	110	11.2	64
Total	\$920.3		\$873.2		\$163.7		\$142.2		\$2,131.5	

Highlights:

- North American gross revenue from the top 30 products represented 78% of total gross revenue. As in Q94-3, the FYTD94 revenue from Win Office, both new and existing users, exceeded plan. Win Office Professional, new users, was 37% of plan. Gross revenue from consumer products was \$117 million, in comparison with plan of \$87 million, as a result of the expanding home PC market. Top consumer products (included above) were Win Works (98% of plan), PC Flight Simulator (277% of plan) and Win Encarta (385% of plan).
- European gross revenue from the top 30 products represented 86% of the total gross revenue for the region. The success of the Office suite in Europe exceeded plan. Win Office volumes were higher than plan, but the sales of the stand-alone products of Win Word and Win Excel were negatively impacted. Most European subsidiaries captured a dominant market share of the suite products, except Spain and Benelux. DDT was 28% below plan primarily due to volume shortfalls.
- ICON gross revenue from the top 30 products represented 82% of total gross revenue. Gross revenue from Win Excel was below plan for FYTD94, in spite of significant sell-in in Q94-3.
- Far East gross revenue from the top 30 products represented 78% of total gross revenue for the region. Gross revenue from Win Office, new users, was 191% of plan. Japan contributed 79% of the region's Office gross revenue. Gross revenue from Win Excel, New Users was 81% above plan, with the recent release of the Japanese version of Win Excel 5.0 contributing to the variance.

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SUMMARY

FINISHED GOODS TOP PRODUCT PRICING FLASH
(US\$ PER LICENSE)

Q94-3

	North America		Europe		ICON		Far East		Worldwide	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Win Office, New Users	5279	5279	5339	5315	5245	5300	5299	5236	5300	5296
Win Excel, New Users	157	150	306	214	120	179	137	117	180	172
Win Office Pro, New Users	342	385	455	509	275	431	194	NM	416	408
Win Word, New Users	115	147	178	210	118	173	135	105	152	169
Win Office, Existing Users	221	221	242	212	160	165	60	243	194	203
Win Excel, Existing Users	38	50	76	89	71	83	34	73	49	64
Windows, New Users	70	59	74	74	38	67	74	70	70	68
Access	110	165	197	207	122	140	139	119	141	173
Mouse Hardware Only	52	65	54	53	42	56	54	53	52	58
Win Word, Existing Users	81	84	114	112	74	83	69	84	98	98
Win Project	322	268	364	324	253	181	371	297	329	275
Mac Office, New Users	337	366	337	329	251	329	232	261	332	353
Win Works	61	76	77	94	39	53	42	120	66	84
WFW, New Users	50	64	44	80	65	106	98	76	49	88
WFW, Existing Users	32	56	48	60	35	48	38	35	42	57
Win Visual C++	149	187	173	171	133	153	274	209	182	187
Win Encarta	71	171	71	189	66	157	57	NM	71	172
Win Powerpoint	30	32	164	64	112	60	82	170	36	41
Win Visual Basic Pro	211	237	199	190	204	198	307	347	223	229
Windows, Existing Users	43	33	44	49	30	45	52	43	42	42
Windows NT Advanced Server	695	808	647	882	426	849	1,417	862	711	883
Mac Excel, New Users	138	130	183	208	70	158	228	128	176	144
Win FoxPro	126	196	144	231	159	160	159	192	136	210
Mac Word, New Users	100	115	164	177	75	140	285	123	122	135
MS-DOS	141	39	43	57	7	51	37	51	32	48
Win Publisher	58	85	81	90	48	68	91	NM	63	85
DOS Works	45	52	77	82	37	54	124	122	64	70
Win Office Pro, Existing Users	173	244	360	464	NM	318	NM	NM	359	287
DOS PostPro	116	215	161	182	153	164	275	200	141	190
Windows NT	260	194	288	237	93	187	304	187	373	207

Highlights:

- For the North America region, the actual revenue per license for Win Office Pro varied from plan due to a shift in sales mix toward Select and maintenance licenses. Win Encarta and FoxPro dropped price points to below plan figures to gain unit share causing variances from plan. The variance from plan for Access was due to a sales mix shift from full packaged product to competitive upgrades. Win Word, new users, varied from plan due to a shift in sales mix from competitive upgrade to academic.
- In Europe, prices for Desktop applications were reduced by 5% to 15% during Q94-3 in order to maintain market share. Prices were also affected by adverse foreign exchange trends, increased product bundling and a shift towards license agreements.
- For the ICON region, the price of Win Office was lower than plan due to a higher mix of Select, special agreements, and competitive sales. Prices for Win Excel and Win Word were lower than plan as a result of a higher mix of academic sales in Australia than planned. In addition, sales of full packaged product of Win Excel and Win Word were selling at approximately 85% and 89% of plan, respectively.
- For the Far East region, prices during Q94-3 were generally stable though they were impacted by foreign exchange rate fluctuation in relation to the budgeted exchange rate. The average exchange rate for the yen during Q94-3 was 107 to each US\$, in comparison with the planned rate of 117. The Japanese version of Win Excel 5.0 was launched in Q94-3, with competitive pricing to existing users.

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SUMMARY

FINISHED GOODS TOP PRODUCT PRICING FLASH
(US\$ PER LICENSE)

FYTD94

	North America		Europe		ICON		Far East		Worldwide	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Win Office, New Users	\$298	\$287	\$366	\$329	\$269	\$302	\$306	\$275	\$319	\$307
Win Excel, New Users	152	149	272	218	129	178	157	122	187	176
Win Word, New Users	139	150	300	217	122	171	145	121	165	175
Win Office Pro, New Users	415	389	499	517	303	431	172	NM	457	417
Windows, New Users	67	60	70	75	55	66	74	73	67	69
Win Office, Existing Users	211	224	234	216	195	169	67	242	201	207
Access	131	183	205	216	130	123	133	134	153	184
Win Word, Existing Users	79	84	125	113	85	83	105	107	97	96
Mouse Hardware Only	53	65	57	53	47	56	57	53	54	59
Win Project	311	282	380	324	242	120	363	299	323	266
Mac Office, New Users	357	368	358	341	265	329	256	263	351	357
Win Excel, Existing Users	39	52	79	81	77	82	67	73	54	67
Win Works	57	71	77	94	42	49	21	115	63	78
MS-DOS	33	39	35	61	29	53	38	50	34	49
Win Visual C++	157	182	177	172	147	151	265	211	184	186
Win Visual Basic Pro	170	199	182	187	171	198	279	347	181	204
DOS Flight Simulator	31	31	34	28	27	28	47	54	32	32
WFW, Existing Users	40	52	51	63	36	49	36	35	45	57
Mac Word, New Users	91	122	159	182	79	138	268	138	107	138
WFW, New Users	56	68	57	90	68	107	112	90	58	90
Mac Excel, New Users	135	129	186	213	94	158	233	163	165	154
Win FoxPro	147	190	165	203	157	161	210	192	157	194
Windows NT	194	194	259	244	173	186	270	186	215	209
Win Encarta	73	189	93	189	69	157	61	NM	74	187
Win Publisher	69	79	91	92	49	58	94	NM	70	81
Win Powerpoint	47	51	195	55	122	80	139	190	59	56
Windows NT Advanced Server	660	698	694	870	528	673	1,144	916	684	760
Windows, Existing Users	43	32	49	50	36	45	17	54	43	44
DOS Works	41	52	76	82	41	54	128	116	63	69
DOS FoxPro	121	208	167	188	152	163	260	201	148	193

Highlights:

- For the North America region, the price variance from plan for Win Office Pro was due to a shift in sales mix toward Select and maintenance licenses. Win Encarta and FoxPro dropped price points to below plan figures to gain market share. Unit volumes for these products increased, resulting in incremental revenue. The price variance from plan for Access was due to a sales mix shift from full packaged product to competitive upgrades. Prices of Mac Word, new users, varied from plan due to a shift in sales mix from full packaged product to academic.
- European prices for Win Office and Win Excel new users were above plan due to conservative assumptions on price reductions and foreign exchange rates during the FY94 planning cycle. Price for Win Word new users were lower than plan due to competitive pressures.
- For ICON, the prices of Win Office were lower than plan due to a higher mix of Select, special agreements, and competitive upgrades. Prices for Win Excel and Win Word were lower than plan as a result of a higher mix of academic sales in Australia. In addition, sales of full packaged product of Win Excel and Win Word were selling at approximately 85% and 89% of plan, respectively.
- For Far East, the FYTD94 prices were impacted by foreign exchange rate fluctuations in relation to the budgeted exchange rate. The average exchange rate for the yen for FYTD94 was 107 to each US\$, in comparison with the planned rate of 117.

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SUMMARY

NET REVENUE AND RESPONSIBILITY MARGIN BY SUBSIDIARY
(IN MILLIONS)

Q94-3

	Excluding OEM				Including OEM			
	Net Revenue		Responsibility Margin		Net Revenue		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America								
United States	3339.1	94.2 %	3131.3	88.5 %	3511.1	106.0 %	3275.5	109.0 %
Canada	36.1	118.7	19.6	132.0	42.0	127.1	24.5	142.3
	<u>375.2</u>	<u>96.1</u>	<u>150.9</u>	<u>92.5</u>	<u>593.1</u>	<u>107.3</u>	<u>300.0</u>	<u>111.2</u>
Europe								
Denmark	5.8	72.8	4.0	71.1	6.5	79.9	4.6	80.6
Finland	4.1	105.4	2.6	105.4	9.3	132.4	7.7	136.0
Norway	6.1	78.5	4.0	74.3	7.9	99.5	5.5	99.5
England	90.6	121.5	53.9	135.9	98.7	123.3	61.0	127.4
Sweden	20.7	104.7	10.6	113.2	22.7	112.2	12.4	127.4
Hungary	1.2	163.9	0.6	498.5	1.4	178.6	0.9	428.1
Russia	1.6	200.5	0.9	NM	2.0	190.8	1.3	851.9
Czechoslovakia	2.3	142.8	1.5	220.1	3.1	172.3	2.3	271.0
Switzerland	23.2	170.0	21.4	214.0	29.3	173.0	22.5	218.3
Germany	94.9	106.5	52.2	111.6	130.6	118.8	87.3	131.2
Poland	2.8	221.8	1.1	252.2	3.9	251.0	2.2	312.2
Austria	10.2	124.1	7.1	147.6	10.8	126.9	7.7	150.8
Netherlands	14.0	100.0	7.8	92.3	18.8	121.2	11.6	118.6
Spain	4.9	81.4	1.9	67.7	6.1	91.8	3.1	90.4
France	64.0	83.3	32.2	77.4	68.1	86.1	35.6	81.7
Italy	26.4	166.8	18.3	211.5	38.2	181.9	29.7	218.5
Belgium	9.6	91.9	5.5	84.2	10.9	101.4	6.7	97.2
Portugal	3.1	86.2	2.0	94.8	3.2	82.9	2.1	88.6
EHQ/Other	1.1	346.2	(2.0)	NM	1.2	297.7	(2.0)	NM
	<u>391.4</u>	<u>109.0</u>	<u>225.8</u>	<u>117.8</u>	<u>472.6</u>	<u>117.8</u>	<u>302.4</u>	<u>131.0</u>
ICON								
Caribbean	0.9	152.6	0.4	251.3	0.9	147.4	0.4	223.3
Ecuador	0.6	146.0	0.2	181.3	0.6	146.0	0.2	218.6
Chile	0.7	46.4	0.1	18.0	0.8	30.2	0.2	26.8
Colombia	1.7	135.5	0.8	163.8	1.7	135.1	0.9	161.1
Venezuela	0.7	97.5	0.3	417.2	1.3	117.1	0.7	164.9
Brazil	5.3	79.7	1.7	55.9	7.0	94.9	3.4	89.4
Argentina	3.2	126.7	1.7	177.6	3.4	126.4	1.9	169.3
Mexico	11.4	99.1	6.2	104.7	12.2	103.1	6.9	110.5
Morocco	-0.3	54.3	0.1	27.3	0.4	52.5	0.1	25.5
Middle East	1.6	53.2	0.3	26.7	1.7	57.6	0.4	37.9
Turkey	1.8	90.7	0.7	88.9	2.0	95.2	0.9	99.0
South Africa	5.3	93.0	2.7	109.4	6.0	101.3	3.4	123.9
Greece	0.8	106.0	0.3	105.5	0.9	110.1	0.3	116.8
Israel	1.2	93.9	0.5	120.6	1.9	129.5	1.2	190.8
India	1.1	188.1	0.6	276.4	1.2	170.7	0.8	208.4
Thailand	0.4	80.3	0.2	91.1	0.4	71.9	0.2	69.5
Malaysia	0.9	61.8	0.4	54.3	1.4	77.9	0.9	82.8
Singapore	2.7	76.7	1.3	80.1	5.4	96.0	4.0	103.9
New Zealand	3.6	81.7	1.4	63.3	4.1	82.1	1.9	74.6
Australia	23.8	95.2	8.9	89.9	29.0	106.0	13.7	112.6
RHQ/Other	0.1	NM	(2.1)	NM	0.1	NM	(2.1)	NM
	<u>68.0</u>	<u>92.1</u>	<u>26.7</u>	<u>93.0</u>	<u>82.6</u>	<u>101.0</u>	<u>40.1</u>	<u>110.7</u>
Far East								
PRC	0.5	48.1	0.1	12.5	0.5	48.1	0.1	12.5
Korea	4.4	139.9	2.3	181.1	11.9	130.1	9.6	133.7
Taiwan	3.7	92.3	1.1	77.9	12.5	87.4	9.8	88.9
Japan	76.1	170.0	44.5	281.1	105.6	189.9	73.8	283.4
Hong Kong	3.4	119.3	1.7	133.9	7.0	136.1	5.0	146.2
RHQ/Other	0.1	NM	(1.0)	NM	0.2	NM	(0.9)	NM
	<u>88.2</u>	<u>157.9</u>	<u>48.7</u>	<u>253.3</u>	<u>137.6</u>	<u>161.5</u>	<u>97.3</u>	<u>206.9</u>
Worldwide								
Other	(1.7)	(23.2)	(70.7)	NM	(1.7)	(23.2)	(71.8)	NM
Total	<u>3921.2</u>	<u>103.9</u>	<u>3381.3</u>	<u>97.6</u>	<u>51,244.1</u>	<u>114.1</u>	<u>3667.9</u>	<u>117.0</u>

* new subsidiaries in FY94

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SUMMARY

NET REVENUE AND RESPONSIBILITY MARGIN BY SUBSIDIARY
(IN MILLIONS)

FYTD94

	Excluding OEM				Including OEM			
	Net Revenue		Responsibility Margin		Net Revenue		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
North America								
United States	\$991.9	100.4 %	\$381.6	106.8 %	\$1,486.8	111.9 %	\$795.5	123.1 %
Canada	87.5	100.4	44.2	108.4	100.1	103.4	54.9	114.1
	<u>1,079.4</u>	<u>100.4</u>	<u>425.8</u>	<u>104.9</u>	<u>1,586.9</u>	<u>111.5</u>	<u>850.4</u>	<u>122.5</u>
Europe								
Denmark	16.4	80.1	10.0	74.7	17.7	84.9	11.3	81.9
Finland	8.7	80.9	5.0	71.7	18.6	94.6	14.6	92.7
Norway	15.2	74.0	9.1	65.9	19.5	92.3	12.9	89.8
England	188.7	99.5	100.3	113.4	210.8	103.0	120.2	118.0
Sweden	47.4	93.4	19.3	94.4	51.7	99.7	23.1	108.9
Hungary	4.2	181.7	2.6	385.9	4.4	172.3	2.8	307.2
Russia	2.9	140.8	1.1	NM	3.5	122.6	1.7	379.6
Czechoslovakia	6.6	155.8	4.5	268.0	7.9	165.5	5.8	267.4
Switzerland	66.2	139.5	46.4	169.2	68.5	141.3	48.6	171.9
Germany	272.8	103.3	152.5	113.7	352.2	109.7	229.9	122.1
Poland	5.3	149.1	2.3	189.2	7.6	170.8	4.5	224.2
Austria	26.6	108.0	17.9	123.1	28.1	109.4	19.3	124.4
Netherlands	26.1	90.3	10.0	76.2	35.3	105.5	18.0	103.4
Spain	12.3	77.6	3.7	55.7	15.0	82.7	6.1	70.5
France	174.8	76.9	87.7	70.2	183.5	78.5	94.8	72.7
Italy	69.9	167.8	47.3	224.8	91.8	167.2	68.4	202.9
Belgium	22.8	84.8	12.4	79.1	25.5	92.3	14.8	90.5
Portugal	7.4	87.3	4.1	90.8	7.8	83.2	4.5	83.5
EHQ / Other	2.6	298.5	(7.4)	NM	2.5	231.9	(8.3)	NM
	<u>976.8</u>	<u>96.6</u>	<u>528.8</u>	<u>106.6</u>	<u>1,151.7</u>	<u>104.1</u>	<u>693.1</u>	<u>114.8</u>
ICON								
Caribbean	1.9	115.0	0.8	205.4	1.9	111.0	0.8	176.5
Ecuador	2.3	194.8	1.1	407.0	2.3	194.8	1.1	289.7
Chile	3.6	75.1	1.4	68.9	3.8	78.9	1.5	75.9
Colombia	5.1	142.5	2.6	174.6	5.3	144.0	2.7	176.5
Venezuela	3.4	102.9	1.8	167.6	5.0	115.4	3.0	143.9
Brazil	16.8	106.6	6.4	109.5	20.6	114.8	10.0	127.5
Argentina	8.6	131.1	4.2	202.7	8.8	126.5	4.4	177.1
Mexico	27.6	82.0	13.9	96.5	28.8	83.5	15.0	88.5
Morocco	1.0	60.8	0.3	33.2	1.0	58.5	0.3	47.6
Middle East	4.0	81.2	1.8	75.6	6.7	87.5	2.3	86.4
Turkey	5.6	96.1	2.5	115.8	5.8	96.1	2.7	112.0
South Africa	13.7	91.0	6.9	109.5	15.1	94.9	8.2	115.4
Greece	2.3	100.6	1.0	124.7	2.5	104.9	1.1	135.0
Israel	4.2	143.4	2.3	300.7	5.6	161.0	3.6	275.7
India	2.2	142.2	1.2	198.0	2.6	128.5	1.6	146.7
Thailand	1.5	75.4	0.6	68.8	1.5	69.8	0.6	58.5
Malaysia	2.7	39.1	1.2	54.8	3.9	72.2	2.4	73.7
Singapore	8.1	81.0	4.0	88.5	15.3	96.6	10.9	105.2
New Zealand	12.3	95.8	6.0	93.4	13.3	97.6	7.0	95.6
Australia	65.9	84.5	22.6	81.7	77.5	93.2	32.2	94.2
RHQ/Other	0.3	NM	(5.8)	NM	0.3	NM	(5.9)	NM
	<u>193.0</u>	<u>91.7</u>	<u>76.7</u>	<u>101.0</u>	<u>227.7</u>	<u>97.0</u>	<u>105.8</u>	<u>109.0</u>
Far East								
PRC	2.1	89.7	1.0	127.1	2.1	89.7	1.0	127.1
Korea	14.3	161.4	8.1	243.5	32.9	125.6	26.1	128.1
Taiwan	12.5	101.2	5.0	110.7	38.3	90.5	30.4	93.2
Japan	162.0	140.8	73.4	206.9	240.6	155.9	147.2	202.6
Hong Kong	9.9	114.1	5.0	130.6	20.2	136.6	15.0	152.1
RHQ/Other	1.5	NM	(1.5)	NM	(0.6)	NM	(3.7)	NM
	<u>202.4</u>	<u>137.3</u>	<u>91.0</u>	<u>201.9</u>	<u>333.6</u>	<u>138.9</u>	<u>215.9</u>	<u>162.0</u>
Worldwide								
Other	55.8	282.7	(69.2)	NM	55.8	282.8	(72.1)	NM
Total	<u>\$2,509.4</u>	<u>102.6</u>	<u>\$1,053.1</u>	<u>108.2</u>	<u>\$3,355.7</u>	<u>111.0</u>	<u>\$1,793.0</u>	<u>120.9</u>

* new subsidiaries in FY94

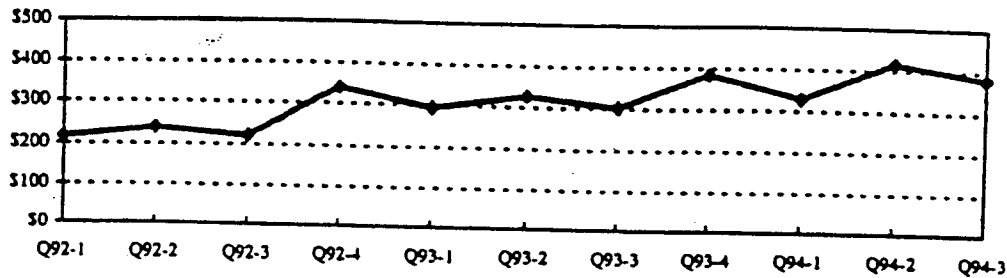
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NORTH AMERICA FINISHED GOODS REVIEW

NORTH AMERICA FINISHED GOODS REVIEW

Net Revenue Stream (in millions)



Key Highlights

- Win Excel 5.0 shipped in late December 1993; sales of this product to both new and existing users generated significant revenue in Q94-3. Revenue of the Excel product unit was 119% of plan in Q94-3.
- Win Office 4.0 was launched in Q94-2, a record quarter for revenue for North America. Sales of this product continued to be strong in Q94-3 with revenue at 142% of plan. FYTD94 revenue was 138% of plan. This positive trend in revenue from Office was offset, in part, by less than plan revenue for stand-alone Win Word. FYTD94 revenue from stand-alone Word was \$31 million under plan.
- Certain key products (MS-DOS 6.2, Windows NT, Windows NTAS, WfW 3.11, Excel 5.0, and Powerpoint 4.0) with compression-related code were impacted by the Stac lawsuit judgment. MS took the conservative step of removing the code. The changes to these products were minor, but the delay in shipment of the products was generally ten days. Long-term demand for these products is not expected to be significantly impacted by this delay.
- Access 2.0 was originally scheduled for RTM during Q94-2, but slipped to an RTM of April 7, 1994. This resulted in Access revenue being 42% of plan for Q94-3 and 68% of plan for FYTD94.
- FYTD94 revenue from the Consumer division was \$31 million over plan due to the expansion of the home PC market and the increased number of MS consumer products offered.

Operational Issues

- Product returns represented approximately 12% of FYTD94 gross revenue. In the US, with the launch of MS-DOS 6.2 in late Q94-2, \$20 million in returns of MS-DOS 6.0 were processed in Q94-2 and Q94-3. Return of MS-DOS products exceeded sales in Q94-3 exceeded sales.

Marketing, Advertising and Sales Programs

- The Select program, which focuses on large accounts, was launched in January 1993. Q94-3 revenue from this program in North America was \$21 million (approximately 56% of plan). FYTD94 revenue was \$41 million (approximately 66% of plan).
- The Microsoft Open License Pack (MOLP) was launched in February 1994, with the purpose of extending many of our Select program benefits to the large and growing medium-sized business segment. MOLP revenue was \$3 million for Q94-3.
- FYTD94 spending relating to Solution Marketing was substantially under plan, with the Envision program, a large account promotional marketing campaign, being launched late in Q94-3. The expense of this program is expected to impact Q94-4.

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NORTH AMERICA FINISHED GOODS REVIEW

Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$375.2	\$390.3	(\$15.1)	\$1,079.4	\$1,074.8	\$4.6
Cost of revenue	87.6	78.3	(9.2)	250.7	214.6	(36.1)
Gross profit	287.7	312.0	(24.3)	828.7	860.2	(31.5)
People expense	65.3	73.6	8.3	196.2	222.4	26.2
Facilities expense	25.3	24.8	(0.4)	65.6	71.9	6.3
Marketing expense	41.7	42.7	0.9	122.7	141.4	18.7
Other expenses	4.5	7.7	3.2	18.5	26.4	7.9
Controllable expenses	136.8	148.8	12.0	402.9	462.0	59.1
Responsibility margin	150.9	163.1	(12.2)	425.8	398.2	27.6
Net shared resources	(7.1)	(7.8)	(0.7)	(21.4)	(23.5)	(2.1)
Shared resource margin	\$158.0	\$170.9	(\$12.9)	\$447.2	\$421.7	\$25.5

Key Ratios

Annualized per employee
(in thousands)

Net revenue	\$423.2	\$398.5	\$24.6	\$399.4	\$364.8	\$34.6
Salespeople expense	102.1	100.5	(1.6)	96.9	99.9	3.0
% Net revenue						
Cost of revenue	23.3 %	20.1 %	(3.3) %	23.2 %	20.0 %	(3.3) %
Marketing expense	11.1 %	10.9 %	(0.2) %	11.4 %	13.2 %	1.8 %
Controllable expenses	36.5 %	38.1 %	1.7 %	37.3 %	43.0 %	5.7 %
Shared resource margin	42.1 %	43.8 %	(1.7) %	41.4 %	39.2 %	2.2 %

Salespeople expense summarizes people and facilities expenses. Ratios reflect period results annualized.

Cost Driver Analysis

Q94-3

- The gross profit margin in Q94-3 for the North American channel was 76.7% of net revenue in comparison with a plan of 79.9%, principally as a result of the \$10 million of inventory adjustments in excess of plan (which was included in other product costs). These inventory adjustments consisted primarily of re-work costs relating to the inventory of products impacted by the Stac judgment.
- Controllable expenses were 8% under plan for Q94-3. People expense was \$8 million (11%) under plan, as a result of below plan hiring. Facilities expense was slightly over plan as a result of telecommunications charges from Q94-2 which were recognized in Q94-3.
- The shared resource margin was 42.1% of net revenue, which was slightly below plan of 43.8%. Inventory adjustments drove this margin down by 3% of net revenue. The increase in cost of revenue was somewhat offset by less than plan controllable expenses.

FYTD94

- The FYTD94 gross profit margin was 76.7% of net revenue in comparison with plan of 80.0%. This was the result of \$22 million of inventory adjustments in excess of plan; \$10 million of royalties on consumer products in excess of plan; and the accrual of \$5 million for product and fulfillment costs relating to the additional boxes of Win Excel 5.0 and Win Powerpoint 4.0 to be provided to purchasers of Win Office 4.0.
- People expense was \$26 million under plan resulting from below plan hiring. Facilities expense was below plan because of less than plan telecommunications expense and depreciation. Marketing expense was \$18.7 million below plan, primarily due to underspending for Solutions Marketing.
- The shared resource margin was 41.4% of net revenue above the plan margin of 39.2%. Less than plan controllable expenses improved this margin by 5.7% of net revenue. The other product costs noted above reduced this margin by 3.3% of net revenue.

Sales, Marketing, & Product Support Update

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Significant Customers (in millions)

	<u>Q92-4</u>	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>	<u>Q94-3</u>
Ingram Micro	\$ 93	\$ 93	\$ 61	\$ 92	\$ 72	\$ 89	\$ 146	\$ 113
Merisel	66	66	56	56	51	67	99	95
Egghead	52	52	51	46	22	22	49	36
Software Spectrum	24	24	11	18	14	10	22	19
Corporate Software	21	21	11	17	10	9	22	18
Intelligent Electronics	6	6	4	5	2	5	14	9
Tech Data	—	—	—	—	—	6	12	9
800 Software	10	10	7	8	8	8	11	9
Sofmart	9	9	6	8	6	6	10	9
Vanstar	10	10	8	6	9	6	6	6
	<u>\$ 291</u>	<u>\$ 291</u>	<u>\$ 215</u>	<u>\$ 256</u>	<u>\$ 194</u>	<u>\$ 228</u>	<u>\$ 391</u>	<u>\$ 323</u>
Percent of gross revenue	<u>75%</u>	<u>75%</u>	<u>75%</u>	<u>77%</u>	<u>73%</u>	<u>74%</u>	<u>81%</u>	<u>81%</u>

- Published financial data for the most recent available quarter for Ingram, Merisel, Egghead, Software Spectrum, Corporate Software and Intelligent Electronics was used to calculate internal market share for these distributors/resellers. (Financial information was not available for Tech Data, 800 Software, Sofmart and Vanstar.) Those distributors/resellers for which financial data was available had a combined quarterly net sales of \$3,136 million. For the same quarter, MS net revenue to those distributors/resellers was \$307 million, or 9.8% of resellers' net sales.
- For the same period of the previous year, those distributors/resellers had combined quarterly net sales of \$2,264 million. For that quarter, MS net revenue to those distributors/resellers was \$202 million, or 6.4% of resellers' net sales. This reflected a 3.3% net share gain from the prior year period, or a 53% gross increase in internal market share for those resellers.
- Inventory for certain key products (MS-DOS 6.2 upgrade, Win NT, Win Office 4.0, Win Word 6.0 and Win Excel 5.0) in the US distribution channel is tracked. As of the end of Q94-3, there was approximately one month of inventory in the channel for the key MS-DOS products and Win Word 6.0 and approximately 1/2 month of inventory in the channel for Win Office 4.0. 6,500 units of Win NT Upgrade were in channel inventory, representing approximately eight months of inventory at the most recent low monthly sell-through rates. There were also 170,000 units of Win Excel 5.0 in the channel, approximating four months of inventory.
- As of the end of Q94-3, the order backlog for USFG was \$59 million. Of this amount, \$53 million was due to stock outs. The key products comprising the stock outs were MS-DOS 6.21 Upgrade, Access 2.0, Win Office Pro 4.2, and Encarta 1994.

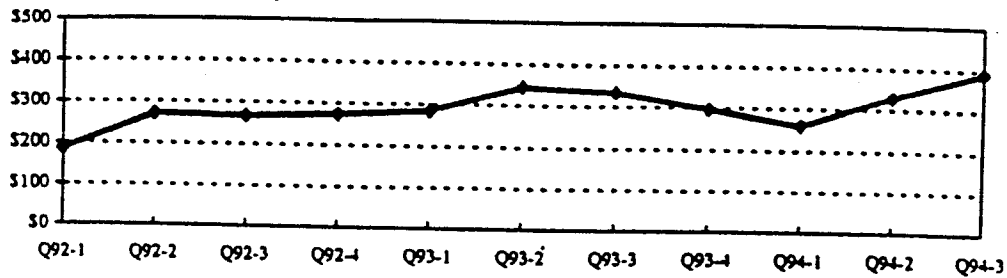
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EUROPE FINISHED GOODS REVIEW

EUROPE FINISHED GOODS REVIEW

Net Revenue Stream (in millions)



Key Highlights

- Net revenue reached a record level. Localized versions of Win Word 6.0 and Win Excel 5.0 were recently released in several countries resulting in strong sell-in during the quarter. The release of WFW 3.11 also contributed to the growth during Q94-3.
- Localized versions of Win Office were introduced in Europe in Q93-2 causing a significant increase from Q93-1.
- Prices for certain localized versions of Desktop Applications were reduced 5% to 15% during Q93-3.

Geographic Factors

- Prices in FYTD94 were generally lower compared to FYTD93. Prices were adversely affected by foreign exchange trends, increased product bundling, a mix shift towards license programs and the previously mentioned price reduction. Prices for Win Office and Win Excel (new users), and Win Office, existing users, exceeded plan for both Q94-3 and FYTD94.
- Favorable foreign exchange trends benefited Q94-3 and FYTD94 net revenue 5% compared to plan. The strengthening dollar caused a 10% (\$95 million) negative impact on FYTD94 net revenue compared to the same period of the prior year.
- Italy grew 126% from the prior year. In late FY93, the Italian government passed strong anti-piracy legislation that created demand by forcing offenders to purchase legal software.

Operational Issues

- The Central European warehouse closed in Q94-3. All other subsidiary warehouses will be closed by Q95-2.
- The number of direct ship distributors will decrease from approximately 1200 to 96 by July 1, 1994. Ireland will begin direct shipping to Ingram and the Nordic direct distributors in May with the remaining customers being served directly by the end of Q95-1.
- All subsidiaries are being converted to commission agents of Ireland which will significantly reduce the administrative burden of processing statutory financial data.
- Project Concorde will result in the eventual elimination of approximately 150 positions in Europe.
- Other initiatives include Project Phoenix, which is evaluating sales and marketing efficiencies, and Project Lynx which is considering PSS efficiencies.

EUROPE FINISHED GOODS REVIEW

Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$391.4	\$359.2	\$32.3	\$976.8	\$990.3	(\$13.5)
Cost of revenue	69.7	62.9	(6.8)	166.5	176.8	10.3
Gross profit	321.8	296.3	25.4	810.2	813.5	(3.2)
People expense	44.9	51.1	6.2	135.5	154.1	18.6
Facilities expense	15.4	17.6	2.3	46.0	52.6	6.6
Marketing expense	30.9	33.5	2.6	90.0	101.1	11.1
Other expenses	4.8	2.3	(2.4)	9.9	9.7	(0.2)
Controllable expenses	96.0	104.6	8.6	281.4	317.5	36.1
Responsibility margin	225.8	191.8	34.1	528.8	496.0	32.8
Net shared resources	1.8	1.3	(0.5)	4.2	4.0	(0.2)
Shared resource margin	\$224.0	\$190.5	\$33.6	\$524.6	\$492.0	\$32.6

Key Ratios

Annualized per employee
(in thousands)

Net revenue	\$655.0	\$531.4	\$123.6	\$547.3	\$498.4	\$48.8
Salespeople expense	100.8	101.7	0.8	101.7	104.0	2.3
% Net revenue						
Cost of revenue	17.8 %	17.5 %	(0.3) %	17.1 %	17.9 %	0.8 %
Marketing expense	7.9 %	9.3 %	1.4 %	9.2 %	10.2 %	1.0 %
Controllable expenses	24.5 %	29.1 %	4.6 %	28.8 %	32.1 %	3.2 %
Shared resource margin	57.2 %	53.0 %	4.2 %	53.7 %	49.7 %	4.0 %

Salespeople expense summarizes people and facilities expenses. Ratios reflect period results annualized.

Cost Driver Analysis

- People expense was 12% lower than plan for Q94-3 and FYTD94. Europe implemented a hiring freeze during Q94-1 due to lower than planned revenue. Minimal headcount additions were approved during midyear business reviews.
- Facilities expense was 13% lower than plan for Q94-3 and FYTD94 periods, due to lower than planned headcount.
- Marketing expense was 11% lower than plan FYTD94 and 8% lower than plan for Q94-3. Costs were under plan due to cost containment measures resulting from the lower than planned revenue as well as timing differences between actual and planned marketing spend. Typically, most of the marketing spend is incurred in the final quarter of the fiscal year reducing the favorable variance to plan.
- Other expenses exceeded plan during Q94-3 by 104%. This variance was primarily caused by additional bad debt provision taken in the French subsidiary resulting from Feeder's bankruptcy.
- FYTD94 controllable expenses increased 24% from the prior year compared to net revenue increase of 16%. As a result of higher average headcount for the current year resulting from the addition of employees late in FY93.

EUROPE FINISHED GOODS REVIEW

Significant Customers in Major Subsidiaries (in millions)

	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>	<u>Q94-3</u>
C2000	\$ 55	\$ 75	\$ 68	\$ 57	\$ 51	\$ 71	\$ 79
Merisel	20	31	33	27	35	33	48
Ingram	14	18	22	23	17	29	46
Olivetti	5	8	11	13	10	14	21
Knotron	6	9	13	6	11	15	13
Raab Karcher	-	-	-	-	6	16	13
Also ABC	4	4	4	4	5	7	11
Scribona AB	6	9	10	7	4	7	9
Softmart	6	11	9	5	5	7	6
Feeder	9	18	7	7	5	14	6
Wyrtsch Trading	4	4	4	3	4	6	6
Ista	6	9	4	5	4	5	4
BSP Software	9	4	-	-	-	-	-
Access	7	9	9	9	5	3	-
Rein	7	8	7	8	-	-	-
	<u>\$ 158</u>	<u>\$ 217</u>	<u>\$ 201</u>	<u>\$ 174</u>	<u>\$ 162</u>	<u>\$ 227</u>	<u>\$ 262</u>
Percent of gross revenue	<u>53%</u>	<u>58%</u>	<u>59%</u>	<u>56%</u>	<u>61%</u>	<u>66%</u>	<u>64%</u>

- C2000 represented 19% of total gross revenue in Q94-3. This percentage has remained relatively constant since Q93-1.
- Merisel increased from 7% of total gross revenue in Q93-1 to 12% in Q94-3.
- Ingram has also gained significant share since Q93-1, increasing from 5% to 11% of total net revenue.
- Feeder filed for bankruptcy protection during Q94-3.
- The top 10 customers accounted for approximately 62% of total European gross revenue, while the top three customers represented 43%.
- Most subsidiaries achieved local currency plan during Q94-3. However, France was 19.4% under plan for the quarter, 26% under plan FYTD94 and 19% lower than the comparable period of the prior year. These trends were the result of a poor economic climate, competitive pricing pressures and a reduction in market share.
- The European channel is planning to decrease the number of direct ship customers significantly during the upcoming quarters to facilitate efficient distribution practices. This should have the effect of increasing sales levels to the remaining individual customers.

Marketing, Advertising and Sales Programs

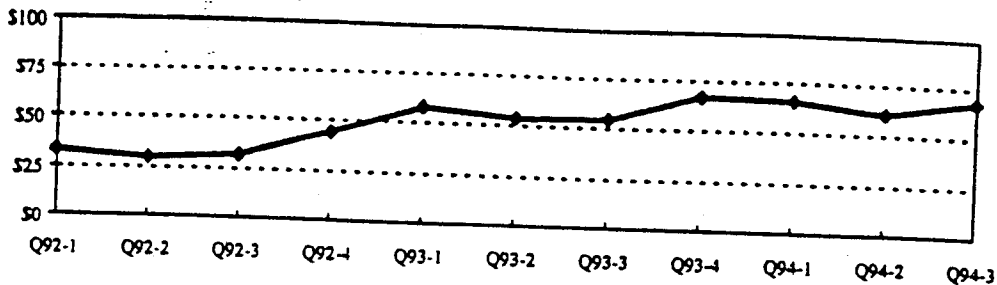
- Europe had a limited roll out of the Microsoft Open License Pack (MOLP) in late Q94-2. Revenues from MOLP were 3% of total net revenue during Q94-3.
- The Select program was released in Europe in late FY93. Select generated 9% of total net revenue for Q94-3. This represented 62% of the total FYTD94 Select revenue.

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ICON FINISHED GOODS REVIEW

ICON FINISHED GOODS REVIEW

Net Revenue Stream (in millions)



Key Highlights

- Net revenue has essentially been flat for four quarters versus a plan that anticipated significant growth. FYTD94 and Q94-3 revenue was 8% below plan. Sales were up 12.5% from Q94-2, in part due to the late March release of Office 4.2.
- Revenue in all three regions (APAC, Latin America and AIME) was below plan for Q94-3 and FYTD94.
- Revenue from Desktop applications was 95% of plan. Office revenue was 17% over plan, but this was not enough to offset unfavorable variances in Word and Excel, especially sales to Word existing users which were 73% below plan. Word 6.0 was released in December and sold in to the distributors, but the sell-through was much less than anticipated (end user demand was fulfilled through Office upgrades) and thus the sell-in during Q94-3 was low. This same phenomenon will probably occur in Q94-4 for Excel 5.0.
- For the quarter, revenue from Consumer products was 187% of plan reflecting the high acceptance of these products in Australia and New Zealand. However, revenue from MS-DOS was only 5% of plan (reflecting poor reviews, a full channel and uncertainty over the Stac lawsuit) and revenue from Win NT was 1% of plan as this product has generally been unsuccessful in the region.
- The forecast for Q94-4 projects an increase over Q94-3 of 29%, but represents only 94% of plan. The increase will come in part from the release of Spanish Office 4.2 and backlog from the Stac lawsuit.

Geographic Factors

- Political unrest is a material factor in much of the region including the assassination of a presidential candidate in Mexico. South African unrest, terrorist activities in Israel, civil war in Algeria and new economic plans in Brazil and Turkey.
- Software import duties in India decreased from 80% to 20%, which favorably affected sales.

Operational Issues

- The Singapore distributed manufacturing site is now building 200 SKUs. This has improved customer service and alleviated capacity constraints at Canyon Park.
- The Australian warehouse closed April 1 and distribution is now handled by RR Donnelley. Distributed manufacturing should be available in June. In addition, distributed manufacturing sites in Mexico and Brazil are being planned.
- For the first time, some products were direct shipped to the AIME region customers from Ireland.

Marketing, Advertising and Sales Programs

- Bill Gates' visit to Australia and New Zealand in February received significant positive media coverage.
- Office campaigns were launched throughout the region: more than 6,000 people attended Comdex Mexico and 10,000 attended the Australian roadshow.

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ICON FINISHED GOODS REVIEW

Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$68.0	\$73.9	(\$5.8)	\$195.0	\$212.7	(\$17.7)
Cost of revenue	16.3	17.9	1.6	45.9	51.4	5.5
Gross profit	51.7	56.0	(4.3)	149.1	161.3	(12.2)
People expense	12.2	13.3	1.1	35.3	40.4	5.1
Facilities expense	4.5	5.3	0.8	13.0	15.5	2.6
Marketing expense	6.4	6.6	0.2	18.1	22.1	4.0
Other expenses	2.0	2.1	0.2	6.1	7.4	1.2
Controllable expenses	25.0	27.3	2.3	72.4	85.4	13.0
Responsibility margin	26.7	28.7	(2.0)	76.7	75.9	0.8
Net shared resources	0.4	0.3	(0.1)	1.0	0.9	(0.1)
Shared resource margin	\$26.3	\$28.4	(\$2.1)	\$75.7	\$75.0	\$0.7

Key Ratios

Annualized per employee
(in thousands)

Net revenue	\$440.8	\$433.7	\$7.1	\$445.1	\$423.9	\$21.2
Salespeople expense	107.7	109.2	1.4	110.1	111.5	1.4
% Net revenue						
Cost of revenue	24.0 %	24.2 %	0.2 %	23.5 %	24.2 %	0.6 %
Marketing expense	9.4 %	8.9 %	(0.5) %	9.3 %	10.4 %	1.1 %
Controllable expenses	36.8 %	37.0 %	0.2 %	37.1 %	40.1 %	3.0 %
Shared resource margin	38.7 %	38.4 %	0.3 %	38.8 %	35.3 %	3.5 %

Salespeople expense summarizes people and facilities expenses. Ratios reflect period results annualized.

Cost Driver Analysis

- The region continued to control expenses during Q94-3 to offset the revenue shortfall. Controllable expenses increased 3.7% (in line with headcount growth of 5%) while revenue increased 12.0% over the prior quarter. Planned revenue per head was maintained by freezing headcount early in the fiscal year.
- The positive variance in people expense resulted from headcount freezes and reductions throughout the region, primarily in Mexico, South Africa and Australia. Headcount at quarter end was 633 versus plan of 683. In addition, the region continued to aggressively manage travel expense.
- Cost of revenue percentage for Q94-3 and FYTD94 was slightly better than plan. The positive variance was due to changes in product mix (primarily a shift toward Select licensing) which were offset by negative manufacturing variances that primarily resulted from outsourcing.
- Despite the revenue shortfall, Q94-3 and FYTD94 controllable expenses were below plan as a percent of revenue.

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Significant Customers in Major Subsidiaries (in millions)

	<u>Q93-1</u>	<u>Q93-2</u>	<u>Q93-3</u>	<u>Q93-4</u>	<u>Q94-1</u>	<u>Q94-2</u>	<u>Q94-3</u>
Australia							
Tech Pacific	\$ 4.2	\$ 4.8	\$ 4.8	\$ 8.1	\$ 8.8	\$ 10.1	\$ 8.7
Merisel	3.4	3.8	6.1	9.0	5.7	5.2	3.6
Datacom	--	--	--	--	--	1.7	4.8
Mexico							
Ingram-Dicom	2.9	3.9	2.1	4.8	1.4	1.7	3.9
Brazil							
Agoal	2.7	4.6	0.4	0.2	0.2	2.8	1.1
Compucenter	1.9	1.8	1.7	2.2	2.3	2.2	2.5
South Africa							
Workgroup	3.1	2.6	2.0	3.5	3.0	2.9	2.6
	<u>\$ 18.2</u>	<u>\$ 21.5</u>	<u>\$ 17.1</u>	<u>\$ 27.8</u>	<u>\$ 21.4</u>	<u>\$ 26.6</u>	<u>\$ 27.2</u>
Percent of gross revenue	<u>32%</u>	<u>40%</u>	<u>31%</u>	<u>41%</u>	<u>32%</u>	<u>40%</u>	<u>39%</u>

- Q94-3 sales to the top 7 distributors decreased slightly as a percentage of gross revenue over Q94-2 primarily due to decreased market share for Merisel in Australia and Agoal in Brazil.
- Agoal, our largest distributor in Brazil, is on the verge of bankruptcy. Though they are in negotiations with several buyers, it appears unlikely that we will fully recover our \$2.3 million receivable. However, we have accrued for any losses that might occur.
- Continued growth in the region is expected to come primarily from smaller distributors in the other ICON countries not represented on this chart where average quarterly sales generally run less than \$1 million.

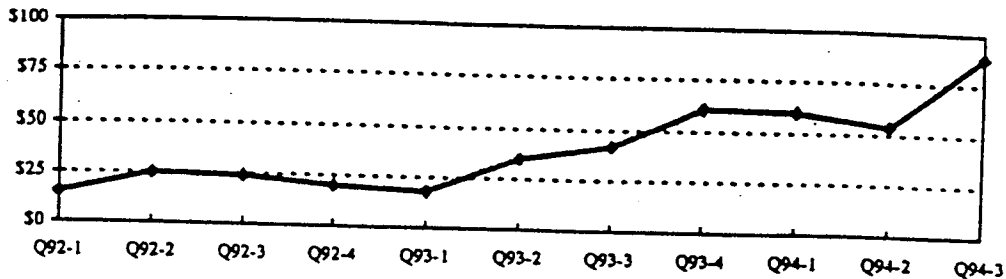
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FAR EAST FINISHED GOODS REVIEW

FAR EAST FINISHED GOODS REVIEW

Net Revenue Stream (in millions)



Key Highlights

- The shipment of localized Excel 5.0 in Japan in March was a success. Although the product was released later than planned, more than 100,000 units were shipped in March. Excel revenue for the Far East was \$10.0 million (77%) in excess of plan for Q94-3.
- Office had the largest favorable revenue variance during Q94-3 (\$14.6 million or 191% above plan). Eighty five percent (\$18.8 million) of Far East Office revenue was in Japan.
- A localized version of Access was launched in Japan in December 1993, and sales subsequent to the launch have been very strong (approximately 15,000 units per month). FYTD94 revenue was \$8.1 million (145%) over plan.
- Language revenue was robust during the quarter: the Basic and Languages product units were \$3.4 million (128%) and \$3.2 million (59%) above budget, respectively. The success of Visual Basic and C++ was largely due to a dearth of localized competitive product in Japan.
- Windows revenue was 33% below plan in Q94-3 reflecting the continued migration of sales from the finished goods to the OEM channel. FG Windows sales comprised less than 10% of total Windows revenues for Q94-3.

Geographic Factors

- The strength of the yen continued to help U.S. dollar revenue during Q94-3: of the \$32.3 million favorable variance in net revenue, \$6.3 million (19% of the variance) was due to foreign exchange variances. The Korean won was also stronger than planned.

Operational Issues

- Efforts to reduce product costs for locally manufactured product in Japan produced visible results in Q94-3. Product costs per unit for Excel 5.0 (Japanese) were 20% lower than per unit costs for Excel 4.0 (Japanese), and per unit costs for Japanese Access were 13% lower than comparable costs for U.S.-manufactured Access.

Marketing, Advertising and Sales Programs:

- The Select program gained momentum in the Far East over the past quarter as three master and 18 enrollment agreements were executed.
- A current emphasis on vertical marketing for financial institutions is showing promise in Japan and Hong Kong, where a number of the world's largest commercial banks are located.
- A recent visit by Bill Gates to the PRC was in part intended to address constraints in that country on sales of localized Windows. It is hoped that his visit will assist Microsoft's short- and long-term prospects in PRC.

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Sales, Marketing, & Product Support Update/

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FAR EAST FINISHED GOODS REVIEW

Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$88.2	\$55.9	\$32.3	\$202.4	\$147.3	\$55.0
Cost of revenue	18.0	15.5	(2.5)	46.1	39.5	(6.6)
Gross profit	70.2	40.4	29.8	156.3	107.8	48.5
People expense	11.1	10.6	(0.5)	32.6	31.5	(1.1)
Facilities expense	3.1	3.4	0.4	9.4	10.3	1.0
Marketing expense	6.4	6.3	(0.1)	20.7	18.5	(2.2)
Other expenses	1.0	0.8	(0.1)	2.6	2.5	(0.1)
Controllable expenses	21.5	21.1	(0.4)	65.3	62.7	(2.5)
Responsibility margin	48.7	19.2	29.5	91.0	44.9	46.1
Net shared resources	6.4	9.3	2.9	25.8	29.9	4.1
Shared resource margin	\$42.3	\$9.9	\$32.3	\$65.2	\$15.2	\$50.1

Key Ratios

Annualized per employee
(in thousands)

Net revenue	\$944.9	\$547.3	\$397.6	\$713.2	\$534.1	\$179.1
Salespeople expense	152.0	137.6	(14.4)	147.8	151.4	3.6
% Net revenue						
Cost of revenue	20.4 %	27.8 %	7.3 %	22.8 %	26.8 %	4.0 %
Marketing expense	7.2 %	11.2 %	4.0 %	10.2 %	12.5 %	2.3 %
Controllable expenses	24.4 %	37.8 %	13.5 %	32.2 %	42.6 %	10.3 %
Shared resource margin	47.9 %	17.8 %	30.1 %	32.2 %	10.3 %	21.9 %

Salespeople expense summarizes people and facilities expenses. Ratios reflect period results annualized.

Cost Driver Analysis

- Foreign exchange variances caused unfavorable controllable expense variances for Q94-3 and FYTD94. Ignoring exchange rate fluctuations, controllable expense variances for the quarter and FYTD94 would have been favorable in the amounts of \$900,000 and \$1.7 million, respectively.
- Excluding foreign exchange variances, all expense categories were under plan FYTD94 except marketing, which was \$750,000 above plan due to above plan expenditures (TV campaign) during Q94-1. Facility expense FYTD94 was \$1.5 million under plan (ignoring foreign exchange variances) primarily due to the reduction in the Tokyo office building rental rate.
- Average headcount FYTD94 was 5% below plan; combined with revenue being well above plan, the net revenue per employee statistic showed a considerable favorable variance.
- Although marketing expense was over plan for both Q94-3 and FYTD94, it was under plan as a percent of revenue because of the favorable variances in net revenue.
- Cost of revenue was significantly under plan (as a percent of net revenue) during Q94-3 because of both a favorable shift in product mix and reductions in product costs for Japanese versions of Access 1.0 and Excel 5.0, which together comprised 31% of total licenses sold in the region during Q94-3.

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FAR EAST FINISHED GOODS REVIEW

Significant Customers in Major Subsidiaries (in millions)

	Q92-4	Q93-1	Q93-2	Q93-3	Q93-4	Q94-1	Q94-2	Q94-3
Japan								
Soft Bank	\$3.3	\$1.1	\$7.2	\$7.1	\$11.6	\$9.4	\$11.8	\$25.4
Software Japan	3.0	1.4	3.3	3.5	5.1	6.2	6.4	7.4
Soft Wing	1.9	0.9	3.5	3.1	4.5	4.0	4.1	6.7
Fujitsu	1.0	1.0	0.9	1.9	1.4	1.9	2.2	3.7
Canon Sales	1.8	2.1	1.2	2.3	1.7	2.0	1.0	2.6
Otsuka Shokai	0.4	0.2	0.3	0.6	0.7	0.9	1.1	2.2
NEC	1.3	1.2	1.0	1.2	2.4	2.3	1.4	1.4
Taiwan								
Acer Sertek	0.6	0.8	0.8	0.6	1.3	2.3	0.5	1.9
Eten	0.3	0.8	0.5	0.9	1.9	2.4	0.6	1.5
Korea								
Infotech	0.4	0.6	0.4	0.5	1.7	3.0	1.9	1.3
	<u>\$14.0</u>	<u>\$10.2</u>	<u>\$19.0</u>	<u>\$21.7</u>	<u>\$32.3</u>	<u>\$34.3</u>	<u>\$30.9</u>	<u>\$54.1</u>
Percent of gross revenue	<u>66%</u>	<u>57%</u>	<u>54%</u>	<u>52%</u>	<u>53%</u>	<u>57%</u>	<u>55%</u>	<u>60%</u>

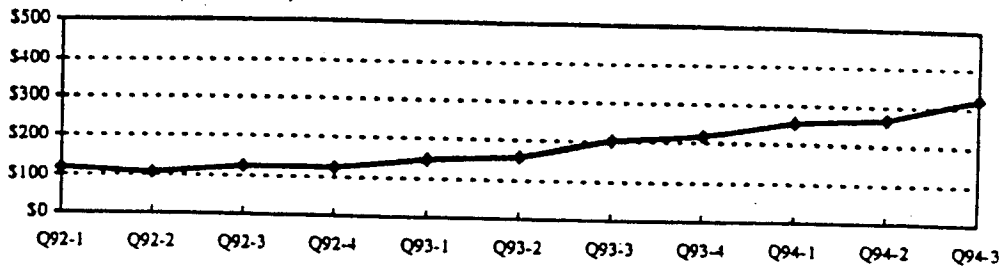
- As a percent of gross revenue, sales to major distributors increased significantly during Q94-3 largely because of sales to Soft Bank associated with the Excel 5.0 (Japanese) launch. Soft Bank represented 28% of regional gross revenue in Q94-3, up from 15% and 21% in Q94-1 and Q94-2, respectively.
- In Q94-3, Microsoft accounted for an increased share of the revenue of two large distributors, Software Japan and Soft Wing. MS's share of the companies' revenues increased from 7% for both in Q94-2 to 12% and 13% for Software Japan and Soft Wing, respectively.
- Microsoft Korea commenced an aggressive program in Q94-3 to restructure its channels of distribution. In the recent past, Infotech has accounted for more than 40% of finished goods revenues in Korea. To reduce dependency on Infotech, Microsoft has recruited two new distributors, SamTech and SunKyung. During Q94-3, Infotech's share of Microsoft Korea's sales decreased from 42% to 29%.

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OEM REVIEW

OEM REVIEW

Net Revenue Stream (in millions)



Key Highlights

- Lower PC prices and a growing consumer market, as well as a higher penetration of naked systems, fueled a record quarter. OEM net revenue of \$323 million was 26% of consolidated net revenue. OEM contribution margin of \$202 million was 47% of consolidated contribution margin.
- FYTD net revenue of \$846 million was 65% greater than prior year, a growth rate of almost four times PC shipments. Factors contributing to the disparity include additional OEMs, more revenue per unit, and increased Windows penetration.
- Decreases in CPU and memory prices carried through to reduce PC prices, permitting businesses and, particularly, home consumers to purchase faster, more powerful computers.

Geographic Factors

- All subsidiaries, but Thailand, Taiwan, and Portugal, exceeded plan for the quarter. North America was 58% over plan, Europe was 92% over plan, and ROW was 72% over plan.
- Europe's variance was largely the result of minimum commitment billings for new agreements with Vobis, Escom, Siemens-Nixdorf, and Actebis. Microsoft Easy Distribution (MED) product was \$11 million over plan, in part due to the inroads made against piracy and unbundling of MS-DOS and Windows.
- Japan accounted for virtually all of the Far East's \$19 million positive variance mostly due to a sharp increase in Toshiba's export business.

Operational Issues

- All OEMs have received MS-DOS 6.21, which excludes compression technology. Some OEMs have complained of lessened functionality due to the removal of DoubleSpace. MS-DOS 6.22 with new compression technology will ship to OEMs in Q94-4.
- A new management team took steps to improve product release and distribution processes by reorganization of Product Release Services to align with the sales structure and creation of a task force from key product groups, OEM Operations, and OEM Sales.

Marketing, Advertising and Sales Programs

- The marketing group continues its "high touch" programs, leveraging funds by going to large OEMs and creating joint marketing programs, such as the Compaq Frontline Partnership.
- A "Demand & Deliver" initiative was started to promote awareness of key buyer groups to genuine MS product and where it can be purchased.

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OEM REVIEW

Top Products (units in thousands, revenue in millions)

Q94-3

	Q94-3			Q94-3 Plan			Variance		
	Units	Revs	\$/Unit	Units	Revs	\$/Unit	Units	Revs	\$/Unit
MS-DOS	7,069	\$ 137	\$ 19	5,934	\$ 99	\$ 17	1,135	\$ 38	\$ 4
Windows	5,901	108	18	4,022	69	17	1,879	39	1
Mouse	1,277	18	14	489	6	12	788	12	2
OS/2	516	13	25	506	8	16	10	5	9
Works	1,032	10	10	581	6	10	451	4	(1)
Other		57	N/A		16	N/A		41	N/A
		343			204			139	
Revenue adjustments		(20)			-			(20)	
Net Revenue		<u>\$ 323</u>			<u>\$ 204</u>			<u>\$ 119</u>	

- Mouse prices have decreased due to introduction of the less-expensive Defender mouse, which is being well-received by OEMs.
- Driven by Works shipments, consumer products continued to grow approximately 24% per quarter.
- A reserve of \$20 million were taken in anticipation of royalty concessions due to removing compression technology from MS-DOS, and no GAAP accrual was posted for the quarter.

FYTD94

	FYTD94			FYTD94 Plan			Variance		
	Units	Revs	\$/Unit	Units	Revs	\$/Unit	Units	Revs	\$/Unit
MS-DOS	16,668	\$ 327	\$ 20	16,759	\$ 285	\$ 17	(91)	\$ 42	\$ 1
Windows	14,885	265	18	8,063	179	22	6,822	86	(4)
Mouse	3,093	47	15	1,366	17	12	1,727	30	3
OS/2	1,249	26	21	1,257	20	16	(8)	6	5
Works	2,604	26	10	1,595	17	11	1,009	9	(1)
Other		139	N/A	2,539	61	N/A	(2,539)	78	N/A
		830			579			251	
Revenue adjustments		16			-			16	
Net Revenue		<u>\$ 846</u>			<u>\$ 579</u>			<u>\$ 267</u>	

- Windows for Workgroups penetration is increasing, with Gateway 2000, Packard Bell, Zenith, Escom, and several other large OEMs shipping it on 100% of their systems.

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OEM REVIEW

Significant Customers (in millions)

	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Large Accounts						
Compaq	\$ 29.2	\$ 21.5	\$ 7.7	\$ 72.6	\$ 57.1	\$ 15.5
IBM	23.0	13.6	9.4	59.4	33.0	26.4
Gateway 2000	18.7	15.8	2.9	48.1	44.7	3.4
AST	14.8	5.9	8.9	33.2	17.1	16.1
Dell	11.8	8.6	3.2	35.2	23.9	11.3
Packard Bell	10.6	8.1	2.5	25.1	21.2	3.9
Solution Providers						
DEC	8.3	4.1	4.2	16.6	10.9	5.7
Hewlett Packard	7.6	6.4	1.2	22.3	15.6	6.7
NCR	5.8	3.3	2.5	13.7	9.5	4.2
Unisys	2.9	1.2	1.7	8.5	4.1	4.4
Other	2.9	2.1	0.8	8.6	6.4	2.2
Named Accounts	18.3	14.4	3.9	48.6	40.0	8.6
New Business Accounts	35.6	17.2	18.4	80.5	57.3	23.2
International Accounts						
Toshiba	12.0	1.9	10.1	24.2	4.0	20.2
Olivetti	9.6	4.0	5.6	15.8	10.0	5.8
Vobis	8.8	5.6	3.2	18.7	10.9	7.8
SNI (Siemens)	7.4	2.9	4.5	12.8	8.3	4.5
Escorn	5.7	2.3	3.4	17.9	5.5	12.4
ICL	4.6	3.0	1.6	8.6	8.3	0.3
Other	97.1	59.4	37.7	244.6	183.6	61.0
Other Accounts	8.4	2.8	5.6	15.5	7.6	7.9
Gross revenue	343.1	204.1	139.0	830.5	579.0	251.5
Revenue adjustments	(20.2)	--	(20.2)	15.8	--	15.8
Net revenue	<u>\$ 322.9</u>	<u>\$ 204.1</u>	<u>\$ 118.8</u>	<u>\$ 846.3</u>	<u>\$ 579.0</u>	<u>\$ 267.3</u>

- The "Big 6" (Compaq, IBM, Gateway 2000, Dell, Packard-Bell, and AST) continued to grow, accounting for \$108 million and 33% of Q94-3 net revenue. Several of these OEMs expanded worldwide manufacturing facilities or entered new distribution channels.
- The New Business group reviewed all licensed MED (Microsoft Easy Distribution) customers, moving low-volume customers to the Delivery Service Partner (DSP) program, where customers buy 5-paks with break-the-seal licenses from distributors. This increased operational efficiency and freed account managers to focus on the larger OEMs.

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DOMESTIC PSS

Highlights

- PSS is preparing to implement Regional Support Centers (RSCs) in the US and internationally. Under the RSC plan, PSS will provide Advanced and Developer cluster support to specified numbers of regions via one centralized location. The support centers are expected to increase the quality of support and help control costs.
- In Q94-3, PSS began detailed planning for the release of Chicago. Based on a 30-day no-charge support policy, PSS will need an additional 590 resources to meet peak demand. We are exploring alternative methods to meet this peak demand while continuing to control costs.
- PSS is expanding its search for new outsourcing partners. MS currently outsources approximately 350 people or 6,000 calls per day. PSS would like to decrease its dependency on a single outsourcing partner and continue to take advantage of this less expensive support option.
- PSS believes support became a competitive advantage for the MS Office product line during Q94-3. PSS expanded competitive upgrade support while WordPerfect and Lotus scaled back their no-charge support to end user customers.

Cost Distribution by Channel Including Domestic Allocations to International (in millions)

	PSS Cost				USFG and US OEM Net Revenue			
	Q94-3		FYTD94		Q94-3		FYTD94	
	Amount	%	Amount	%	Amount	%	Amount	%
USFG	\$32.4	85%	\$89.8	83%	\$339.1	9.5%	\$991.9	9.1%
US-OEM	3.4	9%	10.5	10%	172.0	2.0%	494.9	2.1%
INTL	2.4	6%	7.6	7%	N/A		N/A	
	<u>\$38.2</u>	<u>100%</u>	<u>\$107.9</u>	<u>100%</u>	<u>\$511.1</u>	<u>7.0%</u>	<u>\$1,486.8</u>	<u>6.7%</u>
PLAN	<u>\$39.2</u>		<u>\$116.6</u>					

- PSS costs were 7.0% of revenue in Q94-3, and are expected to remain constant in Q94-4.

Cost Distribution and Cost as Percent of Net US Revenue by Product Unit (in millions)

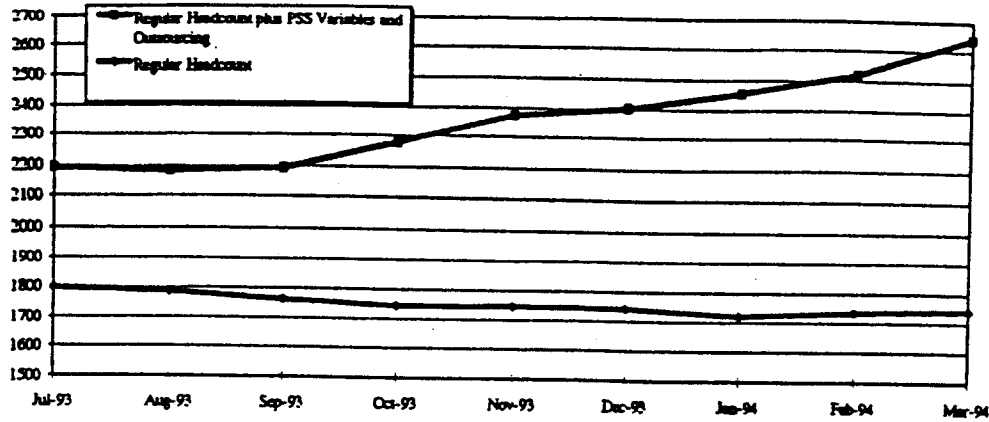
	Q94-3			FYTD94		
	Actual	Act Mix	% of US Rev.	Actual	Act Mix	% of US Rev.
Windows	\$7.5	21.0	1.5%	\$21.5	21.4	1.4%
Word	5.8	16.2	1.1%	15.4	15.3	1.0%
Excel	4.0	11.2	0.8%	10.3	10.2	0.7%
Win NT	2.8	7.8	0.5%	7.6	7.6	0.5%
DBMS	2.6	7.2	0.5%	7.5	7.5	0.5%
MS-DOS	1.9	5.3	0.4%	6.7	6.7	0.5%
Fox	2.5	6.9	0.5%	7.1	7.1	0.5%
OOS	1.6	4.4	0.3%	4.9	4.9	0.3%
Messaging	1.6	4.3	0.3%	4.3	4.3	0.3%
C++	1.3	3.8	0.3%	3.7	3.7	0.2%
Works	0.9	2.5	0.2%	2.6	2.6	0.2%
Project	0.8	2.4	0.2%	2.1	2.1	0.1%
Entry	0.7	2.0	0.1%	2.0	2.0	0.1%
Basic	0.7	1.9	0.1%	1.7	1.7	0.1%
Graphics	0.4	1.1	0.1%	1.1	1.1	0.1%
SET	0.3	0.7	0.1%	0.8	0.8	0.1%
Other	0.4	1.1	0.1%	1.0	1.0	0.1%
Total	<u>\$35.8</u>	<u>100.0%</u>	<u>7.0%</u>	<u>\$100.3</u>	<u>100.0%</u>	<u>6.7%</u>

- For Q94-3, MS Windows, Word and Excel constituted 48% of PSS costs due to major releases in each of the product groups.

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DOMESTIC PSS

PSS Headcount - FY94 YTD



- PSS continues to control costs and meet support demand by leveraging less expensive variable and outsourced staffing.

Average Daily Call Volume - Q94-3

	Average	Daily # of Calls		Handled Ratio	Service Level
	Duration (in min)	Offered	Handled		
Win Word	14	4,604	3,652	79%	30%
Windows	17	2,827	2,784	98%	65%
Win Excel	12	3,031	2,872	95%	67%
MS-DOS	18	1,860	1,847	99%	75%
Win Access	12	2,103	2,073	99%	68%
WFW	23	1,099	1,038	94%	52%
Win Fox	12	883	864	98%	56%
Mac Word	8	823	734	89%	52%
Win NT	18	210	208	99%	97%
PSS Weighted Average	14	23,839	22,056	93%	56.3%

- The handled ratio is a measure of the % of customer calls that reach a support engineer; the remainder of the customers abandon the call prior to reaching an engineer. The handle ratio goal is 95%. Service level is a measure of the percent of customers who reach a support engineer in less than 60 seconds.
- Win Word call volumes were high due to the recent release of Win Word 6.0. The low service level was due to understaffing caused by higher than anticipated sales and special competitive upgrade support policies. PSS is currently staffing to meet demand and service levels were trending upward in March.

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Product Divisions

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PRODUCT BUSINESS UNITS RESULTS OF OPERATIONS SUMMARY
(IN MILLIONS)

Q94-3

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$601.8	115 %	\$495.0	115 %	\$400.3	123 %	\$286.7	134 %
Database & Dev. Tools	89.8	79	69.5	75	22.1	49	5.1	26
Consumer	74.8	126	59.5	125	30.0	182	18.3	340
Workgroup	27.8	132	24.4	138	6.4	427	0.1	NM
Systems	444.9	124	385.0	125	147.5	79	84.0	71
Advanced Technology	1.5	46	0.9	36	(11.8)	NM	(12.2)	NM
Other	3.7	34	2.5	34	(36.7)	NM	(21.6)	(118)
	<u>\$1,244.1</u>	<u>114</u>	<u>\$1,036.7</u>	<u>115</u>	<u>\$537.7</u>	<u>96</u>	<u>\$360.5</u>	<u>102</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	48 %	48 %	82 %	82 %	67 %	62 %	48 %	41 %
Database & Dev. Tools	7	10	77	81	25	39	6	17
Consumer	6	5	80	80	40	28	25	9
Workgroup	2	2	88	84	23	7	0	(20)
Systems	36	33	87	86	33	52	19	33
Advanced Technology	0	0	63	82	(801)	(537)	(829)	(569)
Other	0	1	66	66	NM	44	(581)	169
	<u>100 %</u>	<u>100 %</u>	<u>83</u>	<u>83</u>	<u>43</u>	<u>52</u>	<u>29</u>	<u>32</u>

FYTD94

	Net Revenue		Gross Profit		Responsibility Margin		Contribution Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Desktop Applications	\$1,470.4	106 %	\$1,219.8	107 %	\$925.1	113 %	\$623.1	120 %
Database & Dev. Tools	254.2	87	196.6	84	69.8	75	16.8	57
Consumer	226.9	133	178.7	131	93.5	244	53.5	836
Workgroup	73.9	121	65.2	127	18.1	1,415	(0.5)	NM
Systems	1,255.9	117	1,072.1	116	622.9	113	425.5	123
Advanced Technology	6.5	65	4.4	53	(29.7)	NM	(31.8)	NM
Other	67.9	227	67.8	337	(27.5)	(219)	32.2	NM
	<u>\$3,355.7</u>	<u>111</u>	<u>\$2,804.6</u>	<u>112</u>	<u>\$1,672.2</u>	<u>114</u>	<u>\$1,118.8</u>	<u>136</u>

	Net Revenue Mix		Gross Profit % Net Revenue		Resp Mgn % Net Revenue		Contr Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Desktop Applications	44 %	46 %	83 %	82 %	63 %	59 %	42 %	37 %
Database & Dev. Tools	8	10	77	81	27	32	7	10
Consumer	7	6	79	80	41	22	24	4
Workgroup	2	2	88	84	25	2	(1)	(25)
Systems	37	36	85	86	50	51	34	32
Advanced Technology	0	0	67	82	(454)	(485)	(485)	(515)
Other	2	1	100	67	(41)	42	47	(33)
	<u>100 %</u>	<u>100 %</u>	<u>84</u>	<u>83</u>	<u>50</u>	<u>49</u>	<u>33</u>	<u>27</u>

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DESKTOP APPLICATIONS

Summary (in millions)

Q94-3

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Excel PU	\$285.9	128 %	\$49.5	112 %	\$37.2	93 %	\$199.2	142 %
Graphics PU	54.6	131	12.3	106	8.9	78	33.4	179
Project PU	24.3	70	2.1	91	5.7	84	16.5	65
Word PU	237.0	106	42.9	116	42.9	96	151.1	107
	<u>\$601.8</u>	<u>115</u>	<u>\$106.8</u>	<u>112</u>	<u>\$94.7</u>	<u>92</u>	<u>\$400.3</u>	<u>123</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Excel PU	48 %	43 %	17 %	20 %	13 %	18 %	70 %	62 %
Graphics PU	9	8	23	28	16	27	61	45
Project PU	4	7	8	7	23	20	68	74
Word PU	39	43	18	17	18	20	64	63
	<u>100 %</u>	<u>100 %</u>	<u>18</u>	<u>18</u>	<u>16</u>	<u>20</u>	<u>67</u>	<u>62</u>

FYTD94

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
Excel PU	\$593.4	106 %	\$101.1	91 %	\$118.4	95 %	\$373.9	115 %
Graphics PU	120.5	115	31.6	128	28.2	84	60.7	131
Project PU	69.6	91	5.4	95	17.3	89	46.9	91
Word PU	686.9	107	112.5	103	130.8	94	443.6	112
	<u>\$1,470.4</u>	<u>106</u>	<u>\$250.6</u>	<u>100</u>	<u>\$294.8</u>	<u>93</u>	<u>\$925.1</u>	<u>113</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
Excel PU	40 %	40 %	17 %	20 %	20 %	22 %	63 %	58 %
Graphics PU	8	8	26	24	23	32	50	44
Project PU	5	6	8	7	25	25	67	67
Word PU	47	46	16	17	19	22	65	61
	<u>100 %</u>	<u>100 %</u>	<u>17</u>	<u>18</u>	<u>20</u>	<u>23</u>	<u>63</u>	<u>59</u>

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DESKTOP APPLICATIONS

Desktop Applications Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$601.8	\$523.9	\$77.8	\$1,470.4	\$1,386.3	\$84.2
Cost of revenue	106.8	95.1	(11.6)	250.6	251.0	0.4
Gross profit	495.0	428.8	66.2	1,219.8	1,135.3	84.5
People expense	15.8	16.9	1.1	49.3	52.2	2.9
Facilities expense	4.4	4.0	(0.4)	11.6	12.2	0.5
Marketing expense	46.8	42.1	(4.7)	141.2	134.0	(7.3)
Product dev (ext)	4.1	4.7	0.6	12.9	16.5	3.6
PSS	14.2	24.6	10.4	54.7	73.8	19.2
Other expenses	5.1	5.4	0.3	12.4	14.5	2.1
Net shared resources	4.4	4.9	0.5	12.5	13.7	1.2
Controllable expenses	94.7	102.6	7.9	294.8	316.8	22.1
Responsibility margin	\$400.3	\$326.1	\$74.1	\$925.1	\$818.5	\$106.6
% Net revenue						
Cost of revenue	17.7 %	18.2 %	0.4 %	17.0 %	18.1 %	1.1 %
Responsibility margin	66.5 %	62.2 %	4.3 %	62.9 %	59.0 %	3.9 %
Controllable Expense Mix						
All product development	25.6 %	25.0 %		25.1 %	25.5 %	
Marketing	49.4	41.1		47.9	42.3	
PSS	15.0	24.0		18.6	23.3	
Other expenses	10.0	10.0		8.5	8.9	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

All product development includes people, facilities, and external product development expenses.

Cost Driver Analysis

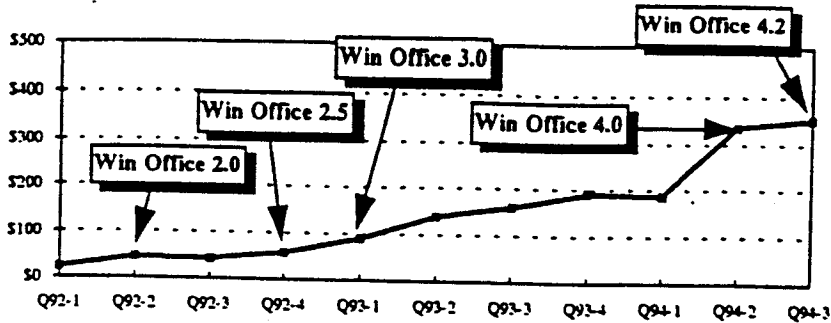
- The shipment of Win Excel 5.0, Win PowerPoint 4.0 and Win Office 4.2 helped push Desktop Applications net revenue \$78 million above plan following Q94-2's \$45 million shortfall. Record revenue of \$602 million for the quarter was 23% ahead of Q94-2. In addition, \$3 million was added to the deferred revenue balance relating to the Office guarantee program. This increased the deferred revenue balance at the end of Q94-3 to \$59 million.
- Cost of revenue as a percent of net revenue was below plan for the quarter and FYTD94, but higher than FYTD93 due in part to the free upgrades shipped in connection with the Office guarantee program.
- People expense was below plan, but slightly higher than plan on a per head basis since the division was 98 heads (10%) below plan.
- Marketing expense was above plan for Q94-3 and FYTD94 due to product launch activities and incremental funding. FYTD94 marketing spend was 34% higher than last year.
- PSS costs were well below plan for Q94-3 due in part to a change in the international PSS allocation methodology. PSS costs were 38% higher than FYTD93 due to increased staffing in international locations.
- The responsibility margin was above plan for Q94-3 due mainly to high sales volumes. The FYTD94 margin was better than plan at 63% of net revenue; the FYTD93 margin was 68%. The difference was primarily a result of: revenue deferred to future quarters, higher cost of revenue as a percent of net revenue relating to free upgrades, marketing costs and PSS costs as explained above.

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OFFICE

Gross Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Win Office 4.2, which includes Word 6.0, Excel 5.0 and PowerPoint 4.0, began shipping in March. Win Office 4.0 (sold from November 1992 through March 1994) included coupons which entitled purchasers to free upgrades to the new versions of Excel 5.0 and PowerPoint 4.0. MS will honor these coupons through the end of the "Technology Guarantee" program in May.
- A similar "Power Guarantee" program on the Macintosh platform provides free upgrades to upcoming versions of MS's Mac Office products for users who purchase Mac Office after April 1, 1994. It is not expected that a revenue deferral account will be established due to the relatively small size of the Mac Power Guarantee program. MS actively participated in Apple's PowerMac launch in New York on March 14.
- Win OfficePro 4.3, which also includes the new version of Microsoft Access (version 2.0) will ship in April. There will be an increased marketing emphasis on this version with a goal of selling 25% of MS Office as OfficePro. For the first time, an OfficePro upgrade will be offered at \$399 with an introductory rebate of \$40 for version upgrades. The SRP for standard OfficePro is \$899 versus \$750 for Office.
- Win Office sales represented 69% of Office application (Word, Excel and PowerPoint) sales in Q94-3.
- In late April, Microsoft will announce the Office Compatible program which allows ISVs to license visual elements and integration features of Office in their products. MS will provide cooperative marketing opportunities including the use of the Office Compatible logo. ISV contracts are now being finalized.
- Win PowerPoint 4.0 was RTM in February and began shipping in March. This new version improved integration and consistency with Excel 5.0 and Word 6.0. Version 4.0 also sought to make the product easier to use by automating some of the repetitive work in formatting a presentation.

Competition

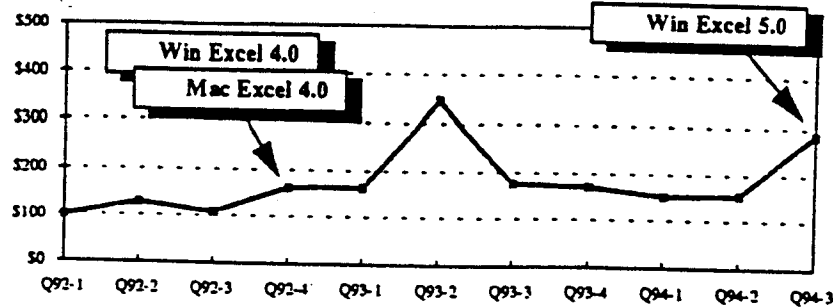
- In January 1994, WordPerfect and Borland announced the availability of Borland Office 2.0 for Windows. This version includes WordPerfect 6.0 for Windows, Quattro Pro 5.0 for Windows Workgroup Edition and Paradox 4.5 for Windows Workgroup Edition. All three products were honored with PC/Computing's Most Valuable Player Award.
- Lotus is expected to release an updated version of SmartSuite with a new version of the Approach database product. It is likely to include minor enhancements to other products in the suite and improved Notes integration. It is expected that none of the SmartSuite applications, with the exception of Approach, will support OLE 2.0 until the Chicago version is released.

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DESKTOP APPLICATIONS

EXCEL

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- In the first eight weeks after RTM, Microsoft shipped 1.5 million units of Win Excel 5.0, making it the fastest selling spreadsheet in history. Approximately half of these units were automatic upgrades shipped to purchasers of Win Office 4.0 starting in November.
- Over 200,000 boxes of Win Excel 5.0 in MS inventory were reworked to remove decompression code from the help facility. This rework disrupted shipments for a short time and resulted in extra rework costs during the last week of February.
- Mac Excel 5.0 is scheduled to release in May. Within two months of the May release, all Mac Excel 5.0 product will include software which optimizes the product for the PowerMac. In the interim, a "PowerGuarantee" will allow purchasers of Mac Excel sold after March 1 to upgrade to the PowerMac version for free.
- Mac Excel 4.0 currently dominates the Macintosh spreadsheet category with a 90% market share.
- French, German, Swedish and Italian Win Excel 5.0 were all released within 30-days of the English version.
- Since 1991, two million users have switched from Lotus 1-2-3 to Microsoft Excel.
- Microsoft Win Excel 5.0 has received top honors in every comparative review and awards category in which it has competed. In February 1994, Excel 5.0 surpassed its competitors by substantial margins in InfoWorld's comparative spreadsheet review.
- Other awards for Win Excel 5.0 include: Software Digest, Rating Report on Spreadsheets; BYTE Magazines, Award of Excellence; Windows Sources, Experts' Pick; CRN, Vision Award for Spreadsheets; PC World, Best Buy, Windows Spreadsheets; Windows Magazine, Recommended Product; SPA, Best Business Application, Numeric or Data.

Competition

- In January 1994, Borland announced that its \$49.95 retail prices promotion for Quattro Pro was extended until May 15.
- In February 1994, Lotus shipped 1-2-3 Release 4 for Windows - Multimedia Edition. This product combines 1-2-3 Release 4 for Windows with 28 animated learning and educational movies. It also includes proofreading technologies and the ability to develop customized help sessions.
- Lotus announced a permanent price cut for Improv to \$129 and is positioning it as a supplement to 1-2-3. This is seen as a response to the success of Excel 5.0's pivot tables.

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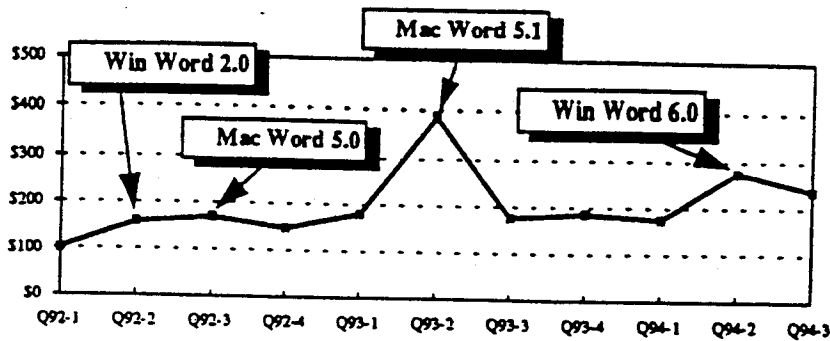
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WORD

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- The Word business unit has developed a Novell/WordPerfect response strategy which includes a \$99 competitive upgrade promotion that runs from April 1 through August 31. The broad marketing theme is "There's never been a better time to switch from WordPerfect to Word". Incremental marketing funds of \$3 million have been allocated to execute the plan.
- The Word marketing team completed a time saving research study in which over 100 word processing users were asked to perform a variety of tasks with the new Microsoft Word 6.0. The preliminary results showed that users of WordPerfect for DOS, WordPerfect for Windows, and Microsoft Word 2.0 were able to perform tasks more quickly and with better results using Win Word 6.0. The findings will be the foundation for a spring/summer promotion highlighting how Win Word 6.0 helps users save time.
- Microsoft issued a press release stating that Win Word 6.0 sold nearly two million copies since it began shipping in November 1993. The release also noted that Word 6.0 for Windows is sold every four seconds and that more than ten million people worldwide use MS Win Word, the most popular word processor for Windows in the world.
- The latest RTM estimate for Mac Word 6.0 is July 1994; an NT (Intel) version is also scheduled to ship one month after Daytona.
- In March, Word 6.0a was released in German, French, French Canadian, Finnish, Hungarian, Spanish and Danish.

Competition

- Lotus claimed that Ami Pro doubled its installed base by selling 1.3 million units including stand-alone and Lotus SmartSuite sales. Ami Pro is now available for OS/2, and a UNIX version is expected to ship in April 1994.
- WordPerfect 6.0 for Windows won PC/Computing's 1993 MVP award for word processing.
- WordPerfect 6.0 for the Macintosh will be the first PowerMac optimized word processor.
- In January 1994, WordPerfect announced it will not release any major new versions of its DOS word processing program. In March 1994, WordPerfect announced WordPerfect 5.1+ for DOS. This upgrade from WordPerfect 5.1 for DOS is targeted for users on lower end machines who want new functionality but do not have the required hardware to support the latest versions of other word processors. WordPerfect also announced that they would discontinue their lifetime 800 product support.

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SYSTEMS

SYSTEMS

Summary (In millions)

Q94-3

	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
MS-DOS	\$148.5	120 %	\$7.8	168 %	\$137.2	942 %	\$3.5	3 %
Windows	186.4	163	14.6	158	41.6	107	130.1	198
Advanced Systems	47.8	60	8.8	93	41.8	84	(2.8)	(14)
Hardware	53.3	121	28.2	110	8.1	73	16.9	238
Other Systems	9.0	NM	0.4	35	8.9	120	(0.3)	NM
	<u>\$444.9</u>	<u>124</u>	<u>\$59.9</u>	<u>119</u>	<u>\$237.5</u>	<u>195</u>	<u>\$147.5</u>	<u>79</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
MS-DOS	33 %	34 %	5 %	4 %	92 %	12 %	2 %	84 %
Windows	42	32	8	8	22	34	70	58
Advanced Systems	11	22	19	12	87	62	(6)	26
Hardware	12	12	53	59	15	25	32	16
Other Systems	2	(1)	5	(40)	99	(252)	(4)	392
	<u>100 %</u>	<u>100 %</u>	<u>13</u>	<u>14</u>	<u>53</u>	<u>34</u>	<u>33</u>	<u>52</u>

FYTD94

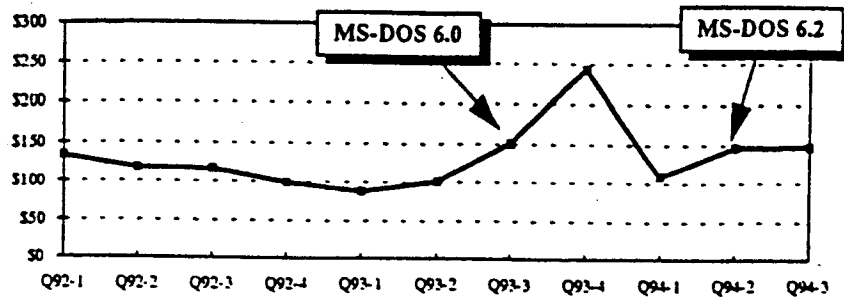
	Net Revenue		Cost of Revenue		Controllable Expense		Responsibility Margin	
	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan	Actual	% of Plan
MS-DOS	\$404.4	109 %	\$24.8	172 %	\$174.9	381 %	\$204.6	66 %
Windows	478.1	146	39.9	135	106.0	91	332.2	184
Advanced Systems	142.0	61	26.3	92	120.5	79	(4.7)	(9)
Hardware	157.1	112	91.4	120	26.1	74	39.6	138
Other Systems	74.2	1,850	1.3	39	21.7	99	51.2	NM
	<u>\$1,255.9</u>	<u>117</u>	<u>\$183.8</u>	<u>121</u>	<u>\$449.2</u>	<u>121</u>	<u>\$622.9</u>	<u>113</u>

	Net Revenue Mix		Cost of Rev % Net Revenue		Contr Exp % Net Revenue		Resp Mgn % Net Revenue	
	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan
MS-DOS	32 %	35 %	6 %	4 %	43 %	12 %	51 %	84 %
Windows	38	30	8	9	22	36	69	55
Advanced Systems	11	22	19	12	85	65	(3)	22
Hardware	13	13	58	54	17	25	25	20
Other Systems	6	0	2	84	29	546	69	(530)
	<u>100 %</u>	<u>100 %</u>	<u>15</u>	<u>14</u>	<u>36</u>	<u>35</u>	<u>50</u>	<u>51</u>

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MS-DOS

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- On February 23, a Los Angeles District Court jury found MS had infringed on two Stac Electronics data-compression patents with MS-DOS's DoubleSpace compression utility. The jury also found Stac guilty of violating a MS-DOS trade secret associated with pre-load features in the company's Stacker software. Stac was awarded \$120 million in damages; MS was ordered to remove DoubleSpace from MS-DOS and was awarded \$14 million in damages. MS-DOS 6.2 inventory already in the channel was unaffected; MS ceased shipping additional 6.2 upgrades. MS will appeal the District Court decision.
- MS-DOS 6.21 was released to PC manufacturers in early March while the retail upgrades released to manufacturing on April 6. The latest release offers users the same functionality as MS-DOS 6.2 except for the DoubleSpace disk-compression utility. Purchasers of the MS-DOS 6.21 upgrade will receive a coupon for the updated disk compression software planned for release in June. MS-DOS 6.21 upgrades are being offered at an SRP of \$77.95.
- Based on internal Microsoft OEM estimates, MS-DOS is expected to ship on 67% of Intel processors in FY94, up from about 58% in FY93.

Competition

- IBM PC-DOS 6.3 is scheduled to release this quarter. The new release will offer enhancements to the RAMBoost memory-management utility and the AntiVirus utility. SuperStor/DS, AddStor's real-time compression product to which IBM now owns rights, will also be packaged into PC-DOS 6.3. Additionally, IBM has also signed a license agreement with Stac Electronics to distribute Stacker disk compression software with its PC DOS and OS/2-based personal computers. The Stac agreement raises questions as to whether SuperStor/DS may also violate Stac's compression patent.
- Novell DOS 7.0, formerly referred to as DR-DOS, was announced in April 1993 and finally reached the market in late January. Novell DOS's new features include pre-emptive multitasking capabilities for multiple DOS applications, disk compression based upon Stac Electronics' Stacker software and integrated peer-to-peer networking allowing users to manage network connections and administrators to control and gather networked workstation information. Also packaged with Novell DOS 7.0 was the Universal NetWare Client which provides integration with Personal NetWare, and NetWare 3.x and 4.0. Compatibility problems have been identified with Novell DOS 7.0: Windows for Workgroups will not run with Novell DOS 7.0. Novell DOS 7.0 is now available at a \$99 SRP. Current DR-DOS customers can take advantage of a 90-day promotional upgrade price of \$39.95.

SYSTEMS

MS-DOS Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$148.5	\$123.6	\$24.9	\$404.4	\$371.9	\$32.5
Cost of revenue	7.8	4.6	(3.2)	24.8	14.4	(10.4)
Gross profit	140.7	118.9	21.7	379.6	357.5	22.1
People expense	0.9	0.9	(0.0)	3.0	2.8	(0.2)
Facilities expense	0.2	0.2	0.0	0.4	0.6	0.2
Marketing expense	2.6	2.4	(0.2)	8.2	7.5	(0.7)
Product dev (ext)	0.1	0.4	0.3	2.5	3.3	0.8
PSS	4.5	2.3	(2.2)	11.2	7.3	(3.9)
Other expenses	125.5	4.1	(121.3)	139.3	12.0	(127.3)
Net shared resources	3.4	4.2	0.8	10.3	12.4	2.0
Controllable expenses	137.2	14.6	(122.6)	174.9	45.9	(129.0)
Responsibility margin	\$3.5	\$104.4	(\$100.9)	\$204.6	\$311.6	(\$106.9)
Excluding Stac:						
Responsibility margin	\$123.5	\$104.4	\$19.1	\$324.6	\$311.6	\$13.1
Resp mgn % Net rev	83.2 %	84.5 %	(1.3) %	80.3 %	83.8 %	(3.5) %
% Net revenue						
Cost of revenue	5.3 %	3.8 %	(1.5) %	6.1 %	3.9 %	(2.3) %
Responsibility margin	2.4 %	84.5 %	(82.1) %	50.6 %	83.8 %	(33.2) %
Controllable Expense Mix						
All product development	7.1 %	10.4 %		10.7 %	14.7 %	
Marketing	15.0	16.3		15.0	16.4	
PSS	26.4	15.9		20.4	16.0	
Other expenses	51.5	57.4		53.8	53.0	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

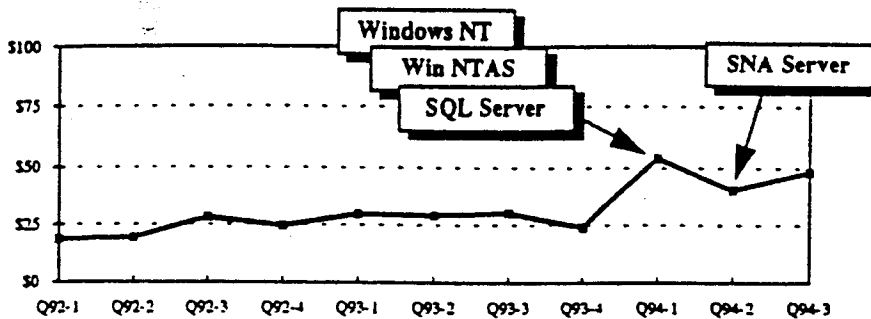
*All product development includes people, facilities, and external product development expenses.
Controllable expenses mix excludes the \$120 million Stac settlement.*

Cost Driver Analysis

- A \$3 million accrual was booked in Q94-3 to cover excess MS-DOS inventory resulting from the Stac verdict. An additional \$1 million in MS-DOS 6.0 upgrade return write-offs were posted in Q94-3, raising the FYTD94 returns write-offs to \$3 million. The remaining cost of revenue variance was the result of unplanned Q94-2 shipments of MS-DOS 6.2 and Step-Up upgrades.
- The PSS variance was the result of a change in the International PSS allocation methodology. The prior allocation rules were based on percent of revenue while the new percentages are driven by call volumes at the German PSS operation and increased staffing in international locations.
- The Stac Electronics damage award of \$120 million was reserved for in March and recorded to other expenses.

ADVANCED SYSTEMS

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Japanese language versions of Windows NT, Windows NTAS, SNA Server for Windows NT, and SQL Server for Windows NT shipped on January 28. The products are currently shipping for the DOS/V (IBM PC-AT compatible) and NEC platforms. More than 100 companies are developing applications for the Japanese version of Windows NT and 31 major systems integrators have been signed on as Solution Providers in Japan.
- Daytona, or Windows NT 3.5, is planning a July RTM. Daytona will reduce memory requirements by about 4MB while significantly improving performance. The current Daytona beta release runs faster within 16MB of memory than Windows NT 3.1 within 32MB of memory. Daytona betas will be delivered in April to over 10,000 developers and corporate accounts. Additionally, Windows NTAS will be better differentiated from Windows NT Workstation by offering better networking features. Daytona also includes support for OLE 2.0 and the PCI bus.
- Systems Management Server (SMS), formerly referred to as Hermes, is a Windows NT server-based suite of tools which makes managing networked PCs and servers easier by offering inventory management, software distribution, network diagnostics, and remote help desk. SMS has received industry support from more than 20 vendors who have pledged to develop or modify existing products to interoperate with SMS. SMS is currently in beta and is scheduled to RTM in Q95-1.
- Microsoft licensed the Windows Libraries for Unix to three partners, creating a good cross-platform strategy for customers needing to run or develop Windows-based applications using Windows APIs on non-Windows systems.

Competition

- Sun Microsystems purchased a fully-paid license for Unix through R4.0 from Novell. They also gained rights to sublicense and distribute their derived code as they desire. Sun additionally signed an agreement with Novell for its NetWare Unix Client technology which will allow Sun Solaris users to be clients to NetWare servers. Many industry analysts believe the Unix license agreement will further thwart efforts to unify Unix across the industry due to fragmentation.
- Sun purchased rights to NextStep, renaming it OpenStep, and are offering it to X/Open. Combined with other components, and a deal with Iona, Sun intends to offer an object environment competitive with Windows/OLE.

SYSTEMS

- Novell announced a further slip in NetWare 4.1 availability to the last quarter of CY94; beta tests are scheduled to start in a few months. To appease current NetWare 4.0 customers, Novell is planning a 4.01 refresh release to fix some NetWare 4.0 bugs. Many Novell customers remain on NetWare 3.1 due to the major upheaval associated with moving to NetWare 4.0, the lack of tools needed to manage a 4.0 environment, overall product quality and cost.
- Hewlett-Packard (HP) has made a 15% partnership investment in Taligent. The companies have agreed to cross-license technology and H-P has committed to integrate Taligent's application and development frameworks into HP-UX, its Unix product offering. In a separate agreement, HP announced it has licensed Apple's Macintosh Applications Environment (MAE) and will offer it on its HP 9000 Series 700 workstations beginning in April. MAE will allow users to execute applications designed for the Macintosh in an X-Window on their workstation and initiate Unix commands using the Mac interface.

Advanced Systems Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$47.8	\$79.7	(\$31.9)	\$142.0	\$232.1	(\$90.1)
Cost of revenue	8.8	9.5	0.6	26.3	28.5	2.2
Gross profit	39.0	70.2	(31.2)	115.7	203.6	(87.9)
People expense	13.0	15.3	2.3	43.0	47.4	4.4
Facilities expense	3.9	4.2	0.3	9.9	12.6	2.6
Marketing expense	5.7	8.5	2.8	18.0	27.0	9.0
Product dev (ext)	4.7	6.8	2.1	11.7	19.6	8.0
PSS	8.2	6.9	(1.3)	19.0	21.7	2.7
Other expenses	1.4	1.3	(0.1)	3.3	3.6	0.3
Net shared resources	4.9	6.8	1.9	15.5	19.6	4.0
Controllable expenses	41.8	49.8	8.0	120.5	151.5	31.1
Responsibility margin	(\$2.8)	\$20.4	(\$23.2)	(\$4.7)	\$52.1	(\$56.8)
% Net revenue						
Cost of revenue	18.5 %	11.9 %	(6.6) %	18.5 %	12.3 %	(6.2) %
Responsibility margin	(5.8) %	25.6 %	(31.5) %	(3.3) %	22.4 %	(25.8) %
Controllable Expense Mix						
All product development	51.6 %	52.7 %		53.6 %	52.6 %	
Marketing	13.7	17.1		14.9	17.8	
PSS	19.7	13.9		15.8	14.3	
Other expenses	15.0	16.3		15.6	15.3	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

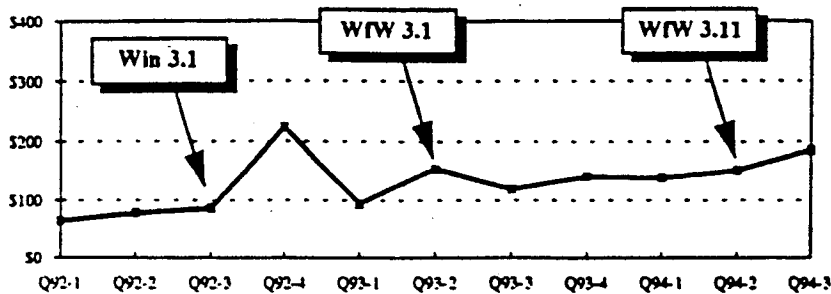
All product development includes people, facilities, and external product development expenses.

Cost Driver Analysis

- While product cost of revenue was below plan year to date, unbudgeted SQL Server and Xenix royalties caused a \$6 million unfavorable variance FYDT94 in other cost of revenue.
- FYDT94 marketing expense was \$9 million behind plan due to below plan channel spending.
- The FYDT94 product development variance was driven by a \$2 million favorable localization variance, code purchase delays and actual code acquisition occurring as license agreements rather than as purchases.
- The Q94-3 PSS variance was the result of a change in the International PSS allocation methodology and increased staffing in international locations.

WINDOWS

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Chicago momentum continues to build as the product moves closer to its RTM in the first half of FY95. Limited beta units were released at the end of March to key developers. A larger beta, which will be distributed to more than 15,000 customers, is expected over the next couple months. Chicago is a 32-bit operating system with integrated networking which will run in 4MB of memory and support existing MS-DOS and Windows 3.1 applications. Chicago will update the Windows user interface, increase support for mobile users and implement Plug and Play functionality, a new standard for auto-configuration of hardware adapters and other peripherals.
- Windows 3.11, a refresh release of Windows 3.1, shipped in mid-February. The latest release implements packaging changes designed to reduce counterfeiting and delivers updated device drivers. The new packaging includes a hologram which makes duplication difficult and expensive.
- WfW 3.11 Point-to-Point Server availability was announced in February. The Point-to-Point Server functionality enables a WfW 3.11-based system to accept incoming calls from Microsoft Remote Access clients and allow access to files and printers shared on the local machine. The Point-to-Point Server can be downloaded at no charge from the Microsoft Download Service or the Internet.
- The number of life-to-date Windows 3.1 licensed users was estimated at more than 50 million in March 1994.
- Windows 3.1 and WfW 3.11 reports through the OEM channel are running at about 75% of MS-DOS reports FYTD94, up from 65% in FY93. Penetration continues to increase as OEMs ship Windows 3.1 and Windows for Workgroups pre-installed on their hardware. More than 5.6 million Windows OEM units were reported in Q94-3 compared to 4.0 million units in Q93-3, a 41% increase.

Competition

- IBM is planning to expand its current OS/2 product line later this year with a 4MB version, a symmetric-multiprocessing (SMP) version, and a peer-services add-on package to its OS/2 client software. These products complement IBM's OS/2 for Windows and Pen for OS/2 offerings. BIS Strategic Decisions estimates the OS/2 installed base grew to 1.9 million at the end of 1993, up from 1.1 million the prior year.
- Apple announced a DOS/Windows-compatible Macintosh Quadra in February. The personal computer includes both a Motorola and an Intel processor, allowing users to work in both the Macintosh and DOS environments at the same time. Quadra users have the ability to toggle and cut and paste between the environments, although two monitors are required for simultaneous viewing.

SYSTEMS

- Apple has announced it is talking to a number of companies about licensing its Mac operating system. Apple hopes the licensing deal will expand its current worldwide market share of 11% and increase the number of software developers writing applications for the Mac operating system.
- Apple announced an agreement with Insignia Solutions to distribute Insignia's SoftWindows (which contains Windows code licensed from MS) product on certain configurations of its new PowerPC-based computers. SoftWindows will allow Macintosh operating system users to run MS-DOS and Windows applications with performance in the range of today's 386- and 486-based systems. Dataquest estimates Apple will ship 700,000 PowerPC-based by the end of 1994.

Windows Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$186.4	\$114.0	\$72.3	\$478.1	\$327.2	\$150.9
Cost of revenue	14.6	9.2	(5.3)	39.9	29.6	(10.3)
Gross profit	171.8	104.8	67.0	438.1	297.5	140.6
People expense	7.4	8.4	1.1	22.3	25.7	3.4
Facilities expense	1.5	1.8	0.2	3.4	5.4	2.0
Marketing expense	7.0	10.6	3.6	17.5	30.8	13.3
Product dev (ext)	2.2	2.8	0.6	4.8	9.0	4.2
PSS	16.3	9.0	(7.3)	34.5	27.9	(6.7)
Other expenses	4.8	3.2	(1.5)	15.8	9.0	(6.8)
Net shared resources	2.5	3.1	0.6	7.6	8.9	1.3
Controllable expenses	41.6	38.9	(2.7)	106.0	116.6	10.6
Responsibility margin	\$130.1	\$65.9	\$64.3	\$332.2	\$180.9	\$151.3
% Net revenue						
Cost of revenue	7.8 %	8.1 %	0.3 %	8.4 %	9.1 %	0.7 %
Responsibility margin	69.8 %	57.8 %	12.1 %	69.5 %	55.3 %	14.2 %
Controllable Expense Mix						
All product development	26.5 %	33.2 %		28.8 %	34.3 %	
Marketing	16.8	27.2		16.5	26.4	
PSS	39.1	23.2		32.6	23.9	
Other expenses	17.6	16.4		22.1	15.4	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

All product development includes people, facilities, and external product development expenses.

Cost Driver Analysis

- The cost of revenue variance was driven by strong Europe and North America FG sales of Windows 3.1 and Windows 3.11. Product cost of revenues as a percent of net revenues FYTD94 was ahead of plan.
- The FYTD94 product development variance was the result of \$1 million favorable variances in contractors, Redmond localization expense and betas.
- FYTD94 marketing spending was \$13 million below plan due to below-plan channel spending.
- The PSS variance was the result of a change in the International PSS allocation methodology.
- The FYTD94 variance in other expenses was due to a \$5 million variance in bad debt expense reserves booked to account for high-risk OEM manufacturers.

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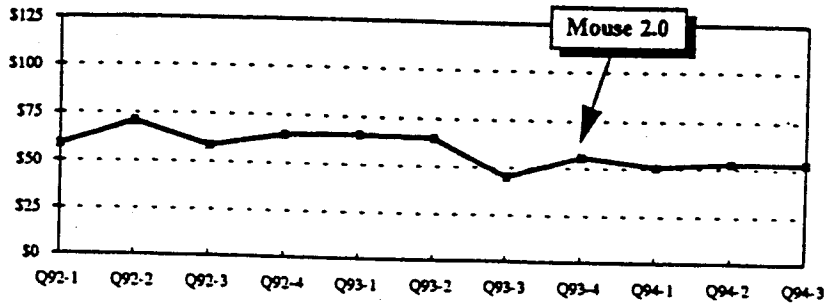
Product Division Update

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HARDWARE

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Microsoft's new ergonomically shaped, low-cost OEM mouse, codenamed Defender was shipped in Q94-3. The Defender cost of revenue averages under \$5.00 versus an average FYTD94 cost of ~\$9.00 for the currently shipping OEM Mouse. Mice are being manufactured at a rate of 180,000 per month, ramping to 200,000 per month, at Sysgration out of Taiwan. However, we will still require increased capacity at our current vendors and the addition of a new vendor in order to eliminate the current backlog of 100,000 Defender Serial mouse units.
- Last fall, there was a pricing promotion to offer the Pro Mouse at a \$59 street price that was continued into this quarter. As a result, unit sales increased 57% FYTD94 over FYTD93. Due to this success, MS has officially lowered the SRP to hit a \$59 street price.

SYSTEMS

Hardware Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$53.3	\$44.0	\$9.3	\$157.1	\$140.3	\$16.9
Cost of revenue	28.2	25.8	(2.5)	91.4	76.3	(15.1)
Gross profit	25.0	18.2	6.8	65.7	64.0	1.8
People expense	2.2	2.5	0.3	7.1	7.5	0.4
Facilities expense	0.7	0.6	(0.1)	1.3	1.8	0.5
Marketing expense	3.2	2.7	(0.6)	9.5	9.9	0.4
Product dev (ext)	1.6	3.1	1.5	4.2	9.2	5.1
PSS	(0.4)	0.8	1.3	1.4	2.7	1.3
Other expenses	0.6	0.7	0.1	1.8	2.3	0.4
Net shared resources	0.2	0.6	0.4	0.8	1.9	1.1
Controllable expenses	8.1	11.1	3.0	26.1	35.2	9.2
Responsibility margin	\$16.9	\$7.1	\$9.8	\$39.6	\$28.7	\$10.9
% Net revenue						
Cost of revenue	53.0 %	58.6 %	5.6 %	58.2 %	54.4 %	(3.8) %
Responsibility margin	31.8 %	16.2 %	15.6 %	25.2 %	20.5 %	4.8 %
Controllable Expense Mix						
All product development	55.1 %	55.9 %		48.2 %	52.7 %	
Marketing	39.8	24.1		36.5	28.1	
PSS	(5.5)	7.6		5.3	7.5	
Other expenses	10.6	12.4		10.1	11.7	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

All product development includes people, facilities, and external product development expenses.

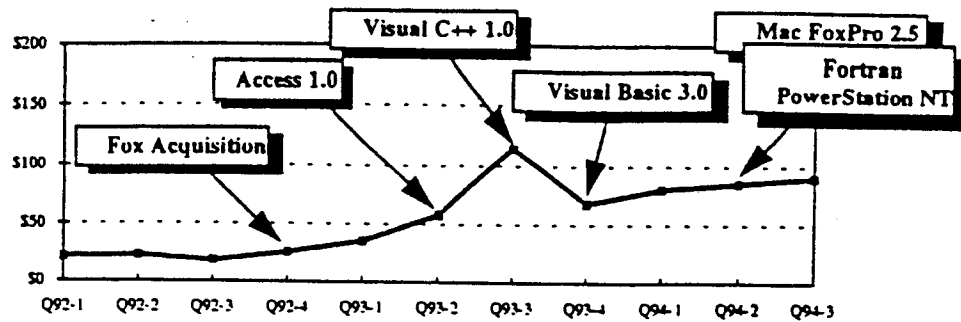
Cost Driver Analysis

- FYTD94 adjustments to International PSS expenditures resulted in a Q94-3 credit.
- Shipments through the lower-priced OEM channel accounted for a larger than budgeted percentage of total mouse units sold, which in turn resulted in cost of revenue as a percentage of net revenue being higher than planned.
- An \$8.5 million FYTD94 charge, taken to reduce obsolete inventory, was the primary reason that cost of revenue was higher than budget. Hardware is trying to sell out Mouse 1.0 inventory (\$2.5 million adjustment) and Windows Sound System sound board inventory (\$6 million adjustment) at severely reduced prices (in some cases, lower than cost).

DATABASE & DEVELOPMENT TOOLS

DATABASE & DEVELOPMENT TOOLS

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Access 2.0, originally scheduled for release to manufacturing on October 6, 1993, was released to manufacturing on April 7, 1994. Sales of Access in Far East FG continued to be strong following the release of the Japanese version in December 1993.
- Visual C++ 1.0J continues to be exceptionally strong in Far East FG, at \$8.0 million for Q94-3 versus a plan of \$4.8 million.
- FoxPro 2.6 (DOS and Win) was released to manufacturing March 2, 1994. In conjunction with the Harvest II campaign aimed at converting existing dBase users over to FoxPro. The product primarily adds features which make it easier for dBase users to convert their files and applications. Only two skus are being offered: a \$99 standard edition and a \$695 professional edition which includes the Library, Construction and Connectivity Kits that were previously sold separately.
- Mac FoxPro 2.5 was released in December 1993. Since then it has received very positive feedback from customers.
- The SET product unit completed an arrangement with Visual Numerics to sell the IMSL Math and Statistical Libraries. IMSL Math and Stat Libraries for Fortran 5.2 released to manufacturing on April 12, 1994.

Competition

- A renegotiation of the agreement between Sybase Inc. and Microsoft was completed and announced on April 12, 1994. It redefines how the companies will work together to deliver complete, compatible solutions across the enterprise, based on Sybase's SQL Server relational database and Windows NTAS. The agreement gives MS the right to develop and market new versions of the currently available Microsoft SQL Server products and related tools while Sybase will develop and market the Sybase System 10 family of products.
- In March, Novell and WordPerfect agreed to merge. Borland also agreed to sell its Quattro Pro spreadsheet business to Novell for \$145 million and licensed Novell to sell up to 1 million copies of Paradox for Windows.

DATABASE & DEVELOPMENT TOOLS

Database & Development Tools Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$89.8	\$114.3	(\$24.5)	\$254.2	\$290.8	(\$36.6)
Cost of revenue	20.2	21.5	1.2	57.6	55.6	(2.0)
Gross profit	69.5	92.8	(23.3)	196.6	235.2	(38.6)
People expense	15.3	15.8	0.6	46.6	47.9	1.3
Facilities expense	3.1	3.2	0.1	7.9	9.6	1.7
Marketing expense	11.1	12.6	1.5	29.9	35.5	5.6
Product dev (ext)	3.1	5.3	2.2	8.9	16.6	7.7
PSS	15.1	10.0	(5.2)	34.1	30.0	(4.1)
Other expenses	0.9	1.2	0.3	2.3	3.1	0.7
Net shared resources	(1.1)	(0.1)	1.0	(3.0)	(1.0)	2.1
Controllable expenses	47.4	47.9	0.5	126.7	141.7	14.9
Responsibility margin	\$22.1	\$44.9	(\$22.7)	\$69.8	\$93.5	(\$23.7)
% Net revenue						
Cost of revenue	22.6 %	18.8 %	(3.8) %	22.7 %	19.1 %	(3.5) %
Responsibility margin	24.7 %	39.3 %	(14.6) %	27.5 %	32.2 %	(4.7) %
Controllable Expense Mix						
All product development	45.3 %	50.8 %		50.0 %	52.3 %	
Marketing	23.4	26.2		23.6	25.1	
PSS	31.9	20.8		26.9	21.2	
Other expenses	(0.6)	2.2		(0.6)	1.5	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

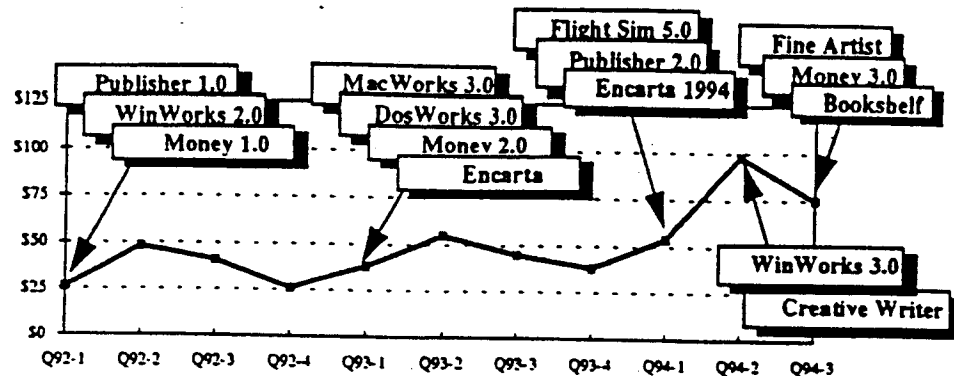
All product development includes people, facilities, and external product development expenses.

Cost Driver Analysis

- Controllable expenses for Q94-3 approximated plan with the exception of product support services. During Q94-3, an adjustment was made to reflect a revision in International PSS allocations resulting in a negative variance.
- Product cost of revenue was 15.7% of net revenue for Q94-3 versus a plan of 14.3%. The variance was due to higher FG costs for Visual C++ in the Far East and higher costs for FoxPro in North America.
- Product development costs continued to be less than planned in Q94-3 due to delaying localization on FoxPro 3.0 (now scheduled for mid-FY95) and less than plan contractor expenses.

CONSUMER

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- Strong Q94-3 multimedia sales, particularly the success of Encarta '94 and the new release of Bookshelf '94, led the Consumer division to 147% revenue growth over Q93-3. Although revenue was lower than Q94-2 due to seasonality, the decrease was in line with post-holiday expectations.
- Encarta '94 and Publisher 2.0 were both winners of a 1994 WIN 100 award from Windows Magazine.
- MS completed an agreement to transfer marketing and development responsibility for Profit, a jointly developed small business accounting package, to Great Plains. MS will receive a 6% royalty on each unit.
- At Intermedia, DK announced that they will launch six multimedia titles beginning this fall. MS and DK are attempting to develop a U.S. distribution agreement for DK's multimedia titles.

Competition

- Q94-3 saw major changes in the competitive environment for consumer software products. This was evidenced by:
 new competitors such as WordPerfect's announcement of their MainStreet line; strategic relationships such as Paramount Publishing and Davidson's relationship to develop, publish and distribute multimedia titles for consumers; mergers such as the Electronic Arts and Broderbund aimed at expanding into new markets; and licensing deals such as Davidson using the Fisher-Price logo, and ESPN and Prodigy announcing an online service.
- Music Pen, producers of our Magic School Bus title, received a minority investment from Paramount.
- In response to the rising competitive threats, the Personal Finance group is pursuing partnerships with Mastercard (online banking), Fidelity (online financial services) and Smart Money Magazine (content) and is also considering an investment proposal to enter the personal tax preparation/planning markets. The Games group recently signed a licensing deal with Storm Front Studios for a baseball simulation game.
- The Consumer division is currently evaluating more than 30 different content licensing proposals.
- The U.S. Patent and Trademark Office repudiated the 41 claims on which the Compton's NewMedia patent was based. If Compton's patent had been upheld, MS might have had to pay a royalty on every multimedia title shipped.

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CONSUMER

Consumer Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$74.8	\$59.2	\$15.5	\$226.9	\$170.4	\$56.5
Cost of revenue	15.3	11.8	(3.5)	48.2	34.5	(13.7)
Gross profit	59.5	47.5	12.0	178.7	135.9	42.8
People expense	10.3	10.2	(0.1)	30.3	30.6	0.3
Facilities expense	2.0	2.1	0.2	5.2	6.2	1.1
Marketing expense	7.1	6.1	(1.0)	18.4	23.5	5.2
Product dev (ext)	5.0	7.6	2.6	15.2	22.8	7.7
PSS	3.0	2.8	(0.1)	8.3	8.4	0.1
Other expenses	1.3	0.8	(0.5)	5.1	2.2	(2.9)
Net shared resources	1.0	1.4	0.4	2.9	3.9	1.0
Controllable expenses	29.5	31.0	1.5	85.2	97.6	12.4
Responsibility margin	\$30.0	\$16.5	\$13.5	\$93.5	\$38.3	\$55.2
% Net revenue						
Cost of revenue	20.4 %	19.8 %	(0.6) %	21.2 %	20.2 %	(1.0) %
Responsibility margin	40.1 %	27.8 %	12.2 %	41.2 %	22.5 %	18.7 %
Controllable Expense Mix						
All product development	58.2 %	64.3 %		59.4 %	61.1 %	
Marketing	24.1	19.6		21.5	24.1	
PSS	10.1	9.2		9.7	8.6	
Other expenses	7.6	6.9		9.3	6.2	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

All product development includes people, facilities, and external product development expenses.

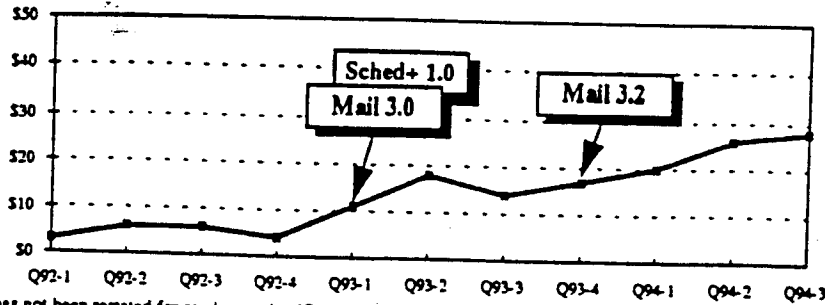
Cost Driver Analysis

- Product development spending remains below plan both for Q94-3 and FYTD94, primarily due to less than plan expenditures on outside contractors. Consumer is preparing to ship several products in Q94-4 and is utilizing contractors to meet ship dates, but product development expense will most likely be under plan for FY94.
- Marketing expense was slightly above plan for Q94-3 due to timing of invoices. Marketing expense was slightly below plan primarily due to favorable variances in international marketing.
- Other expenses were unfavorable to plan for Q94-3 partly due to the transfer to GPS of all remaining Profit units in MS's warehouse. FYTD94, the unfavorable variance reflects the write down of the \$1.7 million advance royalty to GPS. In Q94-4, MS will make a final payment to GPS of \$500,000 to complete the contract terms (also see Other Assets).

WORKGROUP

WORKGROUP

Net Revenue Stream & Key Product Releases (in millions)



FY92 has not been restated for product reclassifications which have been deemed immaterial for the purposes of this graph.

Highlights

- In order to take advantage of increased product interrelation between Workgroup products, the Vancouver-based Connectivity Development group will be consolidated into the Redmond Campus during Q94-4. This group developed MS's first PC Mail product.
- John Hancock announced that their standards committee voted on January 21 to replace cc:Mail with Microsoft Mail as their standard LAN-based email system.
- On February 17, Microsoft announced that Microsoft Mail, Mail Remote and Schedule+ are now the fastest-selling products in their categories. Microsoft Mail gained nearly 2 million users in 1993 and now has a total installed base of more than 4 million users worldwide. Mail Remote is also the market share leader in its segment, and Schedule+ became the best-selling workgroup application in the market (excluding LAN-based email) when it surpassed the 1 million licenses sold mark in December 1993.
- On February 16, Microsoft received the Messaging Company of the Year Award from the Electronic Mail and Micro Systems Publication, based on its annual readership survey. Microsoft Mail also won the Computer Reseller News' Vision Award for Best Email Product for 1993, and received a "recommended buy" designation in competitive email testing by the National Software Testing Laboratories and the Buyers Assurance seal from InfoWorld magazine.

Competition

- On January 31, Lotus announced cc:Mail Mobile for Windows 2.0, an updated mobile version of their LAN-based email system, which gives remote users the ability to send and receive messages over a WAN using a modem, network protocols or wireless connection.
- On February 8, Lotus and SkyTel announced the availability of the Lotus Notes Pager Gateway for The SkyTel System, a wireless messaging solution for Lotus Notes, which enables users to filter and forward mission-critical messages to mobile users carrying SkyWord alphanumeric wireless messaging units and hand-held or laptop computers. Users of cc:Mail with access to Lotus Notes can also take advantage of this pager gateway. The Gateway has an SRP of \$995.
- On March 18, Lotus and AT&T announced a joint venture to bring online services, such as electronic newsletter publishing or real-estate listings, to the mass market. The service, to be called AT&T Network Notes, will be run by AT&T and built around Lotus Notes software. Most analysts believe the financial implications of this venture to Lotus could be substantial, given that Lotus gets a per-transaction or traffic-based royalty.
- Banyan announced that it had agreed to pay \$17.5 million for Beyond. Analysts project this coupling is likely to spark a series of acquisitions as small email vendors such as Enable Software, Futurus and Reach Software look for partnerships to help them compete in a market where their combined products constitute less than 1 million of the current 11 million US email seats.

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WORKGROUP

Workgroup's Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$27.8	\$21.0	\$6.8	\$73.9	\$61.0	\$13.0
Cost of revenue	3.4	3.3	(0.1)	8.7	9.7	1.0
Gross profit	24.4	17.7	6.7	65.2	51.2	14.0
People expense	7.8	7.5	(0.3)	21.9	23.4	1.5
Facilities expense	1.9	1.6	(0.3)	4.9	4.6	(0.3)
Marketing expense	2.7	2.7	(0.1)	7.3	9.1	1.8
Product dev (ext)	2.1	2.3	0.2	5.6	6.6	1.0
PSS	3.5	2.0	(1.5)	7.2	5.9	(1.3)
Other expenses	0.3	0.3	0.1	0.9	1.0	0.1
Net shared resources	(0.3)	(0.1)	0.2	(0.8)	(0.7)	0.1
Controllable expenses	18.0	16.2	(1.8)	47.1	49.9	2.9
Responsibility margin	\$6.4	\$1.5	\$4.9	\$18.1	\$1.3	\$16.9
% Net revenue						
Cost of revenue	12.4 %	15.8 %	3.4 %	11.8 %	16.0 %	4.2 %
Responsibility margin	23.0 %	7.1 %	15.9 %	24.5 %	2.1 %	22.4 %
Controllable Expense Mix						
All product development	65.6 %	70.0 %		69.0 %	69.4 %	
Marketing	15.1	16.4		15.5	18.2	
PSS	19.5	12.2		15.3	11.8	
Other expenses	(0.3)	1.5		0.1	0.6	
Total costs	100.0 %	100.0 %		100.0 %	100.0 %	

All product development includes people, facilities, and external product development expenses.

Cost Driver Analysis

- FYTD94 marketing expense was below budget, however, prelaunch promotional expenses for EMS server (ship date in FY95) are likely to offset this positive variance in Q94-4.
- Steady growth of email client and server market share and phenomenal stand-alone Schedule+ and Mail Remote product sales resulted in record results for Q94-3. Revenues were 32% above plan.
- Increased sales resulted in higher than plan PSS expense.

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Product Division Update

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ADVANCED TECHNOLOGY

ADVANCED TECHNOLOGY

Highlights

- On February 14th, MS signed an agreement to acquire SOFTIMAGE, a developer of high-performance 2-D and 3-D computer animation and visualization software for the entertainment industry, for \$130 million.
- MS agreed to invest \$30 million for an 8.5% stake in Nationwide Wireless Network (also see Other Assets).
- MS agreed to purchase 200,000 shares of Metricom common stock for \$6.05 million and a warrant to purchase an additional 75,000 shares (also see Other Assets).
- MS and TCI announced an agreement in principle to test interactive cable television beginning in the fourth quarter of calendar 1994. Beginning in 1995, the test will be expanded to include a marketing test of interactive TV services among TCI residential cable customers located in the Seattle and Denver areas.
- MS and TCI also unveiled plans to develop a cable television channel targeted at the consumer market for personal computer hardware, software and accessories.
- At the beginning of Q94-3, MS, TCI and the Pacific Gas & Electric Co. announced they had signed a memorandum of understanding to test market energy information services in California via cable television.
- Nippon Telegraph & Telephone and MS announced an agreement in principle to develop services that will allow users to access multimedia information on a communications network in Japan.
- In February, MS closed on the purchase of certain technology, research and product development efforts from Continuum Productions Corp. The core business of Continuum is to create a digital archive and media database, including such media types as video footage, photographic images and sound clips. Approximately 33 Continuum staff joined Microsoft on September 1, 1993.

Competition/Industry Highlights

- The Bell Atlantic/TCI merger agreement was terminated.
- Bell Atlantic is building a studio to support its Stargazer Interactive video system. The technical trial of Stargazer uses a technology called Asynchronous Data Subscriber Line to compress video files through phone switches so it can be delivered to subscribers on ordinary copper wires.
- TCI said it will begin testing new interactive pay-per-view services in Illinois in April using the CFT-2900 set-top converter from General Instruments.
- DEC signed an agreement in January to work with USA Video to increase their market share of the video on demand industry. Together, they will support Bell Atlantic's market trial of video dial tone in Virginia.
- IBM was named as one of the companies that will develop set-top devices for Bell Atlantic using PowerPC as the strategic microcontrollers.
- Bell Atlantic picked Oracle's multimedia database software to deliver movies on demand and interactive shopping services over its phone-line network. Oracle was also chosen by British Telecom for a video on demand trial in the London area.
- Time Warner and US West have undertaken a feasibility study with Itochu and Toshiba on establishing a national television network.
- US West also unveiled plans to build new multimedia networks in 20 cities over the next five years, starting with a \$750 million effort in four markets: Denver, Minneapolis-St. Paul, Portland and Omaha. They claim they will get 750,000 homes interactive by the end of 1995 and will add half a million homes annually thereafter.

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- Ameritech chose ADC Telecommunications to supply the video delivery system for its \$4.4 billion project aimed at building interactive networks in 32 communities across a five-state territory in the Midwest.
- StarSight Telecast has developed navigator software for the "era of 500 channels" and has already drawn investments from leading cable operators including Viacom, Tribune Co. and Cox Enterprises. It has agreements with several large TV and VCR makers including Zenith Electronics, Samsung Electronics and Philips Electronics to build the StarSight chip into this year's new models. In addition, they claim that the largest makers of cable converters have agreed to include the StarSight chip in the boxes they sell to cable operators.
- Viacom beat out QVC Network to purchase Paramount for \$9.75 billion in cash and stock. Viacom also plans to acquire Blockbuster Entertainment and create interactive versions of MTV and VH-1.
- Apple and Oracle signed an agreement that will allow Oracle's Media Server product line to work with a set-top unit based on the Apple Macintosh.
- October 5th, 3DO announced it had teamed up with US West for an interactive television trial in Omaha, Nebraska, scheduled to reach 100,000 customers by the end of next year.
- AT&T announced PersonalLink, a new networking service that is portable and will operate in wired or wireless environments. PersonalLink will be Internet capable, email ready and fax compatible when it is launched this summer. The brains of the service, which includes intelligent assistants for customization, is Telescript, a new communications language developed by General Magic. General Magic is owned by AT&T, Apple, Motorola, Sony, Matsushita and Philips Electronics NV.
- The Lotus Notes Pager Gateway for the SkyTel System shipped in February. It is a uni-directional wireless messaging system.
- The Apple Wireless Messaging Service delivered by MobileCom was made available to users of the Newton MessagePad. The monthly service fee for this service is expected to range from approximately \$21.00 for standard local coverage to \$83.95 for standard nationwide coverage. The service is enabled by the Newton Messaging Card which sells for approximately \$229.
- America Online became the first national online service to offer consumers access to Internet content through an easy-to-use GUI. Their email gateway now handles five million messages per month.
- America Online announced that the number of AOL subscribers has nearly tripled over the past year and topped the 700,000 mark. This growth has caused a major capacity problem that was apparently addressed by adding more servers to the system.
- IBM pushed back the announcement of its third-generation online service, code named In Touch, to the second quarter of calendar 1994. In Touch reportedly will make use of intelligent agents, stress intelligent messaging capabilities and coordinate links among private networks, public networks and wireless communications devices.
- The 835,000 member American Federation of Teachers announced that it had entered into partnerships with both Prodigy and American Online. Teachers will be offered special discounts to use and evaluate one or both of the services. At the end of the one-year test period the AFT will probably choose to stay with one of the services.

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ADVANCED TECHNOLOGY

Advanced Technology Performance

Results of Operations (in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
Net revenue	\$1.5	\$3.2	(\$1.7)	\$6.5	\$10.1	(\$3.6)
Cost of revenue	0.5	0.6	0.0	2.2	1.8	(0.3)
Gross profit	0.9	2.6	(1.7)	4.4	8.3	(3.9)
People expense	8.7	11.7	3.0	23.4	34.2	10.8
Facilities expense	1.3	2.0	0.7	3.2	5.4	2.2
Marketing expense	0.4	0.1	(0.2)	1.0	0.4	(0.6)
Product dev (ext)	0.9	4.8	3.8	3.2	13.9	10.8
PSS	(0.0)	0.0	0.0	0.0	0.0	0.0
Other expenses	0.9	0.1	(0.8)	1.0	0.2	(0.7)
Net shared resources	0.6	1.1	0.5	2.4	2.9	0.5
Controllable expenses	12.8	19.8	7.0	34.1	57.1	23.0
Responsibility margin	(\$11.8)	(\$17.2)	\$5.3	(\$29.7)	(\$48.9)	\$19.1

Controllable Expense Mix

All product development	85.7 %	93.5 %	87.3 %	93.9 %
Marketing	2.8	0.7	2.9	0.7
PSS	(0.1)	0.0	0.0	0.0
Other expenses	11.5	5.8	9.8	5.4
Total costs	100.0 %	100.0 %	100.0 %	100.0 %

All product development includes people, facilities, and external product development expenses. Revenue for products budgeted in AT continues to be reported in the AT P&L, however, responsibility for the products has shifted to other product groups.

Cost Driver Analysis

- People expense was under plan for Q94-3 and FYTD94, due to AT being 141 people behind its hiring plan, although part of this variance was due to a midyear reclassification of certain product units without a corresponding change in headcount plan.
- The favorable facilities expense variance was the result of lower than plan headcount and associated development activity, coupled with lower than plan building and grounds distributions.
- The marketing budget requirement for AT was not fully included in the original FY94 marketing plan. Consequently, the marketing spend is above plan.
- Product development was behind plan in AT overall due to initial budgeted expenses not being incurred. The favorable variance FYTD94 was divide as follows: ACT - \$6.8 million, Advanced Product Development - \$2.0 million, Broadband Applications - \$1.1 million and OLS - \$0.8 million.
- The variance in other expenses was caused by the \$0.4 million paid to Continuum to cover operating expenses between signing and closing. The remainder was due to a write-off of the net book value of the intellectual property rights acquired from Hash Enterprises. The code was found to contain copyrighted features and deemed valueless. MS is currently pursuing action against Hash.

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Cost & Metrics



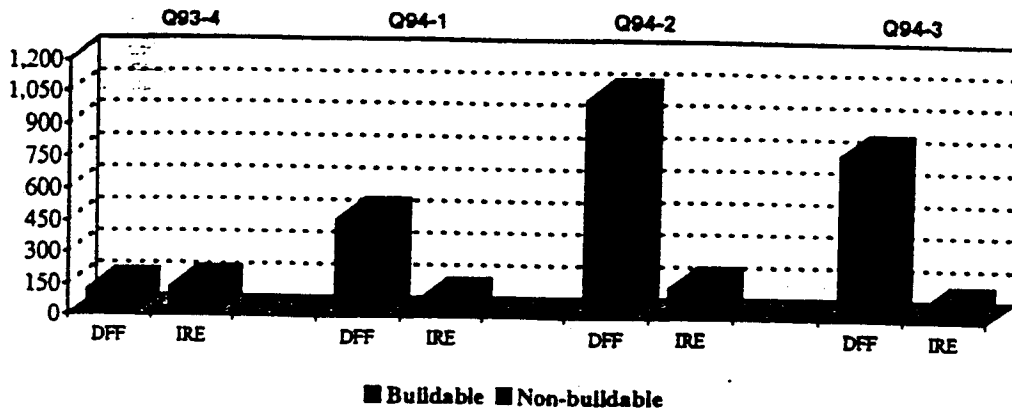
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Worldwide Operations

Backlog Comparison by Plant (units in thousands)



Buildable backlog occurs when customer demand exceeds forecast or when the factory fails to build to forecasted demand. Non-buildable backlog occurs when orders are placed for products that have not been released to manufacturing.

Domestic Focused Factory (DFF)

- Q94-3 domestic backlog of 776,000 units decreased 24% from Q94-2.
- Q94-3 buildable backlog of 71,000 units was primarily Windows 3.11 (17,000) and Office 4.0 (23,000); non-buildable backlog of 705,000 units consisted mainly of MS-DOS 6.21 (373,000), Access 2.0 (101,000), Encarta (33,000), and Space Simulator (41,000). MS-DOS 6.21 and Access 2.0 were released to manufacturing in April 1994.
- Current daily capacity is estimated at 50,000 units.

International Focused Factory (IFF)

- Q94-3 backlog information is not available.
- Current daily capacity is estimated at 20,000 units per day.

MS Ireland (IRE)

- Ireland backlog of 72,000 units decreased by 48%.
- Buildable backlog increased by 29,000 units while non-buildable decreased by 102,000 units.
- Current daily capacity is estimated at 32,000.

WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY METRICS

WORLDWIDE PRODUCT GROUPS & ADVANCED TECHNOLOGY METRICS

(annualized in thousands)

	DAD	DDT	Consumer	Workgroup	Systems	Other	WPG	AT	WPG & AT
Net revenue per employee									
Actual	2,812	483	631	290	1,274	33	1,155	18	1,075
Plan	2,176	541	446	221	888	78	890	28	817
Q94-2	2,312	464	833	269	1,191	91	1,051	39	983
Q94-1	1,814	434	470	236	1,103	525	932	27	870
People expense per employee									
Actual	74	82	87	81	93	64	83	107	84
Plan	70	75	77	78	92	69	79	104	81
Q94-2	78	87	86	75	102	62	86	110	88
Q94-1	81	84	86	81	93	74	85	80	85
Facilities expense per employee									
Actual	20	17	17	20	25	246	44	16	42
Plan	17	15	16	16	22	21	18	18	18
Q94-2	17	13	14	16	19	12	16	13	16
Q94-1	17	14	14	18	18	8	16	12	15
Product development expense per employee									
Actual	19	17	42	22	28	23	25	11	24
Plan	19	25	57	24	39	24	32	42	33
Q94-2	25	18	51	16	26	27	27	21	26
Q94-1	17	13	36	22	21	28	21	8	20
Marketing expense % net revenue									
Actual	8%	12%	10%	10%	4%	287%	8%	25%	8%
Plan	8%	11%	10%	13%	7%	7%	8%	4%	8%
Q94-2	12%	15%	8%	11%	5%	7%	9%	10%	9%
Q94-1	9%	7%	7%	9%	4%	47%	9%	15%	9%

Q94-2 figures have been adjusted from previous report to reflect average quarterly headcounts.

- Total net revenue per employee exceeded plan by 32% due to a quarterly positive Q94-3 revenue variance and business unit headcount remaining 13% below plan. A 9% sequential quarter increase was driven by increased revenues on stable headcount.
- Net revenue per employee was above plan for DAD (29%), Consumer (41%) and Systems (43%) due to favorable revenue variances and below plan headcount. Workgroup net revenue per employee was 31% above plan on headcount that was 3% above plan.
- Net revenue per DDT employee was 11% below plan as a result of unfavorable revenue variances for Access and Fox on a headcount base that was 10% below plan.
- People expense per employee continued to be about 4% above plan; however, the total people expense was 10% below plan for Q94-3 as a result of lower than expected payroll and travel expenses.
- The people expense metric was \$9,000 higher for Systems and \$24,000 higher for AT than the WPG average.
- Excluding a \$26M reserve for an accounting change regarding the depreciable asset life of PC's, facilities expense per employee was on plan.
- Product development expense per employee was 27% below plan and 8% below Q94-2. The higher expense per head for Consumer was driven by contractor and temp expenses associated with increased product development.
- Marketing expense as a percentage of net revenue was on plan for Q94-3 despite a \$10M accrual for anticipated Q94-4 expense.

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Channel Metrics Summary

CHANNEL METRICS SUMMARY

(annualized in thousands)

	Finished Goods					OEM
	No. Amer.	Europe	ICON	Far East	Aggregate	
Net revenue per employee						
Actual 94-3	\$ 423	\$ 655	\$ 441	\$ 945	\$ 533	\$ 6,982
Plan	399	531	434	547	456	4,051
Q94-2	464	545	417	590	494	5,657
Q94-1	314	440	480	607	386	5,426
Q93-4	405	508	524	599	460	4,642
Q93-3	345	619	513	467	454	4,342
Q93-2	388	709	588	408	505	3,444
People expense per employee						
Actual 94-3	\$ 74	\$ 75	\$ 79	\$ 119	\$ 77	\$ 101
Plan	75	76	78	104	77	101
Q94-2	73	77	80	121	77	101
Q94-1	71	76	80	105	76	90
Q93-4	77	75	101	78	78	128
Q93-3	68	78	93	66	73	96
Q93-2	69	83	97	61	74	98
Facilities expense per employee						
Actual 94-3	\$ 28	\$ 26	\$ 29	\$ 33	\$ 28	\$ 17
Plan	25	26	31	34	27	17
Q94-2	23	25	30	34	25	15
Q94-1	21	27	29	34	24	15
Q93-4	21	32	22	33	25	26
Q93-3	18	30	29	30	23	22
Q93-2	18	31	31	21	23	17
Marketing expense as a % of revenue						
Actual 94-3	11%	8%	9%	7%	9%	0%
Plan	11%	9%	9%	11%	10%	1%
Q94-2	13%	12%	9%	12%	12%	0%
Q94-1	10%	8%	9%	13%	9%	0%
Q93-4	5%	10%	9%	20%	8%	0%
Q93-3	21%	6%	8%	12%	12%	2%
Q93-2	19%	10%	12%	19%	15%	3%

- FG revenue per head for Q94-3 was \$533,000 in comparison with plan of \$456,000. For almost all regions, headcount remained flat, while FG revenue exceeded plan. In Europe, FG revenue was 109% of plan, due to the release of localized versions of Win Word and Win Excel. In the Far East, FG revenue was 158% of plan, with the release of the localized version of Win Excel 5.0. FG revenue in North America was 97% of plan and 92% of plan in ICON.
- Q94-3 revenue for both Europe and the Far East reflected a record quarter, and as a result, the revenue per head for those regions substantially improved over Q94-2.
- For the OEM channel, lower PC prices, increased penetration of naked systems and a growing consumer market fueled a record revenue quarter. The average revenue per OEM employee hit \$6.9 million.
- The people expense per employee of \$119,000 in the Far East was in excess of plan of \$104,000 as a result of foreign exchange fluctuations. The actual yen exchange rate was 107 per US\$ compared with a budgeted exchange rate of 117 per US\$. Average FYTD94 headcount in the Far East was 5% below plan. People expense per employee was approximately at plan for the remaining regions.

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INFORMATION TECHNOLOGY

INFORMATION TECHNOLOGY

(in millions)	Q94-3			FYTD94		
	Actual	Plan	Variance	Actual	Plan	Variance
People Expense	\$8.3	\$8.8	\$0.5	\$29.1	\$32.1	\$3.0
Facilities Expense	2.2	2.6	0.4	5.6	7.1	1.4
Other Expense	1.5	0.0	(1.5)	1.6	0.0	(1.5)
Controllable Expense	<u>\$12.0</u>	<u>\$11.4</u>	<u>(\$0.6)</u>	<u>\$36.3</u>	<u>\$39.3</u>	<u>\$2.9</u>

- People expense remained favorable in Q94-3 due to project timing.
- Facilities expense was below plan primarily due to the delay in the release of Online Services and the associated telecommunications costs.
- Q94-3 other expense exceeded plan due to a \$1.5 million writeoff of Next Generation Business Systems (NGBS) costs associated with the prior vendor, Dun & Bradstreet. SAP has been selected as the new vendor.

Top Products Released

- EDI order processing enabled for the first time for all customers outside the US.
- US Sales landed revenue system to collect US customer centric sales data.
- Budget Workbench 2.0 for FY95 revenue, marketing, headcount, operating expenses and capital planning.
- MS Manager (Customer Management System) installed in 11 sites internationally (16 sites total).
- Enhanced tools to support MSN in Europe and other international sites (International PSS Workbench, MS Manager).
- HR Vantage (Personnel Administration System) installed in 11 sites internationally (16 sites total).

Other Significant Achievements

- Plans are complete for redesigning PSS's telecommunications capacity to manage anticipated volume increase during the Chicago launch. IT's plans project additional capacity for future growth as well as improved reliability.
- Finalized Information Systems Plan for ICON region.
- Completed plans for upgrade to WAN based upon anticipated bandwidth needs. Installed ISDN network to domestic sales offices.
- Renegotiated AT&T telecommunications agreement resulting in anticipated savings in excess of \$1M annually.
- Began implementation of time tracking system (Timekeeper) to monitor both internal and external costs of IT product development.

External Costs for Major Applications (in thousands)

Project	Actual- to-date	FY94 project forecast*	FY94 Budget	Release date
NGBS	\$ 216	\$ 750	\$ 1,756	Late FY95
ISS Workbench	971	1800	899	Jul-94
MS Sales	226	850	842	Jun-94
License Revenue System**	750	1650	810	Sep-94
WAM	378	500	562	Jan-94
Budget Workbench 2.0***	558	600	540	Apr-94
PSS Workbench	393	400	499	Nov-93

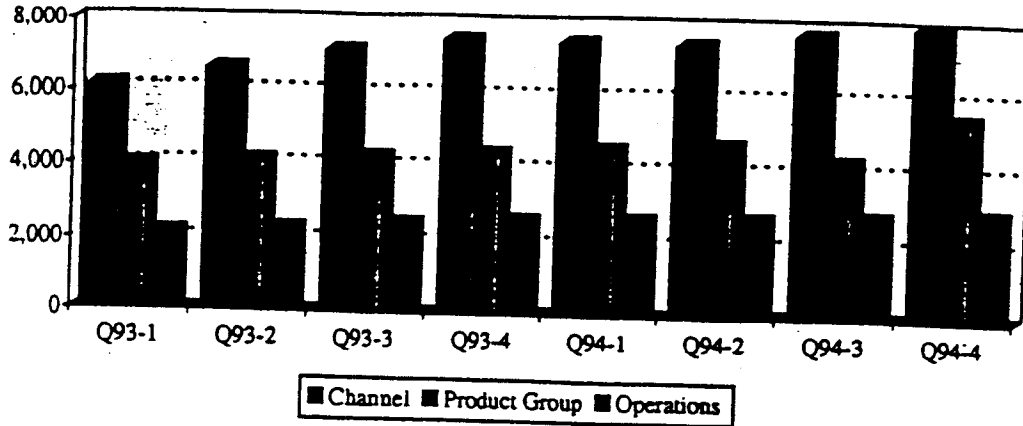
* includes Actual-to-date spending
 ** Funding increased to \$1.137 for further enhancements
 *** Funding increased to \$607 for further enhancements requested by Finance

HEADCOUNT

	Q94-1	Q94-2	Q94-3		Q94-4
	Actual	Actual	Actual	Plan	Plan
North America FG	1,856	1,832	1,825	1,983	1,972
PSS	1,762	1,726	1,711	1,922	1,906
MCS	223	253	264	264	264
Europe FG	2,352	2,405	2,376	2,731	2,742
ICON FG	567	602	633	683	678
Far East FG	357	375	372	411	429
OEM	189	190	180	204	204
Other	62	44	41	42	42
Channels	7,368	7,427	7,402	8,240	8,237
Excel	218	212	192	239	235
Graphics	66	67	74	81	81
Other Desktop Applications	244	229	272	301	307
Project	75	79	77	82	79
Word	243	254	255	265	262
Desktop Applications	846	841	870	968	964
Applications Programmability	126	148	139	149	149
Database Mgmt Systems	203	249	256	269	269
Fox	70	53	70	65	65
DDT Management	66	68	41	74	74
C++	59	43	189	218	210
Scientific and Eng Tools	182	197	32	65	65
Database & Dev Tools	706	758	727	840	832
Entry	62	51	129	153	153
MM Pubs	179	132	133	140	143
Other Consumer	111	120	55	73	78
Works	119	166	162	172	170
Consumer	471	469	479	538	544
Workgroup	379	397	370	359	355
Advanced Systems	599	531	532	609	609
Digital Office Systems	137	154	176	193	193
Hardware	80	81	82	89	89
MS-DOS	36	28	26	39	39
Other Systems	144	136	132	191	199
Systems Marketing	103	110	115	107	107
Windows	349	328	362	420	420
Systems	1,448	1,368	1,425	1,648	1,656
Advanced Consumer Tech	190	234	207	301	303
Advanced Product Dev	42	52	24	60	60
Broad Band Apps	13	13	18	20	20
On-Line Services	25	46	59	68	68
Advanced Technology	270	345	308	449	451
Other WPG	90	91	112	162	162
International R&D	220	167	197	230	229
Other Product Groups	152	164	161	190	191
Product Groups & AT	4,582	4,600	4,649	5,384	5,541
Campus North	552	585	599	619	619
Ireland	402	407	347	420	420
IFF	246	239	251	264	264
Puerto Rico	169	160	169	204	204
Procurement/Mgmt	60	59	47	66	66
Operations	1,429	1,450	1,413	1,573	1,573
ITG	316	308	321	326	326
Law & Corporate Affairs	128	140	145	155	155
Finance	243	260	278	295	295
Human Resources	195	228	223	242	242
Corporate Services	268	244	263	276	277
Executive Staff	5	5	4	7	7
Real Estate & Facilities	75	75	75	92	92
Corporate	2,659	2,710	2,722	2,966	2,957
Microsoft	14,609	14,737	14,773	16,590	16,735

HEADCOUNT

Headcount Trend



The above graph uses actual headcount from Q93-1 through Q94-3 and budgeted headcount for Q94-4.

Worldwide Headcount by Location

- The following chart shows the distribution of total Microsoft employees by location. Approximately 54% of total employees are employed in the Puget Sound Area.

	Q94-3
Corporate campus	40 %
Subsidiaries	33
Field locations	13
Other Puget Sound	9
Canyon Park	5
	<u>100 %</u>

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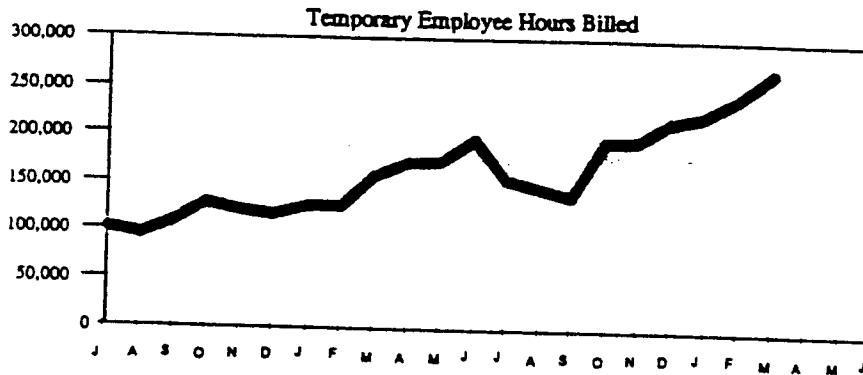
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Profile of Domestic Employees

U.S. Employee Statistics

	No. of Employees	Mix
Sex:		
Female	3,541	36%
Male	6,390	64%
Ethnicity:		
White	8,473	85%
Asian Pacific/Islander	868	9%
African American	269	3%
Hispanic	229	2%
American Indian/Alaska Native	46	< 1%
Other	46	< 1%
Age:		
Under 20	35	< 1%
20 - 29	3,407	35%
30 - 39	4,824	49%
40 and Over	1,665	17%
Average Age:	32.6 years	
Average Tenure:		
Domestic	3.2 years	
Subsidiaries	2.6 years	
Worldwide Average	3.0 years	

U.S. Temporary Employees at Microsoft



- Use of temporary employees at Microsoft increased during Q93-3. FYTD94 expenses for temporary employees are \$0.9 million over a plan of \$32.0 million.

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MS Cost Drivers & Metrics

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CURRENT ASSETS

Cash and Investment Portfolio Balances (in millions)

	Dec. 31, 1993		Mar. 31, 1994	
	\$	%	\$	%
US \$ investment portfolio	\$ 2,587	93%	\$ 2,809	90%
Foreign currency investments	74	3	225	7
Operating bank accounts	135	4	109	3
Worldwide cash and investments	<u>\$ 2,796</u>	<u>100%</u>	<u>\$ 3,143</u>	<u>100%</u>

US\$ Portfolio by Security Type (in millions)

Security type	Dec. 31, 1993			Mar. 31, 1994		
	Cost	% Pre-Tax Yield		Cost	% Pre-Tax Yield	
Municipal bonds	\$ 1,173	45%	4.9%	\$ 1,280	46%	4.9%
Commercial paper	398	15	3.4	463	16	3.5
Treasury securities	270	10	4.0	374	13	3.9
Floating rate notes	195	8	3.3	217	8	4.1
Money market preferred	175	7	4.0	171	6	4.0
Certificate and time deposits	170	7	3.7	123	4	3.9
Corporate bonds	156	6	4.6	115	4	4.5
Other	50	2	5.0	66	2	4.5
US \$ investment portfolio	<u>\$ 2,587</u>	<u>100%</u>	4.3	<u>\$ 2,809</u>	<u>100%</u>	4.4
Yield Comparison:						
90 day T-Bill			3.1			3.5
Donahue Index			2.7			2.9

- The US\$ Portfolio is fully invested in investment grade securities with an average AA credit quality.

Inventories by Location (in millions)

	Q93-4	Q94-1	Q94-2	Q94-3
Subsidiary warehouses				
Japan	\$8	\$7	\$9	\$8
France	3	3	7	4
Australia	4	3	6	6
Sweden	1	1	2	2
Germany	7	5	2	14
Others	10	16	11	9
	<u>33</u>	<u>35</u>	<u>37</u>	<u>43</u>
Campus North	81	54	78	71
Ireland	11	4	14	16
Puerto Rico	2	2	1	1
	<u>\$127</u>	<u>\$95</u>	<u>\$130</u>	<u>\$131</u>

- Inventories decreased by \$12 million during the quarter representing a 9% decline. Canyon Park Inventory decreased by 9% or \$7 million due to the increased production levels resulting from strong Desktop Applications demand. Production levels for DFF increased by 19% during the quarter.
- The \$14 million inventory balance in Germany includes a \$13 million intercompany misclassification between Ireland and Germany in conjunction with the Concorde conversion during March, which will be reversed in the month of April.

CURRENT ASSETS

Ten Largest Worldwide Accounts Receivable (in millions)

	Total	Percent	Aging Summary			
			Current	1-30	31-60	Over 60
Ingram	\$81	12%	\$70	\$9	\$1	\$1
Merisel	61	9%	46	9	4	2
Computer 2000	26	4%	21	3	1	1
Softbank	18	3%	18	0	0	0
Egghead	17	3%	14	2	1	0
Olivetti	12	2%	10	2	0	0
Software Spectrum	10	1%	2	2	6	0
Katena	8	1%	8	0	0	0
Software Japan	8	1%	8	0	0	0
Corporate Software	7	1%	3	1	3	0
Total ten largest	248	37%	200	28	16	4
Other	427	63%	286	70	22	49
Total Q94-3	<u>\$675</u>	<u>100%</u>	<u>\$486</u>	<u>\$98</u>	<u>\$38</u>	<u>\$53</u>
Total Q94-2	<u>\$620</u>		<u>\$448</u>	<u>\$103</u>	<u>\$20</u>	<u>\$49</u>
Aging mix of top ten	<u>100%</u>		<u>81%</u>	<u>11%</u>	<u>6%</u>	<u>2%</u>

Worldwide Accounts Receivable (in millions)

	DSO			Total			Aging Summary			
	Q94-1	Q94-2	Q94-3	Q94-1	Q94-2	Q94-3	Current	1-30	31-60	Over 60
Retail										
USFG	55	43	44	\$161	\$233	\$197	\$143	\$32	\$17	\$5
International	51	58	53	236	299	333	267	39	15	12
				397	532	530	410	71	32	17
OEM	32	24	33	81	68	127	66	23	5	33
Other	84	81	84	14	20	18	10	4	1	3
Total accts receivable	48	45	46	492	620	675	<u>\$486</u>	<u>\$98</u>	<u>\$38</u>	<u>\$53</u>
Aging Percentages							<u>72%</u>	<u>14%</u>	<u>6%</u>	<u>8%</u>
OEM GAAP Adjustments				106	114	115				
Sales returns reserve				(95)	(91)	(99)				
Customer deposits/deferred rev.				(40)	(44)	(43)				
Reseller rebates				(16)	(42)	(19)				
Allowance for doubtful accounts				(83)	(97)	(107)				
Accounts receivable-net				<u>\$364</u>	<u>\$460</u>	<u>\$522</u>				

Worldwide Net Receivables (in millions)

	Net Receivables	DSO	Allowance	
			Dollars	% of AR
Q94-3	\$522	46	\$107	16
Q94-2	460	45	97	16
Q94-1	364	48	83	17
Q93-4	338	46	76	18
Q93-3	438	54	68	13

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OTHER ASSETS

OTHER ASSETS

(in millions)

	Cost			Market Value (if public)		
	Jun. 30, 1993	Mar. 31, 1994	Change	Jun. 30, 1993	Mar. 31, 1994	Change
Financial assets						
Santa Cruz Operation	\$ 20	\$ 20	\$ --	\$ 27	25	\$ (2)
Dorling Kindersley	19	19	--	49	50	1
MicroUnity	--	15	15	--	--	--
Metricom	--	6	6	--	6	6
Monotype	4	4	--	--	--	--
Natural Language Inc.	3	3	--	--	--	--
Citrix Systems	2	2	--	--	--	--
	<u>48</u>	<u>69</u>	<u>21</u>	<u>\$ 76</u>	<u>81</u>	<u>\$ 5</u>
Valuation allowance	(28)	(35)	(7)			
	<u>20</u>	<u>34</u>	<u>14</u>			
Intellectual property rights						
Consumer Software, Inc.	13	13	--			
Other	49	53	4			
	<u>62</u>	<u>66</u>	<u>4</u>			
Accumulated amortization	(32)	(41)	(9)			
	<u>30</u>	<u>25</u>	<u>(5)</u>			
Miscellaneous	<u>38</u>	<u>37</u>	<u>(1)</u>			
	<u>\$ 88</u>	<u>\$ 96</u>	<u>\$ 8</u>			

- Financial assets include equity and equity related investments. MS maintains a valuation allowance to cover operating losses at investee companies and potential losses on disposition. The provision is charged to non operating income in the financial statements.
- Intellectual property rights represent purchased code or other intellectual property and rights. Their cost is amortized over periods of up to five years. Amortization is generally charged to research and development expense.
- Miscellaneous assets include other long-term assets, primarily lease and other deposits and patent rights.

Nationwide Wireless Network (NWN)

- On March 24, MS signed a technology and marketing agreement with NWN, a two-way narrow band Personal Communications Service (PCS) subsidiary of Mtel. Due to its innovative network architecture, NWN was granted a final Pioneer's Preference by the FCC for a license in the 940-941 MHz band. NWN's network is under development and expects to be operational in July 1995.
- MS will assist in the development of an optimized network for the Pulsar client and receive (i) royalty-free access to the NWN Network Operations Center (NOC) to ensure compatibility with the Pulsar NOC; (ii) a 2% royalty on all revenue generated by Pulsar clients on NWN; and (iii) marketing "ownership" of Pulsar's customers on NWN.
- In addition, MS and Mtel signed a shareholder's agreement pursuant to which MS will invest \$30 million (1,500 shares at \$20,000 per share) in NWN and become an 8.5% owner. The investment will fund upon clearance of HSR. Other investors in this financing round include Bill Gates, Paul Allen and Integral Partners. Kleiner Perkins is also an investor. Greg Maffei will join NWN's board.
- MS will also receive 1.150 11-year warrants. The majority of these warrants are subject to certain performance requirements. Assuming conversion and/or exercise of all warrants, MS will own approximately 14% of NWN.

OTHER ASSETS

Metricom, Incorporated

	Year Ended Dec. 31, 1992	Year Ended Dec. 31, 1993	Change \$	Change %
Net revenue	\$ 6.4	\$ 10.1	\$ 3.7	58 %
Cost of revenue	6.1	8.3	2.2	36
Gross profit	0.3	1.8	1.5	500
Controllable expenses	4.8	7.9	3.1	65
Net income	\$ (4.5)	\$ (6.1)	\$ (1.6)	(36) %

- On March 24, concurrent with Metricom's additional public offering, MS purchased 200,000 shares of Metricom common stock for \$6.05 million (\$30.25 per share). MS also received 75,000 3-year warrants (exercisable at \$37.50 per share) that were valued at \$9.75 per share or \$731,000. Subsequent to the end of the quarter, Metricom's stock price fell to \$18.50 as the wireless technology sector declined as a whole.
- Pursuant to our shareholder's agreement, MS's shares must be held at least nine months. Assuming conversion and/or exercise of all warrants, MS will own approximately 2% of Metricom.
- Metricom raised approximately \$80 million (2.7 million shares) in this round of financing. The proceeds will be used to fund the deployment of the Microcellular Data Network.
- MS and Metricom are working on a technology and marketing letter of intent, similar to that signed with NWN, that will complement MS's Pulsar and overall wireless strategy.

Great Plains Software

	10 Months Ended Mar. 31, 1993	10 Months Ended Mar. 31, 1994	Change \$	Change %
Net revenue	\$ 19.1	\$ 25.1	\$ 6.0	31 %
Cost of revenue	4.0	6.2	2.2	55
Gross profit	15.1	18.9	3.8	25
Controllable expenses	16.5	24.5	7.8	47
Net income	\$ (1.4)	\$ (5.6)	\$ (4.2)	300 %

- In connection with the resolution of the MS product relationship with GPS (discussed in the Consumer Division section), MS agreed to loan GPS up to \$2 million for up to three years at an annual rate of prime plus 1.25%. In connection with the loan, MS received a secured, first lien on the Profit product line and a secured, second lien on the remainder of GPS's assets.
- On April 8, GPS borrowed \$500,000. In the event that GPS borrows more than \$500,000, MS has the right to convert a portion of the loan into the equity of GPS. At the full \$2 million loan amount, MS will be able to convert \$500,000 of principal into GPS equity at a valuation of 1.1 times revenues or the valuation set at the next equity investment by a third party.
- GPS has signed an agreement pursuant to which Goldman Sachs will invest \$8 million at a \$40 million pre-money valuation. This investment, which will close next month, will strengthen MS's credit position and fix the valuation for loan conversion, resulting in an MS equity stake of up to approximately 1% if GPS borrows the full \$2 million.
- GPS's financial performance in the current fiscal year has suffered due to heavy investment in both its low-end Windows products (Profit and Payroll) and in its mid-range Dynamics product line. The Dynamics line will roll out this year and is expected to make a significant revenue contribution.

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OTHER ASSETS**Santa Cruz Operation, Inc.**

	Quarter Ended Mar. 31, 1993	Quarter Ended Mar. 31, 1994	Change \$	Change %
Net revenue	\$ 43	\$ 44	\$ 1	2 %
Cost of revenue	12	13	1	8
Gross profit	31	31	0	0
Controllable expenses	27	29	2	7
Net income	\$ 4	\$ 2	\$ (2)	(50) %

- North American revenue remained flat as SCO continued to reduce excess inventory in the channel, while International operations experienced good growth. Revenue for the second quarter of fiscal 1993 included \$3M of non-recurring revenue related to a federal contract.
- Controllable expenses grew due to several factors including increased R&D spending to localize selected products and an increase in the tax rate.
- EPS for SCO's second quarter was \$0.08 compared with EPS of \$0.14 in the year prior period in part due to the increase in shares outstanding due to the IPO in May 1993.
- SCO announced a joint venture with Tomen to distribute SCO's products in Japan.

Dorling Kindersley

	6 Months Ended Jun. 30, 1993	6 Months Ended Jun. 30, 1994	Change £	Change %
Net revenue	£ 39	£ 45	£ 6	15 %
Cost of revenue	25	29	4	16
Gross profit	14	16	2	14
Controllable expenses	11	14	3	27
Net income	£ 3	£ 2	£ (1)	(33) %

- DK's revenue grew as planned due to strong performances in the Adult and Children's division which also enjoyed excellent profitability.
- Overall, DK's profits declined due to increased spending in the Multimedia division, continued distribution problems related to the termination of Tiptree (the distributor of DK's Family Library series) and weakness in the Education and DK Direct divisions.
- Greg Maffei assumed MS's board seat.

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OTHER ASSETS

MicroUnity Systems Engineering, Inc.

- MicroUnity remains in the development phase. MS's ACT group is working closely with MU to insure compatibility with MS's broadband efforts.
- MicroUnity raised \$75M in 1993 with investments from MS, TCI, Time Warner, Cox Cable and Comcast and \$5M through a licensing arrangement. The funds were primarily raised to produce a 128-bit RISC microprocessor for a digital, interactive cable set-top box.
- MS owns 6.5 million shares of convertible Series D Preferred Stock at a cost of \$14.95 million (\$2.30 per share) and a warrant to purchase 2.0 million shares of Series E Preferred Stock at a cost of \$50,000 (exercisable at \$3.75 per share).
- Assuming conversion and/or exercise of all preferred stock, warrants and options, MS owns approximately 6% of the fully-diluted common stock. If the performance of MicroUnity's chips exceeds certain performance benchmarks, MS's position could be diluted. Concurrent with its investment, MS signed agreements with MicroUnity and the other Series D Preferred investors which grant MS access to certain technical specifications for the cable chip and other future developments.

Monotype Typography Limited

	Year Ended Mar. 31, 1994	9 Months Ended Dec. 31, 1993	Quarter Ended Mar. 31, 1994
Net Revenues	\$ 7.8	\$ 6.1	\$ 1.7
Cost of Revenues	2.3	1.9	0.4
Gross Profit	5.5	4.2	1.3
Controllable Expenses	5.9	4.8	1.1
Net Income	\$ (0.4)	\$ (0.6)	\$ 0.2

- Monotype achieved a 12% profit margin during the most recent quarter on revenue of approximately \$1.7 million versus an 11% margin on \$1.9 million for the prior quarter. The improvement in operating margin percentage was due to cost and headcount reduction measures adopted in September, 1993.
- Revenue for the year ended March 31, 1994 was \$7.8 million, with \$4.4 million generated by overseas operations. During this period, the company suffered a loss of \$380,000. The loss included a \$350,000 reserve in the UK for exceptional items. Operating profit for this period was \$107,000.
- Monotype's liquidity continues to remain tight. However, due to cost containment measures, management's outlook for 1994 is optimistic.
- MS's \$4 million investment included the purchase of Monotype's font library, warrants for approximately 36% of the company (which under certain performance conditions can amount to 85% of the company) and a loan of \$1.2 million. The current outstanding loan balance is \$900,000.
- Amar Nehru will join Monotype's board this quarter.

OTHER ASSETS**Natural Language Incorporated**

	Quarter Ended Dec. 31, 1993	Quarter Ended March 31, 1994	Change \$	Change %
Net revenue	\$ 0.4	\$ 1.0	\$ 0.6	150 %
Cost of revenue	0.1	0.1	0.0	0.0
Gross profit	0.3	0.9	0.6	200
Controllable expenses	0.9	0.6	(0.3)	(33)
Net income	\$ (0.6)	\$ 0.3	\$ 0.9	(150) %

- Revenue increased during the quarter as several large orders worked their way through the sales cycle. Revenue from repeat customers has increased and a significant VAR customer has resold all its inventory and is expected to place a significant order this quarter.
- NLI continues to focus on Windows solutions and has become an MS Solution Provider. In the coming months it will release Fox and Access versions of its product and all versions of Natural Language will ship with a full featured report writer.
- NLI discontinued its unsuccessful telesales effort in favor of a Powersoft-style seminar selling model.
- NLI offered the CEO position to Tom Lavey who was an EVP at ASK Computer Systems where he grew sales from \$1 million to \$60 million. Lavey was also the founder of Minx Software. John Manfredelli, a founder of NLI, will remain as Chairman.
- In order to improve cash flow, the company has downsized by 25%.
- NLI is in the final stages of recapitalizing and raising an additional \$600,000 of equity, of which MS will contribute \$104,000. All the existing debt (except for recent bridge loans) and equity will be collapsed into one percent of equity and MS's new ownership position will increase slightly to approximately 13%.

Citrix Systems

	3 Months Ended Mar. 31, 1993	3 Months Ended Mar. 31, 1994	Change \$	Change %
Net revenue	\$ 0.8	\$ 2.0	\$ 1.2	150 %
Cost of revenue	0.1	0.5	0.4	400
Gross profit	0.7	1.5	0.8	114
Controllable expenses	1.5	1.9	0.4	27
Net income	\$ (0.8)	\$ (0.4)	\$ 0.4	(50) %

- Citrix had a record quarter and a record month in March. Revenue was up 31% from the 4th quarter of 1993 and the number of authorized resellers grew from 120 to 160.
- Liquidity has improved with collections of \$800,000 in March and cash was \$1.4 million at quarter end.
- Key events for the quarter included signing an OEM agreement with Intel, completing a credit line with the Bank of Boston, improved major account penetration and some positive press on the positioning of the WinView product as "fast, remote windows".
- The company is targeting to breakeven in its second quarter on \$2.5 million of sales.

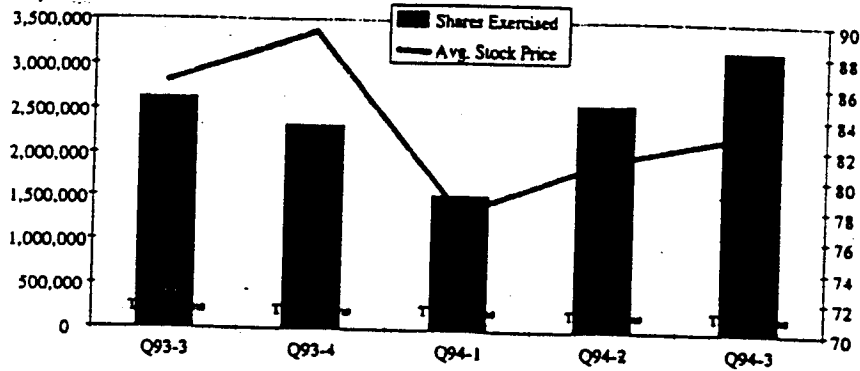
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STOCK MATTERS

STOCK MATTERS

Options and ESPP



- In Q94-3, a total of 3,207,583 options were exercised, a 24% increase over Q94-2 and a 22% increase over Q93-3. A record high 4,684 stock option exercises were exercised in Q94-3 which was an 85% increase over Q94-2 and a 43% increase over Q93-3. Factors contributing to the increase in exercises were an upward trend in the average stock price, first time vesting for non-exempt employees and four major vesting days in January.
- **On Hire Options:** During Q94-3, a total of 155 stock option grants totaling 367,799 shares were processed. In addition, during Q94-3, 165 stock option grants relating to prior quarters and totaling 204,855 shares were processed.
- **ESPP:** 9,265 employees are currently enrolled in the ESPP. Total enrollment has decreased 5% (9,780) from the previous period ending December 31, 1993. This is the first ESPP period in which enrollment has decreased. To date, 383 employees have withdrawn and 423 employees have left MS.

Stock Repurchases

	Shares adjusted for all splits	Amount (millions)	Average Cost
FY90	1,785,375	\$ 46	\$26.14
FY91	5,469,750	197	35.96
FY92	1,979,828	135	68.18
FY93	3,128,500	250	79.92
Q94-1	966,500	72	74.47
Q94-2	1,152,500	92	79.66
Q94-3	1,810,000	147	81.28
FYTD94	3,929,000	311	79.13
LTD	16,292,453	\$792	57.65

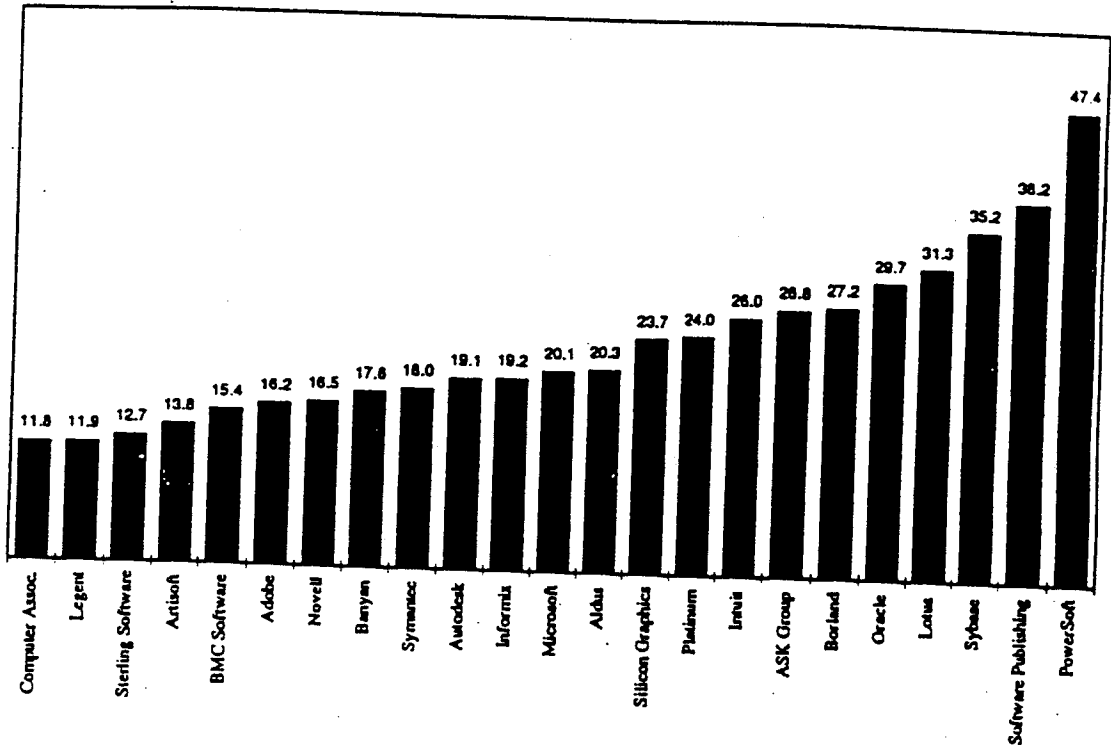
- FYTD94, MS has repurchased 3,929,000 shares at an average cost of \$79.13 per share and a total cost of \$311 million.

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SOFTWARE INDUSTRY FORWARD P/E RATIOS

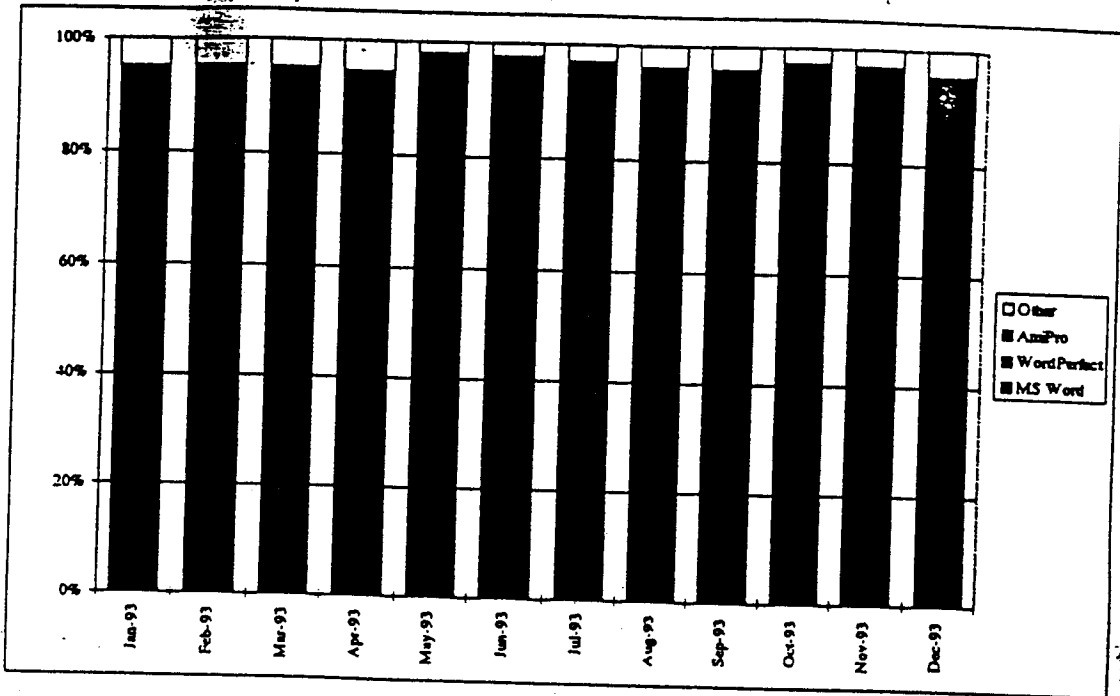


Forward P/E ratios are calculated based upon March 31, 1994 stock prices and analysts's consensus estimates for the next four quarters.

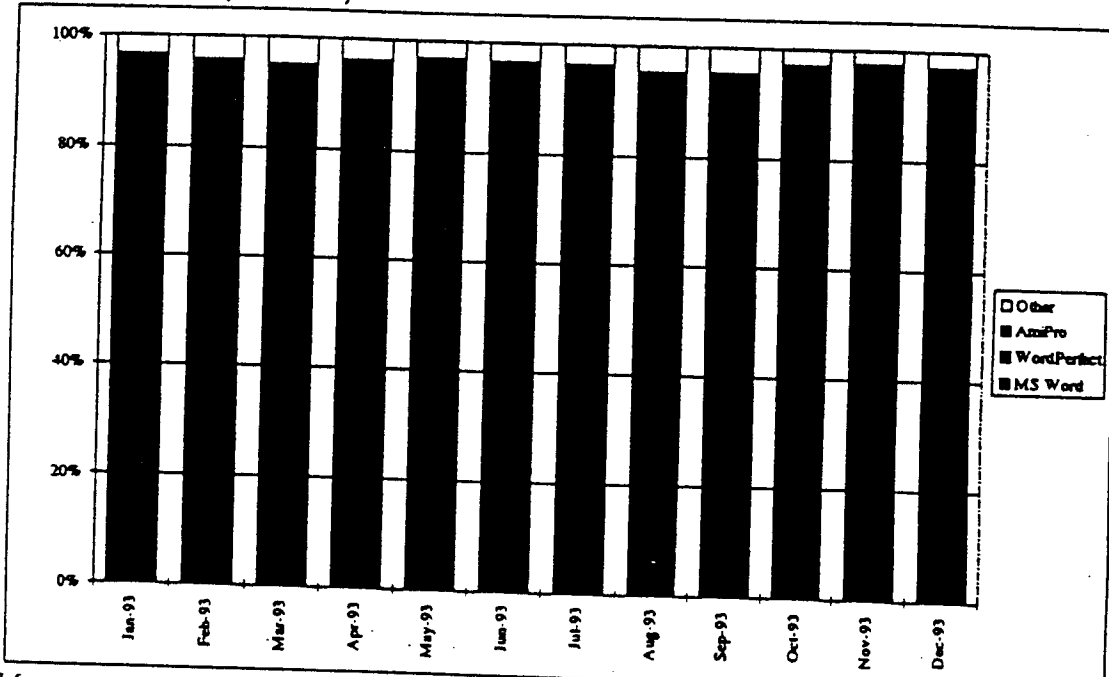
WORLDWIDE MARKET SHARE

WORLDWIDE MARKET SHARE

Word Processors (Units)



Word Processors (Revenues)



Information presented is not version specific and includes MS-DOS, Windows, and Macintosh environments on a worldwide basis. Percentages are three month rolling averages. Market share is calculated by Microsoft Office marketing personnel and is based on SPA, IDC, and DataQuest information.

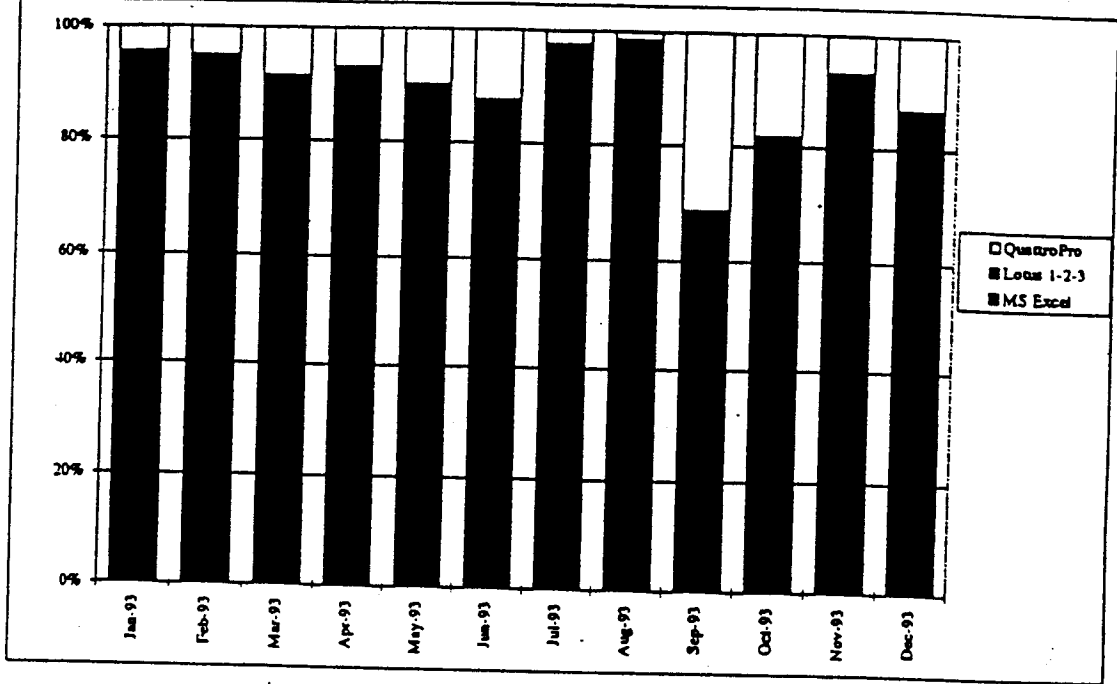
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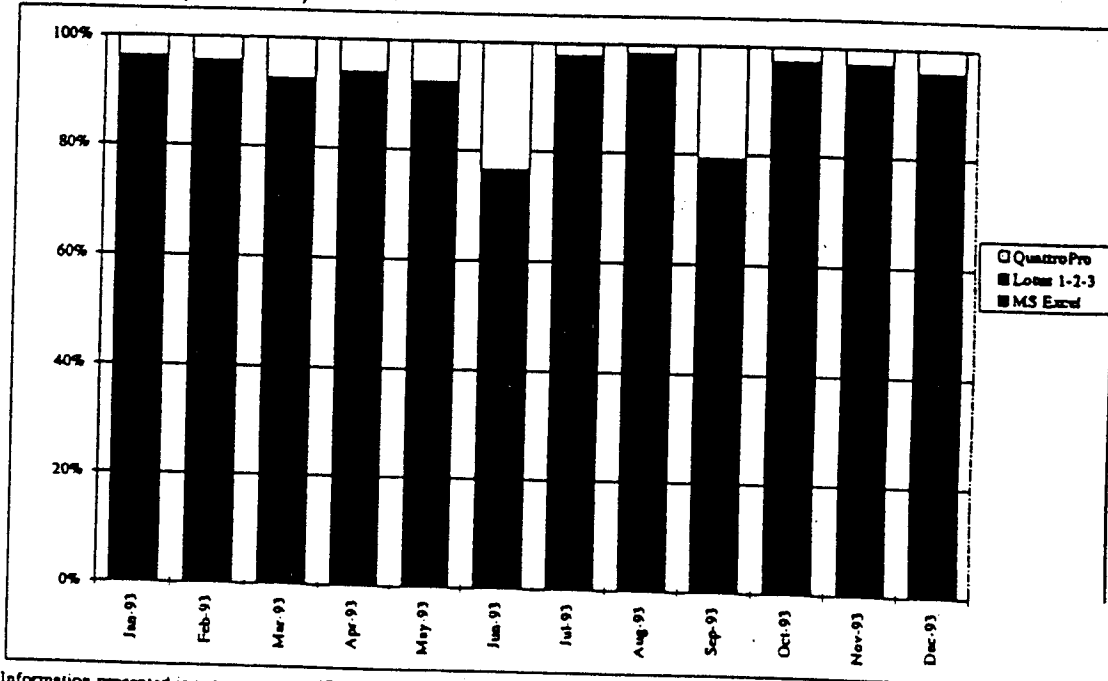
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WORLDWIDE MARKET SHARE

Spreadsheets (Units)



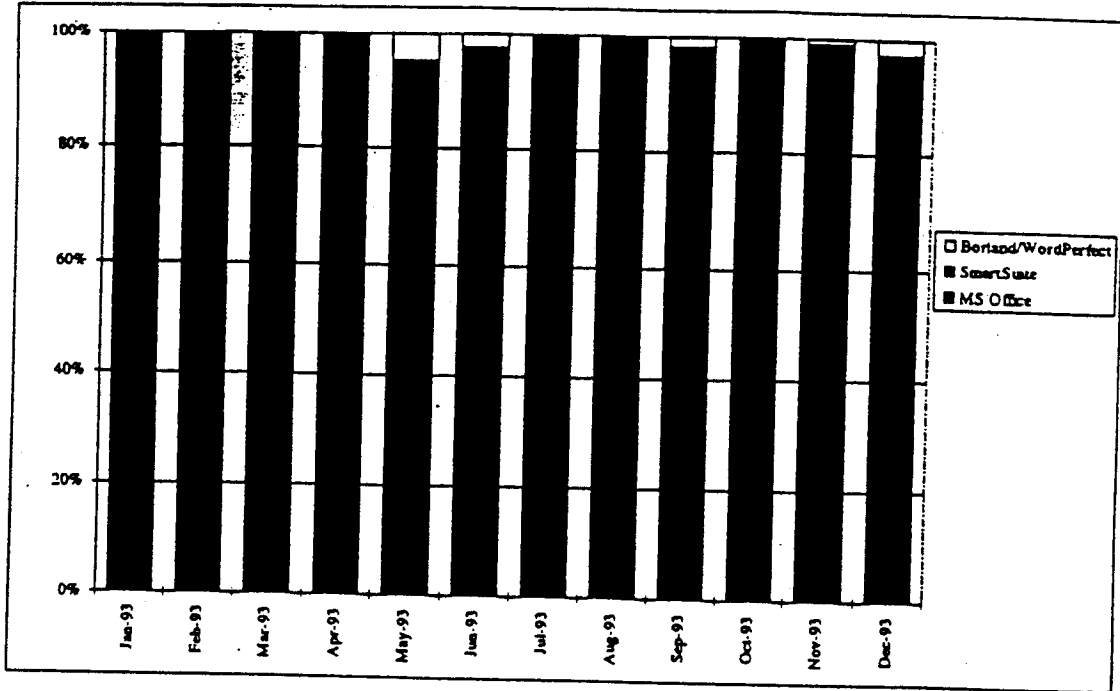
Spreadsheets (Revenues)



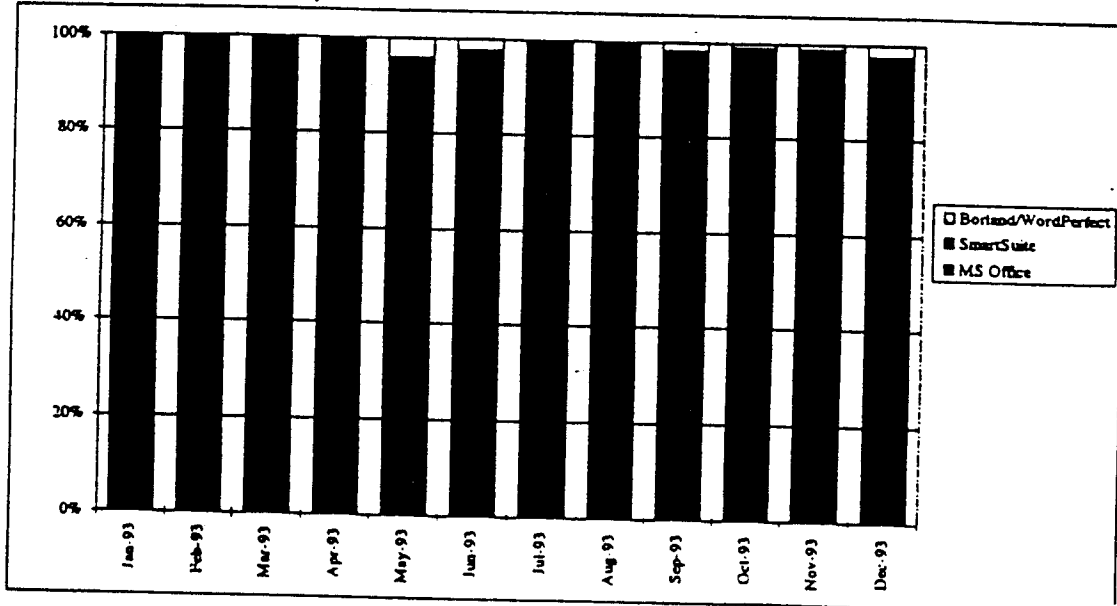
Information presented is not version specific and includes MS-DOS, Windows, and Macintosh environments on a worldwide basis. Percentages are three month rolling averages. Market share is calculated by Microsoft Office marketing personnel and is based on SPA, IDC, and DataQuest information.

WORLDWIDE MARKET SHARE

Bundled Suites (Units)



Bundled Suites (Revenues)



Information presented is for the Windows environment on a worldwide basis.

Percentages are three month rolling averages.

Market share is calculated by Microsoft Office marketing personnel and is based on competitor press releases and product management's estimates.

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TOP FOUR SOFTWARE COMPANIES

TOP FOUR SOFTWARE COMPANIES
(in millions)

Most recent quarter	Microsoft 3/31/94		Novell 1/29/94		Lotus 12/31/93		Borland 12/31/93	
Net revenues	\$ 1,244	100.0%	\$ 311 (a)	100.0%	\$ 278 (c)	100.0%	\$ 112 (e)	100.0%
Cost of revenues	208	16.7	64	20.6	54	19.4	29	25.9
Gross profit	1,036	83.3	247	79.4	224	80.6	83	74.1
Research and development	156	12.5	57	18.3	32	11.5	15	13.4
Sales and marketing	359	28.9	68	21.9	130	46.8	66	58.9
General and administrative	41	3.3	23	7.4	17	6.1	-	-
Litigation charge	120	9.6	-	-	-	-	-	-
Total operating expenses	676	54.3	148	47.6	179	64.4	81	72.3
Operating income	360	29.0	99	31.8	45	16.2	2	1.8
Nonoperating income	22	1.8	11	3.5	1	0.4	-	-
Income before income taxes	382	30.8	110	35.3	46	16.6	2	1.8
Provision (benefit) for income taxes	126	10.2	37	11.8	16	5.8	2	1.8
Net income	\$ 256	20.6%	\$ 73	23.5%	\$ 30	10.8%	\$ -	-
Average shares outstanding	304		314		46		27	
EPS	\$ 0.84		\$ 0.23		\$ 0.64		\$ 0.02	
Trailing twelve months								
Net revenues	\$ 4,395	100.0%	\$ 1,174	100.0%	\$ 981	100.0%	\$ 460	100.0%
Cost of revenues	732	16.7	238	20.3	202	20.6	118	25.7
Gross profit	3,663	83.3	936	79.7	779	79.4	342	74.3
Research and development	578	13.2	187	15.9	127	12.9	61	13.3
Sales and marketing	1,321	30.0	274	23.4	463	47.3	263	57.1
General and administrative	153	3.5	82	7.0	70	7.1	-	-
Litigation charge	120	2.7	321 (b)	27.3	-	-	-	-
Total operating expenses	2,172	49.4	864	73.6	660	67.3	324 (f)	70.4
Operating income	1,491	33.9	72	6.1	119	12.1	18	3.9
Nonoperating income	81	1.8	34	2.9	(17) (d)	(1.7)	3	0.7
Income before income taxes	1,572	35.7	106	9.0	102	10.4	21	4.6
Provision (benefit) for income taxes	523	11.8	139	11.8	46	4.7	7	1.6
Net income	\$ 1,049	23.9%	\$ (33)	(2.8)%	\$ 56	5.7%	\$ 14	3.0%
Average shares outstanding	304		315		45		28	
EPS	\$ 3.45		\$ (0.11)		\$ 1.25		\$ 0.53	

- (a) Novell's first quarter sales grew 20%. Excluding USL revenues, the increase was only 13% due to reductions in channel inventory.
- (b) Novell's results of operations include a charge of \$321 million related to the acquisitions of USL, Software Transformation, Serius and Fluent. The write-off of purchased research and development and other costs represents a one-time charge against earnings of \$1.00 per share.
- (c) In the fourth quarter, SmartSuite represented 47% of Lotus's revenue, more than double the percentage from the end of last year.
- (d) Lotus's nonoperating income includes a charge of \$20 million for purchased research and development related to the acquisition of Approach Software. Before one-time items in 1993 and 1992, net income in the current fiscal year rose 32% to \$75 million.
- (e) Borland's revenues in the December quarter grew 7% over the prior year.
- (f) Borland expects its corporate restructuring, the layoff of 200 U.S. employees, and the transfer of 100 Quattro Pro staff to Novell to save \$50 million annually.

Industry Watch

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TOP FOUR SOFTWARE COMPANIES

Top Four Software Companies (Continued) (in millions)

	Microsoft 3/31/94		Novell 1/31/94		Lotus 12/31/93		Borland 12/31/93	
Balance sheets								
Current assets:								
Cash and short-term investments	\$ 3,143	64%	\$ 766 (a)	53%	\$ 417	46%	\$ 67 (e)	18%
Accounts receivable - net	522	11	302	21	217	24	81	22
Inventories	131	3	-	-	21	2	10	3
Other	116	1	67	5	21	3	10	3
Total current assets	3,912	79	1,135	79	676	75	168	46
Property, plant and equipment - net	918	19	216	15	127	14	176	48
Capitalized software	-	-	-	-	89	10	-	-
Other assets	96	2	88	6	13	1	21	6
	\$ 4,926	100%	\$ 1,439	100%	\$ 905	100%	\$ 365	100%
Current liabilities								
	\$ 884	18%	\$ 218	15%	\$ 298	33%	\$ 146	40%
Long-term liabilities	-	-	-	-	78	9	21	6
Other liabilities	-	-	36	3	-	-	-	-
Stockholders' equity	4,042	82	1,185	82	529	58	198	54
	\$ 4,926	100%	\$ 1,439	100%	\$ 905	100%	\$ 365	100%
Other data								
Closing stock price (March 31, 1994)	\$84.75		\$18.13		\$70.50 (d)		\$14.13 (f)	
Common shares outstanding	304		314 (b)		46		27	
Market value	\$25,764		\$5,693		\$3,243		\$382	
Price/revenues ratio	5.9x		4.8x		3.3x		0.8x	
Price/earnings ratio - trailing twelve	24.6x		" (c)		56.4x		26.7x	
Price/earnings ratio - future 4 quarters	20.1x		16.5x		31.3x		27.2x	
Avg headcount (most recent disclosure)	13,813		4,006		4,350		1,989	
Net revenues/employee	\$18,179		\$293,060		\$223,517		\$231,272	
Book value per share	\$13.30		\$3.77		\$11.50		\$7.33	
Price/book value ratio	6.4x		4.8x		6.1x		1.9x	
Growth statistics (over comparable quarter):								
Revenue	30%		20%		13%		7%	
Research and development	34%		63%		(2%)		(21%)	
Sales and marketing	15%		29%		8%		(18%)	
General and administrative	37%		8%		(2%)		nh	
Net income	5% (g)		3%		103%		101%	

- (a) Novell's cash and short term investments rose by \$102 million to \$766 million during the quarter, while accounts receivable decreased improving days sales outstanding from 98 days to 88 days.
- (b) On March 21, Novell agreed to buy WordPerfect for 59 million shares (\$1.4 billion) of stock and Borland's spreadsheet business for \$145 million. Before the announcement, Novell's shares were trading at \$24.00. As of March 31st, Novell's stock had dropped approximately 24% or \$1.8 billion in market value and reduce the price of WordPerfect to \$1 billion.
- (c) Novell's trailing twelve months P/E ratio is negative due to the \$321 million charge related primarily to the acquisition of USL. Excluding the charge, Novell's trailing twelve month net income was \$284 million, or \$0.87 per share, up 6% from net income of \$268 million in the prior year. Adjusted P/E ratio = 20.1x.
- (d) Lotus closed the quarter up 200% from the 52 week low of \$23.50 and down 18% from the high of \$80.50. Since June 30, 1993, Lotus has released new versions of SmartSuite, 1-2-3 for Windows, and Notes.
- (e) Novell will not assume any liability in connection with Lotus's copyright infringement suit against Borland and its Quattro Pro spreadsheet. Analysts have estimated the damages to range from \$30 million to \$100 million.
- (f) Borland's stock has increased 11% since the announcement that Novell is purchasing their spreadsheet business.
- (g) Excluding the Stac litigation charge, Microsoft's net income growth was 38%.
- Not meaningful

INDUSTRY REVIEW

INDUSTRY REVIEW

Software Company Metrics (in millions)

	Adobe 2/25/94	Aldus 12/31/93	Artisoft 12/31/93	Autodesk 1/31/94	BMC 12/31/93	Banyan 12/31/93
Income statement						
Most recent quarter						
Net revenues	\$81	\$57	\$21	\$102	\$76	\$33
Net income (loss)	15	5	3	15	23	3
EPS	0.32	0.34	0.21	0.63	0.89	0.17
Trailing twelve months						
Net revenues	\$326	\$207	\$80	\$406	\$274	\$128
Net income (loss)	57	10	9	62	81	13
EPS	1.20	0.70	0.51	2.50	3.11	0.70
Net income (loss) as a % of net revenues	17%	5%	11%	15%	30%	10%
Balance sheet						
Cash						
Cash	\$239	\$73	\$23	\$159	\$58	\$55 (c)
Other current assets						
Other current assets	72	50	27	104	72	34
Other assets						
Other assets	48	54	23	119	268	33
	<u>\$359</u>	<u>\$177</u>	<u>\$73</u>	<u>\$382</u>	<u>\$398</u>	<u>\$122</u>
Liabilities						
Equity						
Equity	\$61	\$35	\$9	\$93	\$134	\$43
	<u>298</u>	<u>142</u>	<u>64</u>	<u>289</u>	<u>264</u>	<u>79</u>
	<u>\$359</u>	<u>\$177</u>	<u>\$73</u>	<u>\$382</u>	<u>\$398</u>	<u>\$122</u>
Other data						
Closing stock price (March 31, 1994)	\$24.25	\$26.63	\$19.50	\$58.00	\$61.75	\$16.50
Common shares outstanding (in millions)	47 (a)	14 (a)	15	25 (b)	26	19 (d)
Market value (in millions)	\$1,140	\$373	\$293	\$1,450	\$1,606	\$314
Price/revenues ratio						
Price/revenues ratio	3.5x	1.8x	3.7x	3.6x	5.9x	2.5x
Price/earnings ratio - trailing twelve						
Price/earnings ratio - trailing twelve	20.1x	37.8x	38.4x	23.2x	19.8x	23.6x
Price/earnings ratio - future 4 qtrs.						
Price/earnings ratio - future 4 qtrs.	16.2x	20.3x	13.8x	19.1x	15.4x	17.6x
Avg headcount (most recent disclosure)						
Avg headcount (most recent disclosure)	943	980	313	1,419	846	670
Net revenues/employee						
Net revenues/employee	\$345,889	\$211,000	\$255,799	\$285,832	\$323,877	\$190,701
Book value per share						
Book value per share	\$6.34	\$10.14	\$4.27	\$11.56	\$10.15	\$4.16
Price/book value ratio						
Price/book value ratio	3.8x	2.6x	4.6x	5.0x	6.1x	4.0x
Growth statistics (over comparable quarter):						
Revenue						
Revenue	19%	25%	(11%)	4%	16%	7%
Research and development						
Research and development	12%	23%	39%	6%	16%	18%
Sales and marketing						
Sales and marketing	25%	19%	(2%)	11%	3%	17%
General and administrative						
General and administrative	9%	15%	(3%)	(9%)	5%	1%
Net income						
Net income	(3%)	141%	(8%)	37%	34%	10%

- (a) Adobe will buy Aldus for stock with an indicated value of \$515.8 million, or \$37.375 per share. As of March 31st, Adobe's stock had dropped 28% to \$24.25, while Aldus's stock closed up 4% at \$26.625.
- (b) On January 11, 1994, Autodesk's Board approved the repurchase of up to two million shares of the company's common stock. Since the program's inception in December 1991, three million shares have been repurchased for \$104 million.
- (c) Banyan has entered into a definitive agreement to acquire the stock of Beyond (an enterprise-wide messaging vendor) for \$17.5 million in cash. According to Banyan, a substantial portion of the acquisition costs will be allocated to purchased research and development and will result in a one-time after-tax charge of approximately \$11 million.
- (d) Banyan's Board of Directors has authorized the company to repurchase up to 1 million of its 19 million common shares outstanding.

INDUSTRY REVIEW

Software Company Metrics (Continued)

(in millions)

Income statement	Computer					
	Assoc. 12/31/93	Informix 12/31/93	Inuit 12/31/93	Legent 12/31/93	Oracle 2/28/94	Platinum 12/31/93
Most recent quarter						
Net revenues	\$502	\$101	\$60	\$115	\$483	\$17
Net income (loss)	81	18	(167)	18	70	(7)
EPS	0.48	0.27	(13.00) (b)	0.53	0.24	(0.57)
Trailing twelve months						
Net revenues	\$1,982	\$353 (a)	\$148	\$440	\$1,806	\$58
Net income (loss)	298	56	(163)	49	238	(22) (d)
EPS	1.75	0.82	(14.03)	1.42	0.92	(1.64)
Net income (loss) as a % of net revenues	15%	16%	(110%)	11%	13%	(38%)
Balance sheet						
Cash	\$289	\$144	\$99	\$111	\$323	\$29
Other current assets	560	125	35	234	516	24
Other assets	1,477	58	140	264	490	21
	<u>\$2,326</u>	<u>\$327</u>	<u>\$274</u>	<u>\$609</u>	<u>\$1,329</u>	<u>\$74</u>
Liabilities	\$1,229	\$120	\$93	\$228	\$675	\$17
Equity	1,097	207	181	381	654	57
	<u>\$2,326</u>	<u>\$327</u>	<u>\$274</u>	<u>\$609</u>	<u>\$1,329</u>	<u>\$74</u>
Other data						
Closing stock price (March 31, 1994)	\$30.88	\$20.75	\$36.38	\$25.50	\$32.13	\$11.50
Common shares outstanding (in millions)	168	68	13	34	296	12
Market value (in millions)	\$5,187	\$1,411	\$473	\$867	\$9,509	\$138
Price/revenues ratio	2.6x	4.0x	3.2x	2.0x	5.3x	2.4x
Price/earnings ratio - trailing twelve	17.6x	25.2x	-	18.0x	34.8x	-
Price/earnings ratio - future 4 qtrs.	11.8x	19.2x	26.0x	11.9x	29.7x	24.0x
Avg headcount (most recent disclosure)	7,300	1,283	541	2,250	8,704	207
Net revenues/employee	\$271,536	\$275,078	\$273,845	\$195,635	\$207,448	\$279,444
Book value per share	\$6.53	\$3.04	\$13.92	\$11.21	\$2.21	\$4.75
Price/book value ratio	4.7x	6.8x	2.6x	2.3x	14.5x	2.4x
Growth statistics (over comparable quarter):						
Revenue	0%	6%	81%	(2%)	30%	128%
Research and development	1%	18%	217%	1%	27%	299%
Sales and marketing	0%	7%	89%	(4%)	15%	128%
General and administrative	n/a	(22%)	63%	28%	0%	129%
Net income	1%	(19%)	(5543%)	(4%)	139% (c)	(1150%)

- (a) Excluding two unusual events from 1992 (a contract and a litigation settlement), Informix's 1993 revenues, pretax profit, and net income increased year over year by 35%, 64%, and 31%, respectively. The dramatic drop from pretax profit to net income was due to the utilization of net operating loss carryforwards recognized at the end of 1992.
- (b) On December 12, 1993 Inuit purchased ChipSoft for \$306 million. Results for the quarter ended December 31, 1993 included a charge for purchased research and development of \$151 million and other merger related costs of \$31 million. Excluding the \$182 million of merger-related charges which were incurred in the ChipSoft acquisition, Inuit's net income per share increased 103% from year to year.
- (c) Oracle's comparable quarter of the prior year includes a \$24 million litigation charge. Excluding this non-recurring charge, net income for the period increased 56%.
- (d) During the quarter, Platinum reported a one-time charge of \$8 million associated with purchased research and development from the acquisition of Lotzof & Associates, a privately-held systems integrators and software development firm. This one-time charge, coupled with revenue shortfalls and higher than expected operating expenses, drastically impacted net income.
- Not meaningful.

INDUSTRY REVIEW

Software Company Metrics (Continued) (in millions)

Income statement	Software					
	Poweroft 12/31/93	Publishing 12/31/93	(a) Sterling 12/31/93	Sybase 12/31/93	Symantec 12/31/93	
Most recent quarter						
Net revenues		\$20	\$23	\$109	\$138	\$67
Net income (loss)		3	0	11	18	(9)
EPS		0.26	0.03	0.45	0.34	0.31
Trailing twelve months						
Net revenues		\$51	\$90	\$422	\$427 (c)	\$236
Net income (loss)		8	(38) (b)	(30) (c)	44	(15)
EPS		0.77	(3.07)	(1.68)	0.86	(0.36)
Net income (loss) as a % of net revenues		16%	(42%)	(7%)	10%	(6%)
Balance sheet						
Cash		\$42	\$54	\$79	\$107	\$47
Other current assets		20	22	135	114	68
Other assets		4	9	195	74	38
		<u>\$66</u>	<u>\$85</u>	<u>\$409</u>	<u>\$295</u>	<u>\$153</u>
Liabilities		\$16	\$50	\$292	\$130	\$83
Equity		50	35	117	165	70
		<u>\$66</u>	<u>\$85</u>	<u>\$409</u>	<u>\$295</u>	<u>\$153</u>
Other data						
Closing stock price (March 31, 1994)		\$55.00	\$6.50	\$28.88	\$45.00	\$15.63
Common shares outstanding (in millions)		11	12	18	52 (f)	30 (g)
Market value (in millions)		\$605	\$78	\$520	\$2,340	\$469
Price/revenues ratio		11.9x	0.9x	1.2x	5.5x	2.0x
Price/earnings ratio - trailing twelve		71.6x	-	-	52.5x	-
Price/earnings ratio - future 4 yrs.		47.4x	38.2x	12.7x	35.2x	18.0x
Avg headcount (most recent disclosure)		3,663	588	2,475	1,348	1,049
Net revenues/employee		\$13,915	\$153,895	\$170,467	\$316,542	\$224,520
Book value per share		\$4.55	\$2.92	\$6.50	\$3.17	\$2.33
Price/book value ratio		12.1x	2.2x	4.4x	14.2x	6.7x
Growth statistics (over comparable quarter):						
Revenue		143%	(38%)	10%	66%	38%
Research and development		117%	(36%)	19%	60%	7%
Sales and marketing		138%	(26%)	(5%)	69%	11%
General and administrative		139%	(37%)	n/a	54%	n/a
Net income		29%	(91%)	468% (d)	66%	(125%)

- (a) Software Publishing will lay off half of its 480 employees over the next 90 days, take a restructuring charge of \$9 million and report a substantial drop in sales for its fiscal second quarter ended March 31, 1994. The company expects revenue of \$14 million for its fiscal second quarter, compared with revenue of \$43 million in the same quarter a year-ago.
- (b) Software Publishing's net loss for the trailing twelve months includes a \$20 million restructuring charge related to excess facilities and workforce reductions.
- (c) Included in Sterling's net loss for the trailing twelve months is a \$91 million charge related to the July 1993 acquisition of Systems Center.
- (d) Excluding a 1992 change in accounting principle of \$3 million, Sterling's net income increased 119%.
- (e) Sybase's 1993 revenues increased 61%, reaching record net sales of \$427 million, while net income was up 86% to \$44 million. North American revenues were up 50% to \$305 million and international revenues surged 99% to \$122 million (\$95 million was attributable to Europe).
- (f) In November 1993, Sybase had a 2 for 1 stock split. Shares closed at \$45.00 on March 31, 1994 (down from a 52 week high of \$51 1/4 and up from a low of \$25 3/8).
- (g) Symantec reached an agreement to purchase Central Point Software, one of its biggest rivals for \$64 million in stock. Privately-held Central Point posted sales of roughly \$80 million last year, about one-third the size of Symantec.
- Not meaningful.

Hardware Company Metrics

(in millions)

	AT&T 12/31/93	Apple 12/31/93	Compaq 12/31/93	DEC 1/1/94	Dell 1/30/94
Income statement					
Most recent quarter					
Net revenues	\$18,459	\$2,469	\$2,202	\$3,254	\$743 (e)
Net income (loss)	962	40	151	(72)	16
EPS	0.72	0.34	1.73	(0.53)	0.39
Trailing twelve months					
Net revenues	\$67,156	\$8,446	\$7,192 (d)	\$13,637	\$2,873 (f)
Net income (loss)	(2,545) (a)	(35) (c)	462	(72)	(40)
EPS	(1.88)	(0.30)	5.45	(0.54)	(1.01)
Net income (loss) as a % of net revenues	(4%)	(0%)	6%	(1%)	(1%)
Balance sheet					
Cash					
Cash	\$798	\$1,123	\$419	\$1,147	\$337
Other current assets	27,395	3,085	2,566	5,152	711
Other assets	31,260	834	794	4,070	92
	<u>\$59,453</u>	<u>\$5,042</u>	<u>\$3,779</u>	<u>\$10,369</u>	<u>\$1,140</u>
Liabilities					
Equity	\$45,055	\$2,989	\$1,381	\$5,539	\$669
	<u>14,398</u>	<u>2,053</u>	<u>2,398</u>	<u>4,830</u>	<u>471</u>
	<u>\$59,453</u>	<u>\$5,042</u>	<u>\$3,779</u>	<u>\$10,369</u>	<u>\$1,140</u>
Other data					
Closing stock price (March 31, 1994)	\$51.25	\$33.25	\$97.88	\$29.63	\$25.25
Common shares outstanding (in millions)	1,357 (b)	117	87	136	40
Market value (in millions)	\$69,546	\$3,890	\$8,515	\$4,029	\$1,010
Price/revenues ratio					
Price/revenues ratio	1.0x	0.5x	1.2x	0.3x	0.4x
Price/earnings ratio - trailing twelve					
Price/earnings ratio - trailing twelve	-	-	18.0x	-	-
Price/earnings ratio - future 4 qtrs.					
Price/earnings ratio - future 4 qtrs.	15.2x	11.3x	13.4x	29.3x	11.5x
Avg headcount (most recent disclosure)					
Avg headcount	312,700	11,963	10,921	104,000	3,810
Net revenues/employee					
Net revenues/employee	\$214,762	\$705,970	\$658,540	\$131,122	\$754,112
Book value per share					
Book value per share	\$10.61	\$17.55	\$27.56	\$35.51	\$11.78
Price/book value ratio					
Price/book value ratio	4.8x	1.9x	3.6x	0.8x	2.1x
Growth statistics (over comparable quarter):					
Revenue					
Revenue	5%	23%	55%	(12%)	20%
Research and development					
Research and development	6%	(5%)	10%	(18%)	26%
Sales and marketing					
Sales and marketing	10%	(9%)	29%	(23%)	34%
General and administrative					
General and administrative	n/a	n/a	n/a	n/a	31%
Net income					
Net income	(2%)	(75%)	24%	2%	(50%)

- (a) AT&T's net income for the trailing twelve months included an after tax charge of \$7 billion for the change in how the company accounts for postretirement benefits. The new method of accounting is not expected to have a material effect on net income in future periods.
- (b) A federal judge said AT&T has not yet persuaded him to approve its proposed acquisition of McCaw Cellular, but suggested that he still may clear the deal.
- (c) Included in Apple's trailing twelve month net income is a pre-tax charge of \$321 million, or \$1.63 per share, related to the company's latest restructuring. Exclusive of this charge, trailing twelve month net income would be \$164 million, or 69% lower than the prior year.
- (d) Compaq's sales increased 75% during the year to a record \$7.2 billion and earnings per share increased 112% to a record \$5.45. Every region enjoyed record sales. North America grew 100% to \$3.7 billion; Europe (including Eastern Europe, Middle East and Africa) grew 44% to \$2.7 billion; and other international markets (including Japan, Latin America and Pacific Rim) grew 111% to \$800 million. Worldwide unit shipments reached 3.1 million, an increase of 98% over 1992.
- (e) The sale of Dell's 486-based desktop and workstation systems increased 40% over the comparable quarter to \$596 million (80% of net sales).
- (f) Over the past two years, Dell has added nearly \$2 billion in annual revenue for an annual growth rate of 80%. For the year, Dell experienced a net loss of \$40 million. A primary reason for the loss was \$71 million in unusual charges related to restructuring provisions, inventory writedowns, and costs associated with delayed and canceled notebook projects.
- * Not meaningful.

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INDUSTRY REVIEW

Hardware Company Metrics (Continued)
(in millions)

Income statement	Hewlett	IBM	Intel	Silicon	Sun	3DO
	Packard			Graphics (d)		
	1/31/94	12/31/93	12/25/93	12/31/93	3/27/94	12/31/93
Most recent quarter						
Net revenues	\$5,682	\$19,396	\$2,389	\$370	\$1,196	\$3
Net income (loss)	368	362	594	36	57 (e)	(7)
EPS	1.42	0.62	1.35	0.24	0.60 (f)	(0.35)
Trailing twelve months						
Net revenues	\$21,426	\$62,716 (a)	\$8,782	\$1,262	\$4,548	\$6
Net income (loss)	1,285	(8,034) (b)	2,295	119	194	(44)
EPS	5.04	(14.01)	5.22	0.79	1.85	(3.00)
Net income (loss) as a % of net revenues	6%	(13%)	26%	9%	4%	(72.5%)
Balance sheet						
Cash	\$2,064	\$6,174	\$3,136	\$108	\$911	\$33
Other current assets	8,694	34,078	2,666	578	1,344	1
Other assets	6,443	43,965	5,542	365	596	8
	<u>\$17,201</u>	<u>\$84,217</u>	<u>\$11,344</u>	<u>\$1,051</u>	<u>\$2,851</u>	<u>\$42</u>
Liabilities	\$8,394	\$64,114	\$3,156	\$323	\$1,301	\$12
Equity	8,807	20,103	7,500	728	1,550	30
	<u>\$17,201</u>	<u>\$84,217</u>	<u>\$11,344</u>	<u>\$1,051</u>	<u>\$2,851</u>	<u>\$42</u>
Other data						
Closing stock price (March 31, 1994)	\$82.13	\$54.63	\$67.50	\$24.13	\$27.38	\$23.00
Common shares outstanding (in millions)	259	580	441	154	96	20
Market value (in millions)	\$21,270	\$31,683	\$29,768	\$3,715	\$2,628	\$460
Price/revenues ratio	1.0x	0.5x	3.4x	2.9x	0.6x	75.7x
Price/earnings ratio - trailing twelve	16.3x	*	12.9x	30.4x	14.8x	*
Price/earnings ratio - future 4 yrs.	13.9x	21.8x	10.6x	23.7x	11.8x	nm
Avg headcount (most recent disclosure)	94,400	278,875 (c)	20,200	20,200	13,050	13,050
Net revenues/employee	\$226,970	\$224,889	\$434,751	\$62,474	\$348,481	\$465
Book value per share	\$34.00	\$34.66	\$17.01	\$4.73	\$16.15	\$1.50
Price/book value ratio	2.4x	1.6x	4.0x	5.1x	1.7x	15.3x
Growth statistics (over comparable quarter)						
Revenue	24%	(1%)	29%	37%	5%	n/a
Research and development	17%	(20%)	22%	27%	14%	101%
Sales and marketing	5%	(59%)	9%	22%	9%	524%
General and administrative	n/a	n/a	n/a	n/a	n/a	129%
Net income	41%	107%	39%	52%	11%	(79%)

- (a) IBM's services revenue increased 32% to \$9.7 billion, while all other revenue segments suffered declines.
 (b) IBM's 1993 net loss includes restructuring charges of \$8.9 billion.
 (c) As of December 31, 1993, IBM's worldwide work force totaled approximately 256,000, a decline of 15% from year-end 1992. An additional 10,000 employees are expected to lose their jobs during the first quarter of 1994.
 (d) Chairman and founder James Clark left Silicon Graphics to start a new company which will develop software control products for interactive digital living room devices that act as both televisions and computers.
 (e) Due to an increased product mix of high-end systems, Sun's gross margin of 42.8% was the highest it has been in the last six quarters.
 (f) Sun's earnings per share were 9% below analyst estimates of 66 cents.
 * Not meaningful

INDUSTRY REVIEW

Key Relationships
(in millions)

	RR		
	Egghead 1/8/94	Merisel 12/31/94	Donnelley 12/31/93
Income statement			
Most recent quarter			
Net revenues			
Net income (loss)	\$209	\$949	\$1,310
EPS	1	12	79
Trailing twelve months	0.08	0.39	0.51
Net revenues			
Net income (loss)	\$779	\$3,086 (a)	\$4,388
EPS	2	30	109
Net income (loss) as a % of net revenues	0.12	1.00	0.71
Balance sheet			
Cash			
Other current assets	\$21	\$0 (b)	\$11
Other assets	250	860	1,099
	26	76	2,544
	<u>\$297</u>	<u>\$936</u>	<u>\$3,654</u>
Liabilities			
Equity			
	\$153	\$712	\$1,810
	144	224	1,844
	<u>\$297</u>	<u>\$936</u>	<u>\$3,654</u>
Other data			
Closing stock price (March 31, 1994)	\$8.63	\$18.13	\$28.13
Common shares outstanding (in millions)	17	31	155
Market value (in millions)	\$147	\$562	\$4,359
Price/revenues ratio	0.2x	0.2x	1.0x
Price/earnings ratio - trailing twelve	70.5x	18.1x	39.7x
Price/earnings ratio - future 4 qtrs.	35.9x	12.5x	14.1x
Avg headcount (most recent disclosure)	2,350	1,695	30,950
Net revenues/employee	\$331,514	\$1,821,098	\$141,769
Book value per share	\$8.47	\$7.23	\$11.90
Price/book value ratio	1.0x	2.5x	2.4x
Growth statistics (over comparable quarter):			
Revenue	11%	39%	8%
Sales, general, and administrative	22%	27%	13%
Net income	(75%)	58%	8%

(a) For the year ended December 31, 1993, Merisel's net sales increased 38% to \$3.1 billion, while net income increased 55% to \$30.4 million.
 (b) On January 31, 1994, Merisel completed the purchase of ComputerLand Corp.'s Franchise and Distribution Division. Revenue for this division was in excess of \$1 billion in 1993.

INDUSTRY REVIEW

Recent Software Industry Mergers and Acquisitions (in millions)

Ticker symbol	Adobe - Aldes			Electronic Arts - Broderbund		
	ADBE	ALDC	Pooling	ERTS	BROD	Pooling
	2/25/94	12/31/93		12/31/93	11/30/93	
Most recent financial statement:						
Sales	\$326	\$207	\$533	\$403	\$96	\$498
Cost of goods sold	58	41	99	215	35	251
Gross profit	268	165	433	187	60	248
Operating expenses:						
R&D	67	31	98	59	14	73
S&M	94	81	175	47	16	63
G&A	24	39	63	25	7	32
Total operating expenses	184	152	336	130	37	168
Operating income	84	14	98	57	23	80
Nonrecurring costs	0	(2)	(2)	0	0	0
Nonoperating income (expense)	6	3	9	4	1	5
Income before income taxes	90	14	104	61	24	85
Income taxes	33	4	38	18	9	28
Net income	\$57	\$10	\$66	\$43	\$15	\$58
Average shares outstanding	47		62	50		65
Earnings per share	\$1.22		\$1.06	\$0.85		\$0.88
Valuation data:						
Transaction date:		3/15/94		2/9/94		
Price (millions)		\$506		\$393		
Price/Revenues ratio		2.4		4.1		
Price/Earnings ratio		53.2		26.2		
Premium at announcement		42%		-1%		
Metrics (thousands):						
Revenue per employee	\$346	\$211		\$442	\$238	
Operating expenses per employee	\$195	\$155		\$143	\$93	

Adobe-Aldes:

- The combined entity will have a full product line spanning the publishing arena. However, an overlap will occur in illustrations.
- Aldes strengthens Adobe's presence in Europe and its position in the Windows market given the large installed base of Pagemaker for Windows users.
- Both companies will benefit from the hardware transition of the user base to the Power Mac, given the computer-intensive nature of the publishing software.

Electronic Arts - Broderbund:

- The combined company will be the largest entertainment software company.
- The merger is expected to strengthen ERTS's CD-ROM position and allow Broderbund to capitalize on ERTS's technological lead in cartridge and CD-ROM based videogames.
- Broderbund's market premium was 14% based on its stock price 2 weeks preceding the announcement.

INDUSTRY REVIEW

Recent Software Industry Mergers and Acquisitions (Continued)

(in millions)

Ticker symbol Most recent financial statement:	Intuit - ChipSoft			Novell - WordPerfect, Quattro Pro		
	INTU	CSFT	Purchase	NOVL	WordPerfect	Pooling
	9/30/93	9/30/93		1/31/94	12/31/93 (2)	
Sales	\$121	\$70	\$192	\$1,174	\$700	\$1,949
Cost of goods sold	39	16	55	238	159	397
Gross profit	82	54	137	936	541	1,552
Operating expenses:						
R&D	12	13	25	187	130	327
S&M	51	26	77	274	312	586
G&A	5	7	12	82	49	131
Total operating expenses	69	46	114	543	491	1,044
Operating income	13	9	22	393	50	508
Nonrecurring costs		(4)	(4)			
Nonoperating income (expense)	1	2	2	34	n/a	34
Income before income taxes	14	6	20	427	50	542
Income taxes	5	(1)	4	139	20	159
Net income	\$8	\$7	\$16	\$287	\$30	\$383
Average shares outstanding	11		19	314		373
Earnings per share	\$0.74		\$0.86	\$0.91		\$1.03
Valuation data:						
Transaction date:		9/1/93			3/21/94	
Price (millions)		\$234			\$1,400	
Price/Revenues ratio		3.3			2.0	
Price/Earnings ratio		31.2			46.7	
Premium at announcement		-6%			n/a	
Metrics (thousands):						
Revenue per employee	\$225	\$168		\$293	\$150	
Operating expenses per employee	\$128	\$109		\$136	\$105	

Intuit-ChipSoft:

- ChipSoft intangible assets were \$255 million which included \$150 million of purchased in-process research.
- ChipSoft's market premium was 44% based on its stock price 2 weeks prior to the announcement.
- The merger should increase awareness of tax and financial planning tools and provide recurring revenue from annual updates of tax preparation software.
- On April 7, Intuit acquired Best Program's tax division, which has an installed base of 10,000 customers, for \$6 million.

Novell:

- Novell agreed to pay 59 million shares for WordPerfect.
- Novell also agreed to pay \$145 million in cash for Quattro Pro and 1 million copies of Paradox for inclusion in the Office bundle.
- Assuming Novell paid \$35 per copy for the 1 million copies of Paradox, the company paid \$110 million for Quattro Pro business, or less than 1.5 times revenue.
- Novell share price closed at \$16 1/4 on 4/13/94, a 32% decline since announcing its acquisitions.
- WordPerfect laid off about 1,000 employees in January of 1994.

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P&L RECONCILIATION OF CHANNEL AND PRODUCT TO RESULTS OF OPERATIONS
(IN MILLIONS)

Q94-3

	Channel				Product Group			
	Actual	% Net Rev	Plan	% Net Rev	Actual	% Net Rev	Plan	% Net Rev
Net Revenue	\$1,244	100.0 %	\$1,091	100.0 %	\$1,244	100.0 %	\$1,091	100.0 %
Cost of revenue	207	16.7	186	17.1	207	16.7	186	17.1
Gross profit	1,037	83.3	905	82.9	1,037	83.3	905	82.9
Controllable expenses								
People	145	11.7	163	14.9	97	7.8	109	10.0
Facilities	77	6.2	55	5.0	49	3.9	25	2.3
Marketing	96	7.7	91	8.3	98	7.9	89	8.2
Development	4	0.3	4	0.4	28	2.2	44	4.0
Other	47	3.8	22	2.0	163	13.1	17	1.6
PSS	NA	NA	NA	NA	64	5.2	59	5.4
Total controllable expenses	369	29.6	334	30.6	499	40.1	342	31.3
Responsibility margin	668	53.7	571	52.3	538	43.2	563	51.6
Corporate allocations								
Executive	0	0.0	0	0.0	0	0.0	0	0.0
Corporate F&A	33	2.6	35	3.2	33	2.6	35	3.2
Legal	131	10.5	17	1.6	11	0.8	17	1.6
R&D	140	11.2	165	15.1	NA	NA	NA	NA
S&M non-specific *	NA	NA	NA	NA	130	10.4	156	14.3
Other	4	0.3	2	0.2	4	0.3	2	0.2
Total corporate allocations	308	24.7	219	20.1	177	14.3	211	19.3
Total Expenses	676	54.4	552	50.6	676	54.4	552	50.6
Contribution margin	\$360	29.0 %	\$352	32.3 %	\$360	29.0 %	\$352	32.3 %

FYTD94

	Channel				Product Group			
	Actual	% Net Rev	Plan	% Net Rev	Actual	% Net Rev	Plan	% Net Rev
Net Revenue	\$3,356	100.0 %	\$3,024	100.0 %	\$3,356	100.0 %	\$3,024	100.0 %
Cost of revenue	551	16.4	515	17.0	551	16.4	515	17.0
Gross profit	2,805	83.6	2,509	83.0	2,805	83.6	2,509	83.0
Controllable expenses								
People	435	13.0	491	16.2	295	8.8	325	10.8
Facilities	169	5.0	161	5.3	84	2.5	72	2.4
Marketing	287	8.6	292	9.7	290	8.6	283	9.4
Development	10	0.3	12	0.4	81	2.4	136	4.3
Other	101	3.0	64	2.1	213	6.3	48	1.6
PSS	NA	NA	NA	NA	171	5.1	178	5.9
Total controllable expenses	1,002	29.9	1,070	33.7	1,132	33.7	1,042	34.5
Responsibility margin	1,803	53.7	1,439	49.2	1,673	49.8	1,467	48.5
Corporate allocations								
Executive	1	0.0	1	0.0	1	0.0	1	0.0
Corporate F&A	98	2.9	111	3.7	98	2.9	111	3.7
Legal	135	4.6	52	1.7	35	1.0	52	1.7
R&D	410	12.2	493	16.3	NA	NA	NA	NA
S&M non-specific *	NA	NA	NA	NA	399	11.9	471	15.6
Other	21	0.6	9	0.3	21	0.6	9	0.3
Total corporate allocations	684	20.4	667	22.0	556	16.5	643	21.3
Total Expenses	1,687	50.3	1,687	55.8	1,687	50.3	1,687	55.8
Contribution margin	\$1,119	33.3 %	\$873	27.2 %	\$1,119	33.4 %	\$873	27.2 %

* S&M non-specific is, in general, S&M people and facilities less PSS.

REVENUE SUMMARY ANALYSIS

Reading and interpreting the revenue summary: This report provides a summary view of MS's revenue, associated licenses, and resulting revenue per license. Given the size, multiple sources and complexity of MS's revenue, there are limitations to the conclusions which can be drawn from such highly summarized data. The explanation below may help the reader better understand this data and its relationship to other information presented in this report.

Revenue Summary Categories:

- Lines on the Revenue Summary provide essentially a product unit level view of revenue. Exceptions to this general rule are:
 - ◆ MS Office is further segregated by environment (Windows versus Mac) to give greater visibility to this key Desktop Application product.
 - ◆ The Advanced Systems BU is shown in groups of product families, to provide increased visibility to several key strategic products in this area, including Windows NT and NTAS.
- Revenue Summary principally details software products sold through the finished goods channels, since they are the most complex in terms of:
 - ◆ the number of different products sold,
 - ◆ the variety of ways in which products are sold (full packaged product, competitive upgrades, version upgrades, maintenance, license packs, Select agreements) and
 - ◆ the range of prices of these various product offerings.
- Revenue generated from sales of items such as books, promotional copies of software, manuals and raw materials, is aggregated separately in the line entitled "Other materials", just below the "Finished Goods Revenue" subtotal. These items' prices can differ significantly from those of MS's software products, and are segregated because of their potential to distort Revenue per License calculations.
- OEM Revenue is included at the bottom of the report in a single line.

Bundling:

- The Revenue Summary views products in the ways in which they are sold. For example, Excel is sold both as a stand-alone product and as part of various "bundled" products, principally MS Office. On the Revenue Summary Report, only sales of stand-alone Excel are included in the Excel PU lines. Note that this phenomenon sometimes crosses Product Division lines, as sales of MS Mail sold via the Office and Office Pro bundles will be shown in the Desktop Applications Division section, while stand-alone sales of MS Mail will be shown in the Workgroup BU line.
- Revenue figures shown in the various Product sections of this report include sales of those products, regardless of the vehicle through which they are sold. In other words, Excel revenue shown throughout the Product sections will include sales of both stand-alone Excel and an attribution of sales from MS Office, MS Office Pro, Excel/Word bundles, and any other bundled products of which Excel is a component.

REVENUE SUMMARY ANALYSIS

Mix Issues:

- As stated above, the Revenue Summary report is basically a Product Unit/Business Unit level view. This can differ from the views of various products presented in the Finished Goods Top Products listings shown in the Channel sections which display revenue of specific product families. For example, while the Finished Goods Top Products listings show revenue of the Excel family, the Excel PU line of the Revenue Summary includes several product families in addition to Excel, such as Multiplan.
- Revenue figures shown in the Finished Goods Top Products listings do not include maintenance revenues, unlike the Revenue Summary. Because the nature of the revenue stream generated by the company's maintenance products is substantially different from that generated by the sale of other software licenses, combining it with these other revenue can distort pricing comparisons.
- Below is a reconciliation between the WW Finished Goods figures shown on the Revenue Summary Report for the Excel PU and the Finished Goods Top Products listing for Win Excel, which may illustrate some of the differences between these views:

Family	Environment	Type	Revenues	Licenses	Rev/Lic
Excel New User:					
Excel	Windows	Full Packaged Product	\$109	394	\$276
		License packs	31	135	232
		Competitive Upgrade	30	252	121
		Academic	15	189	78
		Select	6	35	168
		Special Agreements	3	28	96
		OEM Packaged Prod	1	12	114
Total Win Excel New User per Finished Goods Top Products			\$195	1,045	\$187
Excel	Mac	New User	\$27	161	\$165
Multiplan	MS-DOS	New User	2	14	160
Excel	PM & OS/2	New User	1	5	250
Total Excel PU New User per Revenue Summary			\$225	1,225	\$184
Excel Existing User:					
Excel	Windows	Version Upg (Box)	\$46	867	\$53
		Version Upg (License)	3	36	78
		Version Upg (Select)	0	4	79
		Version Upg (Spec Agree)	0	1	84
Total Win Excel Existing User per Finished Goods Top Products			\$49	907	\$54
Excel	Windows	Maintenance	\$4	128	\$27
Excel	Windows	Select Maintenance	0	4	37
Excel	Mac	Existing User	7	81	87
Multiplan	MS-DOS	Existing User	0	1	97
Excel	PM & OS/2	Existing User	0	10	10
Total Excel PU Existing User per Revenue Summary			\$60	1,130	\$53

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Supplemental Information

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REVENUE SUMMARY ANALYSIS

REVENUE SUMMARY ANALYSIS
(REVENUE IN MILLIONS, UNITS IN THOUSANDS)

Q94-3

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	274	181	51%	860	579	49%	\$319	\$313	2%
MAC Office	20	21	(6%)	60	60	(0%)	331	351	(6%)
Excel PU *	104	91	15%	580	546	6%	180	166	9%
Word PU *	67	97	(31%)	468	578	(19%)	142	167	(15%)
Graphics PU *	12	11	4%	77	69	12%	152	165	(8%)
Project PU	24	31	(25%)	68	99	(31%)	345	314	10%
DAD BU New Users **	<u>500</u>	<u>432</u>	16%	<u>2,114</u>	<u>1,932</u>	9%	237	224	6%
WIN Office	53	28	91%	364	153	139%	147	184	(20%)
MAC Office	4	5	(23%)	35	19	85%	105	253	(59%)
Excel PU *	42	40	5%	857	548	56%	49	73	(33%)
Word PU *	28	30	(8%)	298	321	(7%)	93	94	(1%)
Graphics PU *	2	3	(49%)	263	237	11%	7	15	(54%)
Project PU	1	4	(75%)	10	38	(73%)	102	110	(7%)
DAD BU Existing Users **	<u>130</u>	<u>110</u>	17%	<u>1,827</u>	<u>1,315</u>	39%	71	84	(16%)
Basic PU	17	14	21%	111	95	17%	150	145	3%
Database Mgmt (Access) PU *	25	46	(45%)	180	257	(30%)	140	179	(22%)
Fox Database PU *	14	25	(45%)	116	124	(7%)	120	204	(41%)
Languages PU's	21	23	(10%)	117	109	8%	181	216	(16%)
DDT BU *	<u>77</u>	<u>108</u>	(29%)	<u>524</u>	<u>585</u>	(10%)	147	185	(21%)
Entry PU	17	19	(8%)	555	430	29%	31	43	(29%)
Multimedia Publishing PU	22	6	259%	382	110	245%	57	55	4%
Works PU	24	29	(17%)	375	401	(7%)	63	72	(11%)
Consumer BU	<u>63</u>	<u>53</u>	17%	<u>1,312</u>	<u>941</u>	39%	48	57	(16%)
Hardware BU	36	42	(12%)	683	602	13%	53	69	(23%)
MS-DOS BU	3	25	(86%)	118	516	(77%)	29	48	(40%)
Windows BU	<u>80</u>	<u>44</u>	84%	<u>1,531</u>	<u>672</u>	128%	53	65	(19%)
Win NT Family	1	38	(96%)	4	186	(98%)	373	207	81%
Win NT Adv. Server Family	8	13	(38%)	12	15	(22%)	707	883	(20%)
Win NT Server (SQL, SNA)	8	10	(18%)	11	9	29%	750	1,176	(36%)
Other Operating Systems PU	7	4	88%	26	11	128%	276	335	(17%)
Advanced Systems BU	<u>25</u>	<u>65</u>	(62%)	<u>52</u>	<u>220</u>	(76%)	479	297	61%
Workgroup BU *	16	14	12%	380	173	119%	41	80	(49%)
Digital Office Systems PU's	0	2	(94%)	2	21	(93%)	92	110	(16%)
ACT and APD PU's	1	3	(77%)	49	83	(41%)	16	41	(61%)
Other PU's	4	5	(15%)	25	48	(49%)	171	102	66%
Other	<u>5</u>	<u>11</u>	(52%)	<u>75</u>	<u>152</u>	(51%)	69	70	(2%)
Finished goods revenue	935	904	3%	8,616	7,110	21%	109	127	(15%)
Other materials	27	0	n/a	420	0	n/a			
Total FG gross revenue	<u>962</u>	<u>904</u>	6%	<u>9,036</u>	<u>7,110</u>	27%			
Press	8	8	(1%)						
OEM gross revenue	343	204	68%						
Revenue adjustments	<u>1691</u>	<u>(26)</u>	169%						
Net revenue	<u>\$1,244</u>	<u>\$1,091</u>	14%						

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

Note: The Office revenue related to the Office Guarantee Program is included in the detail and the deferral amount is then pulled out through the revenue adjustments line.

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REVENUE SUMMARY ANALYSIS

REVENUE SUMMARY ANALYSIS
(REVENUE IN MILLIONS, UNITS IN THOUSANDS)

FYTD94

	Revenue			Licenses			Revenue per License		
	Actual	Plan	% Var	Actual	Plan	% Var	Actual	Plan	% Var
WIN Office	689	489	41%	2,032	1,518	34%	5339	5322	5%
MAC Office	61	55	11%	174	154	12%	351	355	(1%)
Excel PU*	225	224	1%	1,225	1,300	(6%)	184	172	7%
Word PU*	248	286	(13%)	1,629	1,667	(2%)	152	171	(11%)
Graphics PU*	27	27	0%	179	165	8%	154	166	(7%)
Project PU	68	71	(4%)	204	227	(10%)	332	312	6%
DAD BU New Users**	<u>1,318</u>	<u>1,152</u>	14%	<u>5,442</u>	<u>5,030</u>	8%	242	229	6%
WIN Office	115	70	65%	777	363	114%	148	192	(23%)
MAC Office	8	11	(21%)	73	43	71%	115	250	(54%)
Excel PU*	60	86	(31%)	1,130	1,220	(7%)	53	71	(26%)
Word PU*	87	100	(13%)	977	1,066	(8%)	89	94	(5%)
Graphics PU*	4	6	(39%)	296	345	(14%)	12	17	(29%)
Project PU	7	7	(55%)	47	76	(38%)	70	95	(27%)
DAD BU Existing Users**	<u>277</u>	<u>280</u>	(1%)	<u>3,300</u>	<u>3,111</u>	6%	84	90	(7%)
Basic PU	51	42	22%	379	294	29%	135	142	(5%)
Database Mgmt (Access) PU*	73	101	(28%)	484	536	(10%)	151	189	(20%)
Fox Database PU*	45	80	(45%)	311	401	(22%)	143	201	(29%)
Languages PUs	55	54	1%	342	282	21%	160	191	(16%)
DDT BU*	<u>223</u>	<u>277</u>	(20%)	<u>1,516</u>	<u>1,513</u>	0%	147	183	(20%)
Entry PU	82	59	40%	2,339	1,419	65%	35	41	(15%)
Multimedia Publishing PU	47	19	153%	828	324	156%	57	58	(1%)
Works PU	69	77	(10%)	1,149	1,067	8%	60	72	(16%)
Consumer BU	<u>198</u>	<u>154</u>	29%	<u>4,316</u>	<u>2,809</u>	54%	46	55	(16%)
Hardware BU	<u>111</u>	<u>134</u>	(17%)	<u>1,931</u>	<u>1,895</u>	2%	58	71	(18%)
MS-DOS BU	47	89	(47%)	1,328	1,791	(26%)	35	49	(29%)
Windows BU	<u>205</u>	<u>141</u>	46%	<u>3,708</u>	<u>2,163</u>	71%	55	65	(15%)
Win NT Family	26	120	(78%)	120	574	(79%)	215	209	3%
Win NT Adv. Server Family	20	32	(35%)	30	42	(28%)	682	760	(10%)
Win NT Server (SQL, SNA)	19	30	(37%)	75	30	145%	249	976	(74%)
Other Operating Systems PU	26	17	58%	108	71	52%	242	233	4%
Advanced Systems BU	91	198	(54%)	331	717	(54%)	273	275	(1%)
Workgroup BU*	<u>46</u>	<u>41</u>	11%	<u>1,191</u>	<u>550</u>	116%	38	75	(49%)
Digital Office Systems PUs	1	7	(86%)	10	66	(85%)	103	110	(7%)
ACT and APD PUs	6	11	(43%)	298	289	3%	20	37	(45%)
Other PUs	8	12	(32%)	33	118	(72%)	238	100	139%
Other	<u>15</u>	<u>30</u>	(50%)	<u>341</u>	<u>472</u>	(28%)	44	63	(30%)
Finished goods revenue	2,532	2,494	2%	23,406	20,051	17%	108	124	(13%)
Other materials	78	0	n/a	2,371	0	n/a			
Total FG gross revenue	<u>2,609</u>	<u>2,494</u>	5%	<u>25,776</u>	<u>20,051</u>	29%			
Press	22	22	(1%)						
OEM gross revenue	830	579	43%						
Revenue adjustments	<u>(106)</u>	<u>(71)</u>	49%						
Net revenue	<u>\$3,356</u>	<u>\$3,024</u>	11%						

* excludes allocation from sales of Office bundles

** includes database and MS Mail products sold through Office bundles

Note: The Office revenue related to the Office Guarantee Program is included in the detail and the deferral amount is then pulled out through the revenue adjustments line.

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Supplemental Information

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SUPPLEMENTAL INFORMATION
Abbreviations, Acronyms and Terms

ACT	Advanced Consumer Technology	MLP	Microsoft License Pack
AIME	Africa, India & Middle East	MOLP	Microsoft Open License Pack
APAC	Asia Pacific, Australia, New Zealand, Singapore, Malaysia, Thailand, SE Asia	MS	Microsoft
APD	Advanced Product Development	MSDN	Microsoft Developer Network
API	Applications Programming Interface	MSIN	Microsoft Information Network
Apps	Applications	MSN	Microsoft Support Network
AT	Advanced Technology	MSU	Microsoft University
BIDI	Bidirectional	MU	MicroUnity Systems
BU	Business Unit	NQSO	Nonqualified Stock Option
CPU	Central Processing Unit	NWN	Nationwide Wireless Network
CSA	Client Server Applications	NT	New Technology
CSI	Consumer Software, Inc.	NTAS	New Technology Advanced Server
DAD	Desktop Applications Division	OBU	Office Business Unit
DBCS	Double Type Character Set	ODBC	Open Database Connectivity
DBMS	Database Management Systems	OEM	Original Equipment Manufacturer
DDT	Database and Development Tools	OLE	Object Linking and Embedding
OFF	Domestic Focus Factory	OLS	Online Services
DK	Dorling Kindersley	OS	Operating System
DLL	Dynamic Load Library	OOS	Other Operating Systems
Domestic	Redmond, Campus North, Puerto Rico and Workgroup Canada	OSC	Operations Service Center
DOS	Disk Operating System	PC	Personal Computer
DSO	Days Sales Outstanding	PCI	Peripheral Component Interface
DSP	Delivery Service Partner	PCS	Personal Communications Service
EBIT	Earnings Before Interest & Tax	PPB	Prepaid Balance
ECU	European Currency Unit	PRC	People's Republic of China
EMS	Enterprise Messaging Server	PSS	Product Support Services
EPS	Earnings Per Share	PU	Product Unit
ERISA	Employee Retirement Income Security Act	R&D	Research and Development
ESPP	Employee Stock Purchase Plan	RM	Raw Materials
EU	Equivalent Units	ROW	Rest of World: Far East & ICON channels
F&A	Finance and Administrative	RTM	Release to Manufacturing
FG	Finished Goods	S&M	Sales and Marketing
FX	Foreign Exchange	SCO	Santa Cruz Operation
FYTD	Fiscal Year to Date	SDK	Software Developer's Kit
GAAP	Generally Accepted Accounting Principles	SEC	Securities and Exchange Commission
G&A	General and Administration	SET	Scientific and Engineering Tools
GLVR	Government Large Volume Reseller	SKU	Stock Keeping Unit (part number)
GPS	Great Plains Software	SMS	Systems Management Server (formerly Hermes)
GUI	Graphical User Interface	SMSD	Sales, Marketing and Service Division
GULP	Global Update License Pack	SNA	Standard Network Architecture
ICON	Intercontinental: Latin America, AIME & APAC regions	SP	Solutions Providers
IFF	International Focus Factory	SPA	Software Publishers Association
IFG	International Finished Goods	SPAG	Systems, Peripherals & Accessories Group (hardware)
KOEM	International Original Equipment Manufacturer	SQL	Structured Query Language
IPO	Initial Public Offering	SRP	Suggested Retail Price
IPR	Intellectual Property Rights	Sys	Systems
ISDN	Integrated Switched Digital Network	UPB	Unspecified Product Billing
ISO	Int'l Standards Organization	Upg	Upgrade
ISV	Independent Software Vendor	VGA	Video Graphics Array
ITG	Information Technology Group	VPP	Volume Purchase Program
JIT	Just-In-Time Manufacturing	WAN	Wide Area Network
LCA	Law & Corporate Affairs	WCM	World Class Manufacturing
LMZ	Lan Man 2.0Lng Languages	WW	Windows for Workgroups
LOI	Letter of Intent	WGA	Workgroup Applicators
LTD	Life to Date	Win	Windows
LVR	Large Volume Reseller	Wks	Works
MAE	Macintosh Applications Environment	WOG	Worldwide Operations Group
MCS	Microsoft Consulting Services	WPG	Worldwide Products Group
MD&L	Manufacturing, Distribution & Logistics	WRK	Workgroup
MED	Microsoft Easy Distribution	WWS	Worldwide Sales
MET	Management Expense Tracking	WSSG	Worldwide Sales & Support Group
		WW	Worldwide
		XLA	Extended License Agreement

Supplemental Information

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SURVEY

This redesigned board book reflects informal feedback we have received. Please take a moment to complete the following survey. Your responses will help us keep pace with your information needs. Detach the page, fold, staple, and drop it in the mail. Thanks.

Audience profile

	BOD	BOOP	Sr VP	VP	Mer	Finance
Product Development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Sales & Marketing & PSS	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Worldwide Operations	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Human Resources	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other: _____	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Focus: Domestic International Worldwide

'x' one box that describes your function best & one box that describes your geographic focus

How well does the information meet your needs in the following areas?

	Ineffective / Effective	Improvement suggestions:
Relating business to financial impact	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Fiduciary	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Product sales	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Product development & investments	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Industry	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
International aspects	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Channels, distribution, & customers	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Marketing	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Worldwide Operations (MD&L plus)	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Human resources related	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Stock related	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____
Overall	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	_____

Your style & our progress

	content tradeoffs & mix 0/100 50/50 100/0	
Bullets	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	Paragraphs
Text	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	Tables & charts
Tables (of numbers)	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	Trend graphs
Tables (of numbers)	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	Pie charts
Financials	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>	Business information

Please use the following indicators: 'x' = today's book, 'o' = your ideal book

Comments & additional information

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How to Receive Additional Information

As the book has become increasingly more condensed, you may find that you need additional information. Please email your requests to Lindm, Sharonal or Gregma. Your request will be acknowledged and routed to the appropriate person(s) for action.

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Supplemental Information

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