Q2

digital

Second Quarter Report

On the cover...DECwindows. Some of the new systems that can provide customers with the ability to run MS-DOS, UNIX, and VMS applications from the desktop.

To Our Shareholders

Total worldwide revenue growth during the quarter was led by our international revenues which grew 28% over the comparable period a year ago. This reflects the momentum generated last Fall by DECWORLD '88, held in Cannes, France, where Digital demonstrated enterprise-wide computing before a large gathering of enthused customers.

For the past several quarters, we have been in a period of heavy investment in new programs and business expansion. Many of those investments are now in place and Digital is beginning to see improvement in its cost trends. One example of this cost containment is the fact that Digital's hiring pace has slowed.

Overall, during the second quarter there was increased sales of VAX 6200, MicroVAX and desktop computer systems. In addition, a number of large multinational companies picked Digital for their Computer-Integrated Manufacturing (CIM) needs.

On January 10th Digital responded to the growing customer demand for a fully integrated desktop by introducing a broad set of desktop solutions. At the heart of this announcement is DECwindows software, which gives desktop users a capability that is unique in the industry–the ability to simultaneously access and manipulate information from different computers running different operating systems.

Price and performance of Digital's new personal computers and workstations place the company in a leadership position in the industry. Digital now provides a range of desktop systems that can access far more information than is available on standalone personal computers or small personal computer networks.

Digital's approach to networking is central to the success of the company and its customers. The company's comprehensive networking is the most flexible, cost-effective means toward the full integration of an organization. This gives Digital's customers an elegantly simple way for people to work together more productively, more creatively, more efficiently, and more competitively.

Kenneth H. Olsen
President

Leading Software Developers Endorse DECwindows and Digital's Desktop Strategy

Digital has licensed DECwindows technology to more than one hundred independent software developers. And at a press conference held in November, five of the world's largest independent software companies endorsed Digital's DECwindows strategy.

Joining Kenneth H. Olsen at the podium were James Manzi, President and CEO of Lotus Development Corporation; Edward Esber, Chairman and CEO of Ashton-Tate; Charles Wang, Chairman and CEO of Computer Associates International, Inc.; John Warnock, President and CEO of Adobe Systems, Inc.; and David Boucher, President of Interleaf, Inc.

Their comments on Digital's DECwindows strategy are included as part of this quarterly report.

"We're excited about Digital's desktop strategy because it represents such an important opportunity for expansion of Lotus's multiplatform product line." James Manzi – President and CEO: Lotus Development Corporation

Highlights From The Annual Meeting

The Annual Meeting of Shareholders was held November 3 at the World Trade Center in Boston. Approximately 72 percent of the common shares outstanding, or 92 million shares, were represented at the meeting in person or by proxy. The items of business listed in the Proxy Statement received a majority of the votes cast.

In his remarks at the meeting, Digital President Kenneth H. Olsen reaffirmed Digital's commitment to invest aggressively in new technologies and product development and to concentrate on areas that directly support Digital's long-term competitiveness.

In particular, Olsen cited sizable investment in sales and service, software, high-end computers, sophisticated mass-storage devices, and the desktop initiative described in this Report.

Digital's Desktop Initiative

In a series of announcements, Digital introduced the broadest set of desktop solutions, all with the same "look and feel," ever offered by a single vendor. At the same time, the company introduced the industry's only unifying software environment based on industry standards.

These products implement Digital's strategy to:

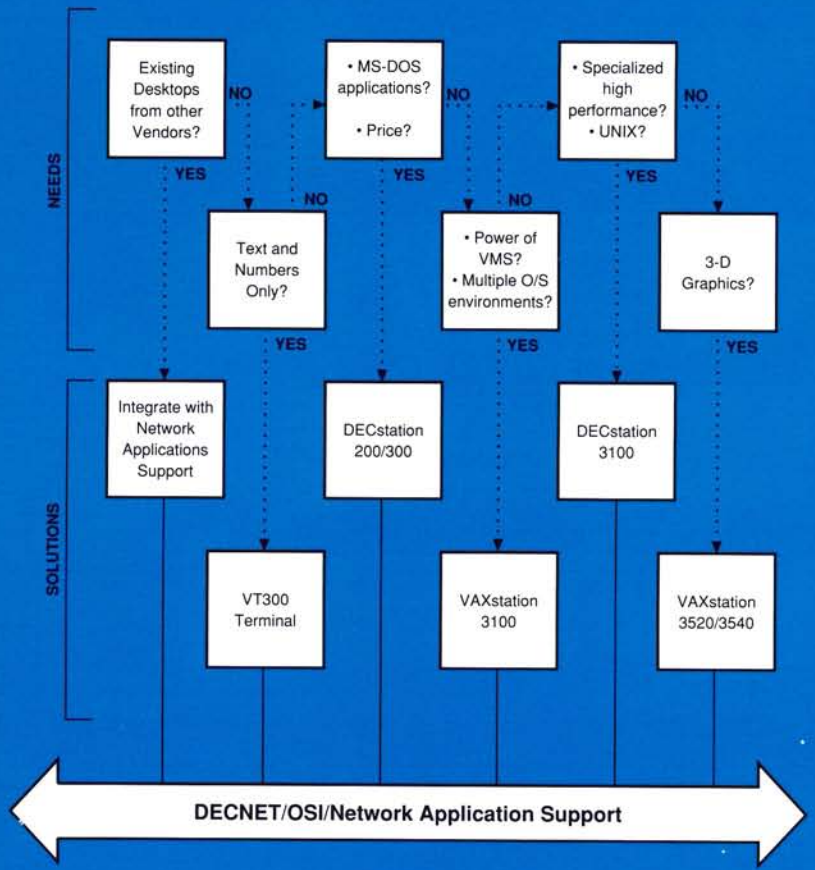
- Create a single user interface for VMS, UNIX, and MS-DOS desktop systems and workstations;
- Form strategic alliances with the world's leading desktop application software vendors;
- Provide easy-to-install and easy-to-use local area networks that link whatever desktop systems customers have;
- Integrate existing and new local area networks into an enterprise-wide corporate network.

Implementing The Initiative – The Desktop Products

Over the past several years, popular thinking equated the personal computer with improving individual productivity. In large organizations, however, users have made it clear that they need access to far more information than what is available on standalone PCs or small PC networks.

"Customers want applications that are portable and compatible across different desktop devices, to protect their investments and minimize their training costs." Edward Esber – Chairman and CEO: Ashton-Tate

Digital's new desktop capabilities create an environment in which users, from the desktop device that best suits their needs, can access and share networked information and resources – whether from inside the enterprise or from suppliers, distributors, and customers.



How Digital's Desktop Strategy Covers Customer Needs

DECwindows: The Single Interface To VMS, UNIX, and MS-DOS Applications

Conventional windowing software organizes work done on a single system. In other words, it organizes the "electronic" desk. But what users can do *from* their desks is far more important than what they do *at* their desks.

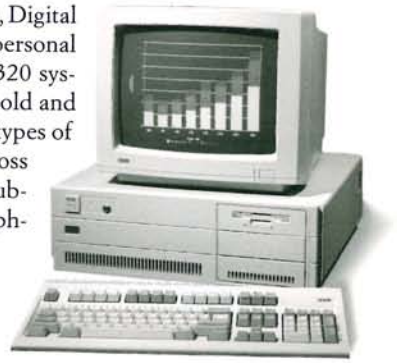
DECwindows software makes it possible for one desktop system to access different computers running different operating systems simultaneously. Users can move data across operating systems no matter where the host machines are located. DECwindows provides a logical, intuitive graphical interface that reduces learning time and increases productivity across a broad range of applications.

"DECwindows can help us achieve our goal by making it easier to port Computer Associates applications across VMS, ULTRIX, and MS-DOS." Charles Wang–Chairman and CEO: Computer Associates International, Inc.

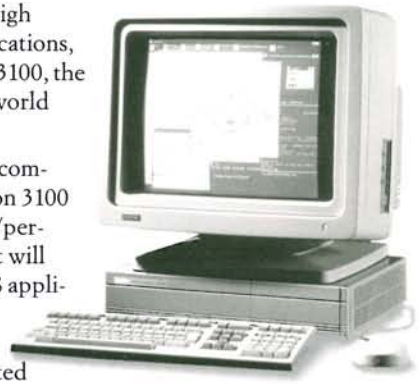
The DECwindows program, the largest software development effort in Digital history, provides the unifying element needed for true desktop-to-datacenter integration. Recently, the Open Software Foundation, a consortium of more than 70 organizations worldwide, chose the software core of DECwindows as the foundation for its industry-standard user interface.

DECstation Industry-standard Personal Computers

For users who require MS-DOS applications, Digital introduced a family of industry-standard personal computers. The DECstation 210, 316, and 320 systems, the first industry-standard PCs both sold and supported by Digital. They are ideal for all types of MS-DOS applications that can be shared across an enterprise–in the office for electronic publishing and work with spreadsheets and graphics, or in the lab for instrument control.



High-performance DECstation for the UNIX User



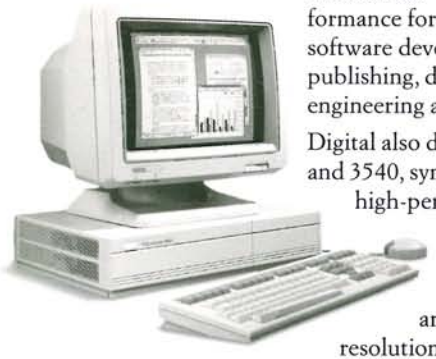
For users who require specialized high performance for UNIX-based applications, Digital introduced the DECstation 3100, the fastest desktop workstation in the world today.

Based on a reduced instruction set computing (RISC) design, the DECstation 3100 represents a breakthrough in price/performance. Through DECwindows it will provide access to VMS and MS-DOS applications for UNIX-based technical workstation users who employ complex simulation and sophisticated financial modeling applications.

VAXstation Price/Performance Tripled, and First X Window 2D and 3D Workstations Unveiled

The new VAXstation 3100 offers three times the price/performance of the entry-level VAXstation 2000—now the world's best-selling single model workstation.

Designed for users who require the broadest range of desktop solutions, the versatile VAXstation 3100 provides excellent performance for a wide range of applications, including software development, technical and business desktop publishing, decision support, and computer-aided engineering and design.



Digital also demonstrated the VAXstation 3520 and 3540, symmetric multiprocessing systems for high-performance graphics applications such as computer-aided design, scientific visualization and health care imaging. These new mid-range workstations are the industry's first to bring high-resolution two- and three-dimensional graphics to the X Window system environment.

New Software, Disk and Tape Drives, and Imaging Products Complement the Desktop Initiative

Digital also announced a bevy of software and storage products that support its Desktop Initiative. These include:

- VMS Version 5.1 and ULTRIX Worksystem Software, Version 2., each with the DECwindows environment included;
- Compound Document Architecture, a set of software applications that allow reports generated from several sources of data to be automatically updated when the source data changes;
- DECwrite and DECdecision, new word processing, spreadsheet, graphics, text editing, data charting and decision support software based on Digital's Compound Document Architecture;

"Standards will be the key to excellence on the desktop, and Adobe has been working closely with Digital to develop a rich desktop software platform." John Warnock – President and CEO: Adobe Systems, Inc.

- VAXpc for VMS, Digital's emulator of IBM PC/AT software that enables VAXstation users to run MS-DOS applications unchanged;
- MS-DOS/DECwindows Display Facility, that will let users access and execute remote applications and display/manipulate results on a local PC;
- Desktop VMS, an easy-to-install VMS operating environment on CDROM;
- VAX Decision Expert, a graphical productivity tool for software engineers building expert systems;
- Several new disk and tape drives that enhance the performance of Digital's new workstations;
- The VAXimage set of products that lets users create image files and transfer images to other applications; and
- DECvoice, a combination of digitized voice, speech synthesis, and voice recognition technologies for voice-response applications.

Full Range of Workgroup Servers to Support Desktop Users

Recognizing that desktop systems are most useful to an organization when they work together, Digital laid the foundation for the desktop products by announcing a series of server products that link PCs in work groups, and PCs and workstations in local area networks.

In local area networks, these systems extend file service to PCs and workstations from Digital as well as to systems from other vendors such as Sun Microsystems and IBM. Continued support of the multivendor desktop environment is ensured through formal working relationships that Digital has established with leading PC manufacturers including Apple, COMPAQ, Olivetti, Tandy, and Zenith.

"Key to those integration capabilities are Digital's broad base of products, the DECwindows user interface, and open specifications for handling revisable compound documents." **David Boucher–President:** Interleaf, Inc.

Worldwide Electronic Data Interchange (EDI) Plans Unveiled

Digital announced its intention to provide worldwide EDI software and services that will support all international EDI standards, as well as the Open Systems Interconnect (OSI) X.400 electronic messaging standard. The announcement was an extension of Digital's support for VAX/EDI systems, already available in Europe.

EDI, one form of extended enterprise communications, is the computer-to-computer exchange of structured business documents–including purchase orders, invoices, shipping notices and acknowledgments–between an organization and its suppliers, customers, and subsidiaries.

Software Grant Program Lowers Costs for Educational Institutions

Digital's Education Initiative, a comprehensive program to make computer technology more widely accessible and affordable to educational institutions, was announced in the period.

The Campuswide Software License Grant Program grants licenses for virtually all of Digital's nonroyalty VAX software products at a nominal charge to educational institutions. The Education Software Library program provides an effective way to control software maintenance and support costs by allowing institutions to share support responsibilities with Digital. The Campus Service Agreement offers a hardware self-maintenance plan that enables educational institutions to reduce the cost of service while receiving essential support from Digital.

New MicroVAX Systems Double MicroVAX II Price/Performance

Digital expanded its presence in the distributed computing market with its announcement of two new MicroVAX systems. The MicroVAX 3300 and MicroVAX 3400 computer systems, which replace larger configurations in the MicroVAX II line, deliver twice their price/performance.

The MicroVAX 3300 and 3400 systems reinforce Digital's commitment to a leadership position in the distributed transaction-processing market, where continuous access to mission-critical information is a prime requirement. When used in conjunction with DECtp, Digital's recently announced database and transaction-processing software, the new systems provide an integrated, cost-effective distributed transaction-processing environment.

Digital and Hughes Corporation Sign $50-million Service Agreement

Digital and Hughes Corporation, a $7-billion company owned by General Motors, signed a first-of-a-kind service agreement that will result in $50 million in Field Service revenue for Digital over the next three years. The agreement calls for Hughes to purchase service for all of the Digital equipment it uses and resells. Digital will also have first right of refusal on servicing non-Digital hardware.

Nekoosa to Modernize Entire Business Operation with Digital Systems

Digital will design and install what is believed to be the most comprehensive computer-integrated manufacturing (CIM) operation in the corrugated packaging industry for Nekoosa Packaging, a subsidiary of Great Northern Nekoosa Corporation.

Digital will modernize Nekoosa Packaging's entire plant business system, from customer order entry to the Programmed Logic Controllers that automate data collection and production monitoring on the factory floor. After the initial $1.7-million project is completed at its Milan, Michigan, manufacturing plant, Nekoosa plans to install the CIM system in 21 other plants across the country.

Pratt & Whitney Signs Five-year Service Contract

Pratt & Whitney, a leading manufacturer of jet engines, signed a comprehensive five-year, $5-million service agreement with Digital to support Pratt & Whitney's more than 150 VAX computer systems used to test turbine and rocket engines.

Included in the new service contract are 14-hour-a-day support, remote diagnostic tools that can predict and help avoid potential system downtime, and access to a toll-free customer support hotline.

Cooperative Marketing Effort Expanded to Provide Single-source Solutions

Digital announced an extension to its Cooperative Marketing Program (CMP) that enables the corporation to distribute, license, and support certain vendor applications with Digital products.

The new Distributed Cooperative Marketing Program (DCMP) enables Digital to provide single-source computer solutions for end users interested in applications from several Digital CMPs. The announcement was made at the AUTOFACT '88 Conference and Exposition, held in Chicago.

Under the DCMP, Digital will license application software in selected market segments for resale under Digital license and warranty terms. The first vendor to expand its CMP relationship under the new program is Matra Datavision. Digital's distribution of the company's EUCLID-IS computer-aided design software will begin in the spring of 1989.

Additions to Cooperative Marketing Programs

The second quarter also saw the addition of a number of new companies to Digital's cooperative marketing efforts, as well as the announcement of attractive new discounts and licensing practices for software products that Digital's Complementary Solutions Organizations (CSOs), Original Equipment Manufacturers (OEMs), and CMPs use for building a wide variety of data-management and transaction-processing applications.

Among the products and companies are:

- *AMDOCS,* Inc., St. Louis, Missouri, for the ADS Family of Products II,™ sophisticated software solutions that integrate and automate telephone directory publishing;
- *Antrim Corporation,* Plano, Texas, for medical laboratory data management, financial, and accounting software;
- *Applied Expert Systems,* Cambridge, Massachusetts, for its expert-systems-based software that creates customized insurance profiles and sales scripts for insurance agents;
- *Cullinet Software, Inc.,* Westwood, Massachusetts, for Enterprise:Expert/VMS,™ Enterprise:Builder,™ and Enterprise:Generator;™
- *Environmental Systems Research Institute,* Redlands, California, for ARC/INFO,® a geographic information system designed for resource and records management and land use or planning;
- *E.I. du Pont de Nemours & Co.,* Wilmington, Delaware, for a new version of the Du Pont Carpet Dealer Management System (CDMS) that supports Digital's new MicroVAX 3300 and 3400 systems;
- *Information Resources, Inc.,* Waltham, Massachusetts, for EXPRESS MDB,® its fully integrated decision support software that includes query, modeling, forecasting, statistics, graphics, reporting and analysis, and a fourth-generation language for application development;
- *Interactive Development Environments, Inc.,* San Francisco, California, for Software Through Pictures,™ an integrated environment that supports several established methods for the analysis and design of software systems;
- *The Montran Corporation,* New York City, for the MONTRAN System,® a fully integrated, automatic international funds solution for the corporate banking market;
- *MTS Systems Corporation,* Minneapolis, MN, for Remote Parameter Control (RPCV),™ a computer-based system used in full-scale fatigue tests of automotive components and vehicles.

Consolidated Statements of Income

(Dollars in thousands except per share data)	Three Months Ended		Six Months Ended	
	December 31, 1988	December 26, 1987	**December 31, 1988**	December 26, 1987
Revenues				
Product sales	**$2,045,166**	$1,825,297	**$3,941,567**	$3,511,369
Service and other revenues	**1,134,340**	956,955	**2,179,738**	1,800,656
Total operating revenues	**3,179.506**	2,782,252	**6,121,305**	5,312,025
Costs and Expenses				
Cost of product sales	**869,205**	729,257	**1,668,827**	1,399,955
Service expense and cost of other revenues	**686,966**	593,875	**1,336,634**	1,119,017
Research and engineering expenses	**376,405**	301,076	**740,401**	599,440
Selling, general and administrative expenses	**891,024**	756,650	**1,739,283**	1,446,162
Operating income	**355,906**	401,394	**636,160**	747,451
Interest expense	**12,085**	9,743	**20,987**	18,598
Interest income	**29,853**	37,864	**64,493**	70,446
Income before income taxes	**373,674**	429,515	**679,666**	799,299
Income taxes	**94,095**	99,983	**176,713**	199,825
Net income	**$ 279,579**	$ 329,532	**$ 502,953**	$ 599,474
Net income per share	**$2.20**	$2.48	**$3.90**	$4.50

Prior year reclassified for comparative purposes.

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 129,036,762 shares and 133,156,190 shares for the six month periods ended December 31, 1988 and December 26, 1987, respectively, and 127,111,940 shares and 133,067,064 shares for the three month periods ended December 31, 1988 and December 26, 1987, respectively.

Consolidated Balance Sheets

(Dollars in thousands)	December 31, 1988	July 2, 1988
Assets		
Current Assets		
Cash and temporary cash investments	**$ 1,679,109**	$ 2,163,580
Accounts receivable, net of allowances	**2,713,547**	2,592,160
Inventories	**1,684,528**	1,575,059
Prepaid expenses	**318,494**	274,160
Deferred income tax charges, net	**348,700**	324,962
Total Current Assets	**6,744,378**	6,929,921
Property, plant and equipment, net	**3,380,274**	3,095,025
Other assets, net	**106,315**	86,610
Total Assets	**$10,230,967**	$10,111,556
Liabilities and Stockholders' Equity		
Current Liabilities		
Bank loans and current portion of long-term debt	**$ 156,568**	$ 154,670
Other current liabilities	**2,335,056**	2,259,434
Total Current Liabilities	**2,491,624**	2,414,104
Deferred income tax credits, net	**68,100**	63,154
Long-term debt	**129,217**	123,924
Total Liabilities	**2,688,941**	2,601,182
Stockholders' Equity		
Common Stock, $1 par value	**130,008**	130,008
Additional paid-in capital	**2,451,002**	2,424,391
Retained earnings	**5,881,942**	5,463,050
Treasury stock at cost, 8,521,558 and 3,718,375 shares	**(920,926)**	(507,075)
Total Stockholders' Equity	**7,542,026**	7,510,374
Total Liabilities and Stockholders' Equity	**$10,230,967**	$10,111,556

Consolidated Statements of Changes in Financial Position

	Six Months Ended	
(Dollars-in thousands)	December 31, 1988	December 26, 1987
Funds from Operations		
Net income	**$ 502,953**	$ 599,474
Depreciation and amortization	**307,719**	226,568
Other	**17,952**	7,245
Total from operations	**828,624**	833,287
Funds to Support Operations		
Increase (decrease) in working capital:		
Accounts receivable	**121,387**	194,479
Inventories	**109,469**	88,675
Prepaid expenses	**44,334**	35,270
Other current liabilities	**(75,622)**	(252,239)
Net increase in working capital	**199,568**	66,185
Additions to property, plant and equipment	**599,045**	646,298
Increase in other assets	**30,883**	23,019
Total to support operations	**829,496**	735,502
Net increase (decrease) in funds from operations	**(872)**	97,785
Funds Provided (Used) by		
Bank loans and long-term debt	**7,191**	6,054
Stock issued under employee stock option and purchase plans	**116,104**	115,823
Purchase of treasury stock	**(606,894)**	0
Total funds from (used for) financing sources	**(483,599)**	121,877
Net increase (decrease) in cash and temporary cash investments	**(484,471)**	219,662
Cash and temporary cash investments at beginning of year	**2,163,580**	2,118,295
Cash and temporary cash investments at end of period	**$1,679,109**	$2,337,957

Digital's common stock is listed and traded on the New York Stock Exchange and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, Midwest Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

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Third Quarter Report

Digital Equipment Corporation
Maynard, Massachusetts 01754

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On the cover...In April, Digital pushed the performance of its MicroVAX line to new levels with the introduction of MicroVAX 3800 and MicroVAX 3900 systems.

To Our Shareholders

U.S. demand fell below expectations during the quarter, while our European and Asian business remained strong.

We are a financially strong company, and are continuing our large investment in future product development. However, we are equally committed to controlling costs and overhead, and increasing productivity.

During the quarter, Digital introduced several new VAX and RISC computer systems that have dramatic speed improvements and lower prices. There is strong customer demand for these newly announced products. By embracing the UNIX™ operating system with as much enthusiasm as we have traditionally exhibited for our VAX/VMS systems, we have broadened our product strategy and given our customers the freedom of choice.

Digital's VAX/VMS workstations are particularly popular where large engineering operations are networked over wide areas. Last year, in fact, our VAXstation 2000 was the world's largest-selling workstation. Where workstations are used in small groups, Digital's new UNIX workstations are already making an impact on the industry because of their high speed and low price.

We are committed to offering complete solutions for our customers. Nearly 700 independent software vendors have been trained on Digital's new desktop products and how to incorporate DECwindows software.

Our objective always has been to provide our customers with the very best computing system technology. Recently, product development cycles have shortened throughout the industry, and Digital is remaining competitive by introducing products with better price-performance. All our products work together in a common application and networking architecture to offer enterprise-wide computing.

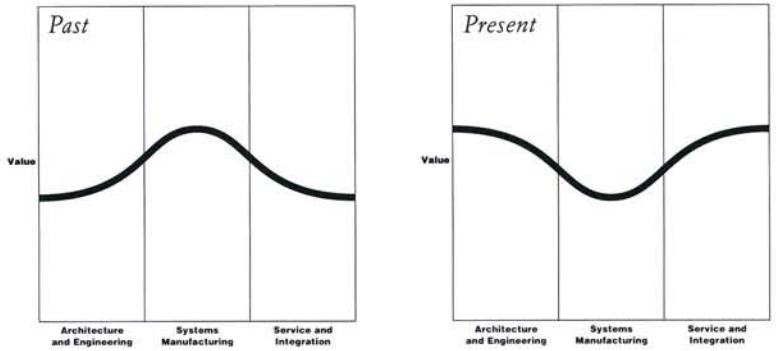
Kenneth H. Olsen
President

Digital Responding to Evolution in Customers' Perception of Value Added

In the 1960s and 1970s most computer makers, Digital included, added value in the manufacture of systems that utilized off-the-shelf components. The "added value" focus was systems engineering – the design and assembly of hardware and the development of operating system software. Thousands and thousands of Digital systems ended up in customers' offices and plants, and they did their separate jobs well.

As it became clear that the bigger challenge was making systems work together, however, customers' perception of the value added point began to shift. They looked for vendors who supported industry standards and developed architectures – for chips, software, and networks – engineering these components before a single systems box was built. These architectures were tremendously capital intensive, but once developed, formed the basis for the design and production of millions of systems serving the needs of millions of users.

Customers' Changing Perceptions of Value Added



Now the focus is shifting again – with increasing demand for program management of all the resources necessary to successfully implement complete solutions for end users. Customers search out companies who not only understand their information system needs but can also custom-tailor a solution out of the available component products – not just the vendor's own.

Digital is responding to this shift. In the past year the company planned, designed, implemented and managed over 5000 custom local area networks incorporating a wide mix of computing resources. Moreover, Digital services and supports over 1000 products from other vendors – including half a dozen IBM-compatible PCs – helping to manage ongoing support once networks are installed.

In 1989 Digital is managing over 100 projects with an average value of $30 million each – equal to a Fortune 100 company in its own right. Yet Digital has not established a separate operating division, choosing rather to draw resources from across the Corporation to work directly with other leading systems integration firms, independent software vendors, and clients' management, engineering, and support teams.

"...Digital is managing over 100 projects with an average value of $30 million each – equal to a Fortune 500 company in its own right."

In the third quarter, for example, Digital's Seattle team began work on a computer integrated manufacturing system for Boeing Commercial Airplanes and Boeing Computer Services. As prime contractor for the largest computer-integrated manufacturing undertaking in Boeing's history, a new $235-million sheet metal facility, Digital will provide program and integration management, as well as networked computer systems.

Support integration for the Boeing program is being provided through the combination of Digital's traditional services and customized support solutions. Ongoing service and support solutions will be tailored to meet the requirements of critical operations like shop floor, where site inventory and resident engineers will ensure fifteen minute response time. Major subcontractors include Consilium, Inc. of Mt. View, California, and ITP Boston, Inc., of Cambridge, Massachusetts, as well as Deloitte Haskins and Sells, Oracle Corporation, Epic Data Corporation, Palette Systems, Inc. and Impell Corporation.

The Shortcut for Software Development – A Common Application Program Interface

Independent software developers know how difficult it is to create different versions of a program for multiple hardware architectures and operating systems.

Digital has simplified this problem.

Digital's DECwindows application program interface helps programmers develop high-quality applications in less time and with reduced maintenance costs. An integral part of Digital's DECwindows Desktop Environment, it provides developers the tools they need to write applications that can run in multiple environments – VMS, ULTRIX (UNIX), and MS-DOS.

These are but a few of the reasons why the Open Software Foundation, a non-profit organization with more than 120 members worldwide, recently selected the DECwindows application program interface as a major part of its OSF/Motif™ user interface.

This interface has also been integrated into "Open Desktop"™ created by the Santa Cruz Operation, Inc., a leading vendor of UNIX software. The Open Desktop provides developers with an environment where they can create workstation-like applications and graphics for industry standard personal computers.

The response of independent software vendors has been equally enthusiastic. More than a thousand developers from over 700 companies have been trained on the DECwindows environment, and several hundred are actively developing products. Digital is supporting them with low-cost hardware and software development kits, access to Digital's software development and technical support personnel through its worldwide videotex and mail network, and pre-release training on unannounced Digital software products. Technical advisors and equipment are also available at Applications Development Technology centers on both the East and West coast.

New Links with Apollo, IBM, and Cray Systems

Digital has long recognized that it must maintain several different relationships with other vendors – as a customer, as a competitor, as a collaborator. Especially when open systems and network standards are concerned, collaboration often makes sense.

Digital and Apollo Computer, Inc., have announced they will work together to enhance Apollo's remote call procedure so that jobs can run on the processors best-suited for each portion of an application. An engineer working on a prototype for a new car, for example, will be able to perform the graphic portion on an Apollo workstation and simultaneously use a VAX system located elsewhere in the network to perform the numerical simulation.

At the same time Digital reconfirmed its commitment to customers with multivendor computing environments. A new Ethernet adapter will let customers bring Digital network functionality to the desktop over IBM's shielded twisted-pair wiring. And an extension of Digital's VAX-to-CRAY gateway, previously available only on the VAX 8250, will let users of higher-powered VAX 6200, VAX 6300, and VAX 8800 systems submit and retrieve jobs from their CRAY supercomputers.

Northern Telecom and MCI Alliances Reflect Commitment to Standards

Adherence to standards has been a significant factor in Digital's success as a computer company. Digital's commitment to a standards-based networking architecture has enabled the company to offer customers a simple migration path to new technologies. In fact, all of Digital's networking products and services are designed to evolve as standards evolve.

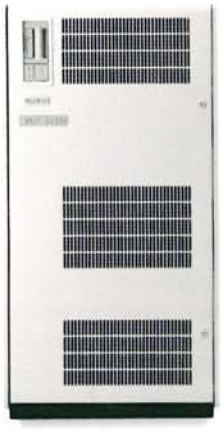
The value of this commitment is reflected in a growing number of joint developments in the telecommunications industry. During the quarter, Digital and Northern Telecom, Inc., announced new communications capabilities that integrate voice and data information resources at the desktop. On answering a phone a customer service representative, for example, will have pertinent information about the caller automatically displayed on the terminal. Related applications are being jointly developed with British Telecom in the United Kingdom.

In the United States Digital established an X.400 connection with MCI Communications Corporation, the first of its kind between Digital's internal electronic mail system and a U.S. public mail carrier. X.400 is the blueprint established by the International Telephony and Telegraphy Consultative Committee to give computer vendors a way to build compatible message systems.

The U.S. link joins similar private and public connections already established in Europe and will eventually be tied to Australia and the Far East, giving Digital a worldwide platform for enterprise-to-enterprise information exchange.

New VAX and MicroVAX Systems Announced

In addition to the desktop products that were highlighted in the Q2 report to shareholders, Digital made three major system announcements during the quarter.



VAX 6300

Digital's new VAX 6300 systems, enhancements to the popular VAX 6200 computer, deliver up to 35-percent higher performance for only 5-percent additional cost. Easily upgraded when additional capacity is required, VAX 6300 systems support enterprise-wide, departmental, and work group environments – meeting customer needs to integrate desktop devices and to distribute data and applications.

Digital also added a multiuser system to its family of RISC-based UNIX computer systems. The DECsystem 3100 computer can support from 4 to 32 users, or it can be used as a file server in a distributed computing environment. A sister product to the DECstation 3100 workstation announced in January, the DECsystem 3100 is Digital's first general purpose RISC system.

In early April, Digital unveiled new top-of-the-line MicroVAX systems along with a comprehensive program of price reductions, conversions, and upgrades to make distributed computing available to more markets than ever before.

The new MicroVAX 3800 and 3900 systems replace the MicroVAX 3500 and 3600 systems. Delivering up to one and a half times the performance and four times their storage capacity, the new MicroVAX systems are available as multiuser systems, server systems, or as realtime systems.

Workstation Sales Pace Major Wins in Quarter

Schlumberger CAD/CAM Division, McDonnell Douglas, Valid Logic, and Sanford C. Bernstein Select VAXstation 3100 and DECstation 3100 Workstations

Several significant orders for VAXstation 3100 and DECstation 3100 workstations demonstrated strong acceptance for Digital's newest desktop systems in the engineering and financial markets.

Schlumberger CAD/CAM Division has placed a $4.4-million order for nearly 300 VAXstation 3100 workstations. The company will include them as part of orders for customers who select Bravo3,® Schlumberger's software product for electromechanical design, engineering, and manufacturing.

McDonnell Douglas's Built Environment Technologies Division has ordered 96 VAXstation 3100 workstations to market with Graphics Design System (GDS)™ software, a civil engineering, facilities management, and geographic information systems package used by state and local governments and by architectural, engineering, and construction firms.

"...significant orders...demonstrated strong acceptance for Digital's newest desktop systems..."

Valid Logic Systems is using Digital's new workstations to port its existing electronic design automation software to Digital's RISC-based DECstation 3100 workstation. The $3.2-million sale will let Valid Logic significantly increase price/performance options for customers who want attractively priced UNIX-based workstations.

In the financial market, Sanford C. Bernstein & Co., Inc., a leading investment research and management company, will use 35 new VAXstation 3100 workstations to boost its ability to get customers in and out of trading positions faster and smarter. Portfolio managers will use the workstation for determining what to buy and sell, distributing the data to the traders' desks immediately, and executing orders faster and more accurately because the transactions are distributed electronically.

Group Health Association Initiates Five-year Multivendor Network Project

Group Health Association, the nation's second oldest health maintenance organization, has chosen Digital to integrate existing multivendor equipment in a new wide area network that will link eight satellite offices with its corporate database.

The initial phase will see a VAX 8810 and MicroVAX 3500 installed at headquarters. Central administrative and clinical information systems will be removed from existing systems and implemented with VMS. Digital's networking software and the ORACLE® relational database-management system will tie headquarters with the approximately 350 Hewlett-Packard workstations already installed.

As Group Health Association grows over the remainder of the contract, large VAX or VAXcluster systems will accommodate the expanding corporate information system, with additional MicroVAX systems handling distributed processing at the remote sites.

"...VAX or VAXcluster systems will accommodate the expanding corporate information system..."

Credit Lyonnais Streamlines $11-billion Funds Transfer Solution with Digital and Montran

Credit Lyonnais, a Paris-based financial institution, has incorporated VAX systems and The MONTRAN System™ to control its $11-billion funds transfer service for 800 international banks that conduct business in the French franc.

Digital's dependable, high-availability systems were chosen to help the bank meet the daily funds transfer deadlines imposed by the Federal Reserve. Together with The MONTRAN System, a fully integrated funds transfer package that runs exclusively on VAX systems, Credit Lyonnais can now easily handle its typical 6,000 funds transfer transactions each day, as well as the 10,000 daily transactions that occur during particularly hectic trading periods.

VMS Documentation Now Online

VMS documentation is now available online, giving programmers, software developers, and system managers easy access to VMS technical information. Using the DECwindows interface, they can now program in one window and display documentation in an adjacent window – all on the same screen.

Packing 30,000 pages of text and graphics onto a single compact disc, the VMS Online Documentation Library gives VMS users desktop access to the full library of VMS documentation – roughly equivalent to 15-feet of office shelf space.

Alliances/Cooperative Marketing Partners

In the third quarter several new alliances and additions to Digital's Cooperative Marketing Programs extended Digital's presence in desktop, transaction processing, and scientific markets.

New agreements are with:

- *Alisa Systems, Inc.,* Pasadena, California, for AlisaShare™ and AlisaPrint™ software for Macintosh® to VAX connectivity.
- *Computer Associates, Inc.,* San Diego, California, for CA-Strategem,™ a financial planning, budgeting, and management application.
- *Datatel,* Fairfax, Virginia for an OEM agreement for Colleague® and Benefactor® software to the higher education and nonprofit fundraising markets.
- *Honeywell, Inc.,* Industrial Automation Systems Division, Minneapolis, for an integrated process control system that can be linked to VAX systems.
- *IMSL, Inc.,* Houston, Texas, to jointly market IMSL's mathematical library to the scientific computing market.
- *Interactive Development Environments,* San Francisco, California, to jointly market Software Through Pictures,™ an integrated set of computer-aided software engineering tools.
- *Mechanical Dynamics, Inc.,* Ann Arbor, Michigan, to cooperatively market ADAMS+,™ a computer-aided-engineering product for dynamic analysis of mechanical systems.
- *The Montran Corporation,* New York, New York, to jointly market the MONTRAN System,™ a fully integrated, automatic funds movement and processing solution for wholesale banks.
- *Network Computing Corporation,* Charlotte, North Carolina, for an OEM agreement to market turnkey information systems for local governments and municipal utilities.
- *Planar Systems, Inc.,* Beaverton, Oregon, for limited, exclusive access to a supply of the industry's first 29-inch electroluminescent flat panel display monitor for workstations.
- *SPSS, Inc.,* Chicago, Illinois, to jointly market SPSS-X,™ a data and statistical analysis and reporting software product.
- *Quotient,* New York, New York, for joint marketing of CMARK,™ a modular line of comprehensive back office and trading solutions for the capital and banking markets worldwide.
- *Voice Processing Corporation,* Cambridge, Massachusetts, for a development agreement to provide speaker independent, continuous speech recognition capability for DECvoice.
- *West Publishing Company,* St. Paul, Minnesota, for WESTMATE,™ a communications software package that customizes VAX systems for accessing West's computer-assisted legal research service, WESTLAW.™

Digital Now Listed on Midwest Stock Exchange

During the quarter, Digital's common stock was approved for listing on the Midwest Stock Exchange in Chicago. Listing on the Midwest will support a competitive and liquid market for the company's common stock.

The Midwest, more than 100 years old, is the second largest stock exchange in the U.S. and fifth largest in the world. It is also among the most automated, based in part on Digital's VAX computer systems and DECnet/Ethernet local area networks. This leadership has generated interest from other exchanges seeking to emulate the Midwest's success, and has increased the visibility of Digital's hardware solutions for stock exchange trading.

"It is also among the most automated, based in part on Digital's VAX computer systems and DECnet/Ethernet local area networks."

Digital Wins Corporate Conscience Award

The Council on Economic Priorities has awarded Digital a "Community Action" Corporate Conscience Award for its corporate citizenship efforts.

The company was cited "for building a large plant in Boston's depressed Roxbury area," its "record of community outreach" for programs focused on job training and dropout prevention, for "purchasing from minorities and women," and for cosponsoring "a nationwide AIDS education program produced by Westinghouse."

The Council is a public interest research organization that evaluates the policies and practices of U.S. corporations and issues affecting national security. Founded in 1969, it seeks to promote corporate social responsibility and international peace.

Corporate Grant Highlights

Pine Street Inn. Digital has donated $387,000 in computer equipment to the Pine Street Inn, one of the largest shelters for the homeless in Massachusetts. Included is a VAX 8350 computer system that will tie Pine Street's terminals into one system and allow workers at all five shelter locations to keep track of guests and their medical records.

American Newspaper Publishers Association (ANPA). The American Newspaper Publishers Association in Reston, Virginia, will use a MicroVAX 3400 to test desktop publishing configurations appropriate for medium-size newspapers. Digital's DECnet/Ethernet will provide high-speed networking to link PCs and other devices in the ANPA laboratory, with the MicroVAX system functioning as a file server for the entire system.

Kids and Company: Together for Safety. Digital has funded the development of Kids and Company: Together for Safety, a project of the Adam Walsh Child Resource Center and the Washington, D.C. National Center for Missing and Exploited Children. Digital has invested over $375,000 during the past three years to assist the center's development of this personal child safety program that will be implemented in elementary grade levels across the country.

Vision Foundation. Vision Foundation, an organization based in Washington, D.C., was awarded a $274,000 equipment grant to assist in its creation of a one-of-a-kind information system containing historical and biographical data about the contributions of Afro-Americans to the history and culture of the United States. Digital's MicroVAX II and VAXmate systems will house the database and allow the foundation to respond to the requests of scholars, journalists, and researchers of black history and culture.

High Temperature Superconductivity Research. Through the European Contributions Program, a $336,000 equipment grant was awarded to ISS, an organization in Turin, Italy, dedicated to researching the findings on the concepts, models, and methods of High Temperature Superconductivity. The equipment donation includes a local area network connecting three MicroVAX systems, video terminals, printers, storage devices, and a wide range of the latest software products. Two high-speed network lines allow scientists to access supercomputers and databases around the world.

Consolidated Statements of Income

(Dollars in thousands except per share data)	Three Months Ended		Nine Months Ended	
	April 1, 1989	March 26, 1988	**April 1, 1989**	March 26, 1988
Revenues				
Product sales	**$1,993,677**	$1,833,751	**$5,935,244**	$5,345,120
Service and other revenues	**1,132,090**	990,231	**3,311,828**	2,790,887
Total operating revenues	**3,125,767**	2,823,982	**9,247,072**	8,136,007
Costs and Expenses				
Cost of product sales	**840,320**	761,018	**2,509,147**	2,160,973
Service expense and cost of other revenues	**680,168**	600,459	**2,016,802**	1,719,476
Research and engineering expenses	**383,699**	322,768	**1,124,100**	922,208
Selling, general and administrative expenses	**901,300**	759,352	**2,640,583**	2,205,514
Operating income	**320,280**	380,385	**956,440**	1,127,836
Interest expense	**8,379**	9,893	**29,366**	28,491
Interest income	**27,738**	36,370	**92,231**	106,816
Income before income taxes	**339,639**	406,862	**1,019,305**	1,206,161
Income taxes	**83,197**	101,716	**259,910**	301,541
Net income	**$ 256,442**	$ 305,146	**$ 759,395**	$ 904,620
Net income per share	**$2.05**	$2.33	**$5.94**	$6.83

Prior year reclassified for comparative purposes.

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 127,796,630 shares and 132,497,396 shares for the nine month periods ended April 1, 1989 and March 26, 1988, respectively, and 125,316,368 shares and 131,179,809 shares for the three month periods ended April 1, 1989 and March 26, 1988, respectively.

Consolidated Balance Sheets

(Dollars in thousands)	April 1, 1989	July 2, 1988
Assets		
Current Assets		
Cash and temporary cash investments	**$ 1,425,690**	$ 2,163,580
Accounts receivable, net of allowances	**2,745,841**	2,592,160
Inventories	**1,744,234**	1,575,059
Prepaid expenses	**275,334**	274,160
Deferred income tax charges, net	**360,300**	324,962
Total Current Assets	**6,551,399**	6,929,921
Property, plant and equipment, net	**3,523,354**	3,095,025
Other assets, net	**110,732**	86,610
Total Assets	**$10,185,485**	$10,111,556
Liabilities and Stockholders' Equity		
Current Liabilities		
Bank loans and current portion of long-term debt	**$ 3,452**	$ 154,670
Other current liabilities	**2,371,901**	2,259,434
Total Current Liabilities	**2,373,353**	2,414,104
Deferred income tax credits, net	**70,100**	63,154
Long-term debt	**127,952**	123,924
Total Liabilities	**2,573,405**	2,601,182
Stockholders' Equity		
Common Stock, $1 par value	**130,008**	130,008
Additional paid-in capital	**2,463,444**	2,424,391
Retained earnings	**6,115,413**	5,463,050
Treasury stock at cost, 9,985,910 and 3,718,375 shares	**(1,096,785)**	(507,075)
Total Stockholders' Equity	**7,612,080**	7,510,374
Total Liabilities and Stockholders' Equity	**$10,185,485**	$10,111,556

Consolidated Statements of Changes in Financial Position

	Nine Months Ended	
(Dollars in thousands)	April 1, 1989	March 26, 1988
Funds from Operations		
Net income	**$ 759,395**	$ 904,620
Depreciation and amortization	**485,222**	369,067
Other	**8,900**	5,174
Total from operations	**1,253,517**	1,278,861
Funds to Support Operations		
Increase (decrease) in working capital:		
Accounts receivable	**153,681**	208,262
Inventories	**169,175**	133,515
Prepaid expenses	**1,174**	47,071
Other current liabilities	**(112,467)**	(416,401)
Net change in working capital	**211,563**	(27,553)
Additions to property, plant and equipment	**904,659**	1,086,610
Increase in other assets	**42,069**	38,285
Total to support operations	**1,158,291**	1,097,342
Net increase in funds from operations	**95,226**	181,519
Funds Provided (Used) by		
Bank loans and long-term debt	**(147,190)**	5,409
Stock issued under employee stock option and purchase plans	**129,029**	129,425
Purchase of treasury stock	**(814,955)**	(363,498)
Total funds used for financing sources	**(833,116)**	(228,664)
Net decrease in cash and temporary cash investments	**(737,890)**	(47,145)
Cash and temporary cash investments at beginning of year	**2,163,580**	2,118,295
Cash and temporary cash investments at end of period	**$1,425,690**	$2,071,150

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

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digital

SECOND QUARTER REPORT
FY 90

Digital Equipment Corporation
Maynard, Massachusetts 01754

digital

Printed in U.S.A. ED 0003I-87/89 05 23 155.0 CTS

On the cover...Digital introduced the VAX 9000 mainframe-supercomputer and brought distributed processing to the high-end. Mainframes will never be the same.

TO OUR SHAREHOLDERS

As we enter the 1990s, we're rededicating ourselves to delivering solutions to our customers based on our leadership in distributed computing, multivendor networking and open standards. There are no changes in the fundamentals of our business that would cause us to alter this strategy.

Digital invests heavily to make its products meet all accepted standards, with a goal of enabling customers to run application software that plays on a variety of computers, and on many different operating systems. It seems clear to us that success will go to the company with the best technology, highest quality, most thorough testing, and most robust hardware systems. This means major investments, and in the first six months of this fiscal year alone we have invested $796 million in research and development; but it is, we believe, the cost of success in this industry.

It appears that the overall market for computers in Europe and Japan is good, but in the U.S. the market is still slow. Uncertain economic conditions are affecting customer purchasing intentions and slowing down the computer industry; consequently, we expect continued pressure on operating results. Digital is a financially strong company; cash flow has been positive and our balance sheet is solid. We have the resources to carry out our strategy of delivering the best solutions to our customers.

The VAX 9000 mainframe and supercomputer has been well received in the marketplace. Interest has been strong in the telecommunications, financial services, health care, and technical and scientific markets, among both domestic and international customers. We are particularly pleased with the level of activity from customers with commercial applications and the number of multiple unit orders being received. Looking ahead to the next several months, expected enhancements to our transaction processing capabilities should further strengthen our momentum in the high-end market.

Kenneth H. Olsen
President

DIGITAL CHANGES THE DEFINITION OF MAINFRAME COMPUTING

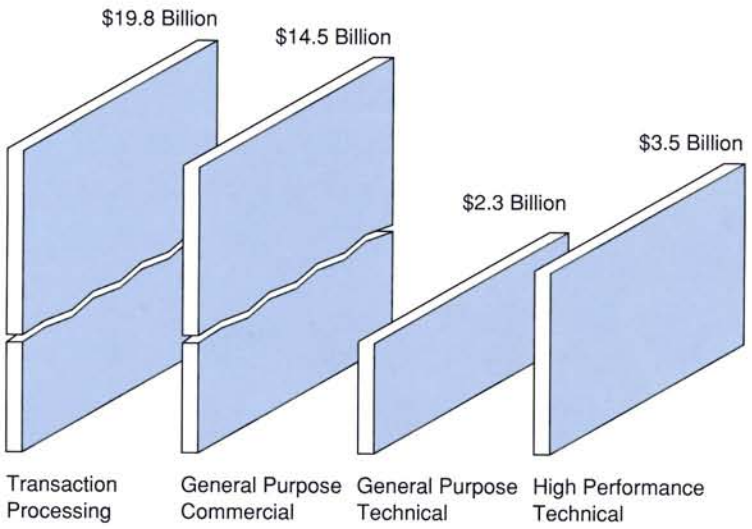
In the past, one style of computing defined the mainframe. Centralized, inflexible, and costly, it was isolated from mainstream office and technical environments.

Many companies have recognized the value of bringing information closer to users. This, of course, does not end their need for mainframes. It means they need a different type of mainframe. A mainframe that is approachable by personal computer and workstation users – regardless of whose equipment they are using. A mainframe that supports a single computing environment – in the data center, the office, the research lab, and on the manufacturing floor. A mainframe that can be distributed or remain in the corporate data center and communicate with applications and systems throughout the enterprise.

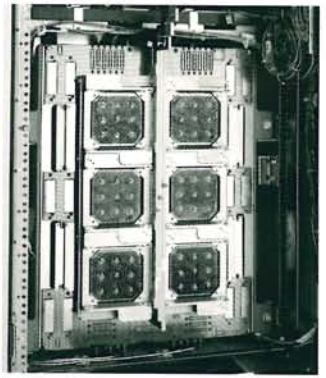
Digital anticipated these customer needs with the introduction of the VAX 9000 mainframe-supercomputer. Because of the VAX 9000 mainframe's price/performance advantage and low lifetime cost of ownership, it should change the dynamics of the mainframe market and stimulate its growth.

High-end computers sales are growing at over 6 percent a year, with a $40-billion market predicted for 1992. The chart below shows the estimated size of each segment (excluding supercomputers) within this market.

High-end Computing Worldwide Opportunity in 1992



Data Source: Gartner Group, IDC, Data Quest



The VAX 9000 is the high-performance engine for Digital's transaction processing capabilities. To this segment of the computer market, growing at 10 percent a year and expected to reach nearly $20 billion by 1992, Digital brings a series of advanced mainframe systems with the balance, throughput, and high availability needed for mission critical applications.

Within the combined $17-billion general purpose commercial and technical computing segments, Digital is attracting business from several sources. It is within these segments, of course, that thousands of large VAX systems need a growth path. Substantial business is anticipated from current owners who want to extend their applications to the highest level of mainframe computing.

"Mainframe computing will never be the same."

VAX 9000 systems will also be an attractive alternative for organizations with a mix of different desktop systems, including Digital, IBM,® Apple,® COMPAQ,® Sun, and Olivetti. Digital's NAS (Network Application Support) computing environment, built on networking and standards leadership, enables these customers to tie together the industry's widest range of multivendor desktop and large system resources.

Finally, the VAX 9000 architecture combines mainframe and supercomputer capabilities on both the VMS and ULTRIX platforms. By offering vector performance, Digital anticipates an increase in sales in high performance technical computing. Expanding at 25 percent per year, this is the fastest growing segment of the high end of the market.

By targeting its new capabilities to growth markets and by making ease of integration the first priority for general purpose computing, Digital has transformed the meaning of high-performance computing.

VAX 9000 WINS WORLDWIDE ACCEPTANCE

Orders for the VAX 9000 have come from the United States, Canada, Great Britain, West Germany, France, Finland, Denmark, Sweden, Italy, Portugal, Israel, Japan, Singapore, and Australia. The applications are equally diverse – including telecommunications billing, distribution, finance and administration, securities analysis, portfolio simulation, claims processing, CIM, network management, molecular modeling, engine simulation, and seismic processing applications.

Among the first U.S. purchasers are LiTel Communications Corporation and Penn State University, both customers who sought mainframe performance and reliability combined with the traditional benefits of the VAX architecture. LiTel, a telecommunications services company in Columbus, Ohio, will use the VAX 9000 to handle records for over 50 million calls placed each month over the company's long-distance fiber optic network. At Penn State, the VAX 9000 will support the library's online catalog. The system, one of the largest in the country, handles between 200,000 and 300,000 queries each week.

The most powerful computer system ever manufactured by Digital Equipment Corporation, the VAX 9000 delivers the well-balanced performance these organizations need for mainframe applications.

COMPUTER ASSOCIATES AND DIGITAL TO JOINTLY DEVELOP SYSTEM MANAGEMENT SOFTWARE

As part of its efforts to provide a wide range of software for the VAX 9000 mainframe and other large VAX and VAXcluster systems, Digital has formed a strategic alliance with Computer Associates International, Inc., to develop system management software to run in the VAX computing environment.

Joint efforts will occur in the areas of security, storage management, automated production control, job accounting, and data center administration. The companies also announced that Computer Associates products developed under the agreement are expected to be qualified for Digital's Cooperative Marketing Program.

The first product will be CA-NETMAN® for VAX systems, with other products being announced as they become available this year. Computer Associates International is the leading independent systems management software vendor in the marketplace.

NEW VAXSTATION SYSTEMS, OS/2 SUPPORT, AND WORKSTATION SOFTWARE UNVEILED FOR DESKTOP USERS

Even as Digital extended the VAX family upward with the VAX 9000 mainframe, it expanded the number of systems and software choices available for the desktop.

Digital added two models to the VAXstation 3100 workstation, enlarging its family of desktop systems. Named VAXstation 3100 Model 38 and Model 48 workstations, the new systems feature 50 percent greater performance than current systems. Also available are two realtime versions of VAXstation 3100 systems for users who need to control or monitor multiple processes and acquire data in realtime.

Expanding integration capabilities for IBM and compatible personal computers, network support for OS/2 was also announced in the quarter. The first deliverable in Digital's program to support OS/2 Standard Edition systems, DECnet for OS/2 enables IBM and selected compatible personal computers users to work as full peers in Digital's open networking environment.

In the workstation arena, a new version of Digital's ULTRIX software will make users and developers even more productive. Running on Digital's full range of VAX and RISC-based worksystems, the new software incorporates Adobe's Display PostScript for accurate what-you-see-is-what-you-get screen displays. Because users can view their documents exactly as they will appear on paper, productivity is greatly enhanced.

ALL-IN-1 RECONFIGURED TO SUPPORT MULTIVENDOR SYSTEMS

Users of IBM, Apple, COMPAQ, and Olivetti personal computers will now be able to choose Digital's ALL-IN-1 integrated office system when they need to work together easily and share information.

In the office of the 1990s, people will use a wide variety of desktop devices from different vendors. Even more than today, users will need to communicate, collaborate, and coordinate their efforts to remain competitive. Some will need a complete office information system. Others will want to select only a few capabilities – electronic mail perhaps, or business intelligence, electronic publishing, and other specialized business applications.

To meet these varied requirements, Digital is restructuring ALL-IN-1 on a client-server model. In this relationship, client software on the desktop gives users access to the network. Server software on a host provides electronic mail and conferencing, editing, calendar functions, or other ALL-IN-1 business applications across a local area or global network.

Users will be able to choose the desktop device they want. MS-DOS,® OS/2,® Standard Edition, Macintosh,® and IBM 3270 users will continue to work with the applications they are familiar with. No longer, however, will they be isolated from colleagues who have chosen other desktop systems.

Work groups will be able to expand or contract spontaneously as needs and tasks change, sharing software, and transmitting data, documents, and pictures. Yet all individuals will retain the freedom to work in the style that best suits their needs.

MULTIVENDOR NETWORK MANAGEMENT SIMPLIFIED

In a major announcement, Digital introduced products to simplify network management and outlined the steps being taken to fully implement its standards-based Enterprise Management Architecture.

With a VAXstation 3100-based console, users can call up one or more of Digital's network management modules on a DECwindows screen and move between them by clicking a mouse. At a later date, Digital will extend this capability so that network management modules from other vendors can "plug and play" on Digital networks.

The first modules, planned for announcement this year, will be delivered by Stratacom, Inc.; Vitalink Corporation; Codex Corporation; TSB International, Inc.; Digital Communications Associates, Inc.; Timeplex, Inc.; and Siemens AG.

Joining them will be vendors with expertise in public and private telephony, telemanagement systems and applications, and network components. 3Com Corporation; NYNEX Information Solutions Group, Inc.; INFONET; Chipcom Corporation; TelWatch, Inc.; and Newbridge Networks Corporation are the currently announced companies who will develop additional modules.

DIGITAL AND THE UNIVERSITY OF CALIFORNIA TO CREATE OSI BACKBONE NETWORK

Digital and the University of California are joining forces to build an Open Systems Interconnection (OSI) network and to form a link with the European Academic and Research Network (EARN).

The project will create an intercampus OSI backbone in the University of California system, gateways between this network and the major national networks in the United States, and a transatlantic link. Extensive use will be made of OSI protocols that are being implemented for DECnet Phase V software, Digital's OSI implementation planned for release in 1990.

"Customers can start building OSI networks now."

The Digital OSI backbone also makes it possible for customers to start building networks that will be consistent with OSI standards. Several newly announced routers, portals, and gateways will enable users of other network protocols – including TCP/IP, X.25, and IBM's SNA environment – to access existing networks and then transition smoothly to DECnet/OSI Phase V when it becomes available.

COMMITMENT TO U.S. GOVERNMENT STANDARDS REAFFIRMED

OSI standards are at the core of the U.S. Government Open Systems Interconnect Profile (GOSIP). Digital reaffirmed its commitment to this standard as well as to the Computer-aided Logistic Support (CALS) initiative.

Sponsored by industry and the U.S. Department of Defense, CALS aims at improving the timeliness and quality of development projects while reducing costs. To satisfy the goals of this effort, defense contractors and technology vendors are working together to establish a framework for exchanging and sharing information electronically.

These capabilities were shown at the 1989 CALS Exposition, where Digital designed, installed, and managed a network for nearly a dozen other vendors. With their applications operating concurrently, Digital was able to demonstrate its expertise in data exchange and sharing.

THE MARKET TURNS TO DIGITAL FOR NETWORKING AND INTEGRATION SOLUTIONS

Working directly with customers and third-party vendors, Digital is providing a wide range of business solutions across many industries.

Digital to Install Enterprise-wide Network for Nation's Largest Poultry Producer

Tyson® Foods, Inc., the nation's leading producer and marketer of poultry-based products, has signed an agreement with Digital that initiates a three year, $9.2-million project for the installation of an enterprise-wide network to integrate Tyson's corporate data center with its satellite plants.

The project calls for an 80-location Ethernet network, and includes VAXcluster systems at Tyson's Springdale, Arkansas, headquarters, as well as numerous VAXstation workstations and MicroVAX 3100 systems at remote locations.

During the first phase of the project, financial applications from McCormack & Dodge will be installed on the VAXcluster system in Springdale, while the VAXstation workstations and MicroVAX systems will allow distributed processing at the various remote sites. Subsequent applications will include sales and marketing, order entry, billing, inventory and warehouse distribution management.

Aetna Turns to Digital for Multivendor Desktop Integration and Service Solution

Aetna Life and Casualty Employee Benefits Division has purchased MicroVAX 3400 systems to integrate Apple Macintosh personal computers into a network that will connect 72 branch locations nationwide.

Digital will install and maintain all Digital systems as well as Aetna's new base of Apple microcomputers. The MicroVAX systems will function as file, print, and data servers for the Macintosh equipment and also connect Macintosh users with IBM host systems located at Aetna's home office in Connecticut.

Digital will be the systems integrator for the multimillion dollar effort, providing consulting for the design of the local area network and wide area network, project management services, and desktop support services. Included will be comprehensive multivendor hardware support for the Apple computers, as well as third-party local area networking and other related products.

Systems Integration Service Alliance Set With Deloitte Haskins & Sells

Digital and the professional services firm of Deloitte Haskins & Sells have signed a formal service alliance agreement to pursue systems integration programs in discrete and process manufacturing industries in the United States.

The outgrowth of a number of joint projects, the nonexclusive agreement covers the full range of consulting services provided by DH&S and all products and services offered by Digital.

The agreement is expected to facilitate joint marketing, sales, and service delivery by the two firms. Digital is especially interested in DH&S's strength in strategic planning and design services, manufacturing strategy development, information systems strategic planning, world-class manufacturing techniques, total quality management, and factory modernization.

Digital and Mitel Integrate Data and Voice Functions at Desktop

Under a new version of Digital's Computer-integrated Telephony (CIT) software, Digital and Mitel Corporation are offering new communication capabilities to integrate voice and data at the desktop.

"Digital is providing a wide range of business solutions across many industries."

With Digital software, users of Mitel's SX-2000 PBX can handle incoming and outgoing calls with the same link. They will also be able to make and break connections and utilize the special call transfer and call and station status services that are essential in an integrated voice and data environment.

Also announced was Digital's own CIT product, the VAX Computer-integrated Telephony Message Desk. The Message Desk enhances standard office telephone systems by providing keyboard dialing, electronic mailboxes, messaging services, and corporate directory functions for a more efficient answering service for people away from their desks.

Digital and General Dynamics to Develop Aerospace/Defense Management System

Digital, General Dynamics Corporation, and Matra Datavision, Inc., have entered into a major business agreement to develop and implement a suite of integrated management systems for General Dynamics' Convair Division in San Diego, California.

Digital will act as systems integrator for the project, which will network thousands of workstations using Digital's ULTRIX software and other vendors' operating systems. Matra Datavision, developer of the EUCLID®-IS CAD/CAM system for engineering and manufacturing applications, will work with Digital to implement the program.

General Dynamics' Convair Division will provide work process architecture and information flow requirements, which will be validated by a cluster of major manufacturers in the aerospace and defense electronics industries.

STOCKHOLDER RIGHTS PLAN ADOPTED

Digital's Board of Directors has adopted a Stockholder Rights Plan in which common stock purchase rights will be distributed as a rights dividend at the rate of one Right for each share of common stock held as of the close of business on December 21, 1989.

The Rights Plan is designed to deter coercive or inadequate takeover tactics and to prevent an acquirer from gaining control of the Company without offering a fair price to all of the Company's stockholders. Its adoption was not in response to any known effort to acquire control of the Company. The Rights will expire on December 21, 1999.

Each Right will entitle holders of Company common stock to buy one share of common stock of the Company at an exercise price of $400. The Rights will be exercisable only if a person or group acquires 20 percent or more of the common stock, or announces a tender or exchange offer which would result in its ownership of 30% or more of the common stock, or a person owning 10% or more of the common stock is determined by the Board to be an Adverse Person, as defined in the Rights Plan.

A summary of the rights was sent to all shareholders of record as of the close of business on December 21, 1989.

VAX 6000 SYSTEM TO POWER NEW EXPERIMENTS IN SPACE

Digital has delivered a VAX system to the National Aeronautics and Space Administration to pioneer high-technology experiments in space.

Raytheon Company's militarized version of Digital's VAX 6000 system was specially modified to make it ready for space. With several times the power of computers now aboard shuttle flights, the VAX 6000 system will play a key role in scientific experiments aboard an upcoming Shuttle mission.

NEW ALLIANCES AND COOPERATIVE MARKETING PROGRAM PARTICIPANTS

Among new companies joining Digital in cooperative efforts were

- **Adobe Systems, Incorporated,** Mountain View, California, to port Adobe Illustrator® to Digital's computing platform.
- **D. Appleton Co., Inc.,** Manhattan Beach, California, to jointly market Personal IDEF/Leverage and IDEF/Leverage database design software for VAX systems.
- **DISC, Inc.,** a NYNEX Company, Baltimore, Maryland, to cooperatively market DISC's Automated Cash Control and Electronic Statement System, DISC ACCESS.
- **Interleaf, Inc.,** Cambridge, Massachusetts, for Digital to provide onsite hardware service to more than 300 Interleaf customers in 38 states.
- **Metier Management Systems, Inc.,** Houston, Texas, to jointly market and sell Metier's family of business and project management software, ARTEMIS 7000, ARTEMIS 7000 Project, and ARTEMIS Team for VAX systems.
- **McHugh, Freeman & Associates, Inc.,** Brookfield, Wisconsin, to jointly market McHugh, Freeman & Associates' turnkey warehouse management and warehouse automation application, Distribution Manager.
- **McDonnell Douglas Systems Integration Company,** St. Louis, Missouri, to cooperatively market Force Management System II (FMS II),™ an integrated telephone operator scheduling system.
- **Schlumberger Technologies CAD/CAM Division,** Ann Arbor, Michigan, for Digital to distribute Bravo3® CAD/CAM/CAE software.
- **UIS, Incorporated,** Lexington, Massachusetts, to jointly market UIS's V-X PACS™ resource management and chargeback software.
- **Wolfram Research, Inc.,** Champaign, Illinois, for Digital to sell and support Wolfram's comprehensive Mathematica® software system for its entire line of VAX and RISC computer systems.

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)	Three Months Ended		Six Months Ended	
	December 30, 1989	December 31, 1988	**December 30, 1989**	December 31, 1988
Revenues				
Product sales	**$2,006,793**	$2,045,166	**$4,001,201**	$3,941,567
Service and other revenues	**1,178,002**	1,134,340	**2,314,784**	2,179,738
Total operating revenues	**3,184,795**	3,179,506	**6,315,985**	6,121,305
Costs and Expenses				
Cost of product sales	**935,025**	869,205	**1,817,155**	1,668,827
Service expense and cost of other revenues	**724,461**	686,966	**1,454,259**	1,336,634
Research and engineering expenses	**391,877**	376,405	**796,008**	740,401
Selling, general and administrative expenses	**961,304**	891,024	**1,900,271**	1,739,283
Operating income	**172,128**	355,906	**348,292**	636,160
Interest expense	**10,703**	12,085	**19,008**	20,987
Interest income	**32,721**	29,853	**63,261**	64,493
Income before income taxes	**194,146**	373,674	**392,545**	679,666
Income taxes	**38,744**	94,095	**86,360**	176,713
Net income	**$ 155,402**	$ 279,579	**$ 306,185**	$ 502,953
Net income per share	**$1.25**	$2.20	**$2.44**	$3.90

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 125,290,571 shares and 129,036,762 shares for the six month periods ended December 30, 1989, and December 31, 1988, respectively, and 124,813,013 shares and 127,111,940 shares for the three month periods ended December 30, 1989 and December 31, 1988, respectively.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	December 30, 1989	July 1, 1989
Assets		
Current Assets		
Cash and cash equivalents	**$ 1,980,236**	$ 1,655,264
Accounts receivable, net of allowances	**2,997,057**	2,965,408
Inventories	**1,708,953**	1,638,001
Prepaid expenses	**310,613**	255,195
Deferred income tax charges, net	**392,100**	381,140
Total Current Assets	**7,388,959**	6,895,008
Property, plant and equipment, net	**3,731,034**	3,645,896
Other assets, net	**134,666**	126,875
Total Assets	**$11,254,659**	$10,667,779
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	**$ 603,716**	$ 553,818
Deferred revenue	**783,040**	833,831
Other liabilities	**1,300,734**	1,006,390
Total Current Liabilities	**2,687,490**	2,394,039
Deferred income tax credits, net	**103,500**	102,048
Long-term debt	**137,384**	136,019
Total Liabilities	**2,928,374**	2,632,106
Stockholders' Equity		
Common Stock, $1 par value	**130,008**	130,008
Additional paid-in capital	**2,489,628**	2,469,711
Retained earnings	**6,573,352**	6,366,418
Treasury stock at cost, 8,147,573 and 8,471,655 shares	**(866,703)**	(930,464)
Total Stockholders' Equity	**8,326,285**	8,035,673
Total Liabilities and Stockholders' Equity	**$11,254,659**	$10,667,779

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended	
(Dollars in thousands)	December 30, 1989	December 31, 1988
Cash Flows from Operating Activities		
Net income	**$ 306,185**	$ 502,953
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	**365,317**	307,719
Other adjustments to income	**57,683**	36,744
(Increase)/decrease in accounts receivable	**(31,649)**	(121,387)
(Increase)/decrease in inventories	**(70,952)**	(109,469)
(Increase)/decrease in prepaid expenses	**(55,418)**	(44,334)
Increase/(decrease) in accounts payable	**49,898**	(2,262)
Increase/(decrease) in deferred revenues	**(50,791)**	29,484
Increase/(decrease) in other liabilities	**308,919**	29,608
Total adjustments	**573,007**	126,103
Net cash flows from operating activities	**879,192**	629,056
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	**(472,182)**	(599,045)
Other assets, net	**(26,220)**	(30,883)
Net cash flows from investing activities	**(498,402)**	(629,928)
Net cash flows from operating and investing activities	**380,790**	(872)
Cash Flows from Financing Activities		
Proceeds from issuance of debt	**0**	7,563
Payments to retire debt	**(22,718)**	(372)
Purchase of treasury stock	**(159,264)**	(606,894)
Proceeds from issuance of treasury shares	**126,164**	116,104
Net cash flows from financing activities	**(55,818)**	(483,599)
Increase/(decrease) in cash and cash equivalents	**324,972**	(484,471)
Cash and cash equivalents at the beginning of year	**1,655,264**	2,163,580
Cash and cash equivalents at end of period	**$1,980,236**	$1,679,109

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

Inquiries relating to investment in Digital Equipment Corporation should be directed to:

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Introducing the VAX 6000 Model 500

Q1

FIRST QUARTER REPORT
FY 91

Digital Equipment Corporation
Maynard, Massachusetts 01754

Printed in U.S.A. ED-00589-87/90 02 04 87.0 CTS

New Semiconductor Plant Demonstrates Digital's Commitment to European Markets.

To effectively compete in Europe, you have to manufacture in Europe. With the opening in Scotland of one of the most advanced semiconductor plants in the world, Digital has become the only manufacturer to work within the U.K. from raw silicon through production of the finished computer system.

Digital gains a competitive advantage as 1992 draws near and as markets in Eastern Europe open to Western companies. Digital is an established, high-technology presence.

In Scotland, Digital is now manufacturing MicroVAX systems from silicon on up. In Ireland, Digital is building VAX 9000 mainframes. Digital also has manufacturing, research and software development facilities in France, Germany, and Italy. Digital has a growing presence in Eastern Europe. Europe now accounts for more than 40 percent of Digital revenues. The company is making the investments needed to support further growth.

The new $165-million South Queensferry plant, ten miles from Edinburgh, represents Digital's largest investment outside the U.S. Together with Digital's semiconductor manufacturing facilities in Hudson, Massachusetts, and its Cupertino, California, facility where unique, semiconductor-like technology is used to manufacture the multiple chip units for the VAX 9000 mainframe, the South Queensferry plant gives Digital the ability to develop state-of-the-art technology for both its VAX and RISC-based computer lines.

THE QUARTER IN REVIEW

VMS Operating System to Conform with POSIX and X/Open Standards

Digital announced that it intends to add to the VMS operating system support for the widely accepted POSIX (Portable Operating System Interface) standards of the IEEE (Institute of Electrical and Electronics Engineers), making it almost as easy to port many UNIX applications to VMS as it is to port to another version of UNIX. POSIX is the set of industry standards designed to enable users and conforming applications to move from one system to another.

Digital also announced it intends to have the VMS operating system "branded" by X/Open, the nonprofit consortium of many of the world's major information system suppliers. X/Open defines an integrated operating environment based on de facto and international standards. To become certified and branded, the company will incorporate into VMS many of the standards outlined by the latest version of the X/Open Portability Guide.

Both Digital's RISC-based and VAX computers can already display the X/Open branding trademark. With the completion of the process for VMS, Digital will offer one of the largest portfolios of standards-compliant platforms in the industry.

Improved Performance for VAX 6000 Systems

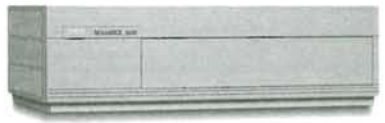
New VAX 6000 systems bring significantly enhanced I/O and CPU performance to Digital's VAX 6000 series, the fastest selling VAX computers ever on a dollar basis. For online transaction processing applications in data centers, for networked configurations that provide timesharing access to large departments, and for client/server systems in large, data-intensive work groups, these new products are part of Digital's strategy to employ the latest technology and provide continuous performance and price/performance gains for VMS customers. The addition of RISC I/O technology to VAX 6000 systems, for example, results in major I/O performance gains.

New VAX 6000 enhancements include double the memory capacity, triple the I/O performance, and quadruple the disk storage capacity (up to 5 huge terabytes) of earlier VAX 6000 systems. The new VAX 6000 Model 500 systems offer 85 percent to 100 percent more CPU performance than the previous VAX 6000 Model 400 systems at a price only 16 percent to 18 percent higher. All 10,000-plus VAX 6000 systems in the field can be easily upgraded – within their original cabinets – to these new performance levels.

VAXstation, MicroVAX, VAXserver, and PCLAN/Server Systems Enhanced

Digital enhanced several of its smaller systems, significantly improving their price/performance over previous models.

The newly announced VAXstation 3100 Model 76 is Digital's highest-performance VMS workstation to date, with two and one-half times the system performance of existing VAXstation systems. Incorporating the VAX 4000 CMOS chipset, the VAXstation 3100 Model 76 brings added power to the desktop in markets such as medical imaging, financial trading, computer-aided design, manufacturing control, military command and control, and realtime simulation.



Digital also boosted by 45 percent the performance of its lowest-priced, highest-volume VAX systems with the announcement of two new MicroVAX and VAXserver 3100 systems, Models 20e and 10e (above). Both systems, which are compact enough to sit on a shelf or tabletop in small-business environments, come with a factory-installed VMS operating system and DECnet communications.

The new PCLAN/Server 3100e, with factory-installed PC integration software, provides information and resource-sharing services for up to 70 simultaneous personal computers in a local or wide area network.

Value Added Resellers to Market System for Small and Medium Businesses

Value Added Resellers (VARs) will market the new applicationDEC 433MP, Digital's most expandable system for small and medium businesses. The system, developed and manufactured by Digital, is based on the popular SCO UNIX System V and the Intel 486 microprocessor.

The applicationDEC 433MP, based completely on industry-standard technology, provides VARs and their customers ease of configuration and a wide range of choices. A multiprocessor system, the applicationDEC 433MP can scale from 1 to more than 128 users and operate simultaneously as a multiuser machine, a PCLAN/Server, and an X Window System server.

The new system runs more than 4,000 SCO UNIX V applications, Open Desktop, 15,000 MS-DOS applications and 1,500 PICK applications.

DECWORLD'90 Demonstrates Innovation That Works

In early July, Digital opened DECWORLD'90 in Boston, giving customers an opportunity to see firsthand how the company has implemented its product and business strategies.

The DECWORLD program included seminars, workshops, demonstrations, and laboratories where customers worked with Digital and third-party specialists to explore the ways computer applications address critical business needs.

Over 34,000 attended the Boston event before it moved on to Canberra, Australia, in August, and to Cannes, France, in September. When DECWORLD'90 closes in Tokyo in November, it is expected that nearly 50,000 will have attended.

Digital Equipment of Canada Limited Wins Major Contracts

Digital Equipment of Canada Limited has been awarded two multimillion-dollar systems integration contracts.

For Hughes Aircraft of Canada, Digital will provide local area networks, computers, and operating system software for the Canadian Automated Air Traffic System (CAATS). Hughes is prime contractor and systems integrator for the $400-million project that will integrate 7 regional air traffic control centers, 56 operational support centers, and 60 air traffic control towers throughout Canada.

For the Treasury Board of Canada's corporate office information network, Digital will be prime contractor for systems integration and facilities management. Under terms of the contract, Digital will design, implement, and manage a multivendor network integrating IBM, UNIX, Amdahl, and WANG systems for some 800 users throughout the Treasury Board's 10 branches in Ottawa.

British Retailer W. H. Smith Awards $28-million Network Contract

Digital has received a five-year, $28-million contract from W.H. Smith, a diversified British retailer.

Digital will provide new technology and equipment, and manage the company's wide area network, which links over 450 stores and distribution centers to administrative offices in Swindon and Bradford, England. Altogether, W.H. Smith operates nearly 2100 outlets in Great Britain, the U.S., and Canada.

Digital to Install MIT's Athena Technology at Two Universities

Athena, the innovative computing environment developed at the Massachusetts Institute of Technology, will soon be up and running at two new campuses.

North Carolina State University (NCSU) and Iowa State University (ISU) have signed contracts totaling $7 million with Digital to install the Athena systems software and link together hundreds of Digital workstations. On each campus, the result will be a large-scale, high-performance network designed to support students, faculty, and researchers using UNIX-based systems.

University of Kansas Boosts Computing Power 500 Percent with VAX 9000 Supercomputer

Researchers at the University of Kansas will be getting answers to questions five times faster with their new VAX 9000 mainframe. Meeting the university's needs for a computer that will operate with VMS today and UNIX in the future, the VAX 9000 vector processor will be used for advanced work in physics, astronomy, aerospace engineering, chemistry, molecular chemistry, pharmaceuticals, and computer science.

The University of Kansas, California State Polytechnic University, Pennsylvania State University, and the University of Pittsburgh are the first four universities to purchase Digital's VAX 9000 mainframe.

New Alliances and Cooperative Marketing Program Participants

Among the companies joining Digital in new cooperative efforts were

- **Brock Control Systems, Inc.,** Atlanta, Georgia, to market its Brock Activity Manager Series of telemarketing, sales account management, marketing, and customer service applications on Digital's VAX and RISC-based systems.
- **Cerner Corporation,** Kansas City, Missouri, to jointly market Healthcare Network Architecture, Cerner's array of integrated information applications for clinical laboratories, radiology and pharmacy departments, and nursing stations.
- **Covalent Systems,** Freemont, California, to jointly market ShopSystem FX, Covalent's advanced graphic arts management information system, on Digital's RISC-based systems.
- **INTERMEC Corporation,** Everett, Washington, to cooperatively market INTERMEC Data Flow Manager, a shop floor and manufacturing data collection system running on VAX systems.

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)	Three Months Ended **September 29,1990**	September 30, 1989
Revenues		
Product sales	**$1,865,558**	$1,994,408
Service and other revenues	**1,227,812**	1,136,782
Total operating revenues	**3,093,370**	3,131,190
Costs and Expenses		
Cost of product sales	**878,015**	882,130
Service expense and cost of other revenues	**779,708**	729,798
Research and engineering expenses	**401,952**	404,131
Selling, general and administrative expenses	**1,023,576**	938,967
Operating income	**10,119**	176,164
Interest expense	**6,946**	8,305
Interest income	**31,729**	30,540
Income before income taxes	**34,902**	198,399
Income taxes	**8,725**	47,616
Net income	**$ 26,177**	$ 150,783
Net income per share	**$.21**	$1.20

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 123,774,888 shares for the three months ended September 29, 1990 and 125,768,130 shares for the three months ended September 30, 1989.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	**September 29,1990**	June 30, 1990
Assets		
Current Assets		
Cash and cash equivalents	**$ 1,597,908**	$ 2,008,983
Accounts receivable, net of allowances	**3,338,580**	3,206,765
Inventories	**1,667,308**	1,538,258
Prepaid expenses	**415,473**	345,797
Deferred income tax charges, net	**500,000**	521,809
Total Current Assets	**7,519,269**	7,621,612
Property, plant and equipment, net	**3,838,061**	3,868,092
Other assets, net	**161,937**	165,117
Total Assets	**$11,519,267**	$11,654,821
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	**$ 665,758**	$ 660,819
Deferred revenue	**931,955**	903,038
Other liabilities	**1,754,714**	1,725,912
Total Current Liabilities	**3,352,427**	3,289,769
Deferred income tax credits, net	**28,000**	33,137
Long-term debt	**150,228**	150,001
Total Liabilities	**3,530,655**	3,472,907
Stockholders' Equity		
Common Stock, $1 par value	**130,008**	130,008
Additional paid-in capital	**2,577,895**	2,565,487
Retained earnings	**6,256,717**	6,257,199
Treasury stock at cost, 10,791,097 and 7,453,501 shares	**(976,008)**	(770,780)
Total Stockholders' Equity	**7,988,612**	8,181,914
Total Liabilities and Stockholders' Equity	**$11,519,267**	$11,654,821

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Three Months Ended September 29, 1990	Three Months Ended September 30, 1989
Cash Flows from Operating Activities		
Net income	**$ 26,177**	$ 150,783
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	**186,500**	175,498
Other adjustments to income	**35,711**	15,318
(Increase)/decrease in accounts receivable	**(131,815)**	(27,942)
(Increase)/decrease in inventories	**(129,050)**	(46,493)
(Increase)/decrease in prepaid expenses	**(69,676)**	(19,432)
Increase/(decrease) in accounts payable	**4,939**	(49,821)
Increase/(decrease) in deferred revenues	**28,917**	(35,646)
Increase/(decrease) in other liabilities	**45,537**	267,598
Total adjustments	**(28,937)**	279,080
Net cash flows from operating activities	**(2,760)**	429,863
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	**(173,235)**	(233,059)
Other assets, net	**(7,072)**	(11,406)
Net cash flows from investing activities	**(180,307)**	(244,465)
Net cash flows from operating and investing activities	**(183,067)**	185,398
Cash Flows from Financing Activities		
Proceeds from issuance of debt	**196**	0
Payments to retire debt	**(32)**	(23,635)
Purchase of treasury stock	**(240,719)**	0
Proceeds from issuance of treasury stock	**12,547**	17,071
Net cash flows from financing activities	**(228,008)**	(6,564)
Increase/(decrease) in cash and cash equivalents	**(411,075)**	178,834
Cash and cash equivalents at the beginning of year	**2,008,983**	1,655,264
Cash and cash equivalents at end of period	**$1,597,908**	$1,834,098

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

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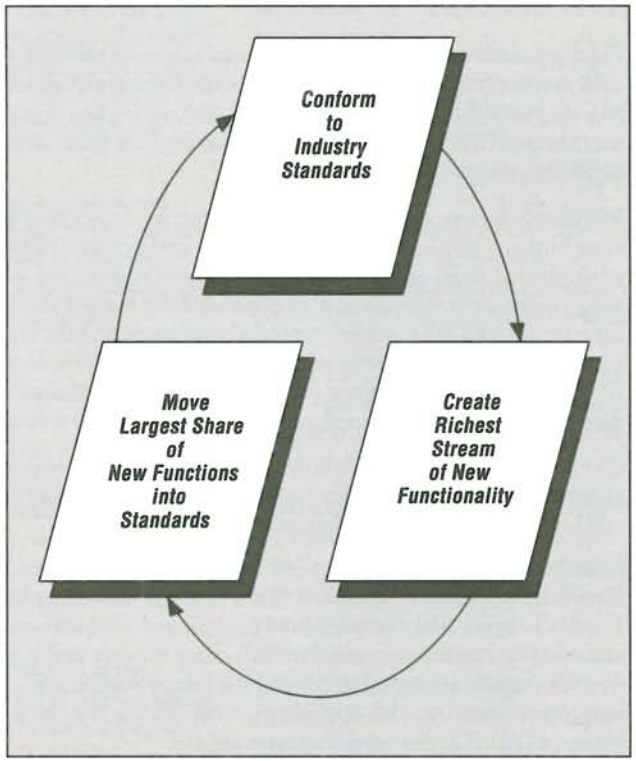
digital



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SECOND QUARTER REPORT
FY 91

Digital Equipment Corporation
Maynard, Massachusetts 01754

digital

Printed in U.S.A. ED 00937 87/90 10 04 83.5 CTS

TO OUR SHAREHOLDERS

With this quarter's results, we are beginning to see the benefits from several investments and our ongoing efforts to control costs and improve revenue growth. Our progress is an indication that we are on the right track but we know there is a lot of work ahead. The industry is changing quickly; we need to adjust our business to these changes and this all has to be done in a very uncertain economic environment.

For the quarter, the Company reported total operating revenues of $3,352,417,000, up 5 percent from the $3,184,795,000 of the comparable quarter a year ago. Net income for the quarter was $111,141,000, versus last year's second quarter net income of $155,402,000. Quarterly earnings per share were $.92 versus $1.25 last year.

Worldwide service revenues grew 16 percent; our Enterprise Integration Services business continues to expand rapidly; and overseas revenue and demand strengthened. Sales of RISC-based workstations and servers using the UNIX operating system grew strongly and we expanded our market share. Customer demand for our new VAX 4000 system exceeded expectations. Interest in Digital's mainframe VAX 9000 system remains high. During the quarter we shipped more than 100 systems and we anticipate exceeding that number in the third quarter. To date the company has shipped more than 180 VAX 9000 systems.

Our financial stability and flexibility allows us to continue investments in high growth business opportunities, customer support, the development of alternative and lower cost distribution channels, and new technology.

Customers are very excited by our integrated approach to multivendor systems, Network Application Support. NAS is a comprehensive implementation of open standards. In parallel, the continued evolution of VMS software to incorporate and comply with industry standard interfaces is being well received by customers who want application portability and the robust computing environment that they expect from the VMS operating system. We are close to achieving our own vision of Digital as the open systems company.

We have shared this vision with more than forty thousand customers who attended DECWORLD '90 in Boston; Canberra, Australia; Cannes, France; and, this November, Tokyo. DECWORLD '90 demonstrated Digital capabilities as a global company.

These capabilities will be enhanced with the acquisition of a 65% interest in a new German company to be formed from the former Kienzle computer systems division of Mannesmann AG. This investment, that strengthens Digital's presence in the emerging markets of Eastern and Central Europe, is described in detail in the text of this report.

Kenneth H. Olsen
President

DIRECTIONS

Digital's Strategy: A Unified Software Environment – The Added Value Digital Brings to its Customers

Five years ago Digital announced its intention to provide the software and services needed to integrate different computing environments. This added value would enable Digital to build a successful and profitable software business.

Digital recognized that existing standards only ensure baseline functionality. Simply meeting those standards would offer the customer nothing more than the next computer company.

But, by adding functionality, Digital would add value. And, so this added value will not be lost in multivendor environments, Digital committed to getting it incorporated into industry standards. The process, as shown on the cover of this report, is continuous. And Digital is implementing it successfully.

Digital has the best record in the computer industry for delivering technology to the Open Software Foundation (OSF). This software has been incorporated into OSF standards. OSF/Motif, the emerging standard for window-based application program interfaces, is a good example. The toolkit, on which Motif is based, was developed by Digital.

While the UNIX operating system can lessen a customer's dependence on a particular vendor, it locks that customer in to a particular software system. It does nothing to help the customer integrate the enterprise from the desktop to the datacenter.

Since announcing its software strategy, Digital has worked closely with other companies to develop Network Application Support (NAS) services that run across multiple operating systems.

The implementation of this strategy means the customer is no longer tied to one computer family, one family of software, or even one computer vendor. For example, Digital's Pathworks software uses NAS services to integrate industry-standard PCs with computers and data resources supported by Digital networks. To date, Pathworks software has been installed on more than 500,000 PCs. And more than 10,000 Macintosh licenses have been sold since Pathworks for Macintosh began shipping at the end of September.

Over a quarter of Digital's engineering staff are directly involved in this software effort. They are working with more than 650 independent software companies who share Digital's vision and who have developed over 1,250 applications that use Digital's Network Applications Support services.

NAS is a vendor-neutral, applications-centered networking environment that can be layered over different operating systems. NAS integrates VMS, UNIX, MS-DOS, OS-2, and Apple Macintosh operating systems. It unifies applications and databases. And, because NAS is based on a widening stream of industry and de facto standards, it provides the technology that could bring IBM MVS and other operating systems into a unified, multivendor environment.

Digital and Mannesmann AG Form Major Company to Build Digital's Infrastructure in Central and Eastern Europe

Shortly before the end of the Quarter, Digital reached agreement with Mannesmann AG to acquire 65 percent of a new company to be formed from the Mannesmann Kienzle Computer Systems Division, and the PROCAD GmbH and PCS GmbH divisions of Mannesmann Kienzle. Mannesmann AG will own 35 percent of the new company.

This investment gives Digital an established infrastructure to support growing sales in Central and Eastern Europe as well as a portfolio of software applications designed for small- and medium-sized businesses.

The new company, headquartered in Villingen, Germany, will be called Digital-Kienzle Computer Systeme GmbH & Co KG, as soon as the necessary regulatory approvals are obtained. Digital will invest $230 million in the new company. While Digital-Kienzle will be managed as a separate entity, its operating results will be consolidated with those of Digital.

Kienzle, with 26 offices throughout Europe, is Germany's second largest domestic computer company with annual sales of over $500 million.

Expanded Marketing, Sales, and Support Programs for the UNIX Operating System

With the formation of Digital-Kienzle, and the continued growth of Digital's RISC product line, Digital has intensified its marketing, sales, and support programs for the UNIX operating system.

Since this past summer, in addition to new RISC servers, lower entry-level workstation prices, and the introduction of the applicationDEC 433MP multiuser, multiprocessing system for small businesses, Digital has:

- Added 1,000 UNIX specialists to the Digital service organization.
- Given 10,000 sales representatives in both the U.S. and Europe intensive UNIX training.
- Opened seven ULTRIX resource centers throughout the world.
- Become the first member of the Open Software Foundation to commit to shipment and announce development of an OSF/1 toolkit.
- Announced its support of SCO UNIX.

DECmessageQ – New NAS Service Highlights Software and System Introductions, Eases Communications

In many applications, programs running on one computer need to communicate with programs running on another. For example, preparing a monthly report might require word processing, a spreadsheet, graphics, and access to a corporate database. Getting these programs to work together over the network can be difficult.

Digital introduced DECmessageQ to manage the process and simplify the task of writing a network application that will produce the updated report automatically. Similar applications exist in many technical and commercial environments where processes running on different systems need to communicate with each other.

In addition to DECmessageQ, Digital introduced its DECbank portfolio of retail banking applications, products, and services. DECbank will support virtually all industry-standard retail banking applications including:

- For customer service, Cross Sell Manager from Berman Technologies, Charlottesville, Virginia.
- For teller automation and branch consolidation, FlexTran from Culverin Corp., Dayton, Ohio, and STF (Financial Transaction System) from SONDA, Santiago, Chile.
- A Retail Delivery System, GENESYS, from Chemical Bank Information Technology Services.

During the quarter Digital also announced the Digital Integrated Security Program, formalizing its commitment to information security and an integrated security architecture for distributed, multi-vendor systems.

The announcement included the introduction of a series of security enhancements that package security technology for single systems, and local area networks, as well as management services to assist organizations in implementing effective security environments.

Alliances Support Software Marketing and Development

During the quarter, the company continued to support and build strategic alliances with independent developers as part of its strategy to make software an added value in Digital solutions.

- Digital sponsored the first International UNIX Software Business Development Forum to help software developers forge new business relationships with distributors, value-added resellers, and dealers. Held in Monterey, California, the Forum brought together developers and resellers from 28 countries.
- Several software companies joined Digital in cooperative marketing program during the quarter.
  - Comshare, Inc., Ann Arbor, Michigan, to jointly market Comshare's Commander EIS (Executive Information System), and System W (Decision Support System) in the U.S.
  - Systems & Computer Technology Corporation (SCT), Malvern, Pennsylvania, to jointly market SCT's BANNER series of administrative programs for institutions of higher education.
  - Andersen Consulting, Chicago, Illinois, to jointly market MAC-PAC/D, an integrated manufacturing planning and control systems for aerospace, defense, and other project-oriented manufacturers.
- Digital signed an agreement with Adra Systems, Inc. of Lowell, Massachusetts, to distribute Adra's CADRA computer-aided design and manufacturing software for Digital VAX, VAXstation, DECsystem, and DECstation systems.
- 28 new applications that adhere to Network Applications Support (NAS) standards were introduced and five new participants were announced in Digital Applications for Science Program.

The new participants are: Stanford University/Fox Chase Cancer Center, Philadelphia, Pennsylvania; M.I.T. Computational Fluid Dynamics Lab, Cambridge, Massachusetts; Brigham Young University, Engineering Computer Graphics Lab, Provo, Utah; National Center for Atmospheric Research, Boulder, Colorado; and the National Center for Supercomputing Applications, Champaign, Illinois.

In addition, Digital announced a cooperative research and development agreement with The Frank J. Seiler Research Lab at the US Air Force Academy, Colorado Springs, Colorado.

- Digital announced five new participants in The Integrated Visualization Environment (IVE) Program. They are: IMSL, Inc., Houston, Texas; Ithaca Software, Ithaca, New York; Ohio Supercomputer Center, Columbus, Ohio; RGB Spectrum, Berkeley, California; and Sterling Software, Palo Alto, California.
- Two leading software vendors announced plans to integrate their business applications with DEC/EDI (Electronic Data Interchange) software, a key NAS component. They are: CODA Incorporated of Manchester, New Hampshire, for their Integrated Accounting System (IAS); and Mitech Computer Systems Incorporated of Montreal, Quebec, for their Retail Master and Distribution Master software.
- Telecom Canada announced that DEC/EDI software and X.400 interconnection has been successfully tested on its TradeRoute VAN service.
- Strategic Systems International Ltd. (SSI), Basingstoke, England has signed a software distribution agreement that gives Digital exclusive U.S. distribution rights for SSI's TROPOS business planning and control software for manufacturers of chemicals, pharmaceuticals, and consumer goods. TROPOS was jointly developed by SSI and Digital.
- Digital and Unidata, Inc., Denver, Colorado, jointly announced that, through SQL Services a NAS component, the UniData relational database management system is now available for Digital's VMS operating system.
- SecaGraphics Inc., Golden, Colorado, announced that its Mapping and Graphics Integrated Computer (MAGIC) system used by the cable TV industry will be developed for Digital's applicationDEC 433 MP system.

Digital Receives Environmental Award

At the 1990 International Conference on CFC and Halon Alternatives, Digital was presented with the 1990 Ozone Protection Award by The U.S. Environmental Protection Agency.

The award was for developing an environmentally safe process for cleaning circuit boards with an aqueous solution rather than chlorofluorocarbons (CFCs), the man-made chemicals that destroy the earth's protective ozone layer. Digital has placed this new technology in the public domain so that other manufacturers can make use of Digital research without paying a licensing fee.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	December 29, 1990	June 30, 1990
Assets		
Current Assets		
Cash and cash equivalents	$ 1,571,679	$ 2,008,983
Accounts receivable, net of allowances	3,376,292	3,206,765
Inventories	1,758,789	1,538,258
Prepaid expenses	401,495	345,797
Deferred income tax charges, net	500,000	521,809
Total Current Assets	7,608,255	7,621,612
Property, plant and equipment, net	3,806,099	3,868,092
Other assets, net	169,165	165,117
Total Assets	$11,583,519	$11,654,821
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	$ 669,887	$ 660,819
Deferred revenue	934,018	903,038
Other liabilities	1,576,529	1,725,912
Total Current Liabilities	3,180,434	3,289,769
Deferred income tax credits, net	28,000	33,137
Long-term debt	152,054	150,001
Total Liabilities	3,360,488	3,472,907
Stockholders' Equity		
Common Stock, $1 par value	130,008	130,008
Additional paid-in capital	2,595,936	2,565,487
Retained earnings	6,251,417	6,257,199
Treasury stock at cost, 8,339,698 and 7,453,501 shares	(754,330)	(770,780)
Total Stockholders' Equity	8,223,031	8,181,914
Total Liabilities and Stockholders' Equity	$11,583,519	$11,654,821

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)	Three Months Ended		Six Months Ended	
	December 29, 1990	December 30, 1989	**December 29, 1990**	December 30, 1989
Revenues				
Product sales	**$1,989,325**	$2,006,793	**$3,854,883**	$4,001,201
Service and other revenues	**1,363,092**	1,178,002	**2,590,904**	2,314,784
Total operating revenues	**3,352,417**	3,184,795	**6,445,787**	6,315,985
Costs and Expenses				
Cost of product sales	**924,077**	935,025	**1,802,092**	1,817,155
Service expense and cost of other revenues	**822,657**	724,461	**1,602,365**	1,454,259
Research and engineering expenses	**403,857**	391,877	**805,809**	796,008
Selling, general and administrative expenses	**1,066,057**	961,304	**2,089,633**	1,900,271
Operating income	**135,769**	172,128	**145,888**	348,292
Interest expense	**8,542**	10,703	**15,488**	19,008
Interest income	**28,591**	32,721	**60,320**	63,261
Income before income taxes	**155,818**	194,146	**190,720**	392,545
Income taxes	**44,677**	38,744	**53,402**	86,360
Net income	**$ 111,141**	$ 155,402	**$ 137,318**	$ 306,185
Net income per share	**$0.92**	$1.25	**$1.12**	$2.44

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 122,550,473 shares and 125,290,571 shares for the six month periods ended December 29, 1990 and December 30, 1989, respectively, and 121,326,058 shares and 124,813,013 shares for the three month periods ended December 29, 1990 and December 30, 1989, respectively.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Six Months Ended December 29, 1990	December 30, 1989
Cash Flows from Operating Activities		
Net income	$ 137,318	$ 306,185
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	389,196	365,317
Other adjustments to income	85,391	57,683
(Increase)/decrease in accounts receivable	(169,527)	(31,649)
(Increase)/decrease in inventories	(220,531)	(70,952)
(Increase)/decrease in prepaid expenses	(55,698)	(55,418)
Increase/(decrease) in accounts payable	9,068	49,898
Increase/(decrease) in deferred revenues	30,980	(50,791)
Increase/(decrease) in other liabilities	(134,013)	308,919
Total adjustments	(65,134)	573,007
Net cash flows from operating activities	72,184	879,192
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	(363,182)	(472,182)
Other assets, net	(30,220)	(26,220)
Net cash flows from investing activities	(393,402)	(498,402)
Net cash flows from operating and investing activities	(321,218)	380,790
Cash Flows from Financing Activities		
Proceeds from issuance of debt	3,625	0
Payments to retire debt	(270)	(22,718)
Purchase of treasury stock	(240,719)	(159,264)
Issuance of treasury shares, including tax benefits	121,278	126,164
Net cash flows from financing activities	(116,086)	(55,818)
Increase/(decrease) in cash and cash equivalents	(437,304)	324,972
Cash and cash equivalents at the beginning of year	2,008,983	1,655,264
Cash and cash equivalents at end of period	$1,571,679	$1,980,236

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

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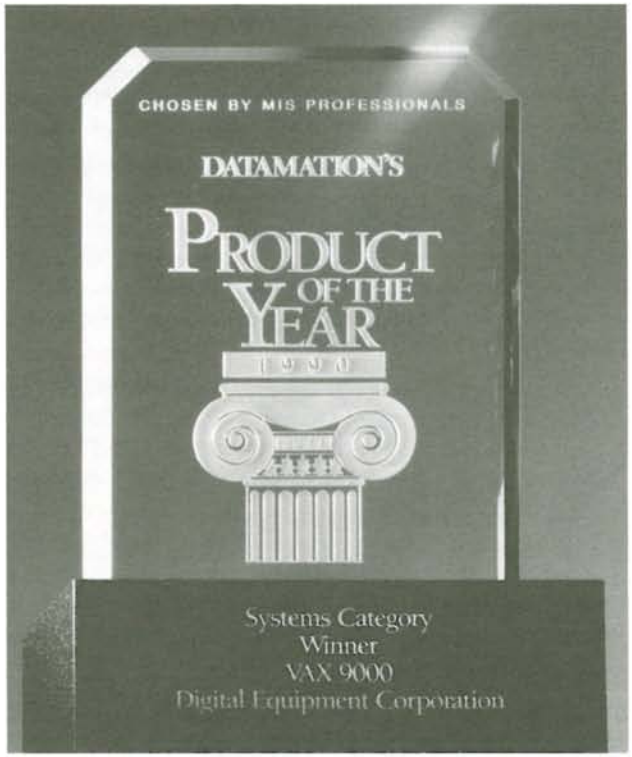
VAX 9000 Wins Product of the Year Award

digital



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THIRD QUARTER REPORT
FY 91

Digital Equipment Corporation
Maynard, Massachusetts 01754

digital

Printed in U.S.A. ED 00938 87/91 01 04 79.0 MCG/CTS

TO OUR SHAREHOLDERS

The difficult economic environment of the past several quarters is still with us. The uncertain business outlook, heightened by the conflict in the Middle East, has delayed customer investments in technology, particularly for large systems.

However, we are seeing the results of investments in key technologies and capabilities. This quarter, our worldwide service revenues grew 20%, as customers recognize Digital's unique capabilities in systems integration, where we manage large, complex projects incorporating technology from numerous vendors.

The Company's RISC/UNIX business doubled year-to-year, as many customers continue to show confidence in Digital's workstation and server products.

Despite the impact of the economy on the demand for VAX 9000 systems, we remain confident in our high-end computing strategy. Digital has shipped more than 250 VAX 9000 systems to date. And we continue to invest in improved price/performance for VAX users by incorporating RISC technology under the VMS operating system. Digital customers can remain confident that their investments yesterday and today will be protected, as we continue to evolve VAX computing into the next decade and beyond.

For the quarter, the Company reported total operating revenues of $3,520,358,000, up 8 percent from the $3,261,263,000 of the comparable quarter a year ago. Net income for the quarter was $116,573,000, versus last year's third quarter net income of $24,934,000. Quarterly earnings per share were $.94 versus $.20 last year.

The quarter's results reflect the consolidation of Digital-Kienzle, a German company, in which Digital acquired a 65% interest from Mannesmann A.G., for $230 million. This includes revenues of $79 million and the addition of 3,900 Digital-Kienzle employees during the quarter. Before the Kienzle consolidation, earnings per share were $1.14.

Continued progress was made in lowering expenses, consolidating facilities, and restructuring our workforce. During the quarter more than 2,200 people left the company.

Despite the adverse economic climate, we are confident of our overall direction and technology strategy. The marketplace views Digital as the leader in open computing, from our Network Application support software, which implements industry standards, to our comprehensive services and our open business approach of satisfying each customer's unique needs.

Kenneth H. Olsen
President

DIRECTIONS

The Evolving Business Environment . . . A Global Context For Digital's Strategy

As business becomes ever more complex, customers are recognizing that information is the only way management can mirror, support, and circumscribe the enterprise and its markets.

This is changing the way business organizes information systems. Flexibility and control have to be balanced. A network of distributed client/server computers can provide that balance. Desktop systems (clients) access data and run applications on network systems (servers).

Open systems – systems that have standards-based interfaces to provide application portability and interoperability across platforms from different vendors – are the key to client/server computing.

Digital's strategy is to deliver open systems with the hardware, software, and services customers need to manage information in this complex new environment. While many companies sell "open systems," Digital is committed to adding value to standards-based products by:

- Implementing and integrating a comprehensive set of standards.
- Being first to deliver products based on existing and emerging standards.
- Developing new functionality that industry groups can incorporate into emerging standards.
- Working in partnership with our customers to build standards-based systems that meet their unique needs.

This strategy is being implemented across Digital's entire product line. Digital's RISC strategy is to deliver a full line of workstations and servers running industry-standard operating systems for optimum price/performance. Digital's VAX strategy is focused on providing dramatic price/performance gains together with enhanced commercial capabilities while adopting all relevant open systems standards. Digital's desktop strategy is to integrate all popular desktop systems, including Digital, IBM, and Apple Macintosh personal computers into existing and emerging standards-based local area and corporate networks.

These strategies are all based on an open architecture, NAS – Digital's Network Application Support. This architecture integrates industry and emerging standards to provide a consistent interface to applications running on different platforms. NAS currently supports VMS, UNIX, MS-DOS, OS/2, and Macintosh, providing the software needed to integrate these systems in a single environment. Other operating systems that follow industry standards will be supported in the future. And, as new standards evolve, Digital will incorporate them into NAS.

This strategy is not just a "statement of direction." Digital and over 750 independent software developers are delivering over 1500 NAS-based applications for open, distributed systems that work.

VAX 9000 Update – Datamation "System of The Year"

Acceptance of the VAX 9000 mainframe computer is reflected in its selection by the readers of Datamation as "System of the Year" competition over competitive offerings including those from IBM, Cray, Amdahl, and Hitachi. (See Cover.)

Over 250 VAX 9000 mainframes and supercomputers are being used by domestic and international customers in 27 different industry segments, from aerospace to education, and retailing to heavy manufacturing. Applications include inventory tracking, payroll and general ledger, LSI circuit design, finite element analysis, manufacturing planning, portfolio modeling, econometrics, and weather modeling.

Twenty Computer Companies Join Digital To Provide the Widest Range of Software

Shortly after the end of the quarter, Digital, Microsoft, Compaq, MIPS Computer Systems, and The Santa Cruz Operation announced an industry initiative which will provide the widest range of system and software compatibility in the industry for high performance systems. The initiative will produce specifications for new systems, based on technologies used in Digital's DECstation and DECsystem line of RISC (Reduced Instruction Set Computing) computers.

In addition to the new computer system specification, new operating system software based on OSF/1 (a version of the UNIX operating system from the Open Software Foundation) will provide user compatibility with existing ULTRIX applications along with access to thousands of UNIX applications from other vendors. A second operating system from Microsoft will include many more thousands of applications formerly used with personal computers. These two new operating systems will allow customers to use the same applications on traditional PCs and the new computers Digital and many other vendors develop.

A total of 21 companies from around the globe supported the initiative at the New York announcement, including those mentioned above, and: Acer, Kubota Computer, Control Data, NEC, NKK, Olivetti, Prime, Pyramid, Siemens AG/Automation, Siemens Nixdorf Informationsysteme AG, Silicon Graphics, Sony, Sumitomo Electric, Tandem, Wang, and Zenith (Groupe Bull company).

New Subsidiary To Open In Czechoslovakia

Digital is continuing to build its presence in Eastern and Central Europe. This quarter, Digital established a subsidiary in Czechoslovakia and announced that it will open offices in Prague and Bratislava. This follows the recent announcements of a joint venture in Hungary and several initiatives addressing opportunities in a unified Germany.

"World's Largest Company" Adopts Digital Standard

NTT (Nippon Telegraph and Telephone), the largest company in the world as measured by market capitalization, selected Digital's ACMS, Application Control and Management System, as the basis for the transaction processing interface in its Multivendor Integration Architecture. This architecture will define NTT's basic procurement requirements for general purpose computers. NTT's Multivendor Integration Architecture, MIA, is based on the same multivendor computing philosophy embodied in Digital's Network Application Support. MIA and NAS implement many of the same standards, including Ethernet, OSF/Motif, and ISO networking protocols.

First to Ship OSF/1 Software

Digital is the first computer vendor to ship a binary version of OSF/1 software with OSF/Motif, the X Window System, the gnu C compiler, and development tools. OSF/1 is the new operating system developed by the Open Software Foundation to provide an open computing environment across systems built by different manufacturers. Digital also announced plans to integrate OSF/1 with its ULTRIX operating system during 1991.

Sales To Toys "R" Us And CVS Lead Major Customer Wins

Two leading retailers, Toys "R" Us and CVS, a division of Melville Corporation, signed orders totaling $16 million. Toys "R" Us purchased 1300 VAX 3100 Systems to be installed in over 700 locations. CVS purchased 1300 DECstation personal computers for communication among CVS pharmacies, distribution centers and corporate headquarters.

Other customer wins announced in the quarter include:

The ICI Pharmaceutical Group, based in Wilmington, Delaware, became the first pharmaceutical company to acquire a commercially available, paperless batch record system. Running on VAX computers, the system uses DECwindows-based applications developed by Palette Systems of Nashua, New Hampshire.

Kaiser Engineers Hanford Company, Richland, Washington, signed a $1.4 million contract of DECstation systems that will be networked in a design and construction application connecting users on a 500 square mile site.

The British Columbia Lottery Corporation awarded Digital a C$2.2 million (US$1.65 million) contract to convert its existing business management system from another vendor's computers to a three-processor VAXcluster system.

NAS Software Now Available For Sun Workstations

As part of its program to provide the software needed to build an open computing environment, Digital announced the availability of DECwindows/Motif and DEC VUIT, Visual User Interface Tools, for Sun workstations.

Based on NAS, Digital's Network Application Support Services, this software provides a high level of interoperability with systems running VMS, ULTRIX, MS-DOS, OS/2, and Apple Macintosh software.

New Fault Tolerant Systems

The market for fault tolerant systems is growing. Digital introduced the four new members of its fault-tolerant VAXft series. The VAXft 410, 610, and 612 systems feature increased storage and computer room packaging. The new models will process 16 to 25 transactions per second.

The expansion of the VAXft series provides Digital with a complete family of fault tolerant systems that have no single point of failure, zero degradation regardless of hardware failure, and that make fault tolerance totally transparent to the user.

More than 70 third-party software developers are providing specialized applications to run on VAXft systems.

Eleven UNIX Porting Centers Support Third-Party Developers

Digital and four major industrial distributors – Avnet, Pioneer Standard, Pioneer Technologies, and Wyle Laboratories – are establishing eleven centers where small and medium-sized software companies can port their applications to UNIX platforms. These new porting centers are part of Digital's continuing program to support and build strategic alliances with independent system and software houses and value-added resellers. They will provide third-party developers and value added resellers with access to the systems, software tools, and supporting services needed to port applications to DECsystems, DECstations, and applicationDEC 433MP systems.

"Imaging" Solutions Highlight Software Agreements

Anything that can be printed or written on paper, or captured with a camera, can be stored, accessed, managed, controlled, and distributed electronically through "imaging" software. Digital's new DECimage Express is a comprehensive, pre-configured document image management system based on Digital's NAS, Network Application Support, the DECimage 1200 X windowing terminal, enhanced capabilities for image display on personal computers and third-party agreements and alliances with:

LaserData, Inc., Tyngsboro, Massachusetts, to distribute and service the Corvette display systems and ADDS+ image software.

Computron Technologies Corp., Rutherford, New Jersey for EPIC/WORKFLOW software.

Digital also strengthened its long-standing relationship with Eastman Kodak, Rochester, New York. The two companies have agreed to work together to bring Kodak's VMS-based KIMS System 5000 document image management system into compliance with Digital's imaging architecture, formats, and standards.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)	March 30, 1991	June 30, 1990
Assets		
Current Assets		
Cash and cash equivalents	**$ 1,669,622**	$ 2,008,983
Accounts receivable, net of allowances	**3,327,718**	3,206,765
Inventories	**1,843,517**	1,538,258
Prepaid expenses	**384,568**	345,797
Deferred income tax charges, net	**500,000**	521,809
Total Current Assets	**7,725,425**	7,621,612
Property, plant and equipment, net	**3,830,202**	3,868,092
Other assets, net	**364,971**	165,117
Total Assets	**$11,920,598**	$11,654,821
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	**$ 676,099**	$ 660,819
Deferred revenue	**1,067,979**	903,038
Other liabilities	**1,635,730**	1,725,912
Total Current Liabilities	**3,379,808**	3,289,769
Deferred income tax credits, net	**28,000**	33,137
Long-term debt	**156,569**	150,001
Total Liabilities	**3,564,377**	3,472,907
Stockholders' Equity		
Common Stock, $1 par value	**130,008**	130,008
Additional paid-in capital	**2,605,692**	2,565,487
Retained earnings	**6,328,662**	6,257,199
Treasury stock at cost, 7,828,904 and 7,453,501 shares	**(708,141)**	(770,780)
Total Stockholders' Equity	**8,356,221**	8,181,914
Total Liabilities and Stockholders' Equity	**$11,920,598**	$11,654,821

The accompanying notes are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)	Three Months Ended		Nine Months Ended	
	March 30, 1991	March 31, 1990	**March 30, 1991**	March 31, 1990
Revenues				
Product sales	**$2,100,437**	$2,079,603	**$5,955,320**	$6,080,804
Service and other revenues	**1,419,921**	1,181,660	**4,010,825**	3,496,444
Total operating revenues	**3,520,358**	3,261,263	**9,966,145**	9,577,248
Costs and Expenses				
Cost of product sales	**989,372**	973,958	**2,791,464**	2,791,113
Service expense and cost of other revenues	**860,405**	730,239	**2,462,770**	2,184,498
Research and engineering expenses	**397,999**	405,059	**1,203,808**	1,201,067
Selling, general and administrative expenses	**1,100,980**	1,014,088	**3,190,613**	2,914,359
Restructuring charge	**0**	150,000	**0**	150,000
Operating income	**171,602**	(12,081)	**317,490**	336,211
Interest expense	**18,971**	601	**34,459**	19,609
Interest income	**26,713**	37,616	**87,033**	100,877
Income before income taxes	**179,344**	24,934	**370,064**	417,479
Income taxes	**62,771**	0	**116,173**	86,360
Net income	**$ 116,573**	$ 24,934	**$ 253,891**	$ 331,119
Net income per share	**$0.94**	$0.20	**$2.06**	$2.65

The accompanying notes are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Nine Months Ended March 30, 1991	Nine Months Ended March 31, 1990
Cash Flows from Operating Activities		
Net income	**$ 253,891**	$ 331,119
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	**601,630**	566,417
Other adjustments to income	**128,760**	76,093
(Increase)/decrease in accounts receivable	**83,917**	(41,657)
(Increase)/decrease in inventories	**(216,052)**	(24,004)
(Increase)/decrease in prepaid expenses	**(27,142)**	(71,715)
Increase/(decrease) in accounts payable	**(63,478)**	(2,363)
Increase/(decrease) in deferred revenues	**106,609**	18,833
Increase/(decrease) in other liabilities	**(288,588)**	476,316
Total adjustments	**325,656**	997,920
Net cash flows from operating activities	**579,547**	1,329,039
Cash Flows from Investing Activities		
Purchase of property, plant and equipment	**(545,958)**	(723,778)
Other assets, net	**(32,393)**	(49,558)
Cash paid for Kienzle business	**(233,261)**	0
Net cash flows from investing activities	**(811,612)**	(773,336)
Net cash flows from operating and investing activities	**(232,065)**	555,703
Cash Flows from Financing Activities		
Proceeds from issuance of debt	**4,612**	0
Payments to retire debt	**(3,061)**	(23,348)
Purchase of treasury stock	**(240,719)**	(159,266)
Issuance of treasury shares, including tax benefits	**131,872**	133,233
Net cash flows from financing activities	**(107,296)**	(49,381)
Increase/(decrease) in cash and cash equivalents	**(339,361)**	506,322
Cash and cash equivalents at the beginning of year	**2,008,983**	1,655,264
Cash and cash equivalents at end of period	**$1,669,622**	$2,161,586

The accompanying notes are an integral part of these financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Earnings Per Share

Net income per share is based on the weighted average number of common shares and common share equivalents outstanding during each period; 123,080,647 shares and 125,180,200 shares for the nine month periods ended March 30, 1991 and March 31, 1990, respectively, and 124,140,995 shares and 124,959,457 shares for the three month periods ended March 30, 1991 and March 31, 1990, respectively.

Acquisition

The current quarter's results reflect the consolidation of Digital-Kienzle, a German Company, in which Digital acquired a 65% interest from Mannesmann A.G. for $230 million.

Note Redemption

The Company called for redemption on April 15th, $100 million of 12⅞% notes which were transferred to short term debt in the accompanying Balance Sheet.

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, and Pacific Stock Exchange (Ticker Symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

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Digital Equipment Corporation
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First Quarter Report FY 94

October 20, 1993

To Our Shareholders:

The Corporation, the world's leader in open client/server solutions from personal computing to integrated worldwide information systems, today reported results for its first quarter, which ended October 2, 1993.

For the quarter, the Corporation reported a net loss of $83,185,000 or $.62 per share, compared with a loss of $260,546,000 or $2.04 per share for the first quarter a year ago. The loss for the first quarter of fiscal 1994 includes a one-time benefit of $20,042,000, or $.14 per share, related to the adoption of a change in accounting principle for income taxes. For the quarter, the Corporation reported total operating revenues of $3,014,948,000 down from $3,314,299,000 for the comparable quarter a year ago.

We reduced the operating loss in the quarter by more than $162,000,000 compared with the first quarter of last year, through continued focus on cost controls. Even so, we were disappointed by the revenue declines from last year. The revenue decline in the seasonally soft September quarter was attributable primarily to continued weakness in Europe – Germany and Italy in particular – as well as negative effects of foreign currency fluctuations. A slight decline in the U.S. also hurt us. Our operations in Asia continued to show good growth, both in products and services, but not enough to offset declines in other areas.

Our focus for this fiscal year remains unchanged. We are committed to improving profitability while successfully growing the Alpha AXP business.

For the fourth consecutive quarter we showed improving operating results over the comparable period of the prior year, driven by a strong emphasis on cost controls and improved efficiency. The effects of the Corporation's restructuring program are on schedule. As a result, Research and Engineering spending declined 22% or $90,760,000 and Selling, General and Administrative spending was down 23%, or $258,980,000 versus the comparable quarter a year ago.

Product gross margins declined five points from last year due primarily to the revenue decline and a continued shift in revenue mix to lower priced, lower

margin products. While we achieved double digit growth in both dollars and units in personal computers and in our UNIX workstations businesses, our competitive pricing for PC's and Alpha AXP systems is contributing to lower margins. Service gross margins improved slightly compared with the first quarter of last year.

We have several programs taking advantage of our product strengths which are focused on accelerating our growth in key areas. We have initiated targeted programs aimed at selling open client/server products such as workstations, servers and networking products.

Just one week ago, nearly 3000 chief information officers and executives from our major customers around the world attended announcement events to learn about Digital's open client/server strategy. The Corporation's initiative included more than 200 new products and services, major enhancements to the OSF/1 and OpenVMS operating systems, new Alpha AXP and VAX systems all very competitively priced. We also announced symmetric multiprocessing under UNIX, integration software products such as LinkWorks and Tuxedo and industry leading network management software. All of these offerings enable customers to easily move to open client/server computing. Customer reaction was very positive and we expect these capabilities to open up many new opportunities for our Alpha AXP systems.

Robert B. Palmer
President and Chief Executive Officer

On October 12, 1993, Digital announced more than 200 new products, services, partnerships, and business practices designed to clearly establish leadership in the client/server marketplace. Included in the announcement were Alpha AXP products, UNIX® products, OpenVMS products, open client/server framework products, network products, new services, and simplified pricing structures.

Digital's principal focus as a corporation is on open client/server computing. Customers view open client/server computing as the one way they can dramatically increase the effective use of their information technology, while keeping their systems flexible to accommodate the changes necessary to respond to a fast changing marketplace.

What is client/server?
Client/server is the style of computing that allows individuals and organizations to design solutions that can continually respond to dynamic business changes. Client/server environments have an architecture and infrastructure that can respond to the quickly changing competitive market.

What does client/server mean?
Client/server means distributing computing resources across an organization. It enables people throughout an enterprise to find the information they need, and to work collaboratively with their colleagues, regardless of geography, function, or desktop tools. Client/server environments can accommodate change and expansion without discarding existing systems and software. It permanently changes the relationship between the users and information system management.

Digital's leadership position in open client/server computing
Digital has three great strengths to bring to the open client/server marketplace – technology, a corporate structure that is organized around industries and accounts, and outstanding expertise on how to implement and support client/server environments.

Digital's technology
There are many distinguishing features in Digital's open client/server technology. The first is a wide range of application software, created in collaboration with major developers. Next, Digital can provide easy open sharing and access to information in a multivendor network. Third, Digital has the comprehensive ability to integrate current and future technology. Fourth, Digital has the highest performance computing at every price level. And finally, Digital offers the highest availability and data integrity, meaning a customer's data is safe, secure, and always there.

Digital's corporate structure
Digital is the only major computer company to be organized by industry and account. Strong account management enables it to better understand the customer's business needs, and to apply the most appropriate technology to address those needs.

Digital expertise
Digital's long experience in providing worldwide support, coupled with a renewed emphasis on strategic consulting, assures customers of on-time, on budget, and on specification performance.

The importance of client/server frameworks
Effective client/server environments depend on frameworks. This is software

that is put on top of networks that enables the easy deployment of client/server applications. Frameworks provide the architecture, methodologies, facilities, and tools to solve basic client/server problems. Once a customer has the capabilities provided by frameworks, they can focus on their applications. There are six types of client/server frameworks: data integration, work group computing, enterprise messaging, production system computing, technical computing, and system/network management. At the heart of the recent announcement is a large array of products and services that addresses the complexities found in these six critical areas of client/server environments.

The importance of Alpha AXP technology

The potential for growth within the Alpha AXP architecture is particularly significant in the client/server context. Also, its power, speed, scalability, and flexibility in diverse operating systems make it ideal in client/server environments.

Digital's strategic intent – an industry leadership role

Digital will lead with the integration of Digital and other vendors' products into flexible client/server environments that address customers' business needs. The announcement of more than 200 products in support of client/server computing is a proof point of this strategy. Digital has all the elements required to establish and maintain that leadership – a full range of components and products, value added computer systems, open networks, open client/server frameworks, applications, consulting and integration services, and worldwide support services.

Client/server computing represents a fundamental change in the way businesses and institutions approach information technology. Digital has invested heavily in the development of enabling technologies to accommodate these new environments. It is committed to every area of the business, and is quickly taking the leadership role in the client/server revolution.

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, the Pacific Stock Exchange and the Montreal Exchange (TICKER symbol "DEC").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

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Consolidated Statements of Operations *(Unaudited)*

(In thousands except per share data)	Three-Month Period Ended October 2, 1993	Three-Month Period Ended September 26, 1992
Revenues		
Product sales	**$1,557,004**	$1,767,821
Service and other revenues	**1,457,944**	1,546,478
Total operating revenues	**3,014,948**	3,314,299
Costs and Expenses		
Cost of product sales	**981,415**	1,019,957
Service expense and cost of other revenues	**943,877**	1,017,650
Research and engineering expenses	**314,717**	405,477
Selling, general and administrative expenses	**872,207**	1,131,187
Total costs and expenses	**3,112,216**	3,574,271
Operating loss	**(97,268)**	(259,972)
Net interest income (expense)	**(2,423)**	9,426
Loss before income taxes and cumulative effect of change in accounting principle	**(99,691)**	(250,546)
Income taxes	**3,536**	10,000
Loss before cumulative effect of change in accounting principle	**(103,227)**	(260,546)
Cumulative effect of change in accounting principle, net of tax	**(20,042)** (a)	–
Net loss	**$ (83,185)**	$ (260,546)
Loss before cumulative effect of change in accounting principle per share	**$ (0.76)**	$ (2.04)
Cumulative effect of change in accounting principle per share	**.14**	–
Net loss per share	**$ (0.62)**	$ (2.04)

(a) Represents the recognition of a one-time benefit resulting from the adoption of Statement of Financial Accounting Standards No. 109 – Accounting for Income Taxes, effective July 4, 1993. The standard was adopted on a prospective basis, and as such, the prior year has not been restated.

Consolidated Balance Sheets

(In thousands)	October 2, 1993 (Unaudited)	July 3, 1993 (Audited)
Assets		
Current Assets		
Cash and cash equivalents	$ 1,273,830	$ 1,643,195
Accounts receivable, net	2,858,832	3,020,252
Inventories	1,920,823	1,755,140
Prepaid expenses and deferred income taxes	465,822	463,928
Total current assets	6,519,307	6,882,515
Property, plant and equipment, net	3,174,490	3,178,291
Other assets, net	931,806	889,537
Total assets	$10,625,603	$10,950,343
Liabilities and Stockholders' Equity		
Current Liabilities		
Bank loans and current portion of long-term debt	$ 19,782	$ 21,335
Accounts payable	732,409	822,434
Income taxes payable	40,910	57,614
Salaries, wages and related items	608,280	556,151
Deferred revenues and customer advances	1,052,263	1,138,323
Restructuring reserve	603,990	738,989
Other current liabilities	549,525	583,868
Total current liabilities	3,607,159	3,918,714
Noncurrent deferred income taxes	26,369	–
Long-term debt	1,018,354	1,017,577
Postretirement benefits	1,153,854	1,128,653
Total liabilities	5,805,736	6,064,944
Stockholders' Equity		
Common stock	135,559	135,490
Additional paid-in capital	2,869,391	2,851,960
Retained earnings	1,852,173	1,937,627
Treasury stock, at cost	(37,256)	(39,678)
Total stockholders' equity	4,819,867	4,885,399
Total liabilities and stockholders' equity	$10,625,603	$10,950,343

Consolidated Statements of Cash Flows *(Unaudited)*

	Three-Month Period Ended	
(In thousands)	October 2, 1993	September 26, 1992
Cash Flows from Operating Activities		
Net loss	$ (83,185)	$ (260,546)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation	144,386	160,461
Amortization	30,174	29,158
Other adjustments to net loss	29,365	110,037
Decrease in accounts receivable	161,420	278,138
Increase in inventories	(165,683)	(163,289)
(Increase)/decrease in prepaid expenses	22,012	(5,231)
Decrease in accounts payable	(90,025)	(142,737)
Increase/(decrease) in taxes	(36,898)	66,720
Increase in salaries, wages, benefits and related items	77,330	98,242
Decrease in deferred revenues and customer advances	(86,060)	(98,054)
Decrease in restructuring reserve	(180,299)	(249,395)
Increase/(decrease) in other current liabilities	(69,571)	13,239
Total adjustments	(163,849)	97,289
Net cash flows from operating activities	(247,034)	(163,257)
Cash Flows from Investing Activities		
Investment in property, plant, and equipment	(167,001)	(131,919)
Proceeds from the disposition of property, plant, and equipment	47,964	24,446
Investment in other assets	(14,130)	(202,220)
Net cash flows from investing activities	(133,167)	(309,693)
Net cash flows from operating and investing activities	(380,201)	(472,950)
Cash Flows from Financing Activities		
Proceeds from issuance of debt	12,950	9,149
Payments to retire debt	(14,154)	(1,987)
Issuance of common shares and treasury shares, including tax benefits	12,040	9,867
Net cash flows from financing activities	10,836	17,029
Net decrease in cash and cash equivalents	(369,365)	(455,921)
Cash and cash equivalents at beginning of year	1,643,195	1,337,172
Cash and cash equivalents at end of period	$1,273,830	$ 881,251

digital

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SECOND QUARTER REPORT FY 94

January 19, 1994

TO OUR SHAREHOLDERS:

Digital Equipment Corporation, the world's leader in open client/server solutions from personal computing to integrated worldwide information systems, today reported results for its second quarter, which ended January 1, 1994.

For the quarter, the Corporation reported a net loss of $72,144,000, or $.53 per share, compared with a net loss of $73,859,000, or $.57 per share for the comparable quarter a year ago. For the quarter, the Corporation reported total operating revenues of $3,254,079,000, down from $3,689,443,000 for the comparable quarter a year ago.

For the six months ended January 1, 1994, the Corporation reported a net loss of $155,329,000, or $1.15 per share, compared with a net loss of $334,405,000, or $2.60 per share for the comparable period a year ago. The net loss for the first six months of fiscal 1994 includes a one-time benefit of $20,042,000, or $.14 per share, related to the adoption of a change in accounting principle for income taxes. Operating revenues for the first six months of fiscal 1994 were $6,269,027,000, down from $7,003,742,000 for the comparable period a year ago.

While we expected revenues to decline somewhat, we are not satisfied with the level of revenues or the loss for the quarter. We continue to navigate a difficult transformation for the Corporation within a difficult economic environment and we continue to work diligently to lower our costs, stabilize and then grow revenues. It took several years for the Corporation to get into this situation and it is taking some time for us to restore profitability and growth.

We remain confident in our strategy to provide leadership open client server solutions based on our strengths in Alpha AXP systems, networking, software frameworks, UNIX workstations and personal computers. Several recent announcements have reinforced this strategy. Among them is the recent agreement with Microsoft Corporation to define a standard for open systems interoperability for object oriented programming.

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For the quarter, we achieved essentially flat operating results compared with last year even with a 12 percent revenue decline, a five point drop in gross margins and negative currency translation. Despite the loss and restructuring activity, we generated positive cash flow from operations for the quarter just ended. We ended the quarter with a total cash balance of $1.1 billion, down $127 million from the previous quarter.

The revenue decline was due principally to continued decreases in VAX systems, associated software and services. Our personal computer business continued to double in units, year over year, and showed strong double-digit revenue growth. Alpha AXP workstations also continued to show good growth in the quarter. Revenue for products such as storage devices, low-end networking products, printers and terminals also grew in the quarter. The effects of foreign currency movements were negative this quarter, similar to the first quarter. Our business in the major economies of Europe and the U.S. remained weak while we experienced growth in Asia Pacific and Latin America.

Product margins declined compared with the same quarter last year primarily due to the mix shift toward more lower-priced, lower profit products such as personal computers and workstations. Digital's products and service are priced very competitively. We expect continued product margin pressure and are adjusting our business unit strategies and cost structure accordingly. Given economic uncertainty, product transitions, and competitive pressures we remain cautious about our outlook for the second half of fiscal 1994.

We further strengthened our sales and marketing efforts with several recent announcements, most notably, the recent hire of Vincenzo Damiani to head our European operations. We also announced expansion of our distribution channels adding volume resellers for our Alpha AXP personal computer products and distributors for our semiconductor components, including the Alpha AXP chip.

We continue to work with customers such as Hoechst Canada, Scott Paper, Corning, Schering-Plough, Exxon USA and Toys-R-Us to provide solutions based on our Alpha-ready VAX and Alpha AXP systems.

Robert B. Palmer
President and Chief Executive Officer

Annual Meeting Highlights

"With the talent we have in Digital, our undeniable technological leadership, our financial strength, and our many loyal customers worldwide, we have every opportunity to be successful – and we intend to be," so stated Bob Palmer, president and CEO, at Digital's Annual Meeting of Shareholders held at the World Trade Center on Nov. 4.

Bob reiterated the commitments he made a year ago, and then matched the actions and results to those promises. He first addressed the idea that Digital would be more customer focused, reviewing the creation of business units organized around the products and services they provide and the industries they serve. He also explained that the model was further refined by combining the industry-oriented customer business units with the Worldwide Sales and Marketing organization.

A second promise was a rationalized engineering effort more closely attuned to customers' needs, with more strategically focused, customer-driven hardware and software products. Bob explained that engineering was consolidated under one chief technology officer, redundant product efforts were eliminated, and costs reduced by approximately $400 million on an annualized basis.

Bob committed last year that he would bring in new senior talent to help run the business. He explained that more than half of the officers of the company are represented by new names and faces – some promoted from within and some brought in from outside the organization.

The fourth promise was for an increased emphasis on systems integration and software, citing the increased commitment to software research and development, focusing on where Digital can add value rather than trying to be all things to all people.

A year ago, Bob forecasted that Alpha AXP systems would be shipping in volume and, today, Alpha AXP revenues are 20 percent of systems revenue.

With his sixth commitment, Bob promised that Digital's vision, messages, and communications would become simpler, clearer, and more focused. He reiterated the new advertising campaign, a refined logo, and a worldwide branding effort to help clarify the perceptions of Digital.

The final commitment was that Digital would have a leaner, more cost-competitive infrastructure to support business goals and strategy. Bob highlighted the new compensation strategy for sales professionals; the elimination of approximately $2 billion of ongoing expense from the cost structure; the decline of the employee population by approximately 15,000 during the past four quarters; the consolidations of facilities; and the decline of expenses for research and engineering, as well as selling, general, and administrative expenses.

Other items in the meeting's agenda included the passage of all items on the Proxy Statement.

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CONSOLIDATED STATEMENTS OF OPERATIONS *(Unaudited)*

(In thousands except per share data)	Three-Month Period Ended		Six-Month Period Ended	
	January 1, 1994	December 26, 1992	**January 1, 1994**	December 26, 1992
Revenues				
Product sales	**$1,659,924**	$1,967,234	**$3,216,928**	$3,735,055
Service and other revenues	**1,594,155**	1,722,209	**3,052,099**	3,268,687
Total operating revenues	**3,254,079**	3,689,443	**6,269,027**	7,003,742
Costs and Expenses				
Cost of product sales	**1,112,292**	1,116,538	**2,093,707**	2,136,495
Service expense and cost of other revenues	**968,473**	1,058,270	**1,912,350**	2,075,920
Research and engineering expenses	**330,948**	404,843	**645,665**	810,320
Selling, general and administrative expenses	**908,688**	1,177,306	**1,780,895**	2,308,493
Operating loss	**(66,322)**	(67,514)	**(163,590)**	(327,486)
Net interest income (expense)	**(3,327)**	1,655	**(5,750)**	11,081
Loss before income taxes and cumulative effect of change in accounting principle	**(69,649)**	(65,859)	**(169,340)**	(316,405)
Provision for income taxes	**2,495**	8,000	**6,031**	18,000
Loss before cumulative effect of change in accounting principle	**(72,144)**	(73,859)	**(175,371)**	(334,405)
Cumulative effect of change in accounting principle	**–**	–	**20,042**(a)	–
Net loss	**$ (72,144)**	$ (73,859)	**$ (155,329)**	$ (334,405)
Loss before cumulative effect of change in accounting principle per share	**$ (.53)**	$ (.57)	**$ (1.29)**	$ (2.60)
Cumulative effect of change in accounting principle per share	**–**	–	**.14**	–
Loss per share	**$ (.53)**	$ (.57)	**$ (1.15)**	$ (2.60)

(a) Represents the recognition of a one-time benefit resulting from the adoption of Statement of Financial Accounting Standards No. 109-Accounting for Income Taxes, effective July 4, 1993. The standard was adopted on a prospective basis, and as such, the prior year has not been restated.

Consolidated Balance Sheets

(In thousands)	January 1, 1994 (Unaudited)	July 3, 1993 (Audited)
Assets		
Current Assets		
Cash and cash equivalents	$ 1,147,257	$ 1,643,195
Accounts receivable, net	2,795,969	3,020,252
Inventories	1,950,356	1,755,140
Prepaid expenses and deferred income taxes	405,669	463,928
Total current assets	6,299,251	6,882,515
Property, plant and equipment, net	3,145,660	3,178,291
Other assets, net	923,846	889,537
Total assets	$10,368,757	$10,950,343
Liabilities and Stockholders' Equity		
Current Liabilities		
Bank loans and current portion of long-term debt	$ 11,574	$ 21,335
Accounts payable	767,055	822,434
Income taxes payable	11,026	57,614
Salaries, wages and related items	552,626	556,151
Deferred revenues and customer advances	960,493	1,138,323
Restructuring reserve	442,705	738,989
Other current liabilities	553,793	583,868
Total current liabilities	3,299,272	3,918,714
Deferred income taxes	26,369	–
Long-term debt	1,017,360	1,017,577
Postretirement benefits	1,195,805	1,128,653
Total liabilities	5,538,806	6,064,944
Stockholders' Equity		
Common stock	137,890	135,490
Additional paid-in capital	2,937,205	2,851,960
Retained earnings	1,754,856	1,937,627
Treasury stock, at cost	–	(39,678)
Total stockholders' equity	4,829,951	4,885,399
Total liabilities and stockholders' equity	$10,368,757	$10,950,343

Consolidated Statements of Cash Flows *(Unaudited)*

	Six-Month Period Ended	
(In thousands)	January 1, 1994	December 26, 1992
Cash Flows from Operating Activities		
Net loss	$ (155,329)	$ (334,405)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation	301,722	346,923
Amortization	60,996	67,240
Other adjustments to loss	84,002	141,000
Decrease in accounts receivable	224,283	462,248
Increase in inventories	(195,216)	(218,196)
(Increase)/decrease in prepaid expenses	82,145	(33,375)
Decrease in accounts payable	(55,379)	(212,856)
Increase/(decrease) in taxes	(66,782)	89,666
Increase in salaries, wages, benefits and related items	63,627	75,238
Decrease in deferred revenues and customer advances	(177,830)	(230,152)
Decrease in restructuring reserve	(341,584)	(451,215)
Decrease in other current liabilities	(65,303)	(61,333)
Total adjustments	(85,319)	(24,812)
Net cash flows from operating activities	(240,648)	(359,217)
Cash Flows from Investing Activities		
Investment in property, plant, and equipment	(348,070)	(256,463)
Proceeds from the disposition of property, plant, and equipment	53,620	25,279
Investment in other assets	(39,993)	(218,633)
Proceeds from the disposition of other assets	3,238	–
Net cash flows from investing activities	(331,205)	(449,817)
Net cash flows from operating and investing activities	(571,853)	(809,034)
Cash Flows from Financing Activities		
Proceeds from issuance of debt	12,950	741,320
Payments to retire debt	(23,573)	(8,051)
Issuance of common shares and treasury shares, including tax benefits	86,538	103,933
Net cash flows from financing activities	75,915	837,202
Net increase/(decrease) in cash and cash equivalents	(495,938)	28,168
Cash and cash equivalents at beginning of year	1,643,195	1,337,172
Cash and cash equivalents at end of period	$1,147,257	$1,365,340

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THIRD QUARTER REPORT
FY 94

April 25, 1994

TO OUR SHAREHOLDERS:

Digital Equipment Corporation reported results for its third quarter, which ended April 2, 1994.

For the quarter, the Corporation reported total operating revenues of $3,258,789,000, down 6% from $3,453,676,000 for the comparable quarter a year ago. This includes product revenues of $1,749,621,000, down 1% and service and other revenues of $1,509,168,000, down 11% from the comparable quarter a year ago.

For the quarter, the Corporation reported a net loss of $183,306,000, or $1.34 per share, compared with a net loss of $30,121,000, or $.23 per share for the comparable quarter a year ago.

For the nine months ending April 2, 1994, the Corporation reported total operating revenues of $9,527,816,000, down 9% from $10,457,418,000, from the comparable period a year ago. This includes product revenues of $4,966,549,000, down 10% and service and other revenues of $4,561,267,000, down 8% from $4,954,991,000 of the comparable period a year ago.

For the nine months ended April 2, 1994, the Corporation reported a net loss of $338,635,000, or $2.50 per share, compared with a net loss of $364,526,000, or $2.81 per share for the comparable period a year ago. The net loss for the first nine months of fiscal 1994 includes a one-time benefit of $20,042,000, or $.14 per share, related to the adoption of a change in accounting principle for income taxes.

Robert B. Palmer, President and CEO, said, "At the end of last week, Digital's Board of Directors reviewed your company's position and supported management's plans to accelerate the next phase of Digital's turnaround strategy.

That strategy has one goal: rebuild shareholder value. That goal can be realized only by improving customer focus, constantly strengthening our product line and delivering our products and services through a stronger, more cost-effective organization. Digital's reputation for quality and dependability is itself an

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important strength upon which we will build the future. Preserving that reputation demands that any turnaround be implemented methodically and over time. While we have a renewed sense of urgency, we realize that any effort to accomplish our objectives too quickly or abruptly could truly jeopardize our viability.

Let me reiterate the strategy. Since we began the turnaround of Digital 18 months ago, we have made many tactical decisions necessary to bring control to the company and to frame the problems. As with any turnaround of this magnitude, there have been stops, starts and turns. The disappointing third quarter results were an unfortunate example, but they should not obscure progress that has been made. For example, during the past 18 months we:

- *revised senior management organization and personnel;*
- *significantly downsized the employee population;*
- *achieved a much leaner and more cost-effective infrastructure;*
- *greatly reduced engineering redundancy;*
- *and transformed Digital from a closed and proprietary systems company to an industry leader in Open Client/Server computing.*

We are now poised at the beginning of the second phase of our turnaround – a planned, strategic refocus driven by what we have accomplished and what we have learned from phase one.

We have laid a strong foundation, and we are ready to move forward... to focus our investments in the segments of this business where we know Digital can prosper... and to ensure progress by giving management even greater accountability and more direct ownership of their resources.

During this second phase, which we expect to take about 24 months, Digital will change in many ways. But we do not expect to alter our single, ongoing strategic customer focus on Open Client/Server systems that deliver solutions. Nor will we alter our belief that customer satisfaction is the surest path to lasting shareholder value and sustained profits.

We will emerge in the third and final phase of this turnaround as a different company, guided by strategic reviews and focused on areas of the business where we can achieve industry leadership.

We bring strength, accomplishment and commitment to the tasks ahead:

- *We have met all of our financial commitments and are financially strong, with a cash position that currently exceeds $1 billion and debt to capitalization ratio of less than 20 percent.*
- *We have, in Alpha AXP, the world's fastest chip, with scalable price-performance leadership throughout our product line.*
- *We have strengthened and streamlined our management and organizational structure; and we will continue to do so.*
- *And we are accelerating the process of aggressively aligning our costs with the changing structure of our business.*

In the months ahead, your company will be concentrated on making steady progress against our goals. And, although we all share the frustration of the inevitable setbacks that go with a turnaround effort, I want you to understand that your board and senior management are committed to our customers, our shareholders, our people, our products and services, and on making this turnaround successful.

I will, of course, report our progress to you from time to time.

Sincerely,

Robert B. Palmer
President and Chief Executive Officer

Digital's common stock is listed and traded on the New York Stock Exchange, the Midwest Stock Exchange, the Pacific Stock Exchange and the Montreal Exchange (TICKER symbol "DEC").

Digital's Series A Preferred Stock is listed and traded on the New York Stock Exchange (TICKER symbol "DEC PRA").

In Europe: Swiss Stock Exchanges of Zurich, Geneva, and Basel and the German Stock Exchanges of Frankfurt, Munich, and Berlin.

Unlisted trading privileges have been granted by the Boston Stock Exchange, Cincinnati Stock Exchange, and Philadelphia Stock Exchange. In Europe: Luxembourg Stock Exchange.

Inquiries relating to investment in Digital Equipment Corporation should be directed to:

Bradley D. Allen
Director, Investor Relations
(508) 493-7182

or

James A. Chiafery
Manager, Shareholder Relations
(508) 493-8009

Digital Equipment Corporation
146 Main Street MLO3-2/F41
Maynard, MA 01754-2571
FAX (508) 493-7633

Transfer Agent and Registrar for Common Stock:

First Chicago Trust Company of New York is the principal stock transfer agent and registrar, and maintains the stockholder accounting records. The agent will respond to questions on change of ownership, lost stock certificates, consolidation of accounts and change of address.

First Chicago Trust Company of New York
P.O. Box 2500
Jersey City, NJ 07303-2500

(201) 324-0498

Depository for the Series A Preferred Stock:

CitiBank, N.A.
Address correspondence to:
Citicorp Data Distribution
404 Sette Drive
Paramus, NJ 07653

(800) 422-2066

(In thousands except per share data)

	Three-Month Period Ended		Nine-Month Period Ended	
	April 2, 1994	March 27, 1993	**April 2, 1994**	March 27, 1993
Revenues				
Product sales	**$1,749,621**	$1,767,372	**$4,966,549**	$ 5,502,427
Service and other revenues	**1,509,168**	1,686,304	**4,561,267**	4,954,991
Total operating revenues	**3,258,789**	3,453,676	**9,527,816**	10,457,418
Costs and Expenses				
Cost of product sales	**1,210,478**	1,049,969	**3,304,185**	3,186,464
Service expense and cost of other revenues	**946,800**	1,030,728	**2,859,150**	3,106,648
Research and engineering expenses	**316,767**	350,423	**962,432**	1,160,743
Selling, general and administrative expenses	**954,903**	1,050,600	**2,735,798**	3,359,093
Operating loss	**(170,159)**	(28,044)	**(333,749)**	(355,530)
Net interest income/(expense)	**(7,846)**	(77)	**(13,596)**	11,004
Loss before income taxes and cumulative effect of change in accounting principle	**(178,005)**	(28,121)	**(347,345)**	(344,526)
Provision for income taxes	**5,301**	2,000	**11,332**	20,000
Loss before cumulative effect of change in accounting principle	**(183,306)**	(30,121)	**(358,677)**	(364,526)
Cumulative effect of change in accounting principle	**–**	–	**20,042 (a)**	–
Net loss	**(183,306)**	(30,121)	**(338,635)**	(364,526)
Dividends on preferred stock	**1,775**	–	**1,775**	–
Net loss applicable to common stock	**$ (185,081)**	$ (30,121)	**$ (340,410)**	$ (364,526)
Loss before cumulative effect of change in accounting principle per share	**$ (1.34)**	$ (.23)	**$ (2.64)**	$ (2.81)
Cumulative effect of change in accounting principle per share	**–**	–	**.14**	–
Loss per common share	**$ (1.34)**	$ (.23)	**$ (2.50)**	$ (2.81)

(a) Represents the recognition of a one-time benefit resulting from the adoption of Statement of Financial Accounting Standards No. 109-Accounting for Income Taxes, effective July 4, 1993. The standard was adopted on a prospective basis, and as such, prior year has not been restated.

Consolidated Balance Sheets

(In thousands)	April 2, 1994 (Unaudited)	July 3, 1993 (Audited)
Assets		
Current Assets		
Cash and cash equivalents	$ 1,263,551	$ 1,643,195
Accounts receivable, net	2,925,188	3,020,252
Inventories	2,164,833	1,755,140
Prepaid expenses and deferred income taxes	402,218	463,928
Total current assets	6,755,790	6,882,515
Property, plant and equipment, net	3,136,489	3,178,291
Other assets, net	902,822	889,537
Total assets	$10,795,101	$10,950,343
Liabilities and Stockholders' Equity		
Current Liabilities		
Bank loans and current portion of long-term debt	$ 10,620	$ 21,335
Accounts payable	877,058	822,434
Income taxes payable	10,154	57,614
Salaries, wages and related items	597,999	556,151
Deferred revenues and customer advances	1,156,952	1,138,323
Restructuring reserve	276,341	738,989
Other current liabilities	544,385	583,868
Total current liabilities	3,473,509	3,918,714
Deferred income taxes	26,369	–
Long-term debt	1,017,427	1,017,577
Postretirement benefits	1,239,573	1,128,653
Total liabilities	5,756,878	6,064,944
Stockholders' Equity		
Preferred stock, at par	4,000 (b)	–
Common stock, at par	137,883	135,490
Additional paid-in capital	3,326,565	2,851,960
Retained earnings	1,569,775	1,937,627
Treasury stock, at cost	–	(39,678)
Total stockholders' equity	5,038,223	4,885,399
Total liabilities and stockholders' equity	$10,745,101	$10,950,343

(b) In March 1994, the Corporation sold 16,000,000 Depositary Shares under the shelf registration statement filed with the Securities and Exchange Commission on January 21, 1994, each representing one-fourth interest in a share of Series A 8¾% Cumulative Preferred Stock, par value $1.00 per share, of the Corporation.

Consolidated Statements of Cash Flows *(Unaudited)*

	Nine-Month Period Ended	
(In thousands)	April 2, 1994	March 27, 1993
Cash Flows from Operating Activities		
Net loss	$ (338,635)	$ (364,526)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation	439,989	528,407
Amortization	82,952	100,826
Other adjustments to loss	104,577	157,037
Decrease in accounts receivable	95,064	584,954
Increase in inventories	(409,693)	(200,842)
(Increase)/decrease in prepaid expenses	85,759	(15,944)
Increase/(decrease) in accounts payable	54,624	(244,428)
Increase/(decrease) in taxes	(67,654)	93,165
Increase in salaries, wages, benefits and related items	152,768	106,399
Increase/(decrease) in deferred revenues and customer advances	18,629	(67,859)
Decrease in restructuring reserve	(507,948)	(672,853)
Decrease in other current liabilities	(76,486)	(55,673)
Total adjustments	(27,419)	313,189
Net cash flows from operating activities	(366,054)	(51,337)
Cash Flows from Investing Activities		
Investment in property, plant, and equipment	(514,382)	(358,419)
Proceeds from the disposition of property, plant, and equipment	76,250	36,079
Investment in other assets	(61,144)	(244,432)
Proceeds from the disposition of other assets	23,516	–
Net cash flows from investing activities	(475,760)	(566,772)
Net cash flows from operating and investing activities	(841,814)	(618,109)
Cash Flows from Financing Activities		
Proceeds from issuance of debt	11,017	741,673
Payments to retire debt	(22,749)	(14,880)
Proceeds from sale of preferred stock	387,258	–
Issuance of common shares and treasury shares, including tax benefits	86,644	106,231
Net cash flows from financing activities	462,170	833,024
Net increase/(decrease) in cash and cash equivalents	(379,644)	214,915
Cash and cash equivalents at beginning of year	1,643,195	1,337,172
Cash and cash equivalents at end of period	$1,263,551	$1,552,087

Digital Equipment Corporation
Maynard, Massachusetts 01754

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