From: Barbara Ethington
Sent: Monday, January 27, 1997 3:18 PM
To: OEM Personnel Sales Communication
Subject: FW: Joachimk Value Leadership Presentation

The presentation is also available on SPIDER, located on the *Events* page, under *Presentations from Past OEM Training/Events.* The direct link is: file:\\webn\oemsales\dioem\value.ppt

It is in PowerPoint 97 format.

Barbara

——Original Message——
From: Gina Fleckenstein
Sent: Monday, January 27, 1997 12:15 PM
To: OEM Personnel Sales Communication
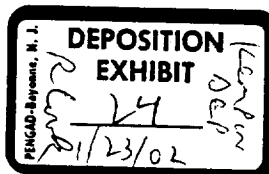Subject: Joachimk Value Leadership Presentation

Attached are the slides from the November DOEM meeting where Joachim gave his Value Leadership presentation. We have included text under each slide so please view and print off in the "Notes Pages" format.

Thanks,--Gina

Value
ChangesFinal.ppt

OEM Sales Organization Concept for the Year 2000

Joachim Kempin
Sr. Vice President
Microsoft, OEM Sales

In today's presentation, I would like to explain the reason behind some of our organizational changes in recent months and the intellectual building blocks for a new sales concept which should enable us to gain larger competitive immunity than we have ever enjoyed. After being employed with this company for nearly 14 years, I have seen a lot of competitive threats and I have been part of a team who has overcome them all. However, I have to admit 'they are really going after us' on all fronts these days and living under fire is not always fun but it keeps you alert.

They Are Really Going After Us...
Competitive Business Threats:

- ◆ NC/TCO/PC image
- ◆ Browser = OS
- ◆ New application programming model (Java)
- ◆ Erosion of application pricing/distribution model
- ◆ Windows experience erosion

In feeling the heat, we are all going to be challenged to increase our personal contributions in improving our position in the market place by fending off the competition. True threats for our business model arise as usual from potential computing paradigm shifts, which move the action away from the Windows franchise. The whole hype about the net computer, the total cost of ownership initiative and the negative image the PC has of being complicated, hard to use, very costly to own, needs to be seen in the same context. It demonstrates that the industry hasn't done it's job in delivering the right value to a changing customer base. We predicted a long time ago that the browser was just a start to attack our OS franchise. And NSCP, with it's recent announcements, is making this very clear to the world. We will face sudden death if we allow them to change our identity, meaning the user interface or the APIs, which endusers and ISVs are used to.

The next big threat we are facing is over the future application programming model. When reading the WSJ article after we announced Office 97 and finding out that they called the product "bloatware" - I had to admit that another perceived paradigm shift was being provoked. Again, we acted in good faith and with a lot of customer feedback- but you have to admit this new product is big and even if it is easier to use than the current product, it is questionable if you need all the functionality. And this is where Java comes in. A totally over hyped programming language which calls for object embedding, therefore less functionality for a core product and the ability to run add-ons as needed on every computing platform as long as an interpreter/compiler is present at runtime. There is a lot of dejay vue there, but the fact is, we need to lead a new APPS-model to find a better balance between functionality and user needs. When you combine this with the huge price erosion of the application pricing model, concern should set it. You see, Corel is selling to Packard Bell a copy for under one dollar and taking on the support burden. Now that's definitely a great model to have every time the user calls they probably lose twenty bucks and they believe that through the sales of future upgrades, where they actually share the revenue with Packard-Bell, they can make up for it later. I hope the model bankrupts them. But in the meantime, they'll definitely get a lot of press coverage and we might lose share. The last issue listed - the Windows Experience erosions, does not need additional comments and I hope by Q2 CY97, the enduser can finally experience the OS as it was originally intended and use it more safely.

This crisis means customers are listening more to competitors than to us.
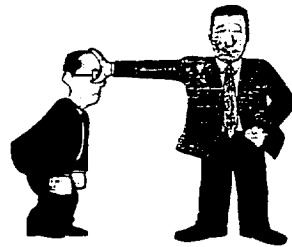
Should we all panic and be paranoid about it? Maybe a little bit. If we are too paranoid and if we panic too much, we might not be able to think clearly. But there definitely seems to be some kind of a crisis. What this really means is that customers are listening more to our competitors than to us. They're saying, "let's keep Microsoft at arms length and listen to the other side and try to find out if they have something to say which benefits us and which we can follow. We have followed Microsoft for such a long time, but we have never prospered as much as MS did." I think there's some real dangerous thinking developing here, and from that point of view I call this a big crisis.
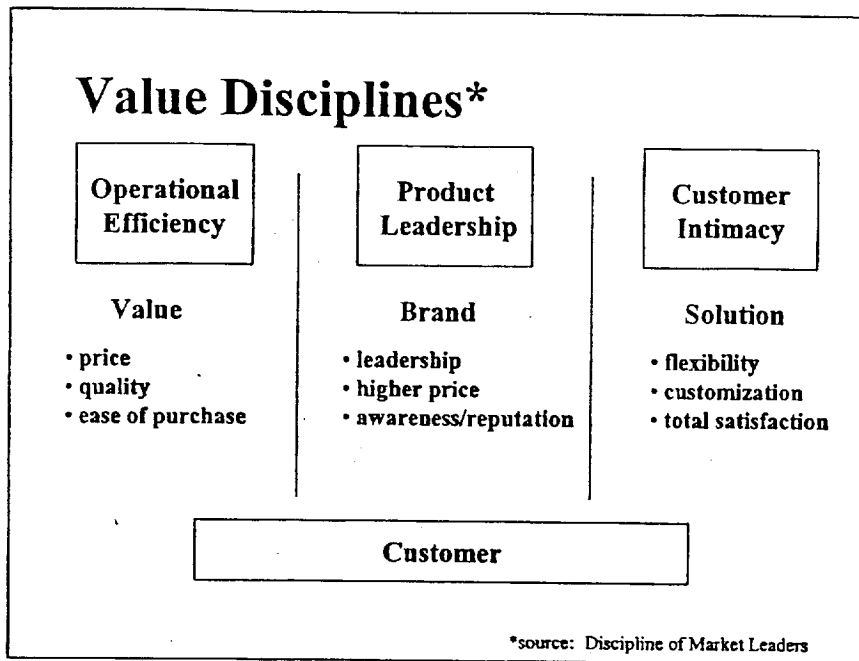
Can we win our customers hearts back?

What role can OEM play in this process?

So how can we win our customers' hearts back and what role can OEM play in this process? Despite the humorous graphic I chose, this is very serious. With this type of background let me step you through an interesting model which I found in a book titled "The Discipline of Market Leaders". I like this book because I like the first word. You know I'm German. Discipline is something which this industry can truly use.

Value Disciplines*

Operational Efficiency	Product Leadership	Customer Intimacy
Value	**Brand**	**Solution**
• price	• leadership	• flexibility
• quality	• higher price	• customization
• ease of purchase	• awareness/reputation	• total satisfaction

Customer

*source: Discipline of Market Leaders

The authors of this book have looked at a lot of companies and analyzed what type of business model these companies are using and what type of leadership positions these companies are enjoying. They found that very often you can sort leading companies into three different categories.
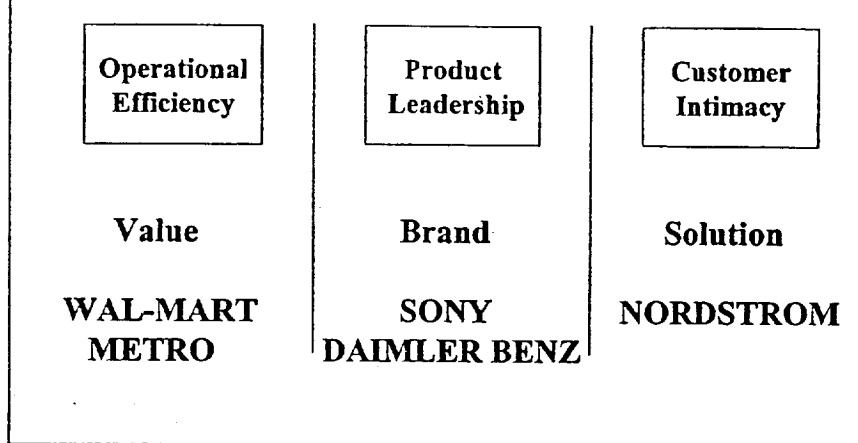
First there are companies around who really shine when it comes to the operational efficiencies. Others shine when it comes to product leadership. And the last type shines when it comes to customer intimacy. What does this mean: The first category is what we always call a **value leader**. These are super efficient companies who follow the every day best price principal. They provide consistent quality and an ease of purchase unmatched in their field. Some examples follow on the next slide.

Next there are the **product leadership** companies. Their biggest strength is their brand. We're probably working for one. They basically hold a leadership position in their product category, very often cutting-edge or perceived of being cutting-edge. They are able to charge a higher price and have a great awareness and position in the marketplace.

The third category, the **customer intimate** companies, really look out for best solutions, defined by their ultimate flexibility in working with customers. These are the companies who basically would provide a different NT version for every single OEM in the world to allow for differentiation. So, these type of companies strive on total customization and total satisfaction of the customer they're dealing with.

Successful Companies Dominate and Focus only in One Category

Operational Efficiency	Product Leadership	Customer Intimacy
Value	Brand	Solution
WAL-MART METRO	SONY DAIMLER BENZ	NORDSTROM

Examples of who these companies are: On the value side, Wal-Mart. They run the leanest shop in the distribution industry and have built a lot of stores at very convenient locations over the years! They follow a fixed margin model. It's very well known that they have a gross margin of around twenty-one percent. And even if they can take more money, they won't. Interesting concept. The customers come back knowing they will never be taken. This is typical value-based selling. They're very successful in doing this, but naturally they're very lean and mean. There are no plush offices, and I guarantee you there's no free Coke for employees either.

The other one is very well known in the Northwestern part of the USA. Nordstrom. The customer who shops at Nordstrom really believes that he gets a very good solution for his personal clothing needs. They actually send a person with the measuring tape into his house, and if needed, they will make sure that the suit is ready on time even when there's only two and a half hours notice. I personally don't like to shop there. It's not because I don't like their clothes, but I don't like to pay their prices. You see, that's the big difference between them and Wal-Mart. They deliver ultimate value for customers who can afford it. And they have no problems in taking you because you don't mind. You will still go back there and shop very happily putting convenience over other values. I'm hearing a lot of women laughing now. Hand over your credit cards right now. You can't use them anymore!

The one in the middle is the ultimate entertainment company in the world who basically sells entertainment devices, and for the last three years, entertainment content as well. Sony, the biggest, most recognized brand name I think by a factor of eight to one when it comes to television sets in every country in the world. And whenever you go in a shop and you buy a Sony, you will find that they are fifteen to twenty percent more expensive than the next brand. A lot of people buy them. Do not assume that they have better products. They might not. They are perceived of having better products. It's costing them a lot of money to keep that lead. They have to constantly create demand for their brand name. When you go shopping and you come home and you can proudly say, I bought the best I could get. That is how it feels when dealing with product leadership companies.

When you look at these examples, you recognize that none of them are from our industry. I will get to this later. When a company dominates in one category, the company has a hard time to really be on the top of any other category. Too many conflicts are the reason.

Thresholds for Success

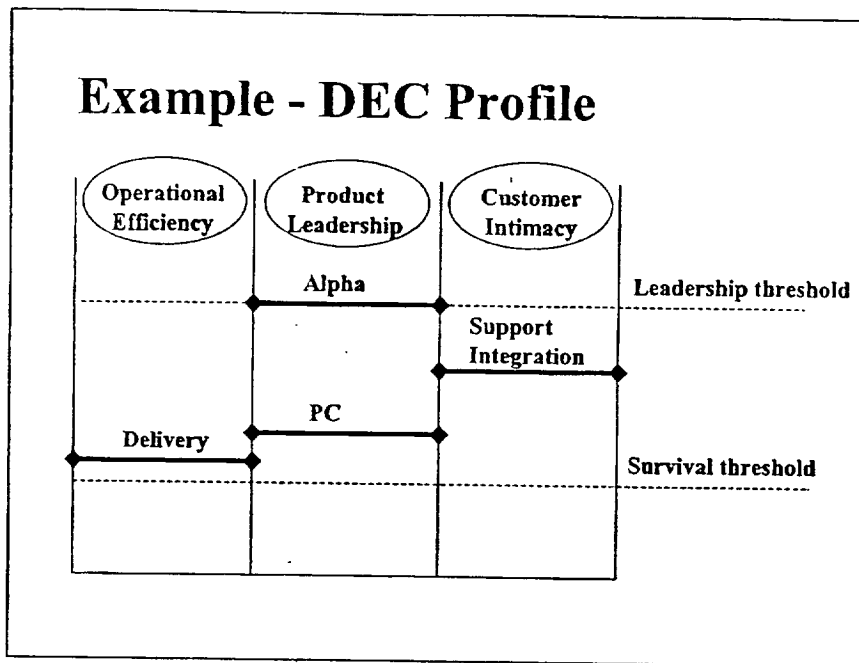| Operational Efficiency	Product Leadership	Customer Intimacy	
			Leadership threshold
			Survival threshold
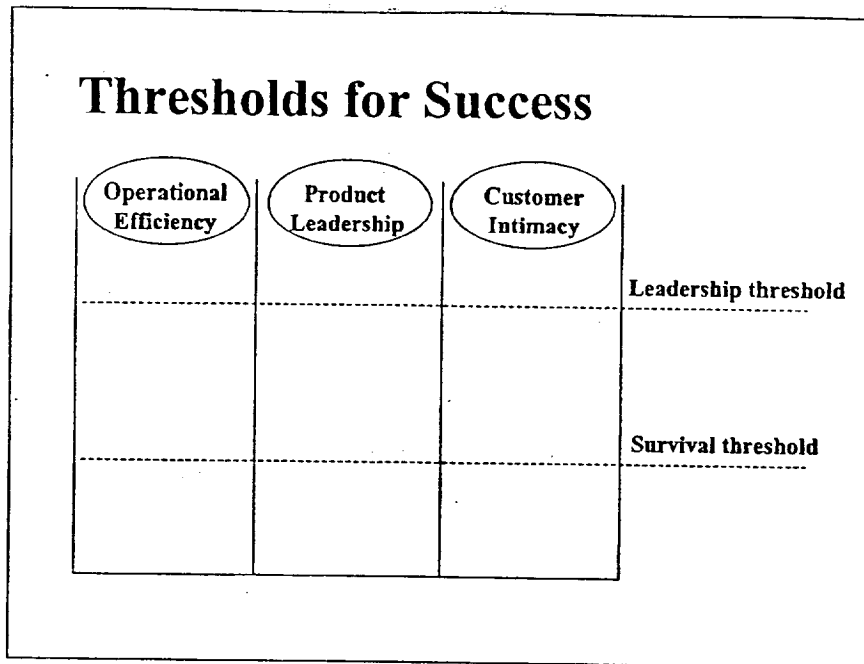
Let's explore this a little bit further. After reading this book, I came up with this theory that in these different categories, operational efficiency, product leadership, or customer intimacy, there are basically two major thresholds. One threshold is the **leadership threshold** which we just explored. The other one is what I call a **survival threshold**. It's basically the minimum a company has to do to be successful in any marketplace regardless of the leadership category they are pursuing. Take for example, Sony. If Sony would out-price itself totally by not being able to manufacture close to industry cost, they would not have product leadership the way they have it today. Their distance would be too big to another company who has operational efficiency. They couldn't make it up with their brand name and demand a price three times as high, compared to the next guy. We have seen this in the PC industry several times. When you go around and ask IS managers today how much premium they would pay for Compaq they will tell you it's in the fifteen to twenty percent range. There has to be a certain value proposition even for Compaq or Sony in order to not only be recognized as a product leader, but to actually sell product.

We can go further with this example. When you talk about customer intimacy, let's take a product leadership company, for instance, like Intel. If they would treat the customers unfairly all the time, they would have zero intimacy, and customers would stop buying from them even if other available products would be inferior. They would try hard to find alternative sources over time. Have you ever heard that before? Even product leaders have to be reasonably close and build relationships with customers without necessarily falling in love with them all the time. At a minimum, this working relationship HAS TO KEEP CUSTOMERS ENGAGED. If you make too many mistakes, these customers will listen and buy from a competitor at the next best opportunity.

Example - DEC Profile

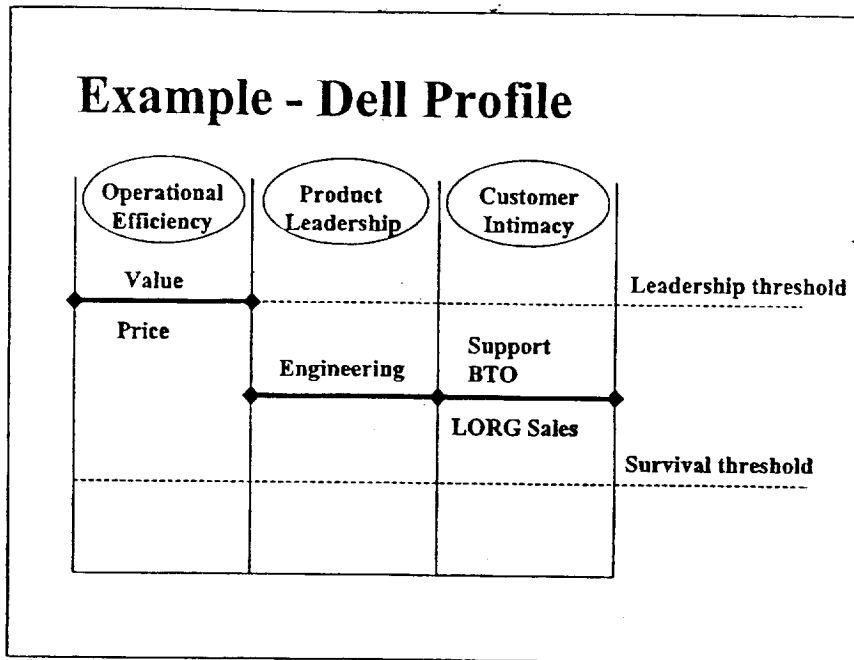| Operational Efficiency	Product Leadership	Customer Intimacy	
	Alpha		Leadership threshold
		Support Integration	
	PC		
Delivery			Survival threshold

I believe every company, even if it's a leader in a certain segment, has a certain profile in this context. Take DEC for example. DEC basically has two product lines. One is the Alpha line as we all know, and the other one is PC based. For the Alpha line, they are definitely a leader in the semiconductor CPU business. They are simply better than Intel. They deliver more bang for the buck. And they are very very good in staying ahead of technology. They have a very good reputation with a lot of customers. But when you look into their PC business, they offer "me too" products, meaning their product leadership and their brand name doesn't extend. At the same time, they have an integration business which helps them greatly. In the case of Alpha systems, they get very close to customers. On the operational efficiency side, they basically deliver on time with minimal screw ups. They have a great support organization so they're definitely above the survival threshold. So, a company like this should basically give up the PC business and focus on their core business and their core competency instead of trying to mingle around in two different markets. As of today they have never been able to expand their product leadership which they have on the Alpha side of the house to the PC side. Just think about it. The Alpha Systems are mostly sold as servers. And when you sell servers, and have the integration expertise, it's truly a shame to find out that DEC, until I think nine months ago, didn't even offer a PC server. So they never leveraged what they knew is their core competence.

If I would've written Sun on this chart, it would've looked a little different. They don't do PC business. They are clearly a product leader on the server side; there's no doubt about it. They don't do a lot of integration so they would have to come down on the customer intimacy side a little bit, but they make up by creating partnerships with ISVs and integrators. They have gone a different route and with their support being sufficient and their delivery on time, they pass the operational bar. Sun is definitely not confused—compared to DEC.

Example - Dell Profile

Operational Efficiency	Product Leadership	Customer Intimacy	
Value			Leadership threshold
Price	Engineering	Support BTO	
		LORG Sales	
			Survival threshold

Let's look at Dell's profile. You could actually argue a little bit about Dell because Dell is a company which focuses on two different sets of customers. Consumers and large organizations. Dell definitely delivers very good value to customers. Very often their PCs are in the top spot when rated in magazines. Very similar to Micron and Gateway. You know these three companies are right up there. Very price competitive and they've delivered good value over the years - even in the support area - to their customers. Therefore, they are basically being perceived as being operationally very efficient. That's the image they have in the marketplace. There's no confusion there.
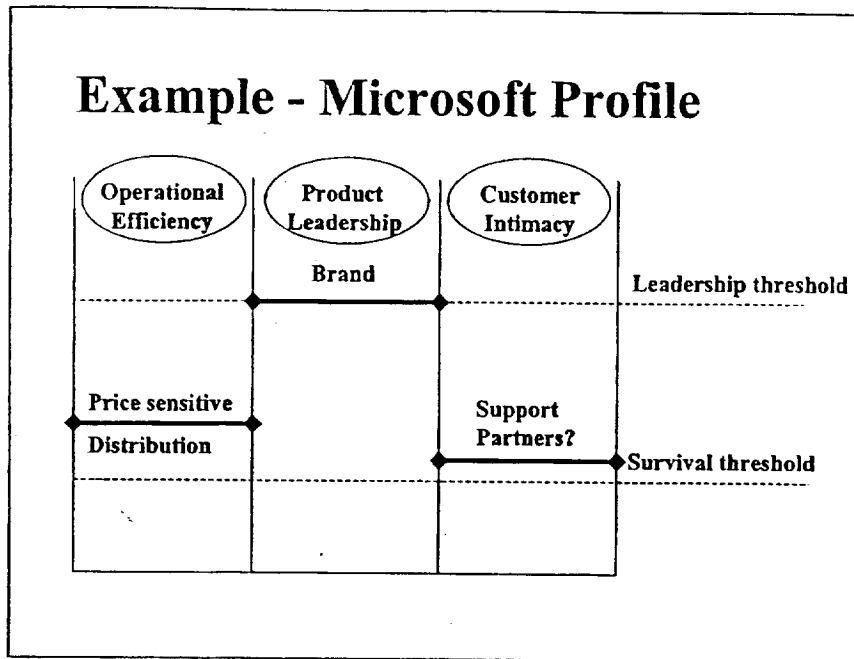
On the other side, Dell does a lot of engineering. They do server engineering, they do notebook engineering, and sometimes that has failed. But recently they have gotten their act together, and are getting over the threshold on the intimacy side by building to order. A lot of customers like that. When it comes to the large organizations, they get very intimate with their customers by loading their own internal software onto machines or preconfiguring network solutions, for instance. They really work hard to accommodate them with delivery schedules as well as onsite support. They've come a long, long way on the customer intimacy side as well.

If you would draw a Gateway profile here you would probably arrive on the operational efficiency at the same point. On the engineering side, I think they would just make it barely over the survival threshold. I actually think most of the time they're below. They have a real hard time to do that one right. They are doing this through outsourcing, but in general I would rate them lower than Dell in that category.

Build to order, when it comes to their large accounts, they have no clue what they have to do there. Not only do they have less people to serve them, but in addition they have no focus there, demonstrated by the fact that they do not differentiate their product line. So you see, depending on where a company is and how far they are beyond the threshold of the survival position, or how close as they can get to the leadership position, the more successful they are in the marketplace. When you compare the Dell with Gateway it's very obvious that Dell has been much more successful than Gateway over the last two years.

Another conclusion to draw is, there is no way you can have a leadership position in all three segments at the same time. The product leader being operational efficient means, that he has to provide best the value at any given point in time. This really means lower prices and lower margins than a product leader is accustomed to and needs for his R&D. In addition, if they would customize for every user which would basically translate for Microsoft into having to customize NT for every single user we would loose our operational efficiency. So there are lots of things you can and you can't do depending where you are in your industry position. But you can definitely always improve from the survival threshold in a meaningful way by, for example, improving relationships with your customer, or becoming more operationally efficient. Naturally, all these thresholds are relative and change constantly with competitive threats, meaning you have to try harder as time goes on!

Example - Microsoft Profile

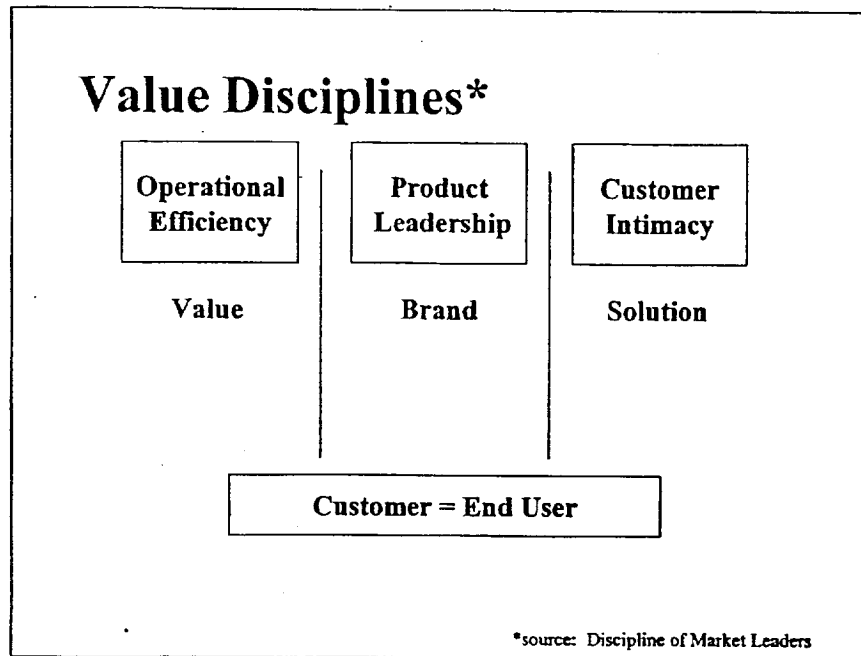| Operational Efficiency	Product Leadership	Customer Intimacy	
	Brand		Leadership threshold
Price sensitive / Distribution		Support Partners?	Survival threshold

Let's see Microsoft next. I think we all know where our main position is. We might not always have the best browser; at the moment I think we do, but hopefully on the operating system side we are perceived as having the best, even if OS/2 might be technically better today or DR- DOS once was.

On the operational efficiency side, even as a product leader, we have always been price sensitive. We have been very careful not to totally overprice our products, particularly in the finished goods area. We do provide great support to customers. So we are, as I would say on that side, above and beyond the operational threshold. If you think about Windows 95, we did build enough boxes and we did get the supply out there. We have learned these types of things as we went.

When it comes to customer intimacy, we have a longer way to go. I could stay just in the OEM arena here, but let me start with the retail channel. The people who sell our goods in the marketplace—none of them has gotten rich. They're all suffering from margin pressure. There are some people in the marketplace who say the only reason they carry us is because we are the product leader. We have the brand image and they can't afford not to carry us. So we're using that as leverage. But how close do we really work with them to improve their position? Read CRN about having Office sold to Gateway and giving VARs a disadvantage. I'm not saying they have a disadvantage, I'm saying they perceive it as one. Talk to the OEMs and think about the MDA process or the Windows 95 licensing process and all the wonderful stuff which we were able to read in the press at that point in time.
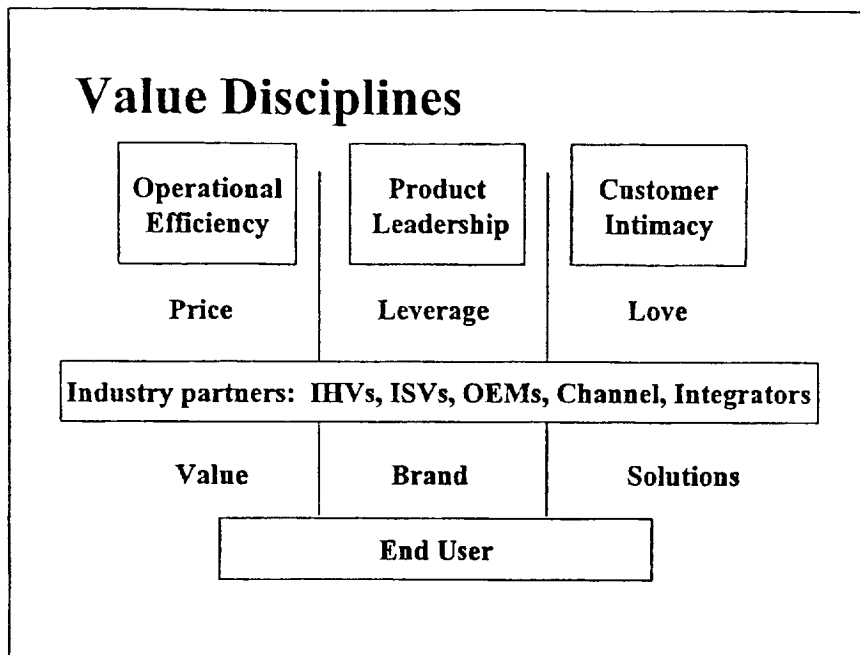
Our OEM partners, in a way, go hot and cold when it comes to us and I think the public recognizes that. The public does not necessarily believe that we are really aligned with these OEMs at all the time. So the customer intimacy area is where we can make much more progress. At the same time we are above the survival threshold. I always tell the story from when I came over here in '87. The person who was running the shop here, Mr. Harris, was sitting with a customer in a meeting. It was the second day since I arrived. He basically told the customer, looking straight into their face, "you know, we know we have an unfair advantage, and we are gonna use it." That speaks for itself in the customer intimacy part of this profile. My question is, do we have a lot of good partners? I'm not saying we don't have any. I can give you some good examples of where we have successfully partnered up over the years. But in general, our partners are not as close to us, as they could be and should be.

Value Disciplines*

Operational Efficiency	Product Leadership	Customer Intimacy
Value	Brand	Solution

Customer = End User

So let me go back to the beginning slide when we talked about the three value disciplines. The key thing to understand is that you have these three areas which companies can focus on. The other thing to understand is when companies do this right and deliver the right value for their targeted customer, they should always think first about the person who really uses the products and services, the person who ultimately pays for it. Any middle man will take second place in these considerations. The PC manufacturer might give us the money, but the real money is going to come from the person who is using that PC. Its not a large organization, it's a person with a name. Whenever companies are successful, they do understand that the end user of their product and services is the one they have to please. I call them the "Ultimate Judges" a little bit later. If you provide the right products to them, with the right value, as perceived by them, you could be a recognized leader in one of the categories.

Now the tricky part is how you deal with the middle man. Because we in OEM always deal with the middle man. We do not sell directly to that end user, we visit the PC manufacturer. Then we have the distributor and a reseller in between us and the user. I want to explore next what to do and what not to do.

Value Disciplines

Operational Efficiency	Product Leadership	Customer Intimacy
Price	Leverage	Love

Industry partners: IHVs, ISVs, OEMs, Channel, Integrators

Value	Brand	Solutions

End User

This is a little bit more OEM specific or Microsoft specific because I used typical industry partners, which we normally face. But regardless of what company you work for, you often have some middle man in between you and the Enduser. There's rarely anybody who sells directly to an end user like Gateway or Dell. The middle man has a function in the delivery chain and if used right it can improve a company's leadership position by strengthening it in areas where it is generally weak. Microsoft as an example is not a logistic leader, but our products get to endusers through our distribution partners in time and with credit, thus enhancing our operational efficiencies. True product leadership companies are the greatest demand creation machines known. Looking at our OEM model, we use partners to make it more convenient for endusers to use non-MS manufactured PCs by simply pre-loading the OS and some applications. This enhances both our positions and when we go further and help OEMs to design better PCs we improve both our values in the eyes of the enduser and our intimacy position with the OEMs. That is called full engagement and it is the hardest thing to do knowing that both sides might have to compromise when working with each other. This is not at all a problem for a customer intimate company who strives on compromises but it is for product leadership companies. The result at the end of a successful project is a long lasting bond and a high degree of competitive immunity.

Most of the time we deal with the middle man through leveraging our leadership position. The worst thing for them is our refusal to let them carry our product. Are there other ways to deal with the middleman, like discounting? This will in general not work, it will lead to price erosion and loss of brand control. But, this is totally different in new markets where we do not have a leadership position. If you are the underdog building market-share through low prices has helped us a lot over the years to build momentum. The real trick is to figure out how to improve the value perception for your products later on so that you can demand higher prices.

One of the key middlemen we have today are the DSPs. Let's see why we are doing well with them. Because we made credit, one of the real essential things in distribution, a non-issue. Everything is on commission. They pay for the COGs, which is maybe four or five dollars on a package at the most, but the royalty itself only comes to us after they have sold it to the next person in the chain. This is definitely something which they really like because we are the only vendor who does that at this point in time.
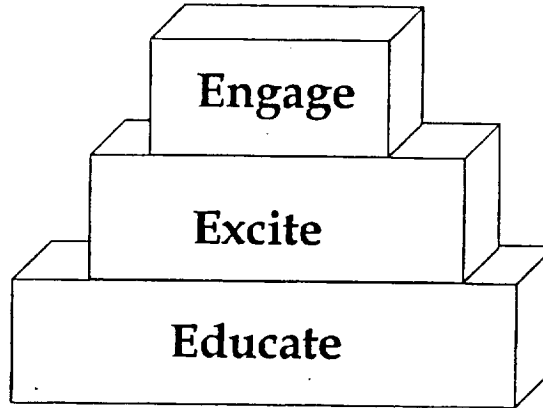
The Market Forces

- ◆ **Enduser - the "ultimate judges"**
- ◆ **Large corporations**
- ◆ **Industry Analysts**
- ◆ **Press**

In addition to direct partners there are a lot of indirect market forces which we often tend to forget. These are influencers and as a product leader, we will need to constantly improve our position with them in order to keep us over the survival threshold. Otherwise, we have the public opinion against us in such a way that it will hurt our leadership position long term. Let us explore this in more detail on one of the greatest examples we have.

The Building Blocks of the Windows 95 Strategy

```
        ┌─────────┐
        │ Engage  │
     ┌──┴─────────┴──┐
     │    Excite     │
  ┌──┴───────────────┴──┐
  │      Educate         │
  └─────────────────────┘
```

Let's embark on a journey which is called Windows 95. I got hold of Brad Chase's old marketing program for Windows 95 because Toshiba asked me to give a speech at a customer breakfast. Because nobody has ever done a good post-mortem presentation of how we pulled the Windows 95 thing off, I was forced to do that myself. Doing this presentation, I thought this would be a great one to share. This is right out of that marketing plan. I have not changed anything because I thought it would fit extremely well in here to explain how we worked the market forces and how we worked the industry partners in the context, of the Win95 launch. The strategy we pursued for Win95 was to educate, excite, and engage.

Job #1
Create massive demand
Activate endusers!

- ◆ Broad trial distribution
- ◆ World tour
- ◆ Coming soon
- ◆ TrainCast
- ◆ 450k copies - Windows Preview Program
- ◆ Explosive launch event
- ◆ Channel promotion
- ◆ Advertising including TV

We figured out from the beginning, job number one was to create massive demand and activate end users in the process. When you go down this list of projects we executed, you see very clearly that we worked with every participant in the market. The industry partners, the press people, the analysts, the large corporations, and the end users. Nearly half a million copies of Windows preview programs in large corporations naturally found their way to end users. Huge launch events, channel promotions, incentives for the trade partners and seminars to address the whole IS community played a role in demand creation. It's clear that nothing was left out and no stone unturned to create a feeling in the marketplace that we really wanted to work with every single partner in the field and engage all the key market forces.

Job #2
Accelerate enterprise migration!

- ◆ **Seminars**
- ◆ **Resource kit**
- ◆ **Preview**
- ◆ **Migration planner**
- ◆ **IS tour**
- ◆ **Migration offer**

Let's go to the next one. Job number two was to accelerate Enterprise Migration. Organizing seminars. A resource kit. The Preview Program. A Migration Plan which helps to save costs, right, so you are touching the operational efficiency nerve. The IS tour to educate people and hopefully get them engaged. And even financial incentives. If you buy now, cost is thirty percent less.

Job #3
Build massive momentum with IHVs, ISVs, PC manufacturers and channel partners

- ◆ **To build the components**
- ◆ **To build PnP PCs**
- ◆ **To build application software**
- ◆ **To merchandise the products**

We again worked all aspects of these market forces. On the IHV, ISV, PC manufacturer partner side, we went out and convinced them to build the components. We did this in a direct and an indirect fashion. When we had the components secured we were able to work with the PC partners to build plug and play machines, which was the cornerstone of Windows 95. We went out to the ISVs to convince them to build application software, which has helped us tremendously, not only to launch Windows 95, but to leverage NT Workstation as well. Last but not least, we convinced everybody in the United States to merchandise the product, which helped us in the OEM group tremendously because the channel wouldn't even buy PCs if Windows 95 wasn't pre-loaded. Some companies who didn't do that last year, like IBM for instance, had a terrible quarter, just because of that. Other companies who were well ahead of the pack, for instance, Packard Bell, had great results. So you see you have to work the whole spectrum, and if you do this right, I think you can improve the position Microsoft is in by moving things up from the thresholds and being perceived as a product leader who cares about it's partners and is aligned with them.

Where Can OEM Sales Help Microsoft?
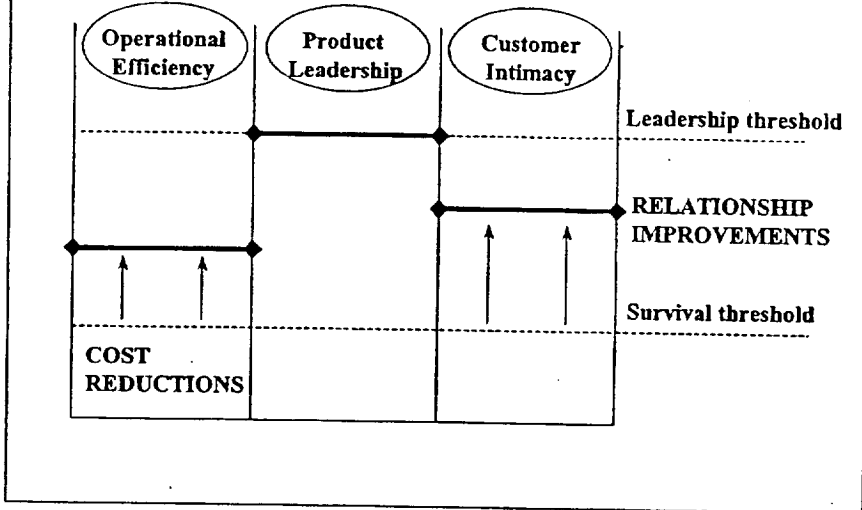
How can OEM help Microsoft? Let's translate this into some kind of sales and marketing strategy for the group. So let's assume we are perceived as a product leader because of our brand and product image in the marketplace, but we find ourselves way down on the relationship side and probably a little bit better on the operational side. What do we really have to start thinking about and how can we improve things way above the survival threshold without having to necessarily cut our prices in half or having to customized versions of NT Workstation for every single end user in the marketplace?

Obvious Benefits

- ◆ **Cost reduction (AR, Support)**
  - ➤ WW availability
  - ➤ consistent quality
  - ➤ better products and customer satisfaction
- ◆ **Relationship Improvements**
  - ➤ less competitive vulnerability
 - ➤ less PR challenges
  - ➤ more market growth

The benefits are obvious. You know, we've actually done some of these things. We are better off on the operational side. We did an AR program. Suddenly our products are available worldwide with very consistent quality. That helped a lot of companies do business with us, cut the cost and very clearly improve the products they were delivering, and their Enduser satisfaction.

Regarding the relationship improvements. If we are to have better relationships with OEMs, DSPs and system builders, they would probably listen less to competition. We would be less vulnerable and we would have less of a PR challenge. We would focus on building the next computing environment and we'd see more market growth instead of being confused by competing concepts. So over all, when the management team was going through this analysis recently, we asked ourselves how to improve our sales proficiencies.

Stages of Sales Proficiency

	Stage 1	Stage 2	Stage 3	Stage 4
Focus	Product	Customer	Competition	Customer's Market
Relationship	Casual	Trust	Mutualistic	Symbiotic
Value	Features	Solutions	Biz Impact	Strategic Direction
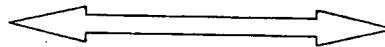
Transactional $\Longleftrightarrow$ **Intimate**
"WHAT" **"HOW"**

When you translate this thinking into sales proficiency, what you will very often find that our relationships with customers go through certain stages. The people who have gone through the Holden program, have seen this picture already.

We are doing business with a lot of companies today, on just a transactional basis. Which means the focus of the relationship is on the "what." What can I get, what's the price, and what does it take to get this thing delivered into my courtyard? This is a typical relationship we have with a lot of system builders and with some of the Named OEMs and maybe even with some of the large OEMs. We basically focus on products, and have a very casual understanding of the marketplace. What we do not do is really help each other to grow the business, or improve each others position. This is what we call Stage One relationship.

When you talk to a Stage Two or Stage Three customer, the relationship goes much further. The Stage Two customer will always talk with you about the value he has to deliver to his customer, and will actually trust you with his plans. Now this is getting a little bit more interesting. It actually gives both of us a road map so that we can think through how to accelerate things. This is still not as good as it can be but it's definitely much better compared to talking about just product features and price. You will probably talk more about solutions, what should I do for the home user, and what type of value do I have to deliver? And you see where marketing comes in here and how they can help to sell. We are getting a little bit more intimate and we are getting away from the "what" a little bit and into what we call the "how"; how do we do things together?

When you go to HP today, they very often talk about Sun. They want to beat Sun. Suddenly the discussion focuses around our mutual competition and not just customers. Now a potential cooperation is much more mutualistic because we can both gain. We can both grow our own share of the market with impact on the bottom line. This is called a Stage Three relationship.

Now, when you go one step further, it gets even more intimate. You basically go to bed with each other on a daily basis. You are completely aligned in Stage Four. You develop marketing plans together. Say Compaq is trying to figure out how to attack the small business segment, they have two choices. They bring us in early in the game and we basically use each other as a consultant, or they present us the plan. If they bring us in very early, we should be able to add better value and we should get much more entrenched. It gets very symbiotic, and we will probably arrive at one strategic direction. This probably means, in a nutshell, that highly improved value will get delivered and a certain competitive immunity will be achieved for both companies.

Make Sure We All Understand

- ◆ We cannot have stage 4 relationship with all customers
- ◆ But, we need a development plan for every customer!

Now that's the ideal world, but do not believe that you can have a Stage IV relationship with every company. You and I might not want it either. Good example, IBM. If I have a Stage IV relationship with IBM, I would share all my product plans with them, I would do marketing planning with them, just to find out that they sell Notes, Smart Suite, and their own database to some customers the next morning after we visited them together. So you see, depending on where you are, depending with whom you deal, you will have to be very careful with this. But regardless of who the customer is, what I'd like to see is that we all understand where we are in this process, what stage are we in, with whom, and then decide with open eyes do we want to develop this from one to two, or from three to two, etc... What is the timeframe and what do we have to do? If we want to really develop relationships we better use an easy to understand model like this one to analyze the situation, and hopefully, as an end result, make a lot more of them listen to us than to our competition.

We all need to understand that we cannot have a Stage Four relationship with all customers, and we need a development plan for every customer to really determine where are we with our customer, and what do we want to do with them. So, OEM's job number one goes like this:

Objective number one has remained to be the same for years. "Develop competitive immunity". We can call it protect the franchise, I don't care. This sounds much better. Objective number two, "Drive market growth". If this market stops growing, the OEM community will run away from us because they will blame us and Intel first. There is no doubt about it. Driving market growth can be done in a lot of ways. The marketing people, in particular, have a bunch of tricks up their sleeves to help OEMs grow as well as the technical people who basically engage with these OEMs to explore and integrate new technologies.

And, don't forget, Objective number three, "capture profitable non-OS revenue". I haven't given up selling mice, keyboards or consumer applications to these OEMs. There's nothing wrong with that. In particular, if you develop a certain immunity, this should be much easier in the future than it is today, because you might not have to discount all the time.

From a strategy point, how do we get there? I think we basically have to establish a process with them which makes us listen to each other, so we can leverage some external and internal thought leadership. I believe that this could be the toughest part of the whole process, knowing we as a group have not developed that skill. That is one of our reasons for the organizational change which we introduced. On a tactical basis, it's relatively straightforward. You adapt the value-based selling discipline, and really focus on value, value, value! You practice partnering, and you share best practices, at least within the group. Hopefully even with the PC manufacturers, the DSPs or the System Builders, with the understanding that there are areas where you are under non-disclosure to prevent the sharing of the latest Packard Bell marketing plan with IBM. I believe we all understand this.

You will see this slide a lot over the next two or three years because we worked very hard on it's content and I hope you understand what I mean when talking about Job Number One in the future.

What is Thought-Leadership?

"The intellectual capital needed to take customers some place they have never been before"

Thought-leadership is the toughest one to exercise but it is the cornerstone of our future success. So let's try to find a definition for that. This one comes from the Holden Training, if I'm not mistaken. It's defined as "The Intellectual Capital needed to take customers to some place they have never been before".

Result of Thought-Leadership in Action

- ◆ **Vision**
  - ➢ **outcome of working together**
- ◆ **Impact**
  - ➢ **growth, competitiveness and value**
- ◆ **Intimacy**
  - ➢ **total strategic alignment**

Thought leadership is hard to exercise if you do not have vision:

"A computer on every desk and in every home..." sounds simple? This was the vision and the proposition made to the PC manufacturers by Microsoft to establish an OS/API standard for the industry. The outcome was clearly defined and the impact is obvious today. We defined and grew an industry. We took business away from traditional mainframe and mini computer companies because we were more competitive and we have delivered great value to endusers like freedom, choice and individual computing power. To do this, we had to be aligned with select leaders like IBM, Compaq, NEC and Olivetti to name a few. This is the big picture of thought leadership in action, but there are other examples.

In an article from the Wall Street Journal, there was a guy who went into CompUSA and he wanted to buy the high end Toshiba notebook which costs around six thousand dollars. He was put on a waiting list and he got the number of nine hundred and thirty-one. So I'm very interested in finding out why Toshiba is in such a leadership position. When you look back two or three years, we did not work very well with Toshiba. But I believe they were our prime partner for Windows 95 when it came to the notebook design. I believe today there is no notebook on the marketplace which beats the Toshiba Notebook in functionality and Windows 95 integration. And I firmly believe that we helped them a lot, and they helped us a lot too to do the right things for the notebook market. You can take customers to places where they have never been before! To have a backlog of several hundred thousand systems is definitely a place Toshiba had never been before.

I want to talk about a DSP operating out of Germany, Actebis, who was a Named OEM for a long time before serving as a DSP. When the traditional OEM business started to flounder, we approached them and we basically tried to talk them into being a DSP and tried to really educate them on what we thought they needed to do in order to serve that market well. They were having trouble making any profit and funding the expansion of their business. But they did it and today, the traditional OEM portion of that business is totally unimportant. I think they might do fifteen million dollars with us in OEM; but could do fifty million dollars this year just on the DSP side. They're not only doing it in Germany now, they expanded into Europe very nicely. I met their CEO at Comdex and he is super happy about that business. Because he believes that we basically helped him to get into it and we opened the doors for him and enabled them to do it. It appears the business is extremely healthy for him, and he says it's one of the most uncomplicated things in distribution he has ever seen when it comes to the DSP program. So that's definitely something where we can say we took him to places he had never been before.

Microsoft Confidential

Think about Compaq. I think that we can work extremely well together. Compaq's position in the server market today to a degree has to do with what Microsoft and Compaq did together. Compaq positioned themselves in the marketplace very early on in working closely with Microsoft on NT Server when NT Server was not a great product. In 1997, they're probably going to sell half a million servers, which is probably thirty-five percent of the total market volume, and they're selling them with extremely good profit margins, and we will sell a lot of NT Servers with it. Other customers, like IBM, talk about competition, for both of us have suffered all the way along, even HP passed them. What did we gain? We gained NT Server reputation, and not only with Compaq. Compaq gained the number one market position and IBM is only number three, and they didn't sell too many OS/2 Lan Servers in the wake. So I think that's what we mean when we talk about "intellectual capital needed to take customers some place they have never been before."

There is one more example worth talking about. I think this is actually a real good one. Acer as a company is not doing too well these days. But, once upon a time, they had the right idea, and they actually provided thought leadership to us. They told us they wanted to conquer the third world countries. They said, "we want to have an assembly plant in every single country in the world, put the chassis on the ship, we're going to ship the motherboards in the airplane and we're gonna buy the hard drives locally at spot price so that we don't have six weeks or four months of inventory in the pipe. We need software which we want to buy locally because we don't necessarily want to pay shipping costs and purchase everything in Taiwan. Our response was to expand the authorized replicator concept, and Acer's subsidiaries could locally buy product. They liked it. Because without that, they would've accrued much more cost, and they actually gave us, I think, the last kick to open up that program from just, industrialized countries into third world countries. I believe listening to thought leadership coming from customers is great because we learned how to do things better and at the end we both gained more market share.

So there's "results" of thought leadership in action, which means vision, impact and intimacy. What we mean under vision is basically what it's going to be like after we work with each other. So, the outcome is important and the result is important. Can we share a certain dream? If there is no vision, you better not engage because there will be no impact regardless of how intimate you get. Sounds a bit like marriage.

Then what's the impact on the business? Can we grow it? Will it be more competitive? Will it provide more value for customers? And last but not least, if it's done right, in total intimacy, we should be totally aligned from a strategic point of view. With some customers, we probably will. With others, we might have conflicting interests as previously explained.

Example of PC Manufacturer's Primary Value Disciplines

◆ **Operational efficiency:**
  ➢ **PB, ACER, GW, IBM (PC), Dell (Consumer), DSPs, ARs**

◆ **Product leadership:**
  ➢ **Compaq, HP, Sony, Toshiba, IBM (Notebook)**

◆ **Customer intimacy:**
  ➢ **IBM (other), DEC (Traditional), Dell (Corporate), System Builders**

So lets take a hard look at some examples of PC manufacturers and their primary value disciplines. I just listed a couple of them. What you see here is actually pretty interesting. It's not very hard to figure out that Packard Bell, Acer, Gateway, DSPs and ARs are in the operational efficiency category. The same is true for these product leader OEMs. Compaq wants product leadership actually in every single segment. HP is trying to do the same. So are Sony and Toshiba.

On the customer intimacy side, it's getting a little more tricky. The ultimate companies here, aren't listed. They're called VARs, value added resellers. True VARs do a lot of integration and customization work. Maybe some System Builders who aren't VARs shouldn't be listed there. Because thesystem builders who aren't VARs might not necessarily be very close to the customer. But in general they do custom solutions. So I thought I'd put them in here as a hint that most of them probably are in this field. Take a look at Dell. You will see them in two spots. Because they basically have two operational models internally. Companiescan do that as long as they have a management process in place which doesn't confuse them internally. Dell was confused for a long time, but today they have mastered it. I believe Dell's consumer business is very much runlike Packard Bell's. Operational Efficiency! Best Value! Not a lot of integration, no special sales force, support is right and that's about it. But, at the same time on the corporate side, they are trying to get very intimate with theircustomers. Entering the server market is as sign and I wouldn't be surprised if they buy an integrator one day, or possibly buy Anderson Consulting in order to increase the intimacy in that top portion of their business. I know they're not totally there today, but the real intimate companies are in a way the old mainframe guys. The traditional DEC business, when I worked for them, was selling VAXs, PDP 11s, PDP 8s, PDP 12s solutions: HW, SW, Services, Integration. That was the ultimate customer intimacy business. They pampered their customers, they had support for them, they had integration services for them, and they have actually had customized solutions for them. I remember the timewhen DEC built the VAX 11780 for one single customer, the Bell Labs. They were the customer that system wasbuilt and optimized for. They turned around and sold it to some others as well, but it was a total customized solution.

IBM has done that for years. They have been very very close to their customers and they have gained account control. I called it competitive immunity - remember! That's why it's so incredibly hard to get into a true blue customer account. IBM will align itself strategically with them in theirIS strategy and in their whole business strategy. They will build products for them in order to improve their businessand to make them grow. Don't let them into our accounts, beat them with their own weapons, create competitive immunity! The IBM Company on the other side, when you look at the PC side of the house, is probably nothing else than Packard Bell or Dell. I believe that IBM as a company is still confused about that. This is why you have seen them floundering for such a long time, and losing massive market share, because every time you look at them you see the traditional IBM managers, with the wrong value propositions, run the PC company. The paradigm they have in their head is completely different from what they should have in their head. Naturally they are recognizing this but I still think they have some time to go. On the Notebook side of the house, they have clearly taken a product leadership position and I think they only lost it to Toshiba because Toshiba worked closer with us.

Compaq made a very clear decision to do their business in three different divisions. The interesting thing is that Compaq's CEO believes firmly that all this should be run separately. There is no need for the consumer guy to think about business models which are successful for the commercial desktop guy. I completely agree with him; he's right. It makes it incredibly hard for us to deal with them because forevery division, we basically have to think through what their basic market value discipline's are, what makes them tick and what hits their nerve.

What does customer intimacy mean for these different companies?

- ◆ **Operational excellence:**
  PB ⟶ deliver on time, quality

- ◆ **Product leader:**
  Compaq ⟶ early engagement, exclusivity

- ◆ **Customer intimacy:**
  IBM ⟶ field engagement, customed versions,
  early customer engagement

When you talk about customer intimacy, you basically have to look at every single company in a different way. Operational excellence companies, like Packard Bell, for instance need to deliver on time. I wrote this down on purpose. It's not that it has to arrive on time in the store. It has to arrive on time for Christmas. If you miss that window, you will lose out. Now, what does it mean for us? If we do not ship an operating system by mid-May, we won't be on these Packard Bell machines at Christmas. It's just that simple. Or we have to really work hard to convince them to redo their system loads and redo their testing. This is incredibly important to understand knowing it is the nerve system for their success.

Everybody in this room should think about their customer and ask what makes my customer tick the most. Quality is an issue for PB. They have a bad reputation today and I believe they are not leading in the category of operational efficiency because of that. It's very obvious to me that they do not, at least from a perception point of view, deliver great value to customers. They have too many returns and too many quality issues. Can we help them to get better at that? Better integration in their manufacturing process is another hot button. If you don't address that properly, you have less advantage. If you just throw a development kit over the fence and leave them alone, they will never install OSR2. I think we addressed that one in the last year but we didn't understand it before.

There are different types of hot spots, depending on what company you're working with and hot points you have to touch in order to get their attention. But if you do this right, it develops into an incredible barrier for any competitor to enter and take the business away. In order to please a product leader like Compaq, the first thing you hear is exclusivity. We hate that and normally shift this to time to market, because product leaders in general invest a lot in R&D. Just look at us, two billion dollars this year. I hope we don't spend it all. Who ever invests would like to see a return on investment. We all know in this industry you can demand a premium price for the first three or six months of a product cycle. Giving them some time to market - exclusivity might go a little bit too far - will go a long way. In regards to the next hot button, when new technology emerges they want early engagement. This would make no sense whatsoever, with a company like Unisys, because they wouldn't be able to invest enough to be out there with an early product implementation. We would all spin our wheels to find out that they can't financially do it. But these product leadership companies like to do this because they know if they are in early, they can make real money.

Customer intimacy. Take IBM. What are they looking for these days? Field engagement! They feel left out. They want to be loved, right? Not in the cards. We need to fear that they will sell Lotus Notes, SmartSuite and their SNA Server the second we leave the account. Working with them will not make us more immune to competition, so why do it? If you touch the right nerve, you can improve your intimacy position with these customers for instance. Customed versions and early customer engagement. Not necessarily engagement with technology but engagement with IBM's customers in a very early stage so that they can work with us to provide provide thought leadership to their customers, in order to make their business more competitive, which in turn, will take them to places where they have never been before.

To Improve Customer Intimacy

- ◆ Understand their primary value proposition (touch the nerve)
- ◆ Understand what customers and their customers value
- ◆ Translate it into an action plan for your account

So that's the type of vision we are embarking on in OEM, and we need to be smart about it over the next two or three years in order to reach our goal to outlove our customers. To improve customer intimacy, we need to understand their primary value proposition. Understand what customers and their customers value the most - very important to look beyond the middle man and then translate it to an action plan for every single account.

The OEM "Value" Implementation

- ◆ **Invest in Marketing**
- ◆ **Develop management consensus**
- ◆ **Adjust organizationally**
- ◆ **Redefine organizational objectives/methods**
- ◆ **Train the group**
- ◆ **EXECUTE!!!**

If we do this right, I truly believe we can improve our position in a fantastic way and help the company to have the best relationships in the marketplace. The way to implement that, is by reorganizing and, investing in marketing. A big step forward this year was accomplished by reorganizing marketing and focus them on a mix of customers and segments.

We have adjusted organizationally. For example, putting the large account organization in place and putting Debbie Flynn into the Program Management role of the business for DSP. We continue to redefine our objectives and methods as we go along and as we see fit because this market is going to change and we just have to stay alert. Train the group. That means everybody including me, and then execute, execute, execute!... as Steve Ballmer would say.

Organizational Changes
Program management function

- ◆ **Development of value based OEM programs**
- ◆ **Value integration into the business function**
- ◆ **Manage coordination with the PGs**

So the organizational changes we just went through were to introduce a royalty program management group under Kurtk. We can learn from what Debbie Flynn has done in the DSP section, and develop value-based OEM programs for the named accounts as well as the Multi-National accounts. This group needs to figure out how to do value integration into the business with the different contracts we have, such as the MDA programs, etc. The challenge is to manage and coordinate this very very closely with the product groups. Not just on the product side of the house, but on the business side as well. Dave Wright is going to continue to work with me and he will be charged to work with the product groups more closely on the product aspects.

Organizational Changes

"Value Champion" - Sales Development

- ◆ **Evangelize a value and thought leadership based sales culture**
- ◆ **Improve account management & selling proficiency**
- ◆ **Implement the value approach WW**

The second change was to ask Mark Buick to take the job as Sales Development Manager and we internally will call him... "The value champion". He's chartered with evangelizing a value and thought leadership based sales culture. I know that we need a lot of help there in order to get that implemented, and we're looking for him to do this, based on his past career as a Sales Training Development Manager in another company. This equates to improved account management and sales proficiency and deployment of the Stage One, Two, Three and Four models for every single account on a worldwide basis.

We Need to Create
"The Cult of the Customer"
in OEM

◆ As expressed in people's attitude and behavior

◆ Where success is measured in "how much value we create for our customers"

◆ Meaning, win their hearts AND their orders

What we really need to do is create the "cult of the customer" in OEM. That's always expressed in people's attitude and behavior. I think the success of this group is going to be measured less on numbers. You will be measured on how much value you personally create for your customer. So we're going to change our reward system quite a lot over the next couple of years, and you'd be surprised when I care less about your contract being six million dollars or sixty million dollars, as long as you can create value for your customers. I will stop talking about numbers and change my attitude as well. We need to win the hearts of the OEMs and their orders. But please, in that order.

How to Live the *"Customer Credo"*

- ◆ **Accelerate actions**
- ◆ **Remove obstacles**
- ◆ **Ask for tools and resources**

I hope we can live up to this. I think what I've seen sometimes is to much inertia and I would like to ask everybody to go back to basics, accelerate actions, remove obstacles, and if you don't have them, ask for the right tools and resources. Your passion will make us listen!

Emotionally and rationally, everybody knows the right thing to do.

So, let's go the extra mile for the customer and start today!

Emotionally and rationally, I believe everybody in this room knows how to transition. So let's go the extra mile for the customer; start today so we can outlove them, and get Job #1 done!