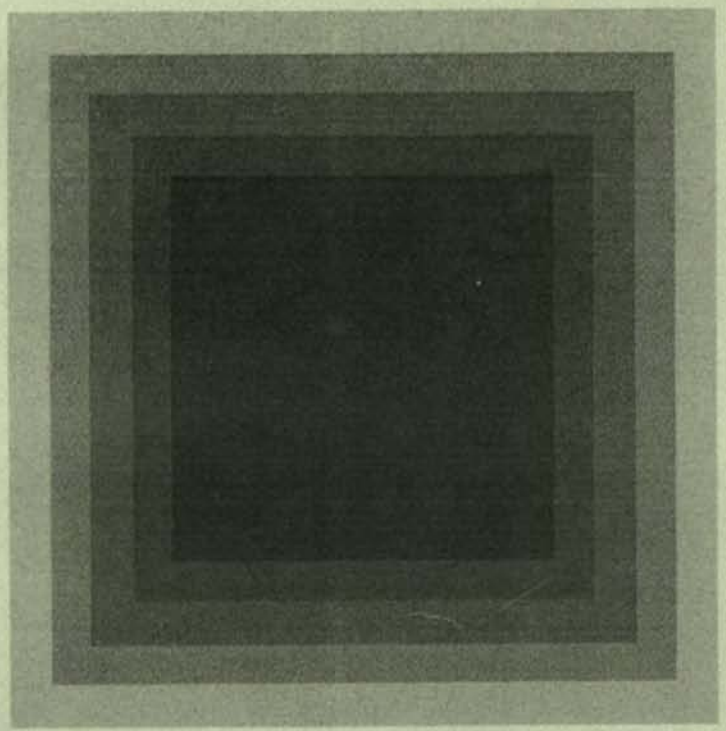
1982 ANNUAL REPORT

Technological Leadership in the Rapidly Evolving Market for On-Line Transaction Processing



TANDEM

BUSINESS REVIEW

TANDEM

FINANCIAL REVIEW

Tandem Computers Incorporated designs, develops, manufactures, markets and supports a unique computer system for on-line transaction processing. The company's customers are primarily large, diversified organizations.

The Tandem NonStop system —the first on-line, distributed computer architecture for mainframe applications—virtually eliminates the risk of system failures; protects users' data bases from damage or loss; expands modularly from a mid-size system to mainframe power without hardware replacement or software conversion; and extends into a distributed data processing network of up to 255 geographically dispersed systems.

Tandem has manufacturing operations in six locations in the United States and one in Germany. The company supports customers' NonStop systems throughout North America, Europe and Asia from 96 offices.

At the end of fiscal 1982, 599 organizations—of which 139 were new customers during the year—were using over 4,000 NonStop processors worldwide. Within the five-year reporting period, Tandem's annual revenue (1982 versus 1978 fiscal years) has grown by a multiple of 13 to $312 million, and stockholders' equity has increased by a factor of 16 to $251 million.

Preface

When commercial data processing was born a quarter of a century ago, it marked the start of using computers as business tools for increasing productivity and improving competitiveness. Business in the Eighties, however, is much faster paced—and much more changeable, complex and competitive—than it was in the Fifties. Consequently, enterprises need a new generation of productivity-enhancing computers that complement today's business environment. Conventional, centralized, mainframe computers are no longer state-of-the-art because they are not 'state-of-the-business,' and large organizations throughout the world are looking for ways to bring their core business functions in line with on-line needs. Only one computer manufacturer, Tandem, has created an entirely new architecture to address those crucial needs for instantaneous and accurate information. This report describes that architecture and the organization that created the NonStop system . . . and explains how Tandem is playing a key role in the dramatically changing marketplace for on-line computer systems.

Providing Comprehensive Solutions to Complex Information Requirements

"A growth rate for fault-tolerant transaction processing of 30–50% may leave traditional mainframes and super-minis in the dust in transaction processing applications, and there will be dislocations for companies which cannot or choose not to respond."

—Gideon I. Gartner
President,
Gartner Group, Inc.

Gideon Gartner is one of the most highly regarded analysts following the information industry.

The marketplace for computers that perform the functions at the heart of business operations is undergoing rapid change. Businesses are redefining the Fifties mainframe concept to address the dramatically changed needs of the Eighties and Nineties. It is no longer adequate to rely on yesterday's information—the output of batch processing—to make today's decisions.

The first major shift started in the Seventies when many businesses began to move applications on-line in order to obtain up-to-the-minute information that accurately reflects the state of the business. The effect of on-line transaction processing is the immediate and automatic capture and updating of business information that supports timely decisions.

The second major change is the shift from centralized to distributed computing, putting information where it is used in the business. As businesses distribute data to sites where transactions occur, they naturally want to be able to link the locations together in on-line networks to vastly enrich the information flow and automation benefits.

These important changes—the clear trends to on-line computing and distributed data processing networks—have made the conventional, centralized mainframe architecture obsolete.

The new requirements for computers in this environment are continuous availability, modular expandability, data integrity, programmer productivity, and efficient system performance, tied together in a network that is transparent to the user.

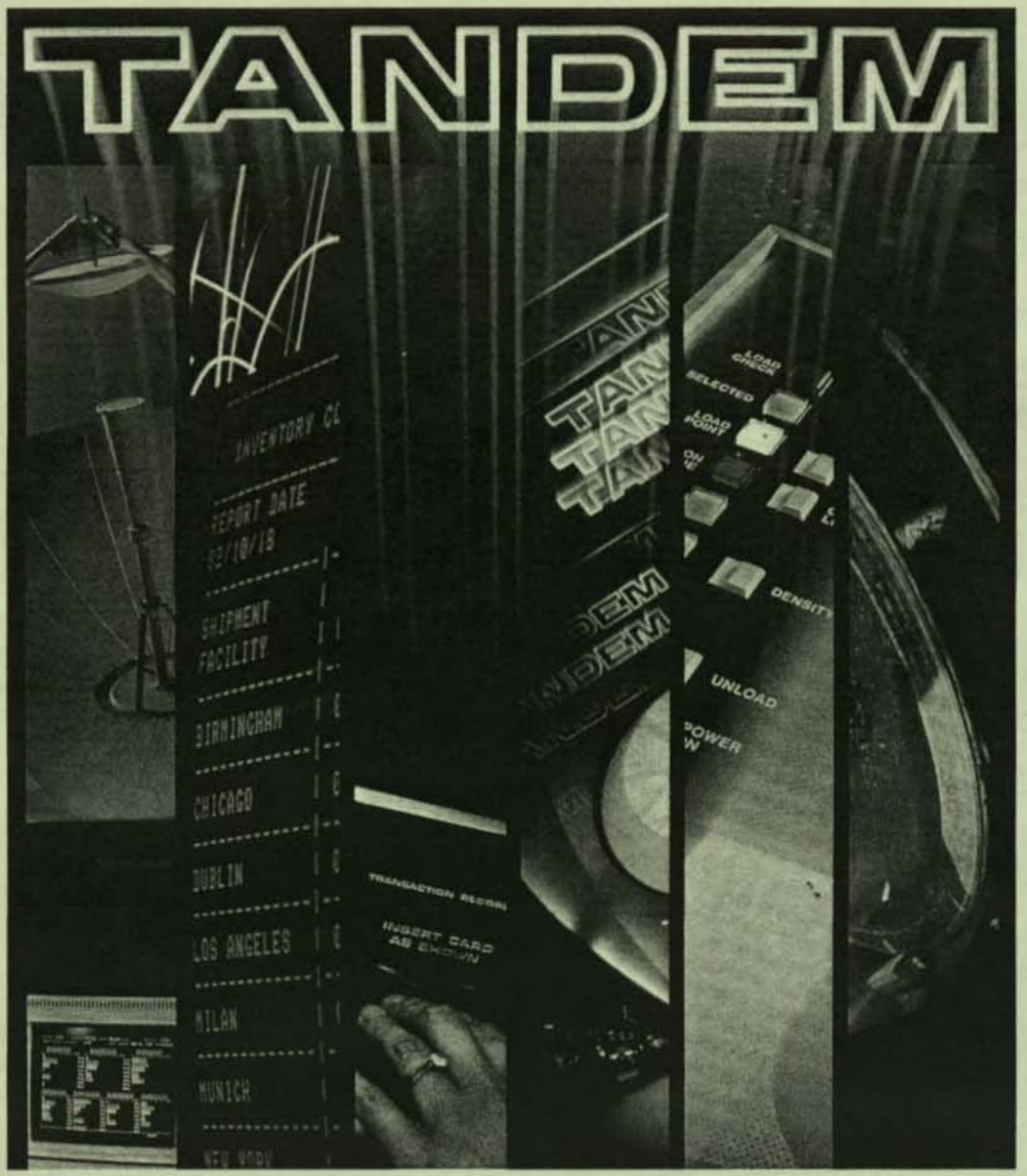
Recognizing the early signs of these trends, Tandem created a totally new architecture designed expressly to serve the emerging on-line transaction processing marketplace. The fault-tolerant, modularly expandable Tandem NonStop system is the first on-line, distributed computer system for mainframe applications.

Tandem's unmatched experience in this new marketplace is the foundation of its leadership position. It is fortified by a strong base of nearly 600 satisfied customers using more than 4,000 Tandem processors, and a capable

"Tandem's vision of the marketplace of the Eighties and Nineties led us to build in the critical features right from the start. This means that Tandem has an unbeatable eight-year lead in understanding and serving this market."

—Charles W. Ryle
Vice President,
U.S. Marketing
Tandem Computers

dation of its leadership position. It is fortified by a strong base of nearly 600 satisfied customers using more than 4,000 Tandem processors, and a capable organization of creative people dedicated to supporting the needs of this dynamic marketplace.



Merging and Moving All Forms of Corporate Information

"Competition has arrived with a vengeance for commercial banks, demanding worldwide, intersystem linkages that go beyond just the traditional processing of data."

—Donald R. Hollis
Senior Vice President,
Systems & Management
Information Services
First National Bank of Chicago

First Chicago, among the top ten U.S. banks, has an extensive and growing series of domestic and international computer applications which are based on 28 NonStop systems and 87 processors in 17 countries.

Large organizations rely upon information in many forms from many sources to make business decisions.

To initiate a routine customer order, an office in Paris may need to send a packet to New York that includes a cover letter, memos, an order form, a purchase order, and a drawing.

Before the transaction is completed, the New York office will communicate with a manufacturing facility in Atlanta which, in turn, will need information from a Chicago warehouse.

The process may entail telephone calls, telex, telecopiers, photocopiers, word processors, electronic mail and a range of incompatible computers. The interdependence of information delivery on these diverse technologies slows and complicates decisions, and keeps communications costs high.

Traditional data processing and centralized mainframe computers cannot efficiently address this spectrum of business information requirements. Business needs demand an on-line computer system with distributed data bases connected in a global network that can merge and manage all corporate information resources while preserving investments in a variety of computers and office devices.

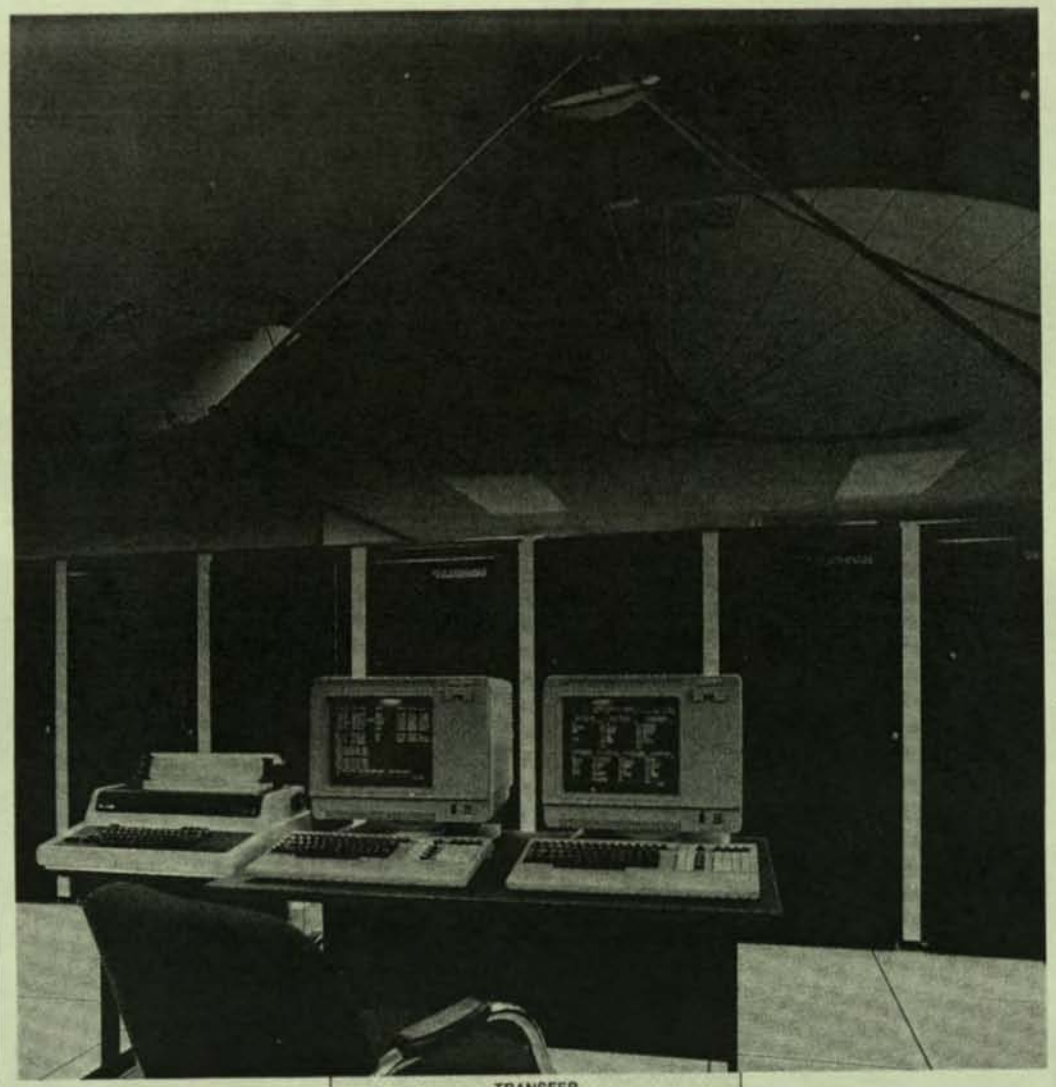
During 1982, Tandem announced a far-reaching new product called TRANSFER that will do just that. Based on an EXPAND network, TRANSFER will manage the dynamic interchange of information. It will link together people, equipment and data independent of form, location or application.

Tandem offers a wide variety of flexible communication links to support such activity. The most innovative among them is INFOSAT, Tandem's newly announced, fully-integrated, low-cost satellite communications network.

The new TRANSFER and INFOSAT capabilities build upon the unique attributes of the powerful Tandem NonStop architecture to provide a flexible, highly reliable backbone network, transforming Tandem NonStop systems into a truly integrated information management and delivery system.

"Tandem provides the leading edge products for innovative customers who are pushing the limits of traditional computer usage."

—David R. Mackie
Vice President,
Tandem Computers



TRANSFER will allow users to merge different forms of information and move them over a Tandem EXPAND network. To facilitate the economical movement of large volumes of information, Tandem has also introduced the first commercially available, fully-integrated satellite communications network. INFOSAT brings all the inherent NonStop system advantages to satellite communications.

Tandem, which runs its own worldwide operations on a 100-node on-line EXPAND network, is testing TRANSFER on this network utilizing INFOSAT earth stations. Tandem provides an ideal test environment for TRANSFER because its on-line network, one of the largest in the world, is the key corporate information resource for managing all aspects of the business. Initial TRANSFER and INFOSAT deliveries are scheduled during 1983.

Logotypes appearing throughout this report are a representative sampling of the 599 organizations worldwide that are using Tandem NonStop systems at the close of fiscal 1982.

Bringing Applications On-Line Quickly and Cost-Effectively

"The most important trend in data processing today is facilities for obtaining results fast . . . to achieve much higher DP productivity. This, coupled with the ability to distribute the relevant data, is essential for putting computers to use to meet end users' true needs."

—James Martin
Author and Lecturer

James Martin is a leading authority on data base and applications development. He is a computer industry author and lecturer of international repute.

Data is the foundation for every business decision. Whether for booking reservations, billing customers, transferring funds, or checking inventory, the information must be complete, current and accurate.

As business grows, data proliferates. The larger the organization, the greater the need to access and exchange information at all levels, yet the more difficult it is to manage and control. If the organization is diversified structurally or geographically, the problem is even more complex.

On-line transaction processing, by its nature, involves large data bases, many users, frequent on-line updates, fast response time, and numerous terminals communicating with the system simultaneously.

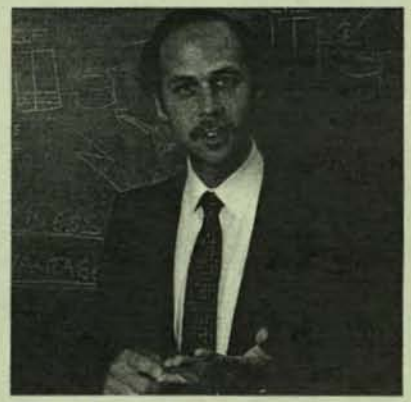
Only Tandem, through its ENCOMPASS relational data base management system, meets these requirements.

ENCOMPASS makes the programmer's job as simple as writing batch processing applications because it monitors every transaction, manages data files, handles the complex terminal functions, and delivers fast, accurate answers ensuring data integrity and consistency.

ENCOMPASS makes the end-user more productive as well as providing an easy-to-use relational query language/report formatter called ENFORM.

Consequently, Tandem users typically become operational with new applications at a fraction of the time and cost—and begin enjoying benefits much sooner—than do users of other systems that require specialized programming and highest-skill programmers.

And that explains why, according to the 1982 Cowen/DATAMATION survey of computer users, Tandem has the highest level of customer usage of data base management and networking software of all computer manufacturers in the survey.



"The key to making business more productive is bringing the information asset closer in time and space to the point of the business transaction."

—Gerald D. Held
Director,
Software Research
Tandem Computers

Tandem's ENCOMPASS software—a powerful tool that makes programming for distributed, on-line transaction processing no more difficult than writing programs for batch processing—is widely used by Tandem customers in all industries to increase both programmer and end-user productivity dramatically.

In the manufacturing sector, Pirelli, a major tire producer, is using ENCOMPASS to bring quickly into production numerous state-of-the-art programs at four manufacturing facilities in Italy. The company's interactive EXPAND network is scheduled to be extended to Pirelli plants worldwide.

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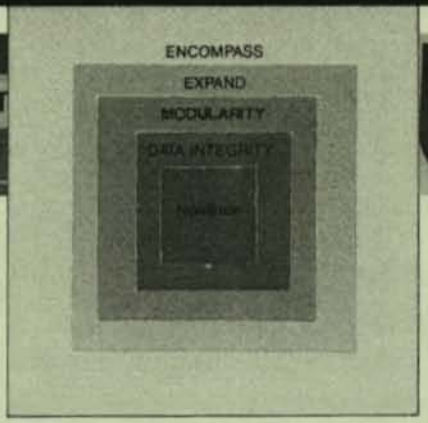


Washington Post

EBV

Years-Ahead Tandem Technology

EXPAND

Easily Integrating Widespread Information Assets into a Fault-Tolerant Network

"We're putting more and more of our business onto computers—including linking together more than 4,400 stores. To make that commitment, we absolutely require computer systems that can be quickly linked together in a rapidly expanding network without having to write new programs."

—Carroll Leu
Vice President,
Data Processing
Tandy Corporation

The purpose of on-line transaction processing networks is to provide everyone in a geographically-dispersed organization some part of the total information asset to make the business function more completely, competitively and efficiently.

Tying together the information assets requires an on-line network of computers that is continuously available, cost-effective, and easy to use.

The only architecture that is ideally suited to on-line networks comes from Tandem technology.

Tandem's EXPAND networking software makes writing applications across a network easy. And, once the network is in place, it can grow and change to accommodate increased business, new functions or new locations swiftly and inexpensively without rewriting application software or retraining people. An EXPAND network can, in fact, painlessly grow to 255 mainframe-power NonStop systems.

Tandem systems are the logical choice for on-line networks. The fault-tolerance of the NonStop system architecture inherently extends across networks of Tandem systems.

In contrast, consider the most advanced conventional mainframe computers claiming 99% availability. A business running its computers around the clock statistically would be out of business eight hours—one full shift—once a month. The statistical probability of failure for such non-Tandem systems tied together in an on-line network is even less acceptable: *In just a 10-system network of conventional computers, the network would be down for eight hours every third day.*

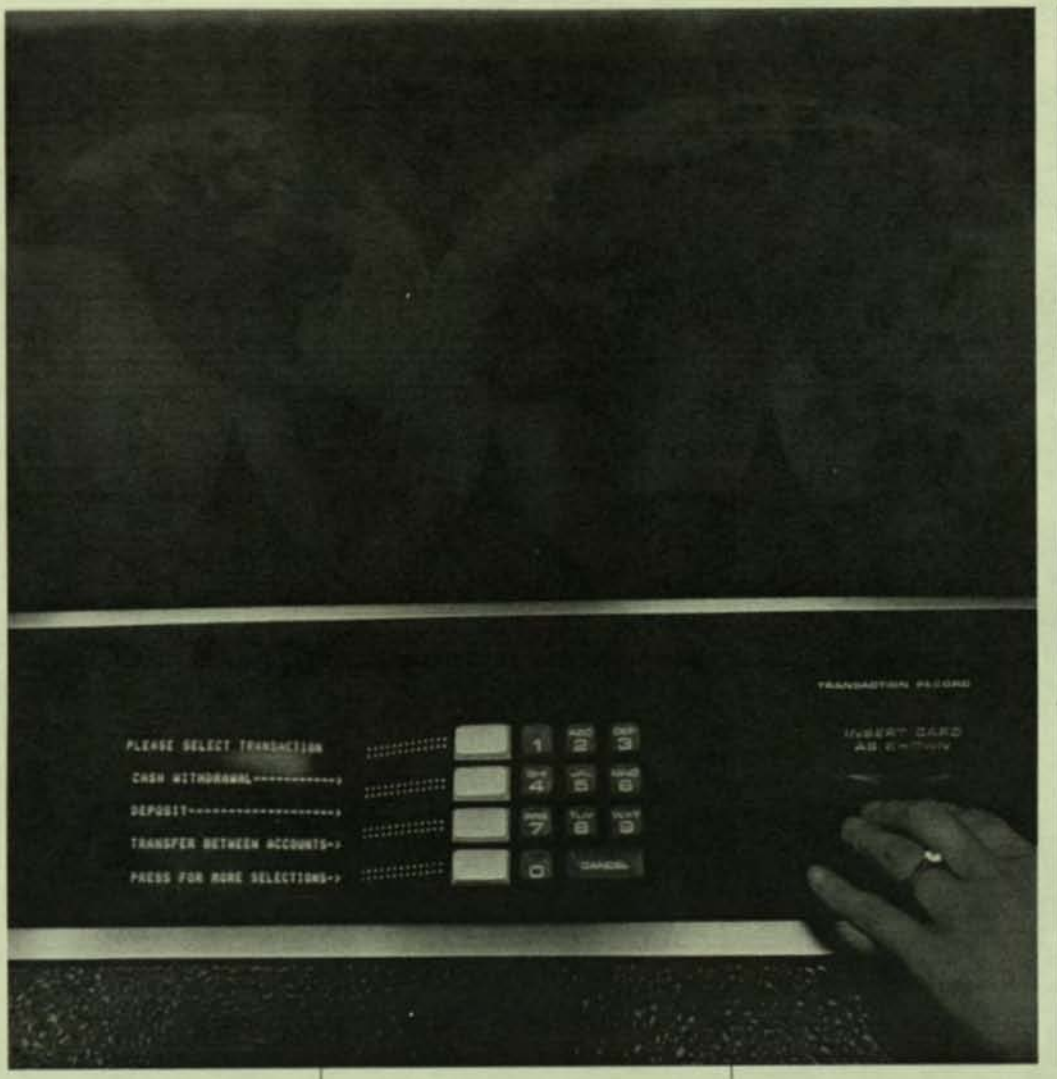
In a 100-node network like Tandem's own corporate information system, an organization using conventional mainframes would be off the air more than on—and that is why NonStop systems will form the backbone networks of the world's largest organizations.

"We understand our customers' networking needs because our own international on-line network is one of the largest in the world."

—Jeanne D. Wohlers
Vice President, Treasurer
Tandem Computers

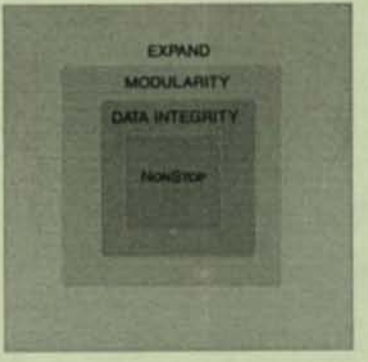
Tandy sells its popular TRS-80 small computers and other electronic

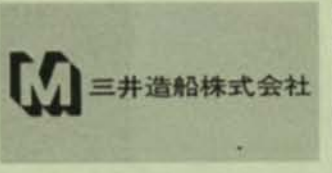
Tandy sells its popular TRS-80 small computers and other electronic products through its nationwide Radio Shack stores that link into a Tandem EXPAND network.



The ultimate size and configuration of a new and growing application may not, during the planning stage, be immediately discernible. With Tandem systems, the network configuration can easily change as the business changes.

At Wells Fargo Bank, some 50 Tandem processors are dispersed at a variety of wholesale and retail banking applications including a network of 500 automated teller machines. Wells Fargo plans to upgrade to an EXPAND network for greater network availability, disaster recovery capability, increased maintainability, and lower communications costs.





Sizing Systems for Today's Needs, Easily Adding Power for Tomorrow's

"Large, dynamic organizations that are constantly adding interdependent functions to their interactive computer networks need a computer system that is quickly and inexpensively expandable without disrupting the business."

—Christer Magnusson
President,
Vingressor

With 35 bureaus in Scandinavia, Vingressor, the travel agency subsidiary of the Scandinavian Airline System, books over 390,000 packaged tours annually to 30 destinations.

Businesses change, as does the environment in which they operate. Yet, traditional data processing systems do not. Once in place, they are immutable until uprooted and replaced by an equally inflexible successor.

Tandem systems, in contrast, are inherently flexible.

Module by module, Tandem systems grow in power from mid-size to mainframe—without reprogramming applications or retraining personnel—and without disrupting business operations. Routinely, Tandem users add incremental processing power to their existing NonStop systems while they continue to run without interruption.

Instead of purchasing a $2 or $3 million mainframe that will ultimately be needed to run an application, Tandem users develop the application on a minimum-size NonStop system for a tenth the investment. Later, when the application goes on-line, the precise amount of required processing power is added with no additional programming.

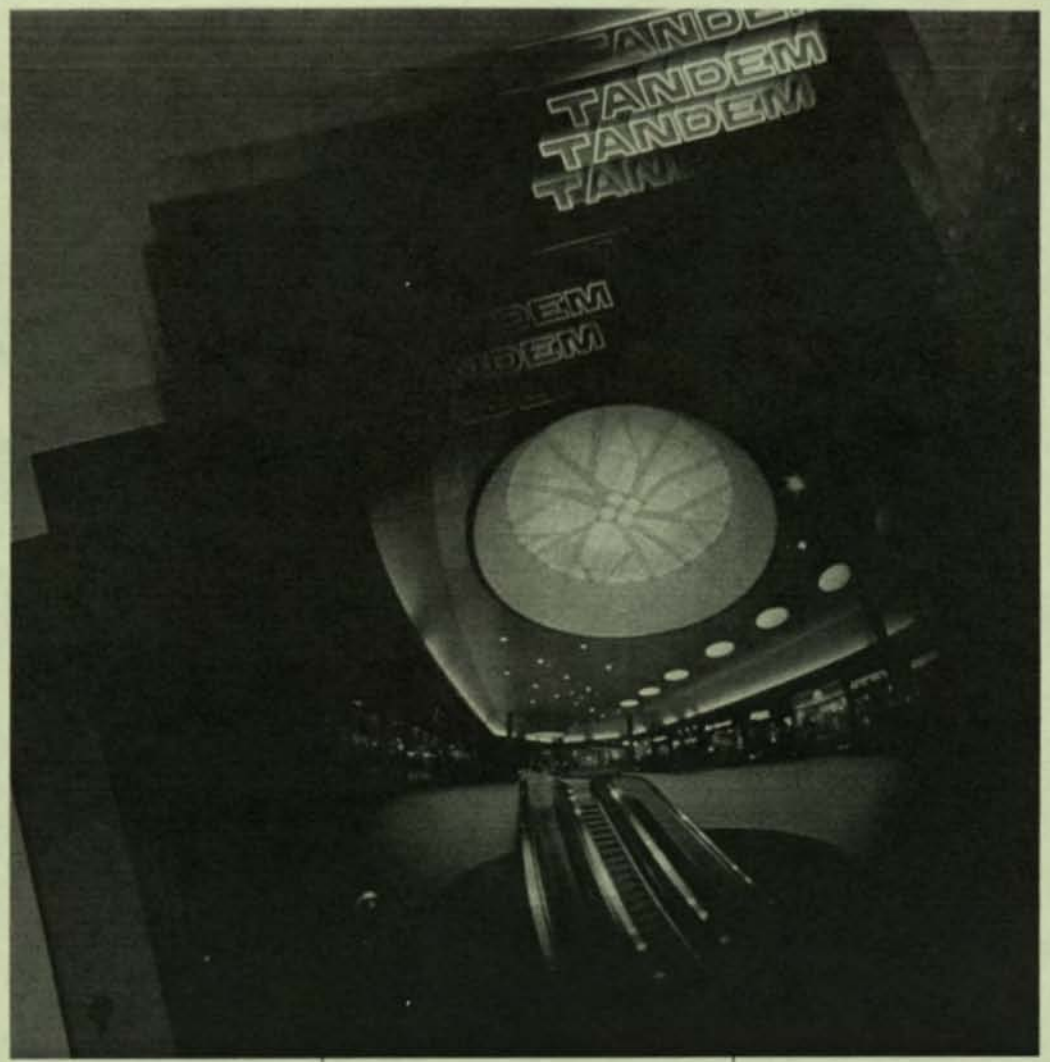
When the application grows, or when new functions are added that will require more computing power, or when the application is distributed to other facilities, or when all facilities are linked together in a network, the requisite power is 'metered' to each system by again simply adding more processor modules.

Each Tandem system can be expanded from two to 16 processors. And up to 255 full-size systems can be interconnected in an EXPAND network without rewriting applications programs.

The dynamics of large organizations and complex marketplaces often change computing requirements between the time an application is planned and the time it is executed, and as the users' needs change. The Tandem architecture is forgiving of changes by virtue of its inherent modularity.

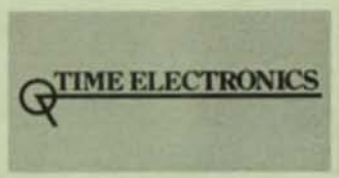
"The beauty of a computer system that can match the requirements of a rapidly growing business is obvious. That it can do it while running continuously and at no cost premium is an undeniable business advantage."

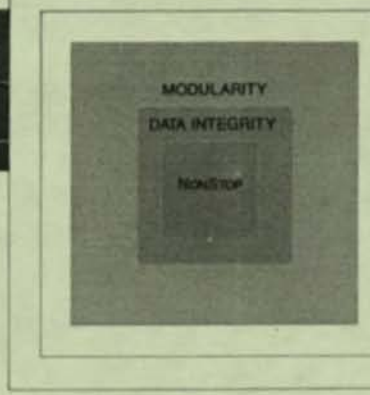
—Laurence A. Laurich
Vice President,
Engineering
Tandem Computers



Growing enterprises need true modularity of computers to accommodate their growth and added on-line activities. In the retail and distribution markets, particularly within large chains, the number of automated locations increase while at the same time the number of on-line services expand. To accommodate both types of growth, an easily expandable computer resource is key to cost-efficiency.

Target Stores, a $2 billion retailer and the largest subsidiary of Dayton-Hudson Corporation, is an excellent example of the need for true modularity. Within three years of installing its first two-processor Tandem system to begin developing applications for distribution centers and a chain-wide network, Target had five Tandem systems on-line using 25 processor modules, with many other on-line applications planned.





Consistently Delivering Information as Accurate as the Input

"Cable television systems in over 950 cities depend on us to accurately and timely bill their 12 million subscribers every month, utilizing their on-line data bases interconnected with ours. We cannot tolerate lost or damaged data—or computer failures—that would jeopardize nearly $2.5 billion of the cable industry's annual revenues."

—Robert J. Matthews
President,
Cable Data

Cable Data, an information systems

Fundamental to the integrity of the corporate information management resource is the assurance that what comes out of the computer is as accurate as what goes in, and that the information is delivered to the intended recipient.

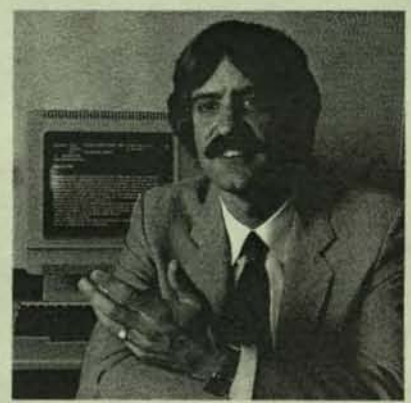
The Tandem architecture and software tools such as Transaction Monitoring Facility combine to achieve an unprecedented level of data integrity, both within a single system and throughout a geographically distributed network.

Data contamination and loss caused by system malfunctions and failures are risks taken by all users of conventional computers. Such occurrences with batch applications are sometimes recoverable, but in fast-paced on-line transaction processing environments—where an organization's critical business functions are dependent upon the accuracy of rapidly changing information—system errors are intolerable.

In passenger reservations systems, for instance, many days of departures could be underbooked or overbooked because of data loss or damage.

In international electronic funds transfers, millions of dollars can be lost if conventional computers inadvertently deposit cash in the wrong accounts.

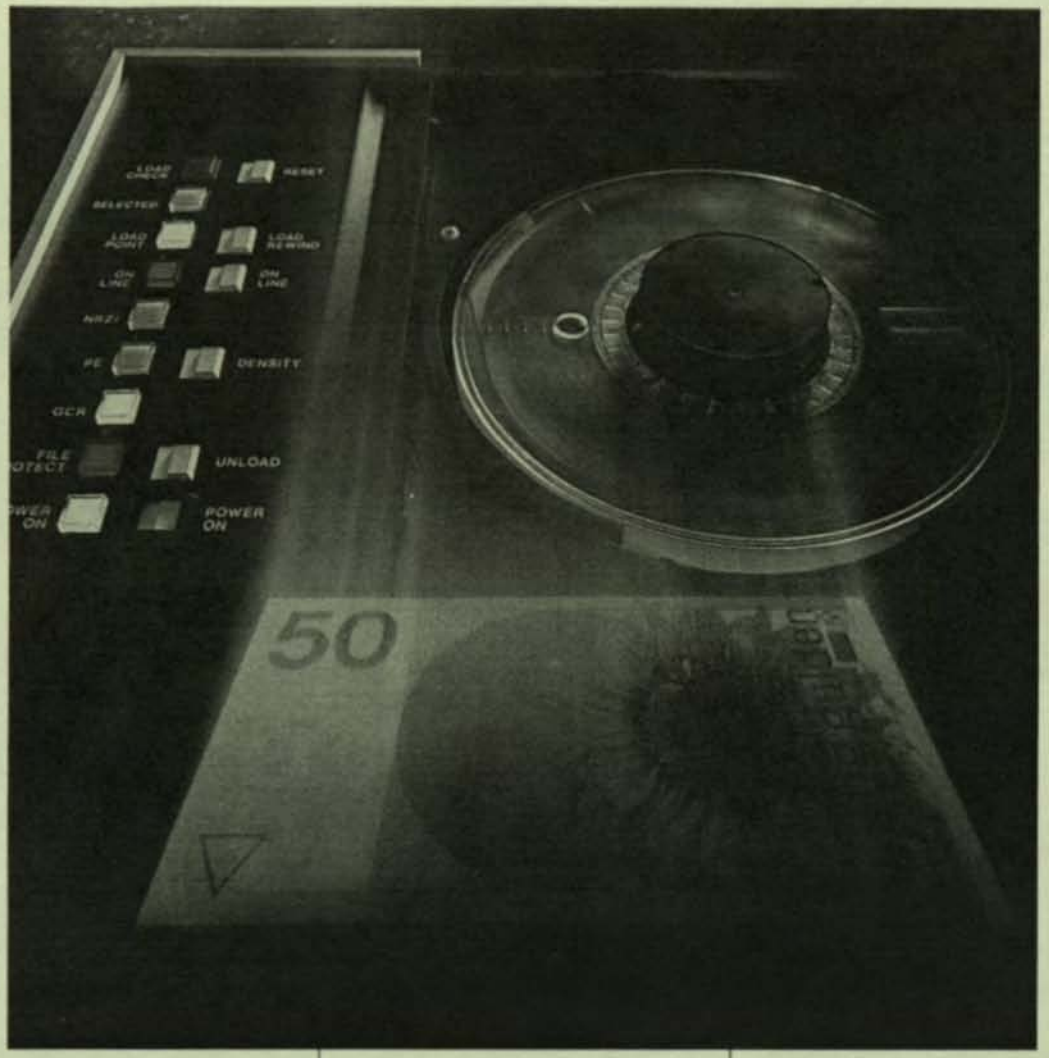
Data integrity is inherent to the Tandem NonStop architecture. To some Tandem users, this feature alone is reason enough to acquire NonStop systems—and all of the other unique capabilities are regarded as free benefits.



"The most valuable part of the computer resource is not the hardware or the software but the data—the information on which the business relies to operate. Tandem offers the highest level of data integrity available today."

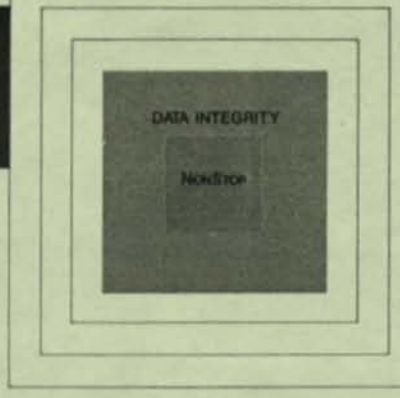
—Dennis McEvoy
Vice President,
Software Development
Tandem Computers

Cable Data, an information systems company, provides complete packages of data processing products and services to over 60% of the U.S. cable TV systems. The company has over 150 Tandem processors deployed in the U.S. and Canada in the growing cable TV industry and at Cable Data offices.



Tandem's data integrity features lend important advantages to all Tandem users, especially to those having extremely active and large on-line data bases. And among the world's largest data bases are those of national governments.

In the Netherlands, where all dependent children are entitled to regular government allowances from birth through college graduation, Tandem's data integrity advantage is an important reason for the government's conversion to NonStop systems. The Sociale Verzekerings Bank is responsible for keeping accurate, current records on some 3.5 million children and making timely, correct payments of over $200 million monthly. The agency's growing Tandem systems are being linked together in an EXPAND network around the country, extending data integrity to hundreds of on-line terminals.



Years-Ahead Tandem Technology

NonStop

Keeping Corporate Information Assets Constantly Available

"According to the results of the survey we conducted with DATAMATION magazine, Tandem users were notable for two factors: the highest levels of usage of both data base management software and networking software, and the highest level of customer loyalty for any vendor covered in the survey."

—Barry Rosenberg
Partner,
Cowen & Company

When enterprises move to on-line systems, if the computer stops, the business stops.

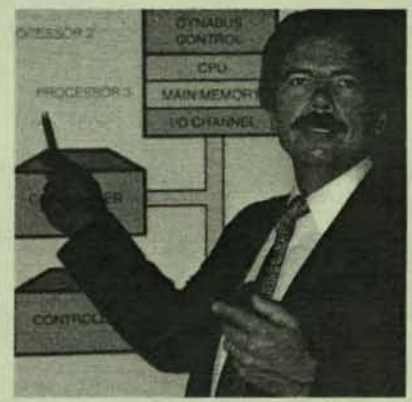
Failures of batch processing mainframes are, by comparison with an on-line system failure, merely nuisance factors. Time lost by idle batch mainframes may be recoverable. But on-line systems deal in real time: Time lost is opportunity lost forever.

At the heart of the NonStop architecture is the technology developed by Tandem that prevents a failure at any single point from causing the system to stop. A component failure is transparent to users; the remaining processor or processors automatically take up the work. Data remains intact, business continues as usual.

Earlier attempts to achieve continuous operations employed redundant, conventional computers hooked together. One system stood idle until the other failed. When that happened, data processing professionals flipped a switch and hoped the second system was healthy. This approach doubled the cost of computer hardware.

The entire NonStop system performs useful work constantly. There is no wasteful redundancy. Even when a NonStop system is undergoing maintenance, the system can continue to run.

And there is no cost premium for fault-tolerance—nor for the other inherent NonStop features of modularity, data integrity and ease of networking. Tandem's price/performance is second to none in on-line transaction processing environments.

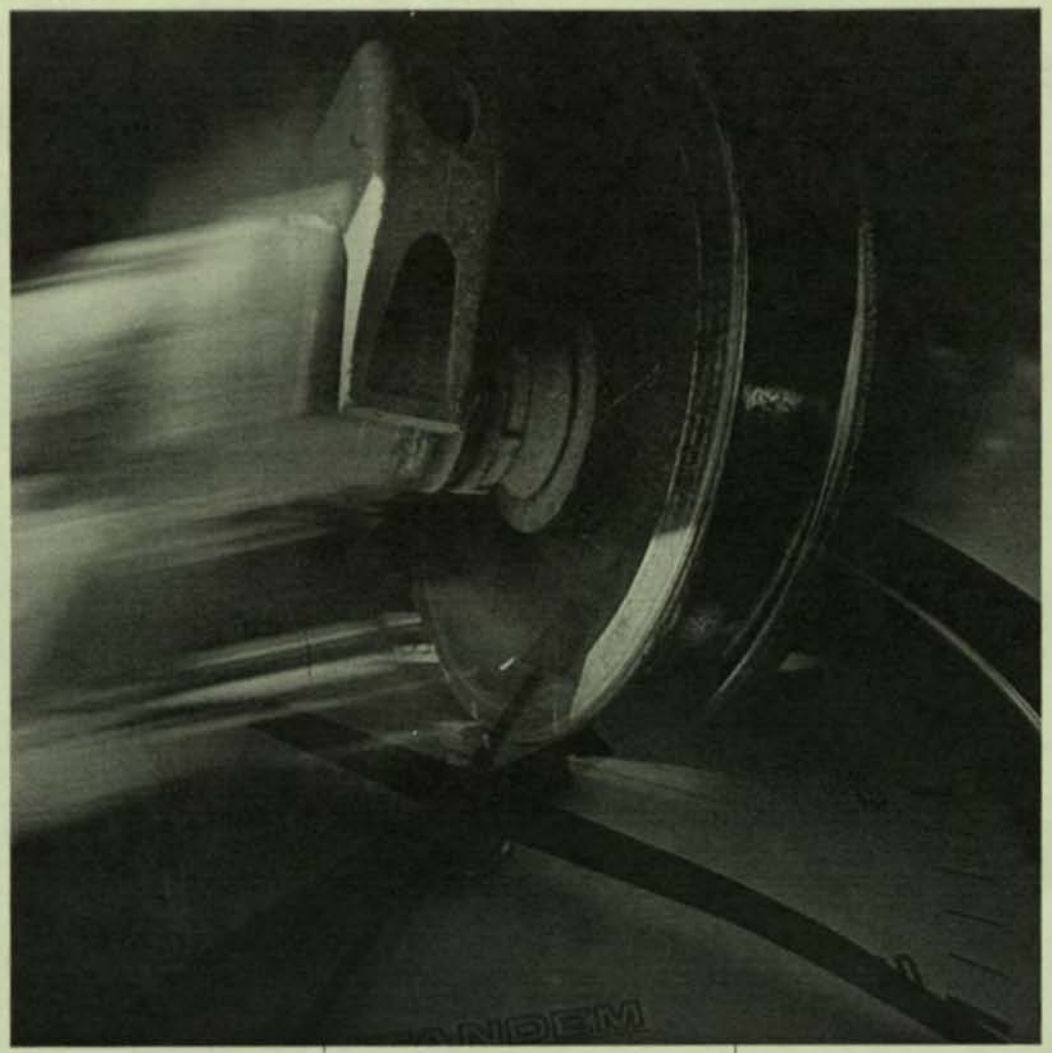


"The basic building block of the Tandem architecture—as well as the foundation of our customer loyalty—is the NonStop feature. Why buy a computer that fails?"

—Gerald L. Peterson
Vice President,
International Marketing
Tandem Computers

Barry Rosenberg is a leading computer industry securities

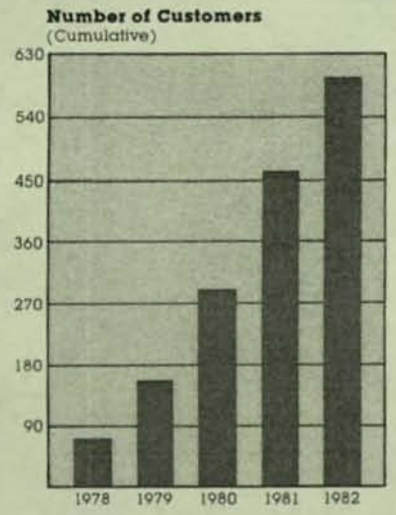
Barry Rosenberg is a leading computer industry securities analyst and director of the annual Cowen/DATAMATION survey of computer users.



Tandem NonStop systems are assuring continual operations and improved customer service for air, rail, sea and road transportation companies worldwide. Around the clock, millions of Tandem transactions occur daily to manage passenger reservations, station operations, cargo bookings and distribution, railroad yards, dockside activities, and total airport facilities.

In railway-dependent Germany, for instance, the heavily traveled national Bundesbahn began converting its domestic and international passenger reservations systems to Tandem in 1982. By early 1983, the network will be handling over 20,000 transactions hourly.

Assuring Successful Customer Applications through Superior Support



Now more than ever, with the movement of critical business applications to on-line transaction processing, users of large systems need responsive, effective and proven support systems from the manufacturer. The best products can be no better than the support, and the support can be no less distributed than the data bases, systems and networks themselves.

That Tandem excels in customer support is clearly evidenced in the 1982 Cowen/DATAMATION survey of computer users in which Tandem, for the third consecutive year, ranked number one in the industry for customer satisfaction and loyalty.

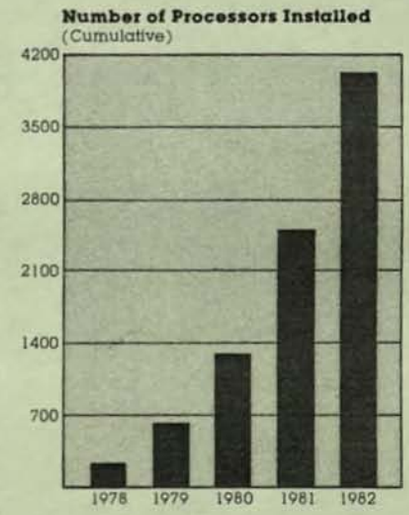
Fully half of the entire Tandem organization—at some 100 locations in 16 countries—is dedicated to some aspect of the company's broad-based, far-reaching support activities including sales support, customer education, field service and applications support.

Even before system delivery, Tandem's responsive attitude is apparent. The Tandem Account Support Team, including both hardware and software specialists, assists prospective users in planning on-line applications.

In many cases, Tandem's unique Application Design Support group conducts in-depth studies of customer plans and intended software, and recommends ways the user can improve the success of the application through changes that take full advantage of the Tandem architecture.

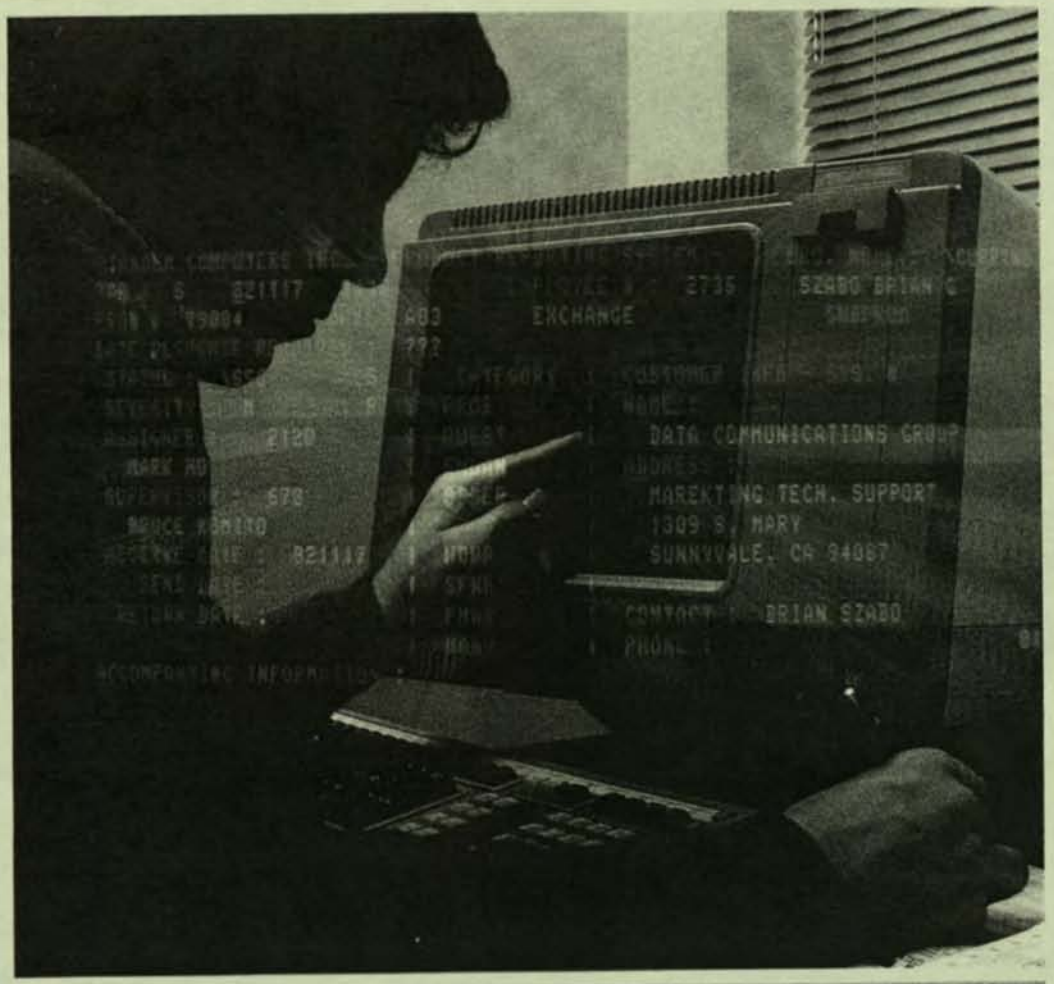
Before shipment, every NonStop system is tested in failed-component modes to ensure continued operation. Once installed, Tandem systems are much more serviceable than conventional computers. The modularity of the architecture lets maintenance and repair take place while the system continues to run user programs uninterruptedly.

Service is provided by an integrated hardware-software Customer Engineering team working with advanced, Tandem-developed diagnostic systems and support techniques as comprehensive as the architecture itself.



Efficiency of Tandem technical

The objective of Tandem customer support in all its aspects is to help make customers' applications successful. One way this is achieved is through Tandem's Application Design Support group which, during 1982, reviewed some 150 customer applications and made recommendations on ways to enhance them by making changes to take maximum advantage of the NonStop architecture. Further assistance was provided during the year via 885 technical training classes for customers totaling over 8,000 student-weeks that were conducted at Tandem customer education facilities.

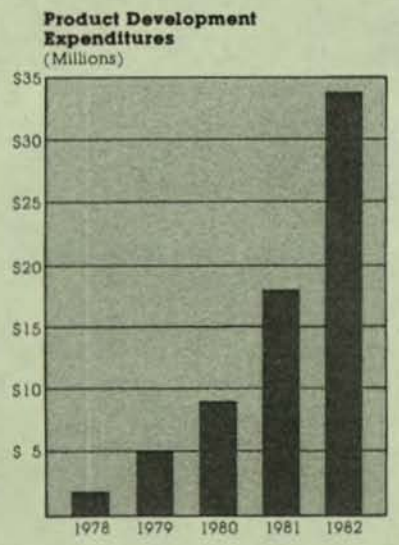


Efficiency of Tandem technical support personnel is enhanced by on-line tools such as the self-contained, microcomputer-based diagnostics console of the NonStop II (above) that is used for on-site and remote trouble-shooting. Customer engineers around the world also use Tandem's corporate EXPAND network to retrieve technical assistance automatically from company headquarters. Low turnover within the Tandem field support organization helps the company maintain a consistently high level of technical support.

Customer feedback as well as service monitoring is facilitated by Tandem's on-line Product Reporting System (left) that captures and disseminates NonStop system service activity as well as customer requests for enhancements and new capabilities.

At Tandem headquarters, the Tandem Executive Institute conducts seminars for senior executives of customer and prospective customer organizations within specific industries. Outside experts define industry trends, Tandem speakers tell how NonStop systems can help companies address those trends competitively, and a Tandem user within the given industry reports on successful NonStop system applications.

Protecting Users' Investment with Flexibility for Future Enhancements



In the final analysis, large organizations that are committing to on-line transaction processing and networks seek a supplier that will preserve and enhance their original investment by remaining responsive to the ever-changing business and technology environments.

Tandem's NonStop architecture provides unprecedented flexibility and adaptability by creating elegant solutions from simple modules.

Since introduction of the original NonStop system, Tandem has spent some $70 million on product development programs—an investment that is heavily leveraged and highly productive for users because the modularity of the architecture, both hardware and software, spreads each enhancement over a full range of system sizes from mid to mainframe. This design also provides unique economies in manufacturing, inventory, and service as well as product development.

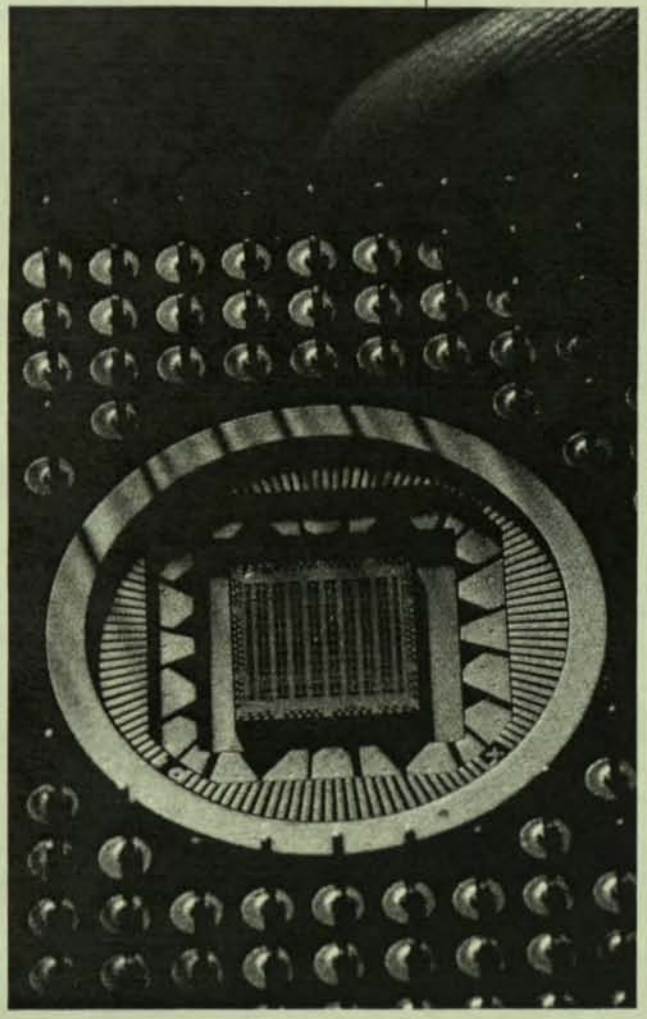
The ultimate goal of Tandem's product development programs is increasing the functionality, efficiency, and ease of operation of the users' backbone resource. Toward this end, the company's spectrum of projects covers new product introductions, enhancements to existing products, and new technology.

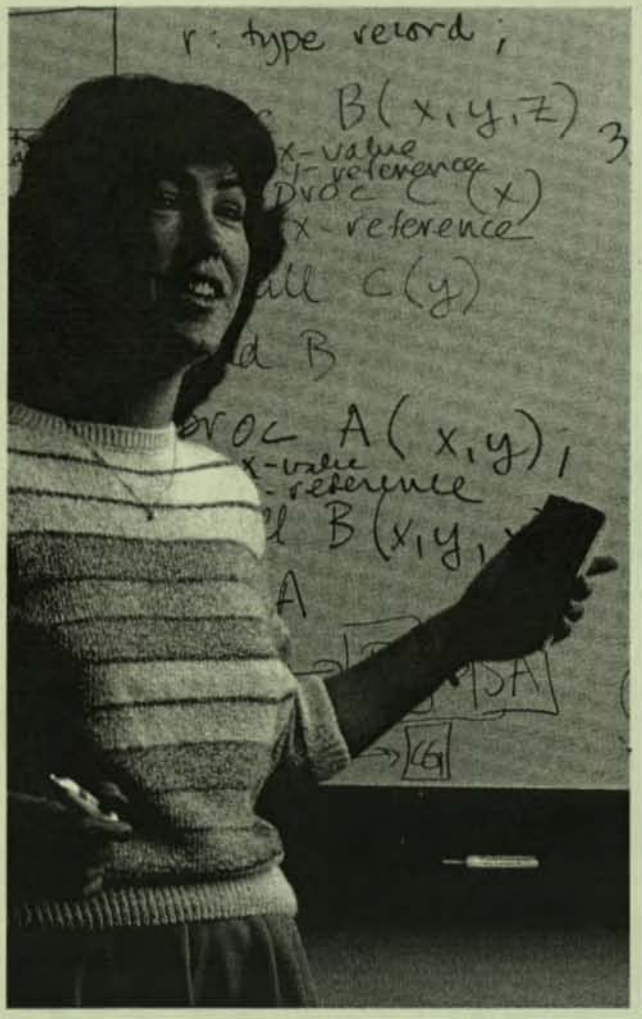
Product enhancements include microcode changes for the NonStop II system that led to as much as a 25% performance improvement at no additional cost to the customer. New products ranged from the 6530 ergonomic terminal, to TRANSFER information management and delivery software, to INFOSAT satellite communications system, to SNAX. SNAX software will enable EXPAND network users to access IBM SNA networks, devices and applications programs while retaining the reliability and flexibility of NonStop systems.

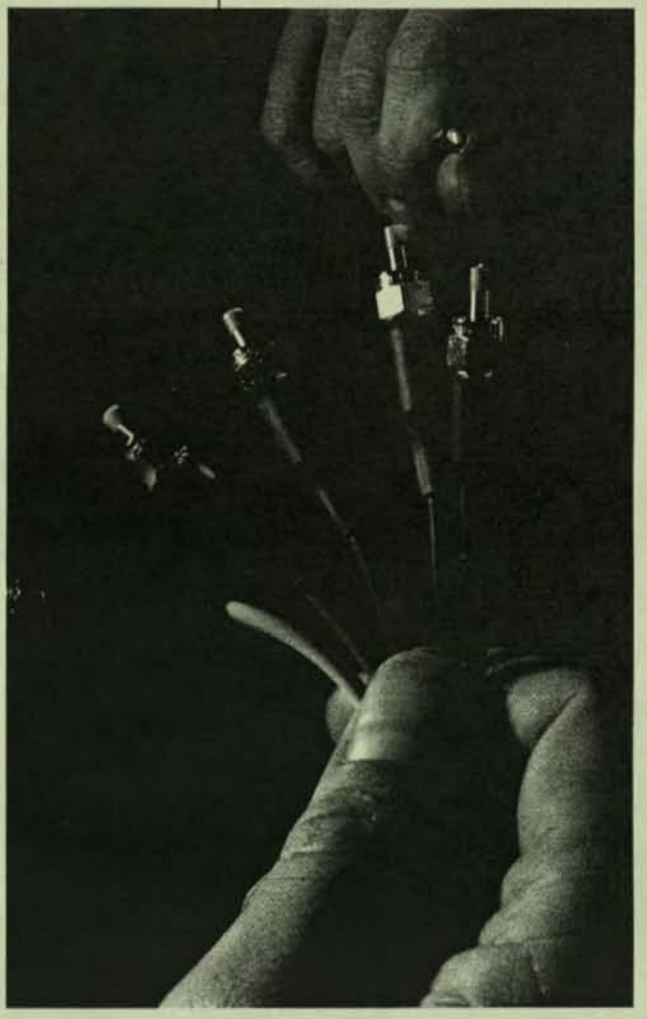
Using Tandem-developed tools for the design of custom logic, the company shipped the first products containing gate arrays of its own design during fiscal 1982. Tandem will soon offer customers a product that is the outgrowth of its work in fiber optics. Tandem customers will be able to link up to 14

maximum-size 16-processor systems that are up to one kilometer apart—without reprogramming—effectively creating a single system with more power than the world's largest conventional mainframe computer.

Tandem's development expenditures—$34 million during fiscal 1982—are divided equally between hardware and software projects. Introduction of LSI gate arrays and fiber optics into NonStop systems is enhancing system performance and reliability, while a steady stream of advanced software products contributes further to system flexibility and ease of programming.

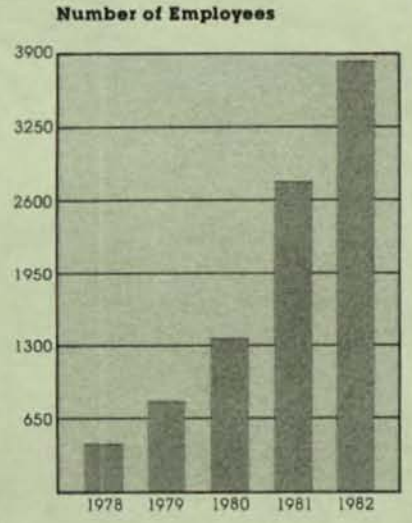






A Unique Organization Focused on

Ensuring Customer Satisfaction through Creative, Dedicated People



Tandem places high value on employee communications to facilitate sharing the responsibility for managing a rapidly growing business, and to perpetuate the successful corporate environment. Although emphasis is on open communications within the company's unstructured environment, formal media are also used.

Earning the industry's highest rating for customer satisfaction is not accidental; Tandem employees care about the company's customers because Tandem cares about its employees. And because Tandem is a good place to work.

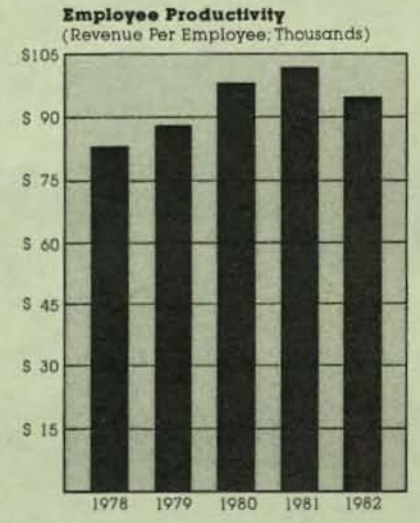
Tandem's ability to recruit and keep quality, creative people is nurtured by the company's reputation for innovativeness and market leadership, the excitement and challenge of being part of a major factor in the industry, and the resultant opportunities for individuals that abound in such a dynamic business.

The Tandem environment is good for its people and good for the company. Employee productivity is far higher than is typical in the computer industry, and the company's turnover rate is less than one-third of the industry average.

High growth consistent with keeping customers satisfied is achieved through shared responsibility, open communications, and performance recognition. Creativity, teamwork and individual dedication flourishes at Tandem in an unstructured environment that is guided by a clear sense of direction communicated throughout the company.

Individual growth is not left to chance. The self-education process that is promoted by the nature of the workplace is augmented with formal training. Over 150 individuals monthly attend courses in the Tandem Management Development Program. And throughout the organization, the company strives to explain the impact of each individual's performance on the company's success—and how that success affects each individual.

Job satisfaction is a major reward at Tandem, but the company also pays its people well, provides stock ownership opportunities (nearly all employees are optionholders or stockholders), gives employees a voice in selecting benefits, and provides North American employees six-week, fully-paid sabbaticals every four years, while employees outside North America take the customary longer vacations annually.



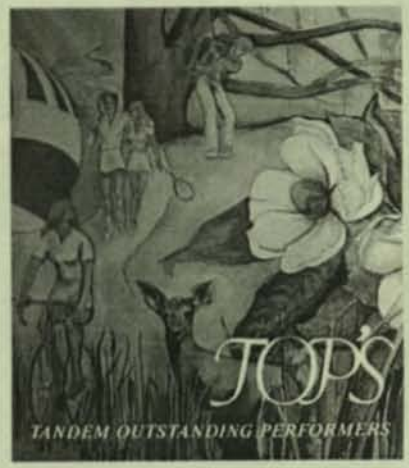
Center magazine focuses on the range of human and business aspects of life at Tandem, candidly written by individuals from all areas of the organization.

Teleconferences, initiated during 1982, communicate technical and business information to all U.S. sites simultaneously and interactively.

Tandem's shared-management philosophy works at the top level of the company as well. Decision-making is shared by the Management Committee, comprised of the senior managers from Tandem's domestic and international operations.

And company facilities are intentionally designed with an open feeling to encourage easy interaction.

One method of employee recognition is the international Tandem Outstanding Performers program that rewards exceptional individuals with a company-paid group trip. The program also promotes idea exchange among many of Tandem's highest achievers.



Quiz

1. The biggest change taking place in commercial data processing within large organizations is
   a. Batch processing is making a comeback.
   b. Companies are consolidating and centralizing data processing.
   c. Businesses are moving their data processing from batch to on-line to better control resources, offer improved service to customers, and have more timely management information.

2. Tandem's marketplace is
   a. Limited niche applications where users require a fail-safe computer.
   b. The rapidly growing realm of on-line transaction processing.
   c. Traditional batch computing applications.

3. Tandem is selling
   a. A minicomputer.
   b. A mainframe computer.
   c. A continuously available computer system that can grow modularly from the power of a minicomputer to that of a mainframe.

4. Why is continuous availability important in an on-line environment?
   a. When the computer stops, the business stops.
   b. When the computer stops, sales are lost.
   c. When the computer stops and you can't take the customer's order, the customer goes somewhere else.

5. Tandem NonStop systems assure continuous availability through
   a. Coupled processors in a "hot standby" mode where the standby waits for the working processor to fail.
   b. Total system redundancy, where processing is replicated on a set of duplicate components.
   c. A combined hardware and software solution that allows the entire system to do useful work at all times.

6. What is the advantage of Tandem's satellite link versus a long distance telephone link in computer communications?
   a. None, because telephones are the established technology.
   b. Costs are lower, speeds are faster, and you can broadcast to multiple locations simultaneously.
   c. You never get a busy signal.

7. The level of Tandem's customer satisfaction and loyalty is determined by
   a. The number of people in Tandem's customer support functions.
   b. The customer's mood on any given day.
   c. How successful the customers' applications are.

8. Who needs Tandem system data integrity features?
   a. A bank that wants a multi-million dollar deposit recorded accurately.
   b. An airline that wants fully booked cargo operations.
   c. A hospital that wants patients to have the correct medication.

9. Which statement is false?
   a. Tandem's employee productivity is really not much different than the industry average.
   b. Tandem's employee turnover rate is well below the industry average.
   c. Paid sabbaticals are a really nice benefit.

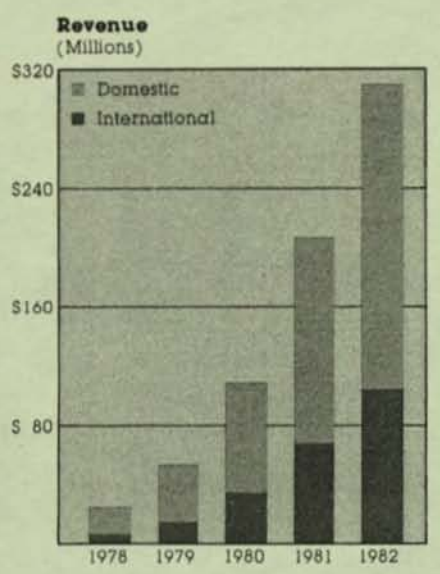
10. Why would anyone buy a computer that fails?
    a. S/he does not yet know about Tandem.
    b. S/he does not understand the cost of downtime.
    c. S/he does not use a computer.

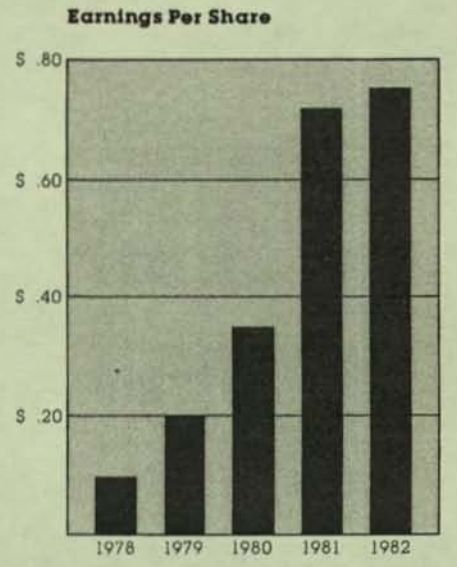
Answers

1. c 2. b 3. c 4. all 5. c 6. b 7. c 8. all 9. a 10. all

HIGHLIGHTS

Fiscal Year Ended September 30	1982	1981	1980
Revenue	$312,143,000	$208,397,000	$108,989,000
Operating Income	$ 40,708,000	$ 40,391,000	$ 19,323,000
Operating Margin	13.0%	19.4%	17.7%
Net Income	$ 29,856,000	$ 26,549,000	$ 10,687,000
Earnings Per Share	$.76	$.72	$.35
Working Capital	$194,761,000	$179,102,000	$ 61,232,000
Total Assets	$337,366,000	$255,971,000	$ 95,701,000
Equity	$250,988,000	$204,810,000	$ 70,294,000
Number of Employees	3,821	2,730	1,387





TO OUR STOCKHOLDERS

In the comparatively short period of time since the Company was formed in November, 1974 until today, Tandem Computers has become a significant factor in the computer industry as well as a leader in the on-line transaction processing marketplace. This outstanding performance is one in which we take a great deal of pride. When a company achieves such success and attendant size, however, it is no longer possible to be totally immune to the effects of the economy. Most of our business regions remained strong relative to the industry in fiscal 1982, but not in line with our traditional growth rates. A few geographic areas have been more affected by the recession, with the result that Tandem's sales in those regions grew at a slower pace this year and our overall growth rate moderated somewhat. At the same time we believe that we strengthened our competitive position, adding to our customer base of large corporations making major commitments to Tandem, investing in new products, and gaining experience lead-time.

For the fiscal year ended September 30, 1982, revenue grew at a rate of 50% to $312,143,000 from $208,397,000 in fiscal 1981. Operating margins were 13% in fiscal 1982, compared with 19% in the previous period. Net income was $29,856,000 or $.76 per share, versus $26,549,000 or $.72 per share, in 1982 and 1981 respectively. The combination of revenue that was below target and continued high investment to support product development and expansion of our organization led to margins that were below our goal.

Nonetheless, as our 50% growth rate indicates, Tandem's marketplace is one of the most robust in the computer industry. We are committed to developing the resources—the products, the sales and service organization, and the people—necessary to continue to be a leader in this high-growth market. As an indication of our level of commitment, the Company spent $34 million on product development and $64 million on property, plant, and equipment in fiscal 1982.

Investment in Products

During fiscal 1982, the Company introduced a number of enhanced products and announced a series of new products that will become available during 1983. Among the product enhancements, the Company began offering a two-megabyte memory board for the NonStop II that provides users with increased memory capacity for each processor. In addition, we introduced a completely new line of higher performance peripheral products, including disk drives, a high capacity tape drive, printers, and a terminal. The most important of these products is the Tandem-designed and manufactured 6530 ergonomic terminal which we introduced at the Annual Stockholders Meeting last February. The market acceptance of this product is very good; we have ramped up production and now ship terminals exclusively of our own manufacture.

Investment in Facilities

In order to maintain our commitment to provide a superior level of support to our customers, Tandem opened twelve new branch sales offices in the United States, Canada, and England; opened new sales subsidiaries in Belgium and Norway; and established distributors in Argentina and Israel.

Facilities expanded with the opening of a plant to manufacture the 6530 terminal in Austin, Texas, a manufacturing facility in Bensenville, Illinois, and an addition to the corporate headquarters in Cupertino, California. Further, the Company broke ground for a printed circuit board automated assembly and testing plant in Watsonville, California.

Investment in Productivity and Technology

Tandem has a continuing dedication to manufacturing efficiency and to developing new technology. Toward this end, a state-of-the-art board testing system was developed by Tandem and introduced into the manufacturing process. Thus far we have attained significant gains in productivity. In addition, a pilot program for automated board assembly was very successful, which has led us to expand our operations in Watsonville.

Investing in technology has resulted in a unique contribution in Tandem-developed tools for design of custom logic. Using these tools, during 1982 we developed and shipped the first products containing gate arrays of our own design.

Outstanding People

This rather formidable list of achievements is the result of the creativity and hard work of Tandem's people. The dedication of our people is indicated by their high productivity: average revenue per employee was $95,000. Turnover, at 9%, remains far below the industry standard.

Each person at Tandem works at maintaining an environment that encourages such outstanding performance. The Company supports its people's efforts by providing technical training as well as management training through the Tandem Management Development Program. The Company also provides recognition of superior performance through its TOPS—Tandem Outstanding Performers—program. TOPS is a way both to reward people, and to provide a mechanism for outstanding people to share their ideas. In addition, we realize that all our people need a time to recharge, and we try to find ways to support that. For example, each employee in the United States earns a paid sabbatical every four years.

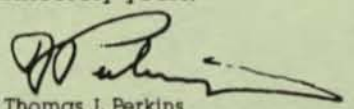
Outlook

We believe that Tandem possesses all the necessary attributes for continuing success. Our marketplace is one of great potential throughout the Eighties. We have an impressive customer base, a unique and innovative product, outstanding people, and a well developed organization.

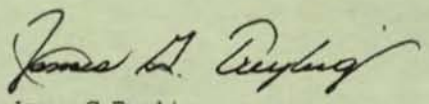
The Company extended its market focus with the announcement of our planned comprehensive corporate information system. The first products, which will be available during 1983, are TRANSFER information delivery system that allows users to move office information along with traditional data processing over a Tandem EXPAND network; TRANSFER/MAIL electronic mail manager; and TRANSFER/FAX facsimile manager. The Company unveiled the first commercially available, fully integrated computer/satellite communications network, called INFOSAT, that will provide a low-cost, highly reliable alternative to terrestrial communications facilities. This product will be marketed jointly by Tandem and American Satellite Company. Tandem also announced a new communications product, SNAX, that will provide users of Tandem distributed networks with access to IBM SNA networks, devices, and application programs while retaining the high-reliability benefits inherent in all Tandem products.

Since the worldwide economic environment continues to be uncertain, we have taken steps to control our expenses better, with the objective of improving our margins to historic rates. Perhaps most importantly, we are educating all our people about their individual responsibility for attaining our goals. Overall, we anticipate fiscal 1983 to be a year of challenge, but also a year when Tandem continues to be a growth leader in the industry.

Sincerely yours,



Thomas J. Perkins
Chairman of the Board



James G. Treybig
President and Chief Executive Officer

December 1, 1982

SELECTED FINANCIAL DATA
For the Five Years Ended September 30, 1982

(In thousands except per share amounts)	1982	1981	1980	1979	1978
Revenue	$312,143	$208,397	$108,989	$55,974	$24,305
Cost of revenue	109,305	75,547	40,831	20,786	9,096
Product development	33,642	17,833	8,786	4,654	2,169
Marketing, general and administrative	128,488	74,626	40,049	20,828	8,808
Operating Income	40,708	40,391	19,323	9,706	4,232
Interest income, net	6,033	10,707	1,759	398	258
Provision for income taxes	(16,885)	(24,549)	(10,395)	(5,184)	(2,337)
Income Before Extraordinary Credit	29,856	26,549	10,687	4,920	2,153
Net income	29,856	26,549	10,687	4,920	3,371
Earnings Per Share Before Extraordinary Credit	$ .76	$ .72	$ .35	$ .20	$ .10
Earnings per share	.76	.72	.35	.20	.16
Total assets	$337,366	$255,971	$ 95,701	$45,947	$22,051
Long-term debt and capitalized lease obligations	21,102	2,054	1,651	1,144	715
Stockholders' investment	250,988	204,810	70,294	31,530	15,538

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Tandem Computers continues its commitment to being a technological leader in the rapidly growing market for on-line transaction processing systems and networks of on-line systems. The Company believes that fault tolerance is a fundamental architectural design criterion for computer systems that support such applications. Achieving the Company's technological leadership goal involves many factors, including strategic market positioning, an ongoing commitment to product development, and an organizational structure and philosophy that fosters employee productivity and creativity. Also critical is maintaining a financial position and operating record that allows the Company to maximize its performance in an environment of rapid growth.

Financial Condition

Financial soundness is a high priority within Tandem. The Company's rapid growth has required increasing investment in working capital and property, plant, and equipment. Working capital has been funded through internally generated sources of funds and external financing, primarily equity issues sold to public investors and to employees through option and stock purchase programs. All profits after taxes have been reinvested in the business. Capital equipment has been funded with equity, lease financing, and Industrial Revenue Bonds. During fiscal 1982 the Company began construction of major facilities in Austin, Texas and Watsonville, California. These facilities are being financed during the construction phase under revolving lines of credit. All existing facilities being used by the Company are leased.

As of September 30, 1982 Tandem Computers has a cash and cash investment balance of $24,816,000, unused revolving lines of credit totalling $63,276,000, and an equity base of $250,988,000. The Company has a current ratio of 5:1, and long-term debt was less than 8% of total capital at fiscal 1982 year-end. The Company's financial strategy includes maintaining a sound ratio of current assets to current liabilities and a conservative capital structure. The Company believes this strategy provides it with maximum near term and long term flexibility to consider the full range of financing alternatives to fund the capital needs of its projected future growth.

Results of Operations

The table below summarizes the changes in important operating indicators for the fiscal years presented. The numbers on the left account for the revenue dollar by showing various income and expense items as a percentage of revenue. The numbers on the right measure the yearly percentage increases (decreases) in the same items.

in the year, and as the new Tandem designed and manufactured 6530 terminal entered volume production and shipment. During the year, the Company shipped 1,542 processors, compared with 1,210 processors in fiscal 1981. Foreign revenue accounted for 33.5% of total revenues for fiscal 1982, compared to 34.3% and 31.4% for fiscal 1981 and 1980 respectively.

Operating Margins

Tandem Computers has a goal of achieving 16-20% operating margins. During fiscal 1982 the Company did not meet this goal because shipments recognized as revenue during the year did not meet projections. This was due primarily to the previously mentioned economy-related pressure on revenue growth and the Company's high level of committed expenses in product development and marketing. In addition, revenue for some $24,000,000 in shipments was deferred into fiscal 1983, but indirect costs associated with these shipments were charged in fiscal 1982.

The Company's cost of revenue as a percent of revenue declined slightly in fiscal 1982 and 1981 despite the opening of new manufacturing facilities in Watsonville, California; Austin, Texas; Bensenville, Illinois; and Reston, Virginia, and despite the start-up costs of manufacturing significant new products including the NonStop II system and the 6530 terminal.

Tandem's product development effort is focused on meeting the needs of computer users who are implementing on-line systems, both at single sites and in geographically distributed on-line information processing networks. The Company believes that the opportunities for technological innovation in this marketplace are enormous. Investment in product development is targeted to be in the range of 9–10% of revenue in fiscal 1983. These funds are being invested in enhancements to existing products and in important new products that will be introduced over the years to come.

The Company has focused its marketing strategy on selling to end-users who are implementing major on-line applications. Providing a high level of service and support is essential to meeting the needs of this customer base. To maximize its long-term opportunities in this marketplace, Tandem has built a direct selling and support organization in the United States and, primarily through wholly-owned subsidiaries, in industrial markets throughout the world. The Company's marketing, general and administrative expenditures in fiscal 1982 were higher as a percentage of revenue than in previous years due to the rapid expansion of the marketing organization during a period of slower revenue growth than anticipated. Looking ahead, the Company believes that a relatively high level of expenditures on marketing and support, such as has been the case in each of the last three years, is required to compete successfully in its marketplace.

% of Revenue				% Increase (Decrease)		
1982	1981	1980		1982	1981	1980
100	100	100	Revenue	50	91	95
35	36	37	Cost of revenue	45	85	96
11	9	8	Product development	89	103	89
41	36	37	Marketing, general and administrative	72	86	92
13	19	18	Operating income	1	109	99
2	5	2	Interest, net	(44)	509	342
15	25	19	Pretax income	(9)	142	109
5	12	10	Provision for taxes	(31)	136	101
10	13	10	Net income	12	148	117
			Earnings per share	6	106	75
			Weighted average shares outstanding	6	22	21

(Totals may not add due to rounding.)

Revenue

Tandem Computers' revenue gains over the last three years have resulted directly from increased shipments of its computer hardware and software products to new and existing customers, and from increases in the number of customers using its support and training services. During fiscal 1982 the Company did experience a slowing in its revenue growth particularly in certain geographic regions, which the Company believes related to unfavorable economic conditions in those areas. Fiscal 1982 was also a year of significant product transitions, as the NonStop II, first shipped in mid-1981, accounted for about 60% of processor shipments

Net Income and Earnings Per Share

Net income growth has differed from operating income growth due to substantial changes in the Company's net interest income and a decline in the effective tax rate. Interest income has been earned on funds raised from public equity financings in advance of operating requirements. As these funds have been drawn into the operating assets of the Company, interest income has declined.

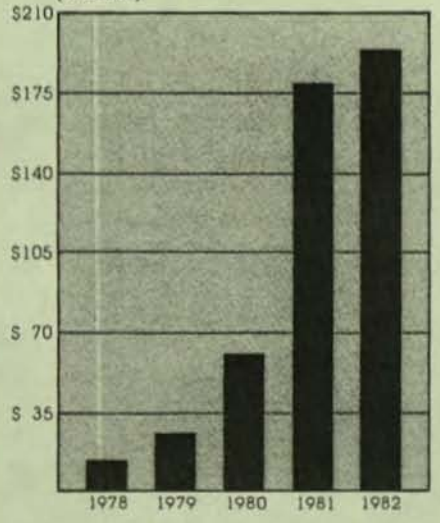
The Company's tax rate was 36% in 1982, compared with 48% in 1981 and 49% in 1980. The decline in the Company's effective tax rate in 1982 resulted primarily from tax incentives provided by the Economic Recovery Tax Act of 1981 for research and development expenditures and investment in capital equipment.

Earnings per share have grown less rapidly than net income due to increases in shares outstanding. The Company's public offerings of common stock in fiscal 1981 and 1980, combined with sales of stock to employees under the stock purchase plan and grants under option plans, resulted in increases in weighted average shares outstanding of 6% in 1982, 22% in 1981, and 21% in 1980. Proceeds from the sale of these additional shares have been used to finance the capital expansion required to support the Company's growth during this period.

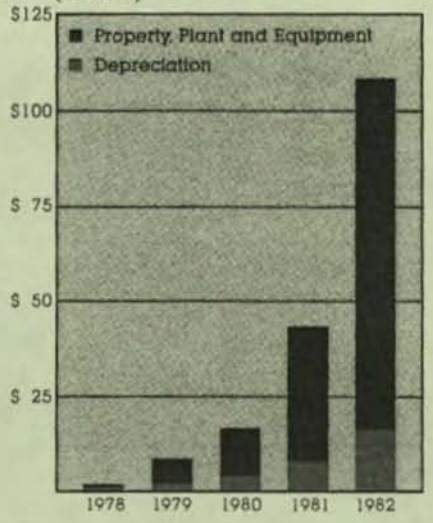
Effect of Inflation

The Company believes that the effect of inflation on labor rates has been offset by increases in productivity and decreases in materials costs.

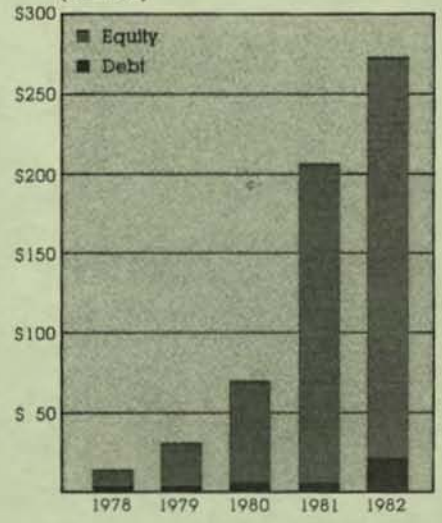
Working Capital
(Millions)



Property, Plant and Equipment
(Millions)



Capitalization
(Millions)



CONSOLIDATED STATEMENT OF INCOME

For the Three Years Ended September 30, 1982

(In thousands except per share amounts)	1982	1981	1980
Revenue			
Product revenue	$272,591	$186,897	$ 98,030
Service and other revenue	39,552	21,500	10,959
Total revenue	312,143	208,397	108,989
Costs and Expenses			
Cost of revenue	109,305	75,547	40,831
Product development	33,642	17,833	8,786
Marketing, general, and administrative	128,488	74,626	40,049
Total costs and expenses	271,435	168,006	89,666
Operating Income	40,708	40,391	19,323
Interest expense	(967)	(282)	(293)
Interest income	7,000	10,989	2,052
Income Before Income Taxes	46,741	51,098	21,082
Provision for income taxes	(16,885)	(24,549)	(10,395)
Net Income	$ 29,856	$ 26,549	$ 10,687
Earnings Per Share	$ .76	$ .72	$ .35
Weighted average shares outstanding	39,221	37,025	30,241

The accompanying notes are an integral part of this statement.

A new facility in Reston, Virginia for systems integration and testing was being readied for occupancy at the close of fiscal 1982. Other new facilities this year include an extension to the corporate headquarters complex in California and leased manufacturing facilities in Bensenville, Illinois and Austin, Texas. Other buildings are under construction, due on-stream in 1983.

CONSOLIDATED BALANCE SHEET

As of September 30, 1982 and 1981

(In thousands)	1982	1981
Assets		
Current Assets		
Cash and cash investments	$ 24,816	$ 89,806
Accounts receivable, net of allowances of $3,000,000 in 1982 and $1,000,000 in 1981	98,810	70,671
Inventories	101,335	54,543
Prepaid expenses and other	17,013	5,046
Total current assets	241,974	220,066
Property, Plant and Equipment, at cost		
Land	4,441	—
Machinery and equipment	25,767	13,154
Computer equipment and spares	44,274	20,439
Leasehold improvements	21,788	8,147
Construction in process	11,196	2,599
	107,466	44,339
Accumulated depreciation and amortization	(18,080)	(8,434)
Net property and equipment	89,386	35,905
Other Assets	6,006	—
Total Assets	$337,366	$255,971

(In thousands)	1982	1981
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of capitalized lease obligations	$ 2,060	$ 682
Accounts payable	22,918	23,634
Accrued liabilities:		
Wages, payroll taxes, and employee benefits	8,913	3,969
Income taxes	7,136	10,275
Other accrued liabilities	6,186	2,404
Total current liabilities	47,213	40,964
Capitalized Lease Obligations	10,378	2,054
Long Term Debt	10,724	—
Deferred Income Taxes	18,063	8,143
Stockholders' Investment		
Common stock $.025 par value, authorized 60,000,000 shares, outstanding 37,634,754 in 1982 and 36,409,631 in 1981	941	910
Additional paid-in capital	177,759	161,468
Retained earnings	72,288	42,432
Total stockholders' investment	250,988	204,810
Total Liabilities and Stockholders' Investment	$337,366	$255,971

The accompanying notes are an integral part of this balance sheet.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' INVESTMENT

For the Three Years Ended September 30, 1982

(In thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Total
Balance September 30, 1979	25,020	$209	$ 25,520	$ 5,801	$ 31,530
Sale of common stock, net of related expenses	4,290	36	24,243	—	24,279
Sale of common stock under stock option plans	589	5	2,037	—	2,042
Sale of common stock under stock purchase plan	176	1	949	—	950
Tax benefit from employee transactions in common stock	—	—	806	—	806
Net income	—	—	—	10,687	10,687
Balance September 30, 1980	30,075	251	53,555	16,488	70,294
Sale of common stock, net of related expenses	4,500	38	95,995	—	96,033
Sale of common stock under stock option plans	1,692	15	7,381	—	7,396
Sale of common stock under stock purchase plan	143	1	2,272	—	2,273
Capitalization of retained earnings for three-for-one stock split	—	605	—	(605)	—
Tax benefit from employee transactions in common stock	—	—	2,265	—	2,265
Net income	—	—	—	26,549	26,549
Balance September 30, 1981	36,410	910	161,468	42,432	204,810
Sale of common stock under stock option plans	863	22	5,028	—	5,050
Sale of common stock under stock purchase plan	362	9	7,190	—	7,199
Tax benefit from employee transactions in common stock	—	—	4,073	—	4,073
Net income	—	—	—	29,856	29,856
Balance September 30, 1982	37,635	$941	$177,759	$72,288	$250,988

The accompanying notes are an integral part of this statement.

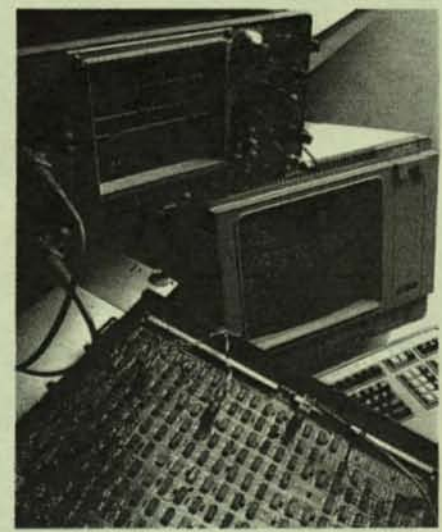
This year Tandem began to manufacture an ergonomic terminal of its own design. The new terminal features user comfort, high throughput, and data integrity. In addition to the 6530 terminal, Tandem introduced a completely new line of higher performance peripheral devices.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Three Years Ended September 30, 1982

(In thousands)	1982	1981	1980
Working Capital Provided From (Used For):			
Net Income	$ 29,856	$ 26,549	$10,687
Add back items not currently using working capital			
Depreciation and amortization	10,196	4,107	2,547
Deferred income taxes	9,920	4,818	2,284
Working capital provided from operations	49,972	35,474	15,518
Acquisition of property, plant and equipment, net	(63,677)	(25,974)	(9,966)
Increase in other assets	(6,006)	—	—
Increase in capitalized lease obligations	8,324	403	507
Increase in long term debt	10,724	—	—
Tax benefit from employee transactions in common stock	4,073	2,265	806
Sale of common stock, net	12,249	105,702	27,271
Net increase in working capital	$ 15,659	$117,870	$34,136
Working Capital Increase Represented By:			
Increase (decrease) in current assets			
Cash and cash investments	$(64,990)	$ 73,561	$ 9,487
Accounts receivable	28,139	28,119	22,671
Inventories	46,792	33,642	9,597
Prepaid expenses and other	11,967	3,081	580
(Increase) decrease in current liabilities			
Current portion of capitalized lease obligations	(1,378)	(206)	(101)
Accounts payable	716	(12,571)	(5,388)
Accrued liabilities other than income taxes	(8,726)	(3,157)	(1,947)
Accrued income taxes	3,139	(4,599)	(763)
Net increase in working capital	$ 15,659	$117,870	$34,136

The accompanying notes are an integral part of this statement.



ORACLE, a Tandem-developed system for automatic testing of printed circuit boards introduced into Tandem manufacturing locations during 1982, provides testing functions not previously possible, and dramatically boosts manufacturing productivity. Other manufacturing enhancements brought on-stream during 1982 include new capabilities for automated assembly of printed circuit boards.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of Tandem Computers Incorporated and its wholly-owned subsidiaries after elimination of intercompany accounts and transactions.

Revenue Recognition

The Company generally recognizes revenue from equipment sales at the time of shipment. Service and other revenue are recognized ratably over the contractual period or as the services are provided.

Exchange Gains and Losses

Foreign exchange and translation gains and losses are not significant and are reflected in the results of operations.

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market and include materials, labor, and manufacturing overhead. The components of inventories as of September 30 were:

(In thousands)	1982	1981
Purchased parts and subassemblies	$56,822	$33,625
Work-in-process	13,413	8,819
Finished goods	31,100	12,099
Total	$101,335	$54,543

Income Taxes

The Company provides for income taxes on total DISC income and accounts for investment and research and development tax credits as a reduction of the provision for income taxes in the year in which the related credits are realized.

Property, Plant and Equipment

Systems spares ($15,869,000 in 1982 and $8,610,000 in 1981) are depreciated over a five-year period using the double declining balance method. All other property, plant and equipment are depreciated using the straight-line method. The estimated useful lives are:

Machinery and equipment	5–10 years
Computer equipment and spares	5– 7 years
Leasehold improvements	Lease term

	1982	1981	1980
Federal statutory tax rate	46%	46%	46%
State taxes, net of Federal income tax benefit	4	4	4
Investment tax credits	(8)	(3)	(3)
Research and development tax credits	(8)	(1)	—
Other	2	2	2
Effective Tax Rate	36%	48%	49%

3. Lease and Other Commitments

The Company leases its headquarters, operating facilities, field offices, and automobiles under operating lease agreements. The Company also has capitalized leases for certain equipment. Future lease payments as of September 30, 1982 are as follows:

(In thousands)	Leases	
Fiscal Year	Operating	Capital
1983	$ 27,084	$ 3,567
1984	25,709	3,481
1985	23,665	3,314
1986	22,699	3,068
1987	19,151	3,873
1988–2004	112,731	—
Total minimum lease payments	$231,039	17,303
Less: Amount representing interest (4%-17%)		4,865
Present value of minimum lease payments		$12,438

Rent expenses were $20,895,000 in 1982, $8,908,000 in 1981, and $4,509,000 in 1980.

The Company has entered into a lease agreement for a new facility in Reston, Virginia, which is expected to be occupied in fiscal 1983, and for which the Company has guaranteed construction financing of $13,495,000. In addition, the Company has standby letters of credit totaling approximately $3,800,000 for other operating purposes.

4. Long Term Debt

As of September 30, 1982 long term debt consisted of $8,724,000 in construction financing and $2,000,000 of Industrial Revenue Bonds, all related to facilities under construction in Watsonville, California and Austin, Texas. Interest costs of $508,000 related to this construction were capitalized in fiscal 1982. The Industrial Revenue Bonds bear interest at 12% and 12⅜% and are due in 1992.

The Company has entered into unsecured credit agreements totaling $72,000,000 with several banks. The agreements provide for revolving borrowings through various dates in 1984, at which time outstanding

Earnings Per Share

Earnings per common share have been computed based upon the weighted average number of common and common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options outstanding that have a dilutive effect when applying the treasury stock method. Fully diluted earnings per share are substantially the same as reported earnings per share.

2. Income Taxes

The provision for income taxes included the following deferred (prepaid) items:

(In thousands)	1982	1981	1980
Current Federal	$ 5,516	$15,356	$ 6,022
Current State	3,633	3,771	1,682
Current Foreign	2,244	1,401	1,120
	11,393	20,528	8,824
Prepaid Federal	(3,333)	(1,205)	(281)
Prepaid State	(253)	(180)	(29)
Prepaid Foreign	(842)	588	—
	(4,428)	(797)	(310)
Deferred Federal	6,656	4,325	2,104
Deferred State	239	194	82
Deferred Foreign	3,025	299	(305)
	9,920	4,818	1,881
Total Provision	$16,885	$24,549	$10,395

Sources of deferred (prepaid) taxes were as follows:

(In thousands)	1982	1981	1980
Installment sale method for income tax reporting	$ 3,657	$ —	$ —
Expenses recognized for financial statements, but not for income tax reporting	(1,505)	(897)	(195)
Effect of intercompany profit eliminations	(2,654)	(2,522)	(611)
Other items	(3,926)	2,622	496
Total Prepaid	$(4,428)	$ (797)	$ (310)
DISC income	$ 3,918	$ 3,230	$ 1,638
Accelerated depreciation	2,799	1,192	538
Other items	3,203	396	(295)
Total Deferred	$ 9,920	$ 4,818	$ 1,881

The provision for income taxes differs from the amount obtained by applying the Federal statutory income tax rate to income before taxes as follows:

amounts may be converted into term loans repayable in equal quarterly installments through 1987. Domestic borrowings bear interest at or below the banks' prime rates during the revolving period and approximately ¼% above these rates during the term period. The Company is required to pay a commitment fee of ⅜% per annum. Of these facilities $22,000,000 have been earmarked by Tandem for the construction referred to above. The remaining $50,000,000 are for working capital purposes and contain provisions for Eurocurrency and foreign local currency borrowings at interest rates prevailing in these markets. There are no compensating balances required under any of these arrangements.

Certain financial covenants and restrictions are included in the loan agreements, including a restriction on payment of cash dividends. The Company was in compliance with all such covenants and restrictions at September 30, 1982.

5. Preferred and Common Stock

PREFERRED STOCK

The Company has 2,400,000 shares of preferred stock authorized.

STOCK OPTION PLANS

The Company has employee stock option plans under which permanent employees may be granted options to purchase shares at 100% of fair market value at the time of the grant. Options generally become exercisable six months after the effective date and expire no later than seven years after the effective date. At the discretion of the Company, options granted under the stock option plans may qualify for Incentive Stock Option treatment under the Economic Recovery Tax Act of 1981.

As of September 30, 1982 options for 5,041,824 shares were outstanding at prices ranging from $.58 to $26.88, with an average price of $16.01. Options for 4,282,209 shares were exercisable as of September 30, 1982. Options for 5,249,407 are available for future grant. Options were exercised at prices ranging from $.17 to $26.88 in 1982, $.08 to $22.88 in 1981, and $.08 to $6.61 in 1980.

EMPLOYEE STOCK PURCHASE PLAN

As of September 30, 1982 the Company has reserved 1,288,526 shares for future issuance under its employee stock purchase plan. Under the plan, the Company may offer shares to employees by two methods. Under one method, eligible employees may elect to purchase shares of common stock at 85% of fair market value at the beginning or end of a three-month offering period. Under the second method, the Company may grant to employees the option to purchase common stock at not less than 85% of fair market value at the grant date. As of September 30, 1982 options to purchase 275,700 common shares at $17.04 per share, 39,600 at $26.90, and 370,400 at $12.75, were outstanding under the second method. Such options are exercisable through January 4, 1983; from November 1, 1982 through January 30, 1984; and from August 16, 1983 through November 15, 1984 respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. Geographic Segment Information

The following table sets forth information about the Company's operations in different geographic regions for the three years ended September 30, 1982.

(In thousands)	Geographic Area: United States	Europe	Other	Adjustments and Eliminations	Consolidated
1982					
Revenue—Customer	$215,154	$74,958	$22,031	$ —	$312,143
Revenue—Intercompany	60,126	—	—	(60,126)	—
Revenue—Total	275,280	74,958	22,031	(60,126)	312,143
Pre-Tax Income	43,949	9,267	22	(6,497)	46,741
Identifiable Assets	276,886	56,685	15,863	(12,068)	337,366
1981					
Revenue—Customer	$144,392	$47,294	$16,711	$ —	$208,397
Revenue—Intercompany	37,580	—	—	(37,580)	—
Revenue—Total	181,972	47,294	16,711	(37,580)	208,397
Pre-Tax Income	50,297	4,145	2,139	(5,483)	51,098
Identifiable Assets	213,693	34,592	12,471	(4,785)	255,971
1980					
Revenue—Customer	$78,758	$25,760	$ 4,471	$ —	$108,989
Revenue—Intercompany	17,452	1,868	56	(19,376)	—
Revenue—Total	96,210	27,628	4,527	(19,376)	108,989
Pre-Tax Income	21,469	801	140	(1,328)	21,082
Identifiable Assets	76,181	19,889	2,109	(2,478)	95,701

Intercompany transfers are made at approximately arm's length prices, which include manufacturing profits attributable to United States operations. Identifiable assets are those assets of the Company that are identified with the operations of the corresponding geographic area. United States customer revenue includes export sales of $7,687,000 in 1982; $7,397,000 in 1981; and $3,973,000 in 1980.

7. Unaudited Quarterly Financial Data

(In thousands except per share amounts)	Quarters Ended: Dec. 31	March 31	June 30	Sept. 30
Year ended September 30, 1982:				
Revenue				
As previously reported	$74,684	$85,593	$84,440	$91,182
As restated	70,985	74,101	79,823	87,234
Gross Margin				
As previously reported	48,208	54,914	55,855	59,302
As restated	45,804	47,444	52,855	56,735
Operating Income				
As previously reported	13,669	15,634	13,385	12,903
As restated	11,352	8,434	10,493	10,429
Net Income				
As previously reported	$ 8,944	$ 9,815	$ 8,956	$ 9,568
As restated	7,788	6,222	7,513	8,333
Earnings Per Share				
As previously reported	$ .23	$ .25	$ .23	$ .24
As restated	.20	.16	.19	.21
Year ended September 30, 1981:				
Revenue	$40,609	$47,417	$55,865	$64,506
Gross Margin	25,708	29,933	34,957	42,252
Operating Income	7,521	9,012	11,468	12,390
Net Income	$ 4,662	$ 6,476	$ 7,191	$ 8,220
Earnings Per Share	$ .14	$ .17	$ .19	$ .21

The Company's previously reported fiscal 1982 quarterly results have been restated primarily to reflect the deferral of certain sales transactions into subsequent fiscal quarters. In connection with the preparation of its year-end financial statements, the Company determined that these transactions were more properly recognized in the later quarters.

AUDITORS' REPORT

To Tandem Computers Incorporated:

We have examined the consolidated balance sheet of Tandem Computers Incorporated (a Delaware corporation) and subsidiaries as of September 30, 1982 and 1981, and the related consolidated statements of income, stockholders' investment, and changes in financial position for each of the three years in the period ended September 30, 1982. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Tandem Computers Incorporated and subsidiaries as of September 30, 1982 and 1981, and the results of their operations and the changes in their financial position for each of the three years in the period ended September 30, 1982, all in conformity with generally accepted accounting principles applied on a consistent basis.

Arthur Andersen & Co.

San Jose, California
December 14, 1982

TANDEM STOCK PRICE

Calendar Quarter Price	High	Low
1982 3rd Quarter	25 3/8	14 1/2
2nd Quarter	29	22
1st Quarter	28 1/2	21
1981 4th Quarter	34	27 1/4
3rd Quarter	32	24
2nd Quarter	34 5/8	24 3/4
1st Quarter	25 1/2	20 1/2
1980 4th Quarter	25 3/8	18 1/8
3rd Quarter	18 5/8	9 7/8
2nd Quarter	9 7/8	6 1/2
1st Quarter	9	6 1/8

In the second calendar quarter of 1982, Tandem Computers Incorporated common stock began trading via the NASDAQ National Market System under the trading symbol TNDM. For the second and third quarters of 1982, the quotations represent the high and low sales prices. Quotations that pertain to earlier periods represent prices between dealers without adjustment for mark-up, markdown, or commissions and may not represent actual transactions. All prices have been adjusted for stock splits. No dividends have been declared on the common stock.

Board of Directors

Thomas J. Perkins (1),
Chairman of the Board; Partner,
Kleiner, Perkins, Caufield & Byers

Morton Collins (2),
Partner, DSV Associates

Thomas J. Davis, Jr. (1) (2),
Partner, Mayfield II

Franklin P. Johnson, Jr.,
Chairman, Asset Management
Capital Company

Eugene Kleiner (2),
Partner, Kleiner, Perkins, Caufield
& Byers

Robert C. Marshall,
Senior Vice President and Chief
Operating Officer, Tandem
Computers Incorporated

Alvin C. Rice,
President and Chairman,
Imperial Bank

Robert G. Stone, Jr.,
Chairman of the Board, West India
Shipping Company

James G. Treybig (1),
President and Chief Executive
Officer, Tandem Computers
Incorporated

(1) Member of Executive
Committee
(2) Member of Audit Committee

Officers

James G. Treybig,
President and Chief Executive
Officer

Robert C. Marshall,
Senior Vice President and Chief
Operating Officer

Michael D. Green,
Senior Vice President

Jan E. Jensen,
Vice President–Human Resources

Laurence A. Laurich,
Vice President–Engineering

David R. Mackie,
Vice President

Dennis McEvoy,
Vice President–Software
Development

Henry V. Morgan,
Vice President, Controller and
Secretary

Charles W. Ryle,
Vice President–U.S. Marketing

Jeanne D. Wohlers,
Vice President, Treasurer and
Assistant Secretary

Vice Presidents and Operating Managers

Michael D. Bateman,
Vice President, Central Division

Thomas Bechler,
Director, Eastern Division

Jack W. Chapman,
Director, Central European
Division

Victor DeSouza,
Vice President

George Eckert,
Vice President, Reston Operations

Lary Evans,
Vice President, Product
Manufacturing

Gerald D. Held,
Director, Software Research

James A. Katzman,
Vice President

D. Chris Larson,
Director, Austin Division

Michael C. Moore,
Director, Western Division

Gerald L. Peterson,
Vice President, International
Marketing

Jerald D. Reaugh,
Vice President, Systems
Manufacturing

Charles J. Yazel,
Director, Pacific/Latin America Division

Auditors

Arthur Andersen & Co.,
San Jose, California

Registrar and Transfer Agent

Bank of America N.T. & S.A.,
San Francisco, California

Form 10-K

A copy of the company's Form
10-K, as filed with the Securities
and Exchange Commission, is
available on written request.
Please direct request to:

Treasurer's Office
Tandem Computers Incorporated
19333 Vallco Parkway
Cupertino, California 95014-2599

Annual Meeting

The annual meeting of
stockholders will be held at 10:00
a.m. on Friday, February 25, 1983, at
the corporation's headquarters.

Tandem

Corporate Headquarters
19333 Vallco Parkway
Cupertino, CA 95014-2599
(408) 725-6000

Domestic Sales and Service Offices

ARKANSAS, Little Rock

ARIZONA, Phoenix

CALIFORNIA, Los Angeles, San
Diego, San Francisco, Sunnyvale,
Santa Clara, Long Beach,
Universal City

COLORADO, Denver

CONNECTICUT, Hartford, Stamford

FLORIDA, Tampa, Orlando,
Jacksonville, Miami

GEORGIA, Atlanta

HAWAII, Honolulu

ILLINOIS, Chicago, Schaumberg,
Itasca

INDIANA, Indianapolis, Ft. Wayne

IOWA, Des Moines

KANSAS, Kansas City

LOUISIANA, New Orleans

MARYLAND, Baltimore

MASSACHUSETTS, Boston

MICHIGAN, Detroit, Ann Arbor,
Grand Rapids

MINNESOTA, Minneapolis

MISSOURI, St. Louis

NEBRASKA, Omaha

NEVADA, Las Vegas

NEW JERSEY, Hasbrouck Heights,
Atlantic City

NEW MEXICO, Albuquerque

NEW YORK, New York City,
Rochester, Jericho

NORTH CAROLINA, Greensboro,
Charlotte

OHIO, Cincinnati, Cleveland,
Columbus

OKLAHOMA, Tulsa

OREGON, Portland

PENNSYLVANIA, Philadelphia,
Pittsburgh

TENNESSEE, Memphis

TEXAS, Dallas, Fort Worth, Houston,
Austin

UTAH, Salt Lake City

VIRGINIA, Falls Church, Richmond,
Reston

WASHINGTON, Seattle

WEST VIRGINIA, Charleston

WISCONSIN, Milwaukee

International Subsidiaries

AUSTRALIA
Tandem Computers Limited
Sydney, Melbourne

BELGIUM
Tandem Computers SA/NV
Brussels

CANADA
Tandem Computers Canada
Limited
Calgary, Edmonton, Montreal,
Ottawa, Toronto, Vancouver,
Victoria, Windsor

DENMARK
Tandem Computers A/S
Taastrup

ENGLAND
Tandem Computers Limited
Birmingham, High Wycombe,
London, Northolt

FRANCE
Tandem Computers S.A.
Paris

GERMANY
Tandem Computers GmbH
Dortmund, Dusseldorf, Frankfurt,
Hamburg, Mannheim, Munich,
Stuttgart

HONG KONG
Tandem Computers (Hong Kong)
Limited
Kowloon

ITALY
Tandem Computers Italia S.p.A.
Milan

JAPAN
Tandem Computers Japan Limited
Tokyo

THE NETHERLANDS
Tandem Computers BV
The Hague

NORWAY
Tandem Computers (Norway) AIS
Oslo

SINGAPORE
Tandem Computers International
Incorporated
Singapore

SWEDEN
Tandem Computers (Sweden) AB
Stockholm, Malmo

SWITZERLAND
Tandem Computers AG
Zurich

International Distributors

Argentina

Finland

Greece and The Middle East

Israel

Korea

Mexico

Philippines

Taiwan

Venezuela

Trademark

TANDEM

December 28, 1983

Dear Stockholder:

You are cordially invited to attend the Annual Meeting of Stockholders which will be held on Friday, February 10, 1984, at 10:00 A.M. at the offices of the Company at 19333 Vallco Parkway, Cupertino, California.

The formal notice of the Annual Meeting and the Proxy Statement have been made a part of this invitation.

After reading the Proxy Statement, please mark, sign and return, at an early date, the enclosed proxy in the prepaid envelope addressed to the Bank of America, our agent, to assure that your shares will be represented. YOUR SHARES CANNOT BE VOTED UNLESS YOU SIGN AND RETURN THE ENCLOSED PROXY OR ATTEND THE ANNUAL MEETING IN PERSON.

A copy of the Company's Annual Report to Stockholders is also enclosed.

The Board of Directors and Management look forward to seeing you at the meeting.

Sincerely yours,

Thomas J. Perkins
Chairman of the Board

James G. Treybig
President and Chief Executive Officer

TANDEM COMPUTERS INCORPORATED

19333 Vallco Parkway • Cupertino, CA 95014 • (408) 725-6000

TANDEM COMPUTERS INCORPORATED

Notice of Annual Meeting of Stockholders
To Be Held February 10, 1984

The Annual Meeting of Stockholders of Tandem Computers Incorporated (the "Company") will be held at the offices of the Company at 19333 Vallco Parkway, Cupertino, California, on February 10, 1984, at 10:00 A.M. for the following purposes:

1. To elect three Class I directors to hold office until 1987.

2. To consider and vote upon a proposal to amend the Company's Certificate of Incorporation to provide for the creation of one or more series of Junior Common Stock.

3. To consider and vote upon a proposal to adopt the Tandem Computers Incorporated 1984 Junior Common Stock Plan.

4. To ratify the selection of Arthur Andersen & Co. as the Company's independent auditors.

5. To transact such other business as may properly come before the meeting and any adjournment thereof.

The Board of Directors has fixed the close of business on December 16, 1983 as the record date for determining the stockholders entitled to notice of and to vote at the Annual Meeting and any adjournment thereof. A complete list of stockholders entitled to vote will be available at the Company's headquarters, 19333 Vallco Parkway, Cupertino, California, for ten days prior to the meeting.

IF YOU DO NOT EXPECT TO ATTEND IN PERSON, PLEASE PROMPTLY SIGN AND RETURN THE ENCLOSED PROXY.

HENRY V. MORGAN
Secretary

December 28, 1983

TANDEM COMPUTERS INCORPORATED

PROXY STATEMENT

This Proxy Statement is furnished in connection with the solicitation by the Board of Directors of Tandem Computers Incorporated, a Delaware corporation (the "Company"), with principal executive offices at 19333 Vallco Parkway, Cupertino, California 95014, of proxies in the accompanying form to be used at the Annual Meeting of Stockholders to be held on February 10, 1984, and any adjournment thereof. The shares represented by the proxies received pursuant to this solicitation and not revoked will be voted at the Annual Meeting. A proxy may be revoked at any time before it is exercised. On the matters coming before the meeting as to which a choice has been specified by a stockholder by means of the ballot on the proxy, the shares will be voted accordingly. If no choice is so specified, the shares will be voted FOR the election of the three nominees for director listed in this Proxy Statement and FOR approval of proposals 2, 3 and 4 described in the Notice of Meeting and in this Proxy Statement.

Stockholders of record at the close of business on December 16, 1983 are entitled to notice of and to vote at the Annual Meeting. On December 1, 1983, the Company had 39,770,197 shares of Common Stock outstanding. Each holder of Common Stock is entitled to one vote for each share held on the record date, except that, in voting for directors, each stockholder is entitled to one vote for each share held as of the record date and to cumulate votes for the election of directors whose names have been placed in nomination; that is, a stockholder may cast as many votes as there are directors to be elected multiplied by the number of shares which the stockholder holds. All such votes may be cast for one candidate or distributed among the nominees for director as the stockholder sees fit. The persons authorized to vote shares represented by executed proxies in the enclosed form (if authority to vote for the election of directors is not withheld) will have full discretion and authority to vote cumulatively and to allocate votes among any or all of the nominees for election to the Board of Directors as they may determine or, if authority to vote for a specified candidate or candidates has been withheld, among those nominees for whom authority to vote has not been withheld.

The expense of printing and mailing proxy materials will be borne by the Company. In addition to the solicitation of proxies by mail, solicitation may be made by certain directors, officers and other employees of the Company by personal interview, telephone or telegraph; no additional compensation will be paid for such solicitation.

This Proxy Statement and a form of proxy are being mailed to stockholders on or about December 28, 1983.

IMPORTANT

Please date and sign the enclosed proxy and return it at your earliest convenience in the enclosed postage-prepaid return envelope so that, if you are unable to attend the Annual Meeting, your shares may be voted.

ELECTION OF DIRECTORS

The Company has three classes of directors serving staggered three-year terms, each consisting of three directors. Three Class I directors are to be elected at the Annual Meeting for three-year terms expiring on the date of the Annual Meeting in 1987 or until each such director's successor shall have been duly elected or appointed.

Unless authority to vote for directors is withheld, it is intended that the shares represented by the enclosed proxy will be voted for the election of Messrs. Morton Collins, Andrew Knight and Robert C. Marshall as Class I directors. Mr. Collins and Mr. Marshall are currently members of the Board of Directors of the Company. Mr. Eugene Kleiner, currently a Class I director, has decided not to stand for reelection; upon the recommendation of the Nominating Committee, the Board of Directors has nominated Mr. Knight for election as a Class I director. In the event any of such nominees becomes unable or unwilling to serve, the shares represented by the enclosed proxy will be voted for the election of the balance of those named and such other person as the Board of Directors may select. The Board of Directors has no reason to believe that any such nominee will be unable to serve.

Set forth below are the names and ages of the nominees and directors, the class to which each has been elected or nominated for election, their principal occupations at present and for the past five years, certain directorships held by each and the year in which each became a director of the Company. Information with respect to the Company includes the Company's predecessor California corporation.

Name and Principal Occupation at Present and for the Past Five Years; Directorships	Director Since	Age
Class I		
Morton Collins(1)	1975	47
General Partner since 1974 and 1981 of DSV Associates and DSV Partners III, respectively, Princeton, New Jersey private investment partnerships.		
Andrew Knight	—	44
Editor, *The Economist,* Economist Newspaper Ltd., since 1974; Member of Council of Chatham House (The Royal Institute of International Affairs); Governor of Imperial College of Science and Technology, University of London; Member of the Advisory Board of the Center for Economic Policy Research, Stanford University; Trustee of the Victoria and Albert Museum, London.		
Robert C. Marshall	1980	52
Senior Vice President and Chief Operating Officer of the Company since July 1980; Vice President and Chief Operating Officer since 1979; Vice President since 1975.		
Class II		
Franklin P. Johnson, Jr.(2)	1975	55
Owner since 1967 of Asset Management Company, a Palo Alto, California private investment proprietorship; President since 1974 of Asset Management Capital Company, a Palo Alto, California small business investment company; General Partner since 1982 of Asset Management Partners, a Palo Alto, California private investment partnership; Director of Amgen, California Microwave, Inc., Coherent, Inc., SBE, Inc. and Teradyne, Inc.		

Thomas J. Perkins(3) 1974 51

Chairman of the Board of the Company since 1974; General Partner since 1972, 1978, 1980 and 1982 of Kleiner & Perkins Venture Capital, Kleiner, Perkins, Caufield & Byers Venture Capital, Kleiner, Perkins, Caufield & Byers II and Kleiner, Perkins, Caufield & Byers III, respectively, San Francisco, California private investment partnerships; Director of Collagen Corporation, Corning Glass Works, Genentech, Inc., Hybritech Incorporated, LSI Logic Corporation and Spectra-Physics, Inc.

John B. M. Place(1)(4) 1983 58

Chairman of the Board and Chief Executive Officer of Crocker National Corporation and of Crocker National Bank since 1982; Director of Crocker National Corporation and of Crocker National Bank since 1978; President of Crocker National Corporation and of Crocker National Bank from 1978 to 1982; Director of Atlantic Richfield Co. and of Pacific Gas & Electric Co.

Class III

Thomas J. Davis, Jr.(1)(3) 1976 71

General Partner since 1973, 1979 and 1981 of Mayfield II, Mayfield III and Mayfield IV, respectively, Menlo Park, California private investment partnerships; Director of Equatorial Communications Co.

Robert G. Stone, Jr.(2) 1978 60

Chairman of the Board of Kirby Exploration Company and of its predecessor, General Energy Corporation, since 1971; Chairman of the Board of West India Shipping Company, Inc. from 1974 to 1983; Director of The Chubb Corporation, Combustion Engineering, Inc., Core Industries, Inc., Corning Glass Works, Great Northern Nekoosa Corporation, Hamilton Brothers Petroleum Corp., The Japan Fund, Inc., R. H. Macy & Co., Inc. and Western Pacific Industries, Inc.

James G. Treybig(3) 1974 43

President and Chief Executive Officer of the Company since 1974.

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(1) Member of Audit Committee.
(2) Member of Nominating Committee.
(3) Member of Compensation Committee.
(4) Mr. Place was elected by the Board of Directors, pursuant to authority vested in the Board by the Company's By-Laws, to fill the vacancy created by the resignation of Mr. Alvin C. Rice in January 1983.

STOCK OWNERSHIP OF DIRECTORS AND OFFICERS

The following table sets forth information as of December 1, 1983, as to shares of Common Stock beneficially owned by the directors and nominees named under "Election of Directors" and the directors and officers of the Company as a group. Except as otherwise indicated, each person has sole investment and voting power with respect to the shares shown. Ownership information is based upon information furnished by the respective individuals.

	Beneficial Ownership of Common Stock	
	Number of Shares(1)	Percent of Class
James G. Treybig	537,812(2)	1.3%
Thomas J. Perkins	499,468	1.2
Eugene Kleiner	457,293	1.1
Franklin P. Johnson, Jr.	259,998(3)	0.6
Robert C. Marshall	180,900(4)	0.4
Robert G. Stone, Jr.	110,050(5)	0.3
Thomas J. Davis, Jr.	82,644	0.2
Morton Collins	31,304(6)	0.1
John B.M. Place	14,000	(7)
All officers and directors as a group (19 persons including the nine named above)	2,626,622	6.5

(1) Includes shares which may be acquired within 60 days pursuant to the exercise of options as follows: Mr. Place, 12,000 shares; Mr. Treybig, 82,088 shares; Mr. Marshall, 88,000 shares; and all officers and directors as a group, 458,670 shares.

(2) Includes 1,800 shares of Common Stock held by a trust, of which Mr. Treybig is the trustee.

(3) All such shares are held by Asset Management Capital Company, a corporation all of the stock of which is owned by Mr. Johnson and members of his family.

(4) Includes 655 shares held in a trust for the benefit of a minor child of Mr. Marshall, of which the trustee is Mr. Marshall's wife, and as to which Mr. Marshall disclaims any beneficial interest.

(5) Includes 60,568 shares of Common Stock held by trusts, of which Mr. Stone is a trustee, and 49,482 shares owned by Mr. Stone's wife and children, as to which shares Mr. Stone disclaims any beneficial interest.

(6) Includes 1,400 shares of Common Stock held in a trust for the benefit of Mr. Collins' children, of which Mr. Collins is a trustee, and as to which Mr. Collins disclaims any beneficial interest.

(7) Less than one-tenth of one percent of class.

COMPENSATION OF DIRECTORS AND EXECUTIVE OFFICERS

Information is set forth on the following pages as to the compensation paid during the 1983 fiscal year by the Company and its subsidiaries to each of the five most highly compensated executive officers of the Company individually, to all executive officers as a group and to directors. Information is given only for the period each served as an executive officer or director of the Company. Information for the past five fiscal years as to stock options granted and amounts allocated to such persons, to all officers and directors as a group and to employees under the Company's employee benefit plans is set forth under "Stock Options" on page 6 or the description of each plan under "Description of Other Plans" commencing on page 11 of this Proxy Statement.

Cash Compensation of Executive Officers For Fiscal 1983

Name of Individual or Number in Group and Capacities in Which Served	Amount
James G. Treybig, President, Chief Executive Officer and Director	$ 178,269
Robert C. Marshall, Senior Vice President, Chief Operating Officer and Director	$ 163,413
Dennis L. McEvoy, Vice President Software Development	$ 128,750
David R. Mackie, Vice President U.S. Marketing	$ 123,333
Lawrence A. Laurich, Vice President Hardware Development	$ 113,943
All executive officers as a group (12 persons including the five named above)	$1,292,367

Directors who are not officers of the Company are paid an annual retainer of $8,640, plus expenses, payable quarterly. Directors who are members of one or more of the Executive, Compensation, Nominating or Audit Committees are paid an additional annual retainer of $3,600. The Chairman of the Board is paid an additional annual retainer of $2,160. If elected by the stockholders, Mr. Knight will serve without annual retainer.

STOCK OPTIONS

With respect to options to purchase shares of the Company's Common Stock granted to certain executive officers, all executive officers as a group and all directors as a group during the period October 1, 1978 to December 1, 1983, the following table sets forth (i) the aggregate amount of Common Stock subject to options granted during the specified period, (ii) the weighted average per share option exercise price thereof, (iii) the net value of shares (market value less any exercise price) realized during the specified period upon the exercise of such options during the specified period and (iv) the numbers of shares of Common Stock sold by the named persons and by all executive officers as a group and by all directors as a group during the specified period. Information is given only for the period each served as an executive officer or director of the Company.

Common Stock(1)	James G. Treybig	Robert C. Marshall	Dennis L. McEvoy(2)	David R. Mackie(2)	Lawrence A. Laurich(2)	All Executive Officers as a Group(2)	All Directors as a Group
Granted-October 1, 1978 to December 1, 1983:							
Number of shares	102,600	105,600	10,200	53,600	104,200	528,700	24,000
Weighted average per share exercise price	$13.00	$12.38	$26.63	$15.30	$8.76	$13.76	$16.88
Exercised-October 1, 1978 to December 1, 1983:							
Net value realized in shares (market value less exercise price)	$405,274	$371,746	$165,187	$306,504	$908,240	$3,105,150	$266,508
Sales-October 1, 1978 to December 1, 1983:							
Number of shares(3)	220,750	91,500	20,000	63,800	28,000	533,180	207,416

(1) Adjusted for a two-for-one stock split effective June 30, 1980, and a three-for-one stock split effective June 30, 1981.

(2) Includes options granted under the Stock Option Grant Program of the Company's Employee Stock Purchase Plan all of which have an exercise price of 85% of the market value of the shares on the date of grant. The numbers of options granted under such Plan to Messrs. Mackie, Laurich, McEvoy and all executive officers as a group are 200, 600, 600 and 3,200, respectively, and the weighted average per share exercise price of such options and the market price of the Common Stock on the date of grant are $20.90 and $24.59, respectively.

(3) Shares sold were not necessarily acquired by the exercise of options.

During the period from October 1, 1978 to December 1, 1983, employees were granted options under the Company's stock option plans and the Stock Option Grant Program of the Employee Stock Purchase Plan to purchase a total of 9,380,087 shares at a weighted average exercise price of $14.38 per share, adjusted to reflect a two-for-one stock split effective June 30, 1980, and a three-for-one stock split effective June 30, 1981. Of these, 6,722,827 were not "qualified" stock options, incentive stock options or options granted pursuant to an "employee stock purchase plan," as the quoted terms are defined in sections 422 through 423 of the Internal Revenue Code of 1954, as amended. The weighted average per share exercise

price for such options is $12.88. Of the total number of options granted, 863,300 were granted under the Stock Option Grant Program of the Company's Employee Stock Purchase Plan at 85% of the market price of the Common Stock on the date of grant. The weighted average per share market price of the Common Stock on the dates of grant is $18.47.

As of December 1, 1983, there were outstanding options under the Company's 1981 Stock Option Plan, 1979 Stock Option Plan, Non-Qualified Stock Option Plan and Qualified Stock Option Plan to purchase 5,153,805 shares held by 3,578 participants and there were approximately 4,580 employees eligible to participate. The expiration dates of all such options range from December 14, 1983 to October 20, 1990, and the weighted average purchase price per share is $22.20.

APPROVAL OF PROPOSED AMENDMENT TO ARTICLE FOUR OF THE CERTIFICATE OF INCORPORATION

Proposed Amendment

The Company's presently authorized capital stock consists of 2,400,000 shares of Preferred Stock and 60,000,000 shares of Common Stock. On November 1, 1983, the Board of Directors authorized an amendment to the Certificate of Incorporation of the Company to reclassify the common equity of the Company as 60,000,000 Common Shares, consisting of 56,000,000 authorized shares of Common Stock and 4,000,000 authorized shares of Junior Common Stock. This reclassification will not effect any further change in the presently authorized or outstanding shares of Common Stock. The proposed Amended Certificate of Incorporation will provide that the Junior Common Stock may be issued in one or more series by resolution of the Board of Directors. The proposed amendment would give the Board of Directors the authority to determine the designation and number of shares to constitute each series, and the powers, preferences and relative, participating, optional or other special rights and the qualifications, limitations or restrictions (including without limitation the voting rights, if any, the dividend rate, conversion rights, redemption price or liquidation preference) of any series of Junior Common Stock without further stockholder approval, except as otherwise required by law. *It is expected that the Junior Common Stock will be subordinated to the Common Stock with respect to dividends, liquidation preferences and voting rights, and that it will be convertible into Common Stock upon the occurrence of certain events as may be determined by the Board of Directors from time to time.* Accordingly, it is proposed that Article Four of the Certificate of Incorporation be amended in its entirety to read as set forth in Exhibit 1 to this Proxy Statement.

Purpose and Effect of Amendment

The purpose of the proposed amendment to the Certificate of Incorporation is to give the Board of Directors the authority and flexibility to provide for the issuance of Junior Common Stock as an equity incentive for attracting and retaining directors, officers and key employees, without delay and without the need for further action by the stockholders. The Board of Directors has adopted a plan, subject to stockholder approval, under which key employees and certain directors of the Company may be given the right to purchase Junior Common Stock, subject, generally, to the right of the Company to repurchase such shares at cost in the event a purchaser's employment with the Company is terminated during a prescribed period. The Junior Common Stock will be sold at a price based upon its fair market value as determined by a committee of directors administering such plan which may, from time to time, seek an independent appraisal. Because of the subordination of such shares to the Common Stock as to certain matters and the

uncertainty of the conversion of such shares into Common Stock, the price for shares of Junior Common Stock is expected to be substantially below the market price for the Common Stock. In the event shares of Junior Common Stock are converted into shares of Common Stock, the other stockholders of the Company may experience some dilution. The Company believes that, in view of the ratio of authorized Junior Common Stock to Common Stock, such dilution will be minimal and will be compensated for by the retention of key employees, including officers and directors, who respond to the incentive features of the Junior Common Stock.

The proposed amendment will give the Board of Directors the authority to issue, in series, shares of Junior Common Stock and to determine the relative rights and restrictions of each such series.

Required Vote

The adoption of the amendment to the Certificate of Incorporation requires the affirmative vote of not less than a majority of the issued and outstanding shares of Common Stock entitled to vote.

THE BOARD OF DIRECTORS RECOMMENDS APPROVAL OF THE AMENDMENT TO ARTICLE FOUR OF THE CERTIFICATE OF INCORPORATION.

APPROVAL OF THE TANDEM COMPUTERS INCORPORATED 1984 JUNIOR COMMON STOCK PLAN

The Tandem Computers Incorporated 1984 Junior Common Stock Plan (the "Junior Stock Plan") was adopted by the Board of Directors on November 1, 1983, and will become effective on February 10, 1984, if the amendment to the Company's Certificate of Incorporation authorizing the Junior Common Stock, described in this Proxy Statement, and the Junior Stock Plan are approved by the stockholders. If such amendment or the Junior Stock Plan are not approved, the Junior Stock Plan will not be implemented. A total of 4,000,000 shares of the Company's Junior Common Stock will be reserved for issuance under the Junior Stock Plan, subject to such stockholder approval. Shares repurchased by the Company will again be available for the purposes of the Junior Stock Plan.

The purpose of the Junior Stock Plan is to assist the Company in the recruitment, retention and motivation of key employees who have outstanding qualifications and who are in a position to make material contributions to the Company's progress. A limited number of directors is also eligible to participate in the Plan. The Junior Stock Plan is designed to offer such individuals a significant incentive by enabling them to acquire shares of the Company's Junior Common Stock, thereby increasing their interest in the Company's growth and success.

The full text of the Junior Stock Plan is set forth as Exhibit 2 to this Proxy Statement. The following summary of the main provisions of the Junior Stock Plan is qualified by reference to the full text thereof.

Administration of the Plan

The Plan will be administered by a committee (the "Committee") consisting of not less than three disinterested members of the Board of Directors. The Committee will have full authority to construe and implement the Junior Stock Plan, to select the individuals who will be eligible to purchase shares of Junior Common Stock, to determine the number of shares that such individuals may acquire as well as the purchase price thereof and to prescribe all other terms and conditions of each purchase under the Junior Stock Plan.

Eligibility

The Committee may grant rights to purchase shares of Junior Common Stock to directors (other than Messrs. Collins, Davis, Johnson and Perkins) and key employees of the Company and its more than 50% owned subsidiaries. Since the grant of rights to purchase Junior Common Stock under the Junior Stock Plan is discretionary, it is not possible to estimate the number of shares of Junior Common Stock which would have been distributable under the Junior Stock Plan had it been in effect during the 1983 fiscal year.

Purchase of Stock

Rights to purchase shares under the Junior Stock Plan will not be transferable and will lapse if they are not exercised within 30 days after the date of grant, or within such other period as the Committee may determine. The purchase price will be equal to the fair market value of Junior Common Stock on the date of grant, as determined by the Committee, which may from time to time seek an independent appraisal. Due to the characteristics of Junior Common Stock (including its subordination to Common Stock with respect to voting rights, dividend rights and liquidation preferences as well as lack of marketability and the contingent nature of its conversion feature), it is expected that the fair market value of the Junior Common Stock offered for sale will be substantially lower than the fair market value of Common Stock on the same date. The fair market value that shares of Junior Common Stock issued under the Junior Stock Plan will have cannot be determined at the date hereof. In the event of a reorganization, recapitalization, reclassification, split-up, consolidation or similar adjustment of Junior Common Stock, the Committee will make appropriate adjustments in the number of shares of Junior Common Stock available under the Junior Stock Plan.

Payment for shares of Junior Common Stock will be made in cash when the shares are purchased or, if the Committee approves, in the form of an interest-bearing, full-recourse promissory note. Although permitted, it is not presently anticipated that the Committee will accept payment in the form of shares of the Company's Common Stock. Any shares of Common Stock which are accepted as payment will be valued at their fair market value on the date the Junior Common Stock is purchased.

Transfer Restrictions

It is anticipated that all shares issued under the Junior Stock Plan (both before and after any conversion) will ordinarily be subject to the Company's right to repurchase the shares, at the price for which they were originally acquired, in the event that the holder's relationship with the Company is severed before the shares become vested. Vesting will occur under such terms as the Committee may specify at the time of the sale. Prior to any conversion into Common Stock, the shares may be subject to a right of first refusal by the Company and such other transfer restrictions as the Committee may determine. The shares will not be transferable for the duration of the Company's right of repurchase, subject to limited exceptions.

Amendment and Termination of the Plan

The Board of Directors may amend, suspend or terminate the Junior Stock Plan at any time and for any reason. The approval of the Company's stockholders is required only for amendments which increase

the number of shares available for issuance under the Junior Stock Plan, which materially increase the benefits available under the Plan, or which materially change the classes of persons eligible to participate. The Junior Stock Plan will automatically terminate on February 9, 1994, unless it has previously been terminated by the Board of Directors.

Federal Tax Effects

No taxable income results from the grant of a right to purchase Junior Common Stock, nor is the Company entitled to a deduction with respect to such grant.

All purchasers who are subject to United States income tax liability, as a condition of any grant under the Junior Stock Plan, will be required to file a timely election under section 83(b) of the Internal Revenue Code of 1954, as amended, and under any corresponding provision of applicable state and local tax laws. The consequence of such an election is that the amount of any taxable income is measured at the time of the purchase and not at the time of vesting.

When an individual exercises his right to purchase shares and files the election under section 83(b) with the Internal Revenue Service within 30 days after the purchase, the individual has no taxable income in the year of the purchase (provided that the purchase price is equal to the fair market value of the shares of Junior Common Stock on the date of acquisition, determined without regard to any right of repurchase). Likewise, the individual has no taxable income when his or her shares vest; i.e., the Company's right of repurchase (if any) lapses as to such shares. The Company is not entitled to a deduction in the year of the purchase or in the year of vesting.

Upon the disposition of stock acquired under the Junior Stock Plan, any gain (or loss) will be taxed as short- or long-term capital gain (or loss), depending upon how long the individual has held such stock from the date of purchase. The amount of the capital gain (or loss) is the difference between (i) the sale proceeds and (ii) the fair market value of the shares at the time of purchase. The deductible portion of any net long-term capital gain may be subject to the alternative minimum tax.

A conversion of Junior Common Stock into Common Stock, if and when it occurs, should be treated as a tax-free exchange and should not affect the tax consequences outlined above. For purposes of the long-term capital gain holding period, it should be permissible to aggregate the period for which Junior Common Stock had been held with the period for which the Common Stock acquired upon conversion has been held.

Proposed Change in Accounting Treatment

At the request of the Securities and Exchange Commission, the Financial Accounting Standards Board has proposed accounting guidelines requiring companies to account for issues of junior common stock as compensation to recipients. Presently, such issues, if sold at fair market value, are not treated as compensation for accounting purposes. If the Financial Accounting Standards Board adopts such accounting standards, the Company will reevaluate whether or not to proceed with implementation of the Junior Stock Plan.

Required Vote

The adoption of the Junior Stock Plan requires the affirmative vote of not less than a majority of the shares of Common Stock present and voting at the meeting in person or by proxy.

THE BOARD OF DIRECTORS RECOMMENDS APPROVAL OF THE TANDEM COMPUTERS INCORPORATED 1984 JUNIOR COMMON STOCK PLAN.

DESCRIPTION OF OTHER PLANS

Tandem Computers Incorporated Employee Stock Purchase Plan

Since 1978, the Company has had in effect the Tandem Computers Incorporated Employee Stock Purchase Plan (the "Stock Purchase Plan"). The Stock Purchase Plan has two segments, a Payroll Withholding Accumulation Program and a Stock Option Grant Program, and is administered by a committee of not less than three directors appointed by the Board of Directors (the "Option Committee").

All employees of the Company and its 50% or more owned subsidiaries, including officers, who customarily work more than five months in a calendar year are eligible to purchase shares under the Stock Purchase Plan. Directors of the Company may not participate. As of December 1, 1983, approximately 4,580 employees were eligible to participate in the Stock Purchase Plan, of whom 2,323 were participating, and 2,494,158 shares remained available for purchase.

Under the Payroll Withholding Accumulation Program, an eligible employee may authorize the Company to withhold from 1% to 10% of his compensation to be applied to the purchase of the maximum number of whole shares (up to 1,500) of the Company's Common Stock which can be purchased with the amount withheld during a participation period (calendar quarter). The per share purchase price for each participation period is the lesser of (i) 85% of the market value of a share of Common Stock on the last trading day before the participation period commences, or (ii) 85% of the market value of a share of Common Stock on the last trading day during the participation period. During the period October 1, 1978 through December 1, 1983, 1,170,607 shares of Common Stock were purchased under the Plan by all employees of the Company as a group.

Under the Stock Option Grant Program, options for an identical number of shares are granted periodically at the discretion of the Option Committee to every person who is eligible to participate in the program on the date of grant. The exercise price, determined by the Option Committee, can not be less than 85% of the market value of the Common Stock on the last trading day before the date of grant. Options expire no later than 27 months after the date of grant. Shares purchased upon the exercise of an option must be paid for in full at the time of exercise or, with the Option Committee's approval given at the time the option is granted, may be purchased by delivery of a full-recourse, interest-bearing promissory note.

Four grants have been made since the inception of the Stock Option Grant Program of the Stock Purchase Plan in 1980. A grant of 100 shares was made to each employee in 1980, 1981, 1982 and 1983 (without giving effect to a stock split in 1981). As of December 1, 1983, there were outstanding options under the Stock Option Grant Program to purchase 629,600 shares held by 4,466 employees at a weighted average exercise price of $24.74 per share. The expiration dates of such options range from January 29, 1984 to January 20, 1986.

Stock Option Plans

Tandem Computers Incorporated 1981 Stock Option Plan. The Tandem Computers Incorporated 1981 Stock Option Plan (the "1981 Plan") was approved by the stockholders at the Company's 1982 Annual Meeting of Stockholders. The 1981 Plan is administered by the Option Committee.

All employees of the Company and its 50% or more owned subsidiaries are eligible to receive options. Options are granted from time to time by the Option Committee in its discretion. The Option Committee determines employees who will be granted options and the number of shares to be optioned to each. Options granted must have an option price of not less than 100% of the market value of the Company's Common Stock on the date of grant. Options may be made exercisable at such times as determined by the Option Committee. Shares purchased upon exercise of an option must be paid for in full at the time of exercise or, with the Company's consent, may be purchased by delivery of a full-recourse, interest-bearing promissory note. Options may not be exercised after seven years from date of grant and are not transferable except by will or intestate succession. In the event of a reorganization, stock split, combination of shares, stock dividend or other recapitalization, the Board of Directors may make appropriate adjustments in the number of shares reserved for issuance and in the number of shares and the option price per share specified in any agreement with respect to any unpurchased shares. The Option Committee may determine that an option will provide that the shares to be issued upon exercise of the option shall be subject to certain rights of repurchase at the Company's option.

The Option Committee may designate certain options as Incentive Stock Options under section 422A of the Internal Revenue Code of 1954, as amended. An Incentive Stock Option may not be exercised by an optionee while there is outstanding any previously granted Incentive Stock Option. The optionee recognizes no income upon the exercise of an Incentive Stock Option. Upon sale of the shares, the difference between the exercise price and the fair market value on the date of exercise is considered long-term capital gain, provided certain conditions (including holding period requirements) are satisfied.

Tandem Computers Incorporated 1979 Stock Option Plan. The Tandem Computers Incorporated 1979 Stock Option Plan (the "1979 Plan") was approved by the stockholders at the Company's 1980 Annual Meeting of Stockholders. The 1979 Plan is administered by the Option Committee. The provisions of the 1979 Plan and the terms of the options granted under the 1979 Plan are substantially similar to those of the 1981 Plan, except as follows. Only employees of the Company and employees and directors of its 80% or more owned subsidiaries are eligible to receive options. Options do not have any special tax status, except that certain options granted prior to January 1, 1982, may have been designated as Incentive Stock Options.

Tandem Computers Incorporated Non-Qualified Stock Option Plan. The Tandem Computers Incorporated Non-Qualified Stock Option Plan was approved by the stockholders at the Company's 1978 Annual Meeting of stockholders and, as amended, at the 1979 Annual Meeting of stockholders. The terms of the options granted pursuant thereto are substantially similar to those of the 1981 Plan, except that only employees of the Company and its wholly owned subsidiaries are eligible to receive options.

Tandem Computers Incorporated Qualified Stock Option Plan. The Tandem Computers Incorporated Qualified Stock Option Plan was approved by the stockholders in 1976 and is administered by the Option Committee. The provisions of the Qualified Stock Option Plan and the terms of the options granted pursuant thereto are substantially similar to those of the 1981 Plan described above, except as follows. Only key employees of the Company and its subsidiaries may be granted options. Options may not be exercised after five years from the date of grant. All shares issued pursuant to the exercise of options are

subject to certain rights of repurchase by the Company. Under certain circumstances, options may not be exercised while the optionee holds another option previously granted at a higher option price. The Qualified Stock Option Plan expires on November 12, 1985; however, under certain amendments to the Internal Revenue Code, no option granted under the Qualified Stock Option Plan which is exercised after May 20, 1981, will be afforded the special tax treatment available to "qualified" stock options under the Internal Revenue Code.

Individual Stock Option Agreements. In addition to the 1981 Plan, the 1979 Plan and the Qualified and Non-Qualified Stock Option Plans, the Company has entered into two separate Non-Qualified Stock Option Plans and Agreements with Mr. John B.M. Place who is a director of the Company. Under these Plans, Mr. Place was granted options to purchase 2,000 and 10,000 shares of the Company's Common Stock, respectively. The exercise prices of the options per share are $26.75 and $29.125, respectively, which equal 100% of the market value of the Company's Common Stock on the dates of grant. The provisions of these Plans are substantially similar to those described in the description of the Non-Qualified Stock Option Plan except that no further grants are permitted under either of the two Plans.

Incentive Cash Bonus Plan. The Company has in the past had an incentive cash bonus plan (the "Bonus Plan") in which the executive officers of the Company were eligible to participate. Awards under the Bonus Plan were made if certain target increases in revenues, operating profits and asset management ratios (established by the Board in its discretion) were attained by the Company. No awards were made under the Bonus Plan during fiscal 1983. The Bonus Plan is not currently in effect.

The Company has no annuity, pension or retirement plans.

RATIFICATION OF INDEPENDENT AUDITORS

Upon the recommendation of the Audit Committee, the Board of Directors has reappointed the firm of Arthur Andersen & Co. as the Company's independent auditors for the 1984 fiscal year, subject to ratification by the stockholders. Representatives of Arthur Andersen & Co. are expected to be present at the Company's Annual Meeting. They will have an opportunity to make a statement, if they desire to do so, and will be available to respond to appropriate questions. Ratification will require the affirmative vote of a majority of the shares of Common Stock present and voting at the meeting in person or by proxy.

THE BOARD OF DIRECTORS RECOMMENDS RATIFICATION OF THE APPOINTMENT OF ARTHUR ANDERSEN & CO.

BOARD OF DIRECTORS MEETINGS AND COMMITTEES

The Company's Board of Directors held four meetings during the 1983 fiscal year. All directors attended at least three meetings except Mr. Stone, who attended two.

The Board of Directors of the Company has appointed an Audit Committee, Nominating Committee and a Compensation Committee of the Board.

The members of the Audit Committee are Messrs. Eugene Kleiner, Morton Collins, John B.M. Place and Thomas J. Davis, Jr. The Audit Committee held four meetings during the 1983 fiscal year. Its functions are to monitor the effectiveness of the audit effort, to supervise the Company's financial and accounting organization and financial reporting and to select a firm of certified public accountants, whose duty it is to audit the books and accounts of the Company for the fiscal year for which they are appointed.

The members of the Nominating Committee are Messrs. Eugene Kleiner, Franklin P. Johnson, Jr. and Robert G. Stone, Jr. The Nominating Committee held no meetings during the 1983 fiscal year. The Nominating Committee's function is to select nominees for election as directors. The Committee will consider nominees recommended by stockholders. Such recommendations should be submitted in writing to the Nominating Committee in care of the Secretary of the Company at its address set forth on the first page of this Proxy Statement.

The members of the Compensation Committee are Messrs. Thomas J. Perkins, James G. Treybig and Thomas J. Davis, Jr. The Compensation Committee held two meetings during the 1983 fiscal year. The Compensation Committee's functions are to review and determine salaries and other compensation of officers and directors of the Company.

CERTAIN BENEFICIAL OWNERS

The following table sets forth information as of December 1, 1983, as to stockholders that have advised the Company, by filing a Schedule 13G under the rules of the Securities and Exchange Commission, that each is the beneficial owner of more than 5% of the Company's Common Stock.

	Beneficial Ownership of Common Stock	
	Number of Shares	Percent of Class
Jennison Management Corporation(1) 455 Lexington Avenue New York, NY 10017	4,087,104	10.3%
Donaldson, Lufkin & Jenrette, Inc.(2) 140 Broadway New York, NY 10005	2,750,200	6.9%

(1) In its Schedule 13G dated November 3, 1983, Jennison Management Corporation stated that it has sole voting and investment power with regard to 3,889,904 and 4,087,104 of such shares, respectively.

(2) In its Schedule 13G dated February 14, 1983, Donaldson, Lufkin & Jenrette, Inc. stated that it had sole voting power, shared voting power and shared investment power with regard to 1,100,080,

1,100,080 and 2,750,200 of such shares, respectively. The shares are held in discretionary accounts managed by Alliance Capital Management Corporation, a wholly-owned investment advisory subsidiary of Donaldson, Lufkin & Jenrette, Inc.

STOCKHOLDER PROPOSALS

To be considered for presentation at the Annual Meeting of Stockholders to be held in 1985, a stockholder proposal must be received at the offices of the Company, 19333 Vallco Parkway, Cupertino, California 95014, not later than August 30, 1984.

OTHER MATTERS

The Board of Directors knows of no other business which will be presented to the meeting. If any other business is properly brought before the meeting, it is intended that proxies in the enclosed form will be voted in respect thereof in accordance with the judgment of the persons voting the proxies.

Whether you intend to be present at this meeting or not, we urge you to return your signed proxy promptly.

By order of the Board of Directors,

Henry V. Morgan
Secretary

EXHIBIT 1

PROPOSED AMENDMENT TO CERTIFICATE OF INCORPORATION

ARTICLE FOUR

The total number of shares of stock which the corporation shall have authority to issue is sixty-two million four hundred thousand (62,400,000) shares, of which two million four hundred thousand (2,400,000) shares of the par value of ten hundredths dollars ($.10) each, amounting in the aggregate to two hundred forty thousand dollars ($240,000), shall be preferred stock and sixty million (60,000,000) shares of the par value of twenty-five thousandths dollars ($.025) each, amounting in the aggregate to one million five hundred thousand dollars ($1,500,000), shall be common stock.

The preferred stock may be issued from time to time in one or more series. The Board of Directors is hereby expressly vested with authority to fix by resolution or resolutions the designations and the powers, preferences and relative, participating, optional or other special rights, and the qualifications, limitations or restrictions (including, without limitation, the voting powers, if any, the dividend rate, conversion rights, redemption price or liquidation preference) of any series of preferred stock, to fix the number of shares constituting any such series, and to increase or decrease the number of shares of any such series (but not below the number of shares thereof then outstanding). In case the number of shares of any such series shall be so decreased, the shares constituting such decrease shall resume the status which they had prior to the adoption of the resolution or resolutions originally fixing the number of shares of such series.

Fifty-six million (56,000,000) shares of the common stock authorized hereinabove are designated "Common Stock" and four million (4,000,000) shares of the common stock authorized hereinabove are designated "Junior Common Stock," such Junior Common Stock to be issuable from time to time in one or more series. The Board of Directors is hereby expressly vested with authority to fix by resolution or resolutions the designations and the powers, preferences and relative, participating, optional or other special rights, and the qualifications, limitations or restrictions (including, without limitation, the voting powers, if any, the dividend rate, conversion rights, redemption price or liquidation preference) of any series of Junior Common Stock, to fix the number of shares constituting any such series of Junior Common Stock, and to increase or decrease the number of shares of any such series of Junior Common Stock (but not below the number of shares thereof then outstanding). In case the number of shares of any such series of Junior Common Stock shall be so decreased, the shares constituting such decrease shall resume that status which they had prior to the adoption of the resolution or resolutions orginally fixing the number of shares of such series.

The number of authorized shares of any class or classes of stock may be increased or decreased (but not below the number of shares thereof then outstanding) by the affirmative vote of the holders of a majority of the stock of the corporation entitled to vote in the election of directors.

EXHIBIT 2

TANDEM COMPUTERS INCORPORATED
1984 JUNIOR COMMON STOCK PLAN

ARTICLE 1.

ESTABLISHMENT AND PURPOSE.

The Plan was adopted by the Company's Board to become effective February 10, 1984, subject to the approval of the Company's stockholders. The purpose of the Plan is to authorize the sale of Shares of the Company's Junior Common Stock to key employees and certain directors of the Company and its Subsidiaries, thereby providing these individuals with an equity interest in the Company as well as a significant incentive to advance the growth of the Company and to remain in its service, while offering the Company a valuable tool for the recruitment of additional persons of outstanding ability.

ARTICLE 2.

ADMINISTRATION.

2.1 *Committee Membership.* The Plan shall be administered by the Committee. The Committee shall consist of not less than three (3) disinterested members of the Board. The members of the Committee shall be appointed by the Board for such terms as the Board may determine and may be removed by the Board at any time. Vacancies on the Committee, however caused, may be filled by the Board.

2.2 *Disinterested Directors.* A member of the Board shall be deemed to be "disinterested" only if he, at the time of his appointment to the Committee and within the 12 preceding months, was not eligible, under this Plan or under any other plan of the Company or an affiliate of the Company, for the purchase of stock, for the grant of rights or options to purchase stock, or for the grant of stock appreciation rights.

2.3 *Committee Procedures.* The Board shall designate one of the members of the Committee as chairman. The Committee may hold meetings at such places and times as it shall determine. The acts of a majority of the Committee members present at a meeting at which a quorum exists, or acts reduced to or approved in writing by a majority of all Committee members, shall be valid acts of the Committee.

2.4 *Powers of the Committee.* Subject to the provisions of the Plan, the Committee shall have full authority and discretion:

(a) To interpret the Plan and to apply its provisions;

(b) To determine when Shares are to be offered for sale;

(c) To select the Offerees who are to have the right to purchase Shares;

(d) To determine the number of Shares that each Offeree may purchase;

(e) To determine the fair market value of Shares for purposes of Section 5.3;

(f) To prescribe the terms and conditions of each sale of Shares, including (without limitation) the purchase price, and to prescribe the provisions of the Stock Purchase Agreement relating to such sale;

(g) To modify or amend any outstanding Stock Purchase Agreement, but only with the consent of the Offeree who entered into such agreement;

(h) To authorize any person to execute, on behalf of the Company, any instrument required to implement the Plan or to effect a sale of Shares under the Plan;

(i) To adopt, amend or rescind rules, procedures and forms relating to the Plan; and

(j) To make any other determinations deemed necessary or advisable for the administration of the Plan.

All decisions, interpretations and other actions of the Committee shall be final and binding on all Offerees and on all persons deriving their rights from Offerees.

ARTICLE 3.

Eligibility.

Rights to purchase one or more Shares shall be offered only to individuals in the following classes:

(a) Directors of the Company other than Messrs. Collins, Davis, Johnson and Perkins; and

(b) Key employees of the Company or a Subsidiary.

The Committee, at its sole discretion, shall select the Offerees among the foregoing classes, except that no individual who owns stock possessing more than ten percent (10%) of the total combined voting power or value of all classes of stock of the Company, its parent (if any) or any Subsidiary shall be selected as an Offeree.

ARTICLE 4.

Stock Subject to Plan.

Subject to Article 7, the maximum number of Shares that may be issued and sold under the Plan is four million (4,000,000). Such Shares may be authorized but unissued Shares of Junior Common Stock or reacquired Shares of Junior Common Stock. Shares may be issued and sold under the Plan in multiple series with different restrictions, preferences, rights and privileges. In the event that Shares sold under the Plan are repurchased by the Company pursuant to a right of repurchase or a right of first refusal under a Stock Purchase Agreement, such Shares shall become available for reissuance and sale under the Plan (unless the Plan then has terminated). The Company, during the term of the Plan, shall at all times reserve and keep available a number of Shares sufficient to satisfy the requirements of the Plan.

ARTICLE 5.

TERMS AND CONDITIONS OF SALES.

5.1 *Stock Purchase Agreement.* Each sale of Shares under the Plan shall be evidenced by a Stock Purchase Agreement between the Offeree and the Company. Each sale shall be subject to all of the terms and conditions of the Plan and may be subject to any other terms and conditions which are not inconsistent with the Plan and which the Committee deems appropriate for inclusion in a Stock Purchase Agreement. The provisions of all Stock Purchase Agreements under the Plan need not be identical.

5.2 *Duration of Offers and Nontransferability of Rights.* Any right to purchase Shares under the Plan shall automatically expire if not exercised by the Offeree within thirty (30) days after the grant of such right was communicated to him by the Committee, except that the Committee, at its sole discretion, may make a longer period available. Any right to purchase Shares under the Plan shall not be transferable and shall be exercisable only by the Offeree to whom such right was granted.

5.3 *Payment for Shares.* The purchase price of Shares to be offered under the Plan shall in no event be less than one hundred percent (100%) of the market value of such Shares on the date of the offer, as determined by the Committee. Subject to the preceding sentence, the purchase price shall be determined by the Committee at its sole discretion. The entire purchase price of Shares sold under the Plan shall be payable in cash at the time such Shares are purchased, except that the Committee, at its sole discretion, may accept payment from any Offeree (for all or any part of the purchase price) in one or both of the following forms:

(a) A full-recourse promissory note executed by the Offeree. The interest rate, term, repayment schedule and other provisions of such note shall be as specified by the Committee; provided, however, that such note shall bear interest at a rate not less than the applicable test rate of interest prescribed by section 1.483-1(d)(1) of the Income Tax Regulations, or its successor, as in effect at the time when the Shares are purchased, and that the term of such note shall not exceed five (5) years. The Committee may require that the Offeree pledge his Shares to the Company for the purpose of securing the payment of such note, and the Company may hold the certificate(s) representing such Shares in escrow in order to perfect its security interest.

(b) Shares of the Company's Common Stock owned by the Offeree and surrendered to the Company in good form for transfer. Such shares shall be valued at their fair market value, as determined by the Committee, at the time when the new Shares are purchased under the Plan.

5.4 *Restrictions on Transfer of Shares.* Any Shares sold under the Plan shall be subject to such rights of repurchase, rights of first refusal and other transfer restrictions as the Committee may determine. Such restrictions shall be set forth in the applicable Stock Purchase Agreement.

5.5 *Election Under Section 83(b).* In the applicable Stock Purchase Agreement, each Offeree subject to United States income tax liability shall agree to file a timely election under section 83(b) of the Internal Revenue Code of 1954, as amended, and under any corresponding provision of applicable state and local income tax laws with respect to the transfer of Shares to him.

ARTICLE 6.

RIGHTS AS AN EMPLOYEE.

Nothing in the Plan shall be construed to give any person the right to remain in the service of the Company or a Subsidiary or to affect the right of the Company and its Subsidiaries to terminate any person's employment at any time, with or without cause.

ARTICLE 7.

ADJUSTMENT OF SHARES.

Subject to the provisions of the Company's Certificate of Incorporation, as amended, and any required action by the Company's stockholders, the number of Shares available for issuance and sale under the Plan shall be proportionately adjusted if any reorganization, recapitalization, reclassification, split-up, consolidation or similar adjustment of Junior Common Stock is effected or if any distribution other than a cash dividend is made to the holders of Shares. The Committee, at its sole discretion, shall determine how the number of Shares available under the Plan is to be adjusted.

ARTICLE 8.

SECURITIES LAW REQUIREMENTS.

Shares shall not be issued under the Plan unless the issuance and delivery of such Shares complies with all applicable legal requirements, including, without limitation, the Securities Act of 1933, as amended, the rules and regulations promulgated thereunder, state securities laws and regulations, and the requirements of any stock exchange on which the Company's securities may then be listed.

ARTICLE 9.

AMENDMENT OR TERMINATION.

9.1 *Term of the Plan.* The Plan shall become effective on February 10, 1984, subject to the approval of the Company's stockholders at the Company's regular annual meeting of stockholders held on that date. The Plan shall be null and void if such approval is not obtained. The Plan shall terminate automatically on November 8, 1994, and may be terminated on any earlier date pursuant to Section 9.2.

9.2 *Right to Amend or Terminate the Plan.* The Board may amend, suspend or terminate the Plan at any time and for any reason; provided, however, that any amendment of the Plan which materially increases the number of Shares available for issuance under the Plan (except as provided in Article 7), which materially increases the benefits available under the Plan, or which materially modifies the classes of persons eligible to purchase Shares under the Plan, shall be subject to the approval of the Company's stockholders. Stockholder approval shall not be required for other amendments of the Plan.

9.3 *Effect of Amendment or Termination.* No Shares shall be issued or sold under the Plan after the termination thereof. However, the termination of the Plan, or any amendment thereof, shall not affect any Share previously issued and sold (unless the applicable Stock Purchase Agreement otherwise provides).

ARTICLE 10.

DEFINITIONS.

10.1 *"Board"* shall mean the Board of Directors of the Company, as constituted from time to time.

10.2 *"Committee"* shall mean the committee described in Section 2.1.

10.3 *"Company"* shall mean Tandem Computers Incorporated, a Delaware corporation.

10.4 *"Junior Common Stock"* means one or more series of the Company's Common Shares, excluding the first series thereof (designated as "Common Stock"). Where required by the context, the term "Junior Common Stock" also includes the Common Stock into which a subsequent series of Common Shares has been converted pursuant to the Certificate of Determination applicable to such series.

10.5 *"Offeree"* shall mean a key employee or director described in Article 3 to whom the Committee offers the right to purchase Shares under the Plan.

10.6 *"Plan"* means this Tandem Computers Incorporated 1984 Junior Common Stock Plan, as it may be amended from time to time.

10.7 *"Share"* means one (1) share of Junior Common Stock, as adjusted in accordance with Article 7 (if applicable).

10.8 *"Stock Purchase Agreement"* means the agreement entered into by the Company and an Offeree who purchases Shares under the Plan and containing the terms, conditions and restrictions pertaining to the purchase of such Shares.

10.9 *"Subsidiary"* means any corporation, more than fifty percent (50%) of the combined voting power of which is owned by the Company and/or by one or more other Subsidiaries.

ARTICLE 11.

EXECUTION.

To record the adoption of the Plan by the Board on November 1, 1983, the Company has caused its authorized officers to execute the same.

TANDEM COMPUTERS INCORPORATED

By JAMES G. TREYBIG

James G. Treybig
President and Chief Executive Officer

By ROBERT C. MARSHALL

Robert C. Marshall
Senior Vice President and Chief Operating Officer

TANDEM

1983
ANNUAL
REPORT

FINANCIALS

Tandem Computers Incorporated designs, develops, manufactures, markets and supports a family of unique computer systems for on-line transaction processing. The Tandem NonStop system concept provides the first on-line, distributed computer architecture for mainstream business applications. Customers' systems are supported from over 100 locations throughout North America, Europe, Asia and the Pacific. The company operates six manufacturing facilities in the United States and one in Germany. At the close of fiscal 1983, Tandem's 725 customers — principally large, diversified organizations — were using 5,824 NonStop processors worldwide, an increase of 44% over the preceding year.

As the pace and complexity of conducting business intensified in the Seventies, two major trends emerged in the data processing marketplace.

The first trend was to on-line transaction processing. Businesses began to move critical applications on-line in order to obtain timely information that accurately reflects the state of the business.

Following closely on this development, businesses began distributing the computer resource, putting information where it is used. The desire to tie together these distributed locations evolved naturally: on-line networks would vastly increase the information flow and automation benefits.

Aggressive organizations began envisioning innovative ways to apply data processing to control daily operations, enhance productivity, reduce costs, improve customer service and sharpen competitiveness. But their mainstay resource—batch-processing, centralized mainframe computers—proved inherently inadequate to the new automation tasks.

Batch processors are not designed to automatically capture, instantly update and immediately deliver constantly changing information. Further, in on-line applications, when the computer stops, the business stops.

Recognizing the early signs of these trends, Tandem alone tailored technology to fit the rapidly evolving requirements for the Eighties and Nineties.

Tandem bases the family of NonStop systems on a revolutionary, proprietary architecture for on-line, distributed mainstream applications that virtually eliminates the risk of system failures. At the same time, the system protects users' data from damage or loss. NonStop systems expand modularly from mid-range to mainframe power—and into networks of up to 255 mainframe-size, geographically dispersed systems—without hardware replacement or software changes.

Complemented by an extensive variety of software tools, NonStop systems uniquely meet the requirements of the growing market for on-line transaction processing.


TAPE

Nearly a decade ago, Tandem alone responded decisively to what is now widely regarded as one of the most significant marketplace changes in the history of commercial data processing. By contributing the only technology and architecture specifically designed to meet the needs of the new on-line transaction processing marketplace, Tandem has enjoyed rapid growth. Tandem has earned a strong position in an $11 billion market segment that is expected to increase to $27 billion by 1986.

Building on strength in a dynamic marketplace

Few companies in the world are as ideally positioned in their marketplace as Tandem. Five fundamental reasons explain why.

First: Tandem accurately foresaw the impact of an evolving, yet dramatic, change in the marketplace. Needs shifted from centralized, batch-processing computers to distributed, on-line transaction processing systems interacting within networks.

Second: We developed a revolutionary computer architecture to specifically address what we correctly judged would be the critical needs of this changing marketplace.

Third: We carefully built a quality organization that has won us a broad base of prestigious customers worldwide.

Fourth: We have attracted the level and quality of creative, productive people we need to sustain high growth. We are perceived in our industry not only as a principal contributor to technological excellence, but also as a major contributor to quality of work life.

And fifth: We accomplished all of that years before the world recognized the market trend for what it is: *The biggest change in market demand for medium- and large-scale computer applications since the beginning of commercial data processing.*

Potential Transaction Processing Market Size

$ Billions

1981	1982	1983	1984	1985	1986
$6.4	$8.3	$11.0	$15.0	$20.5	$27.8

Source: InfoCorp

As a result, even in the changeable economy of the four year period from 1979 to 1983, our annual revenues grew seven-fold from $56 million to $418 million. Shareholders' equity expanded nearly ten times from $32 million to $311 million. And we earned more than $100 million during the period—nearly a third of it in fiscal 1983 alone.

We are well positioned to take maximum advantage of market opportunities.

Now, as Tandem approaches its second decade as a strong organization with established market presence, we believe we are well positioned to take maximum advantage of market opportunities for these reasons:

The marketplace for on-line transaction processing systems is huge and rapidly growing. In the short span of a decade, the potential market has grown, according to independent research, from an insignificant level to $11 billion. And the market likely will more than double to over $27 billion by 1986.

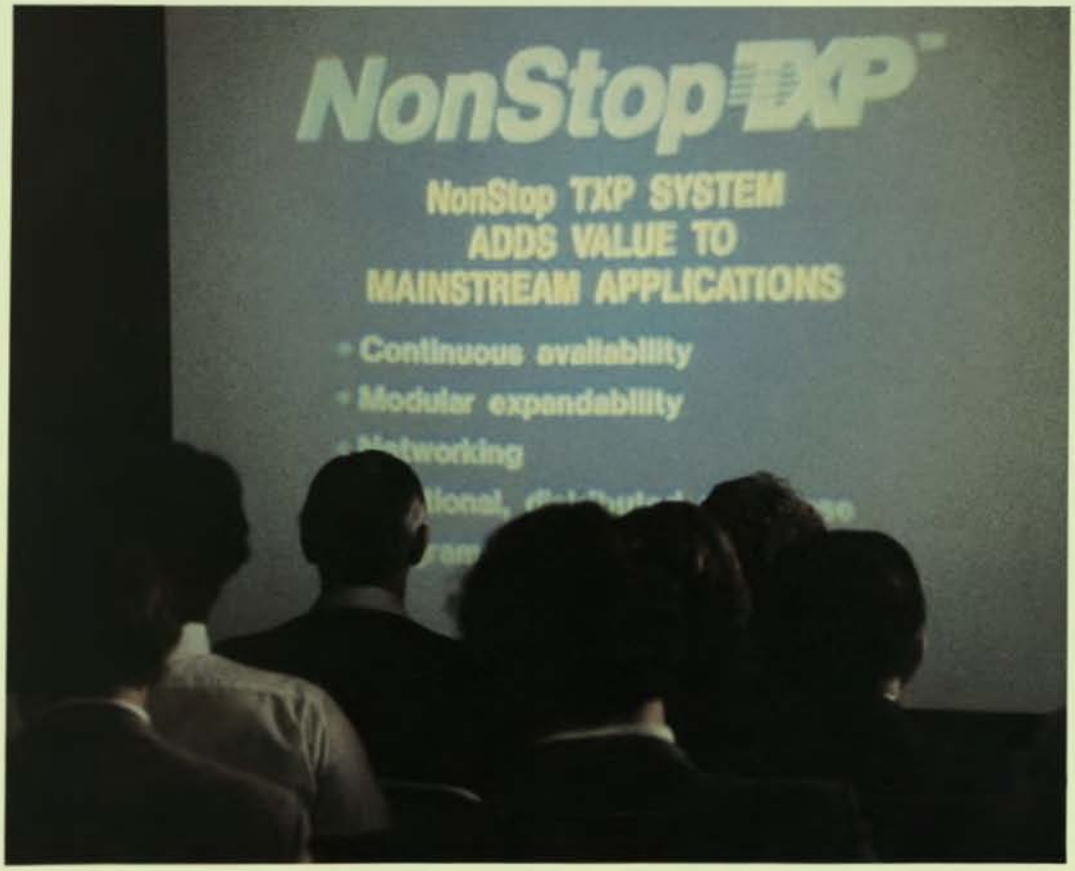
The world's largest organizations are making major, long-term commitments to Tandem as the supplier of multi-million-dollar systems to run their mainstream business operations. They are deploying large Tandem systems as distributed mainframe computers linked in geographically dispersed networks. Only Tandem's NonStop architecture and advanced software tools meet their needs for uninterrupted computer operations, modular expandability, assurance of data integrity, ease and low cost of programming, inherent networking capability and high-speed, low-cost transactions.

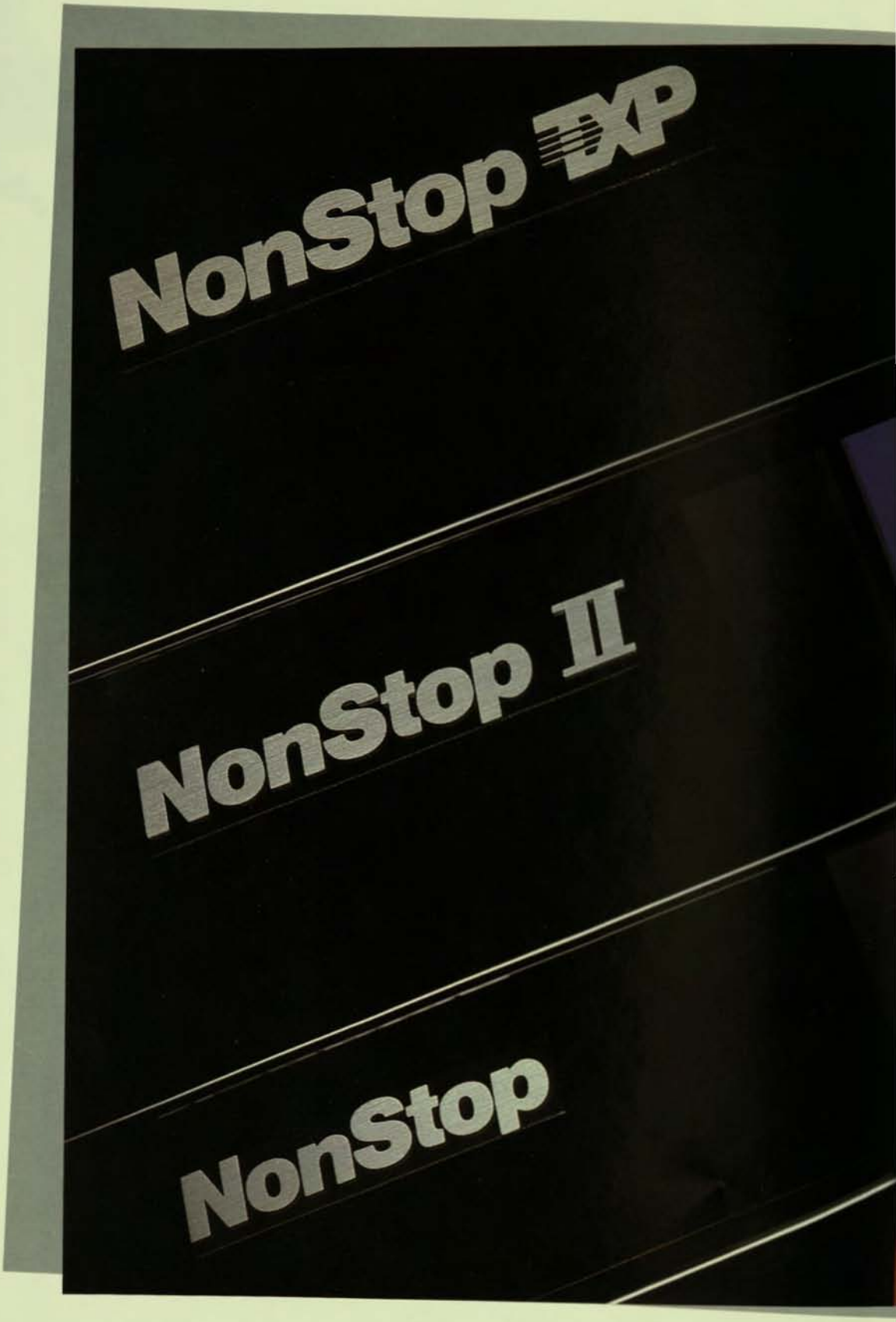
Tandem ranks first in satisfied customers. For the fourth consecutive year, Tandem in 1983 ranked number one in customer loyalty and satisfaction in the bellwether Cowen/DATAMATION survey of computer users.

The market trend favors distributed processing. The same survey shows that Tandem has the industry's highest percentage of customers using data base management and networking software. Two-thirds of all Tandem users are employing software to manage large data bases, as compared to an industry average of only one-third. And use of networking software at Tandem installations is nearly double the industry average.

Our installed base has built-in growth potential. NonStop systems expand modularly from minicomputer to mainframe size, and from single systems to networks of up to 255 systems—all without programming changes. This modular expandability creates a natural growth potential for Tandem. We ended 1983 with 725 customers using 5,824 processors—four-and-a-half times more customers using nine times more processors than five years earlier. During fiscal 1983 alone, Tandem shipped 1,773 processors, adding 44% to our installed base. Three-quarters of our 1983 shipments were to customers who are expanding their systems, adding new systems or developing new applications. And 126 customers were first-time users.

In simultaneous customer teleconferences across the country in October 1983, Tandem unveiled the new, high-end NonStop TXP system. The TXP system expands the family of NonStop systems to accommodate the full spectrum of on-line transaction processing price/performance requirements. First TXP processor shipments were made to customers in August 1983.




NonStop TXP
NonStop II
NonStop

The dynamic state of the on-line transaction processing marketplace produces a range of rapidly changing requirements for the new backbone networks of Tandem distributed mainframe computers. Tandem's three-tier family of systems leads the industry not only in capabilities, functionality and versatility, but in price/performance, too. Tandem's new NonStop TXP system, announced in October 1983, is the world's highest performance computer for on-line transaction processing applications.

NonStop NonStop II NonStop TXP

Tandem's family of systems is unprecedented in reliability, functionality and compatibility. And they offer the best price/performance for on-line transaction processing.

Tandem's single focus on transaction processing has allowed us to extend our original contribution of system fault tolerance, data integrity and inherent expandability. A stream of new products and product enhancements has met the rapidly evolving requirements of the marketplace. And we fill those needs more cost-effectively than anyone in the market while providing an easy growth path to accommodate users' expanding applications.

Users are making major commitments to Tandem and enjoying the benefits of compatibility and an easy growth path from relatively modest to massive transaction rates.

The Union Bank of Finland, for example, chose Tandem systems to replace their conventional mainframe system whose processing power had become a major bottleneck. Tandem met the new requirements for 99.9% system availability, high transaction rates with short response time, easy expandability, fast application development and reasonable cost. On the very first day of operation, the three-system, 36-processor NonStop II installation processed 500,000 transactions with a peak load of 30 transactions per second (tps). Ten weeks later, transaction volume exceeded one million, and peak load reached 45 tps. With the addition of the new NonStop TXP system, the Union Bank of Finland not only will be able to handle increasing transaction levels. They also will be able to enhance applications and add new services cost-effectively, and without performance penalty.

Tandem's three-tier family of compatible systems spans the performance spectrum from relatively modest to massive transaction rates.

NonStop TXP. Tandem's new high-end system is the world's highest performance computer for on-line transaction processing. The NonStop TXP system is the most cost-effective system for handling transactions in the range of 100 per second. An increasing number of new services and rapidly growing businesses are developing applications requiring such performance. The 32-bit TXP processor has two to three times the performance of the NonStop II processor and reduces the cost per transaction by up to 50%. NonStop TXP processors can be added to an existing NonStop II system.

NonStop II. This system is cost-effective for the middle level of transaction rates. In large configurations, the NonStop II system can process in the 50 tps range, satisfying the current performance requirements of a wide array of applications in all industries. As those requirements change, users can add NonStop II processors or fully compatible NonStop TXP processors to existing NonStop II systems to meet transaction volume demand.

Tandem Installed Base

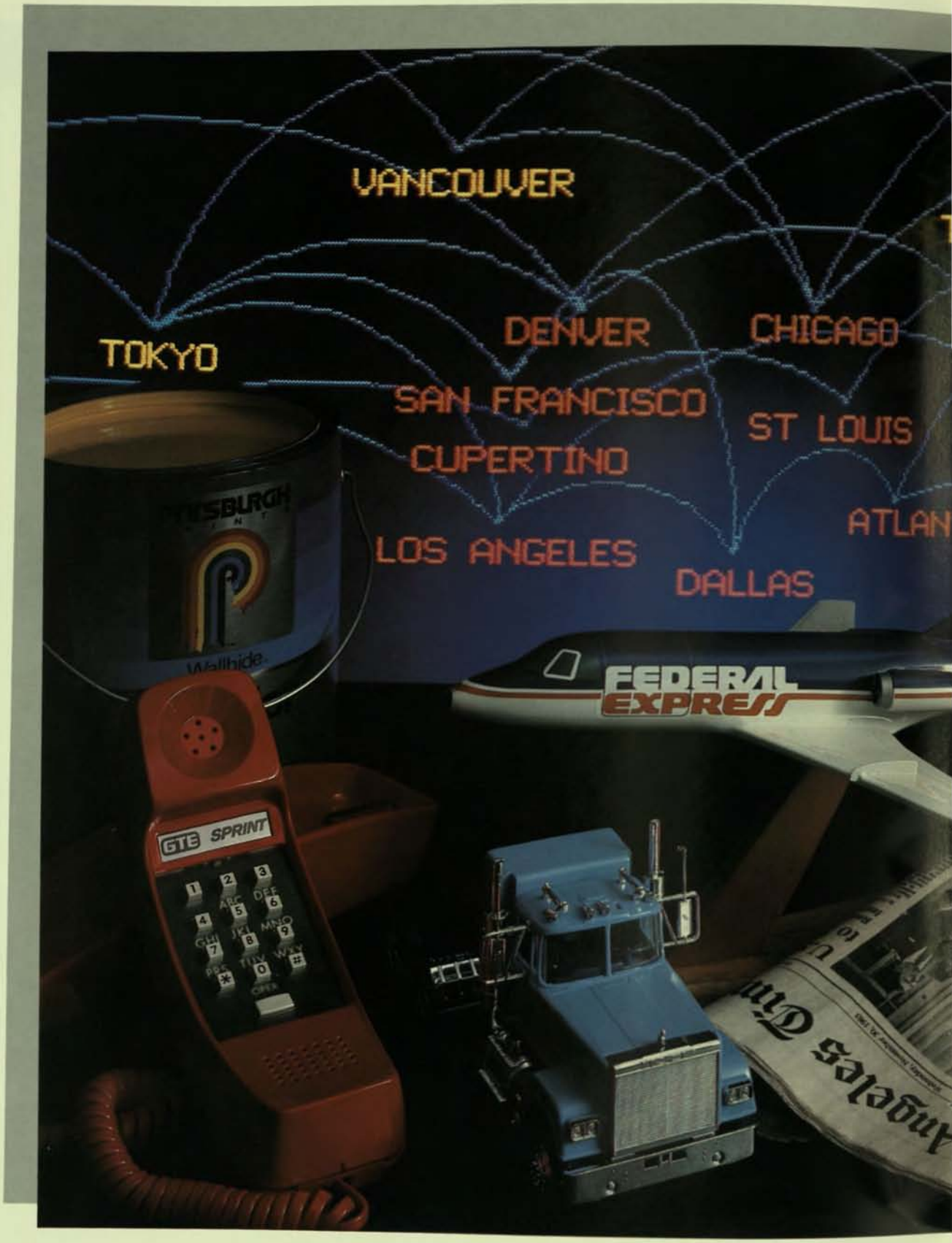
cumulative

	1979	1980	1981	1982	1983
Customers	160	290	460	599	725
Processors	646	1299	2509	4051	5824

NonStop I+. The NonStop I+ system fills customers' needs for fault-tolerance, easy expandability and NonStop software at lower-demand nodes in a network of NonStop systems. An attractively priced, entry-level system, the NonStop I+ system is cost-effective for smaller applications in major organizations. This system can access data and share information with NonStop II and TXP systems.

Tandem's contribution does not end with processors. Leading-edge communications subsystems and state-of-the-art peripheral products, including our own terminal, enhance system performance. And the company offers the most advanced and complete complement of software tools available for developing distributed, on-line transaction processing applications.

Wells Fargo Bank has made a multi-million-dollar commitment to Tandem to automate its entire retail banking delivery system using NonStop systems in a backbone network of distributed host processors. Transaction rates are expected to begin at ten transactions per second and grow to over 300. Seen here working with Barry E. Young (right), Wells Fargo senior vice president, is Christopher L. Palombi, Tandem major account manager.


VANCOUVER
TOKYO
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ST LOUIS
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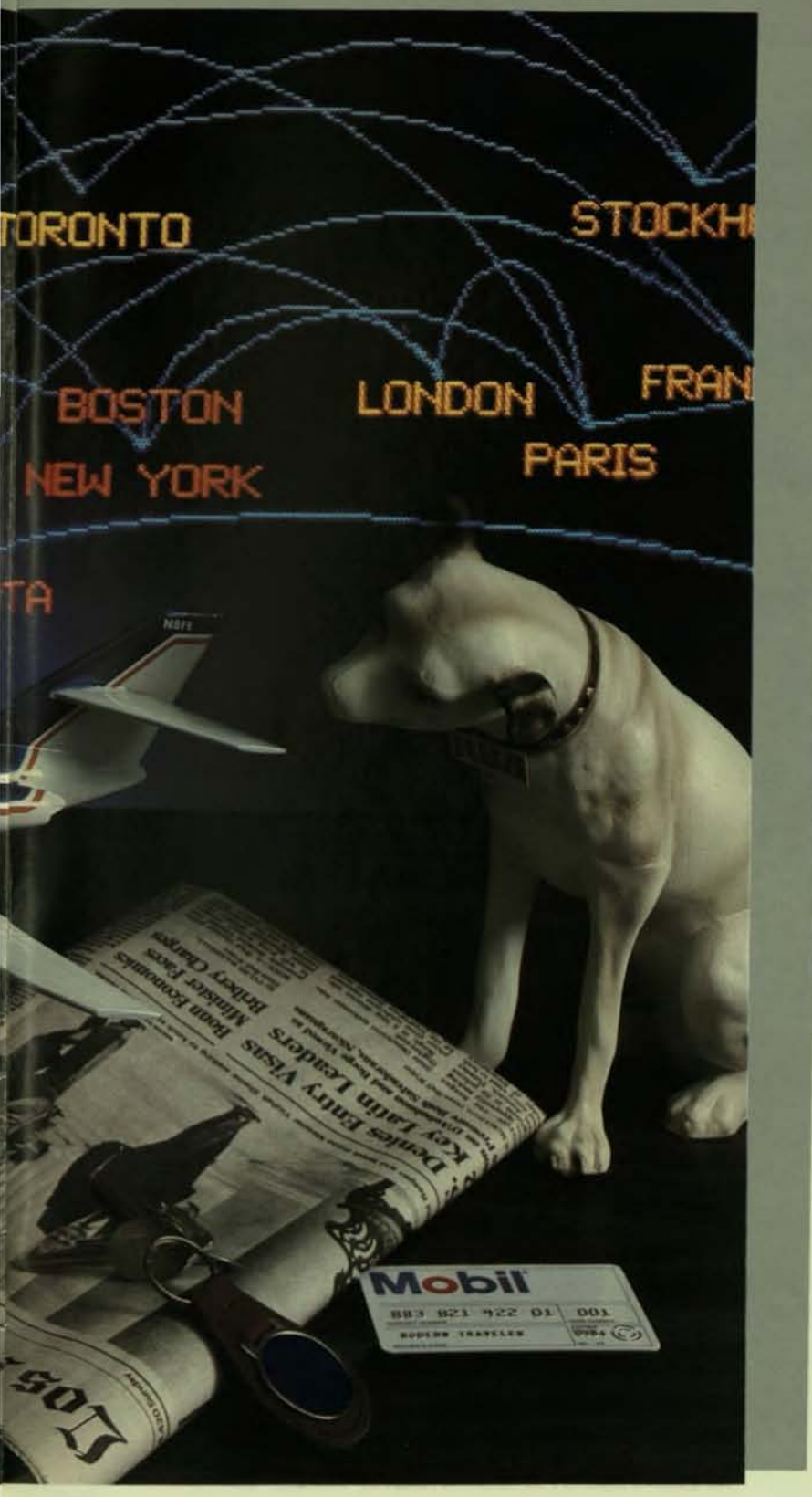

Tandem systems are penetrating major organizations worldwide for a wide range of mainstream applications. Some companies became customers to automate a single function. Later, they moved Tandem systems into multiple mainstream applications at the heart of their business. Others immediately made Tandem systems their new backbone network. Customers buy Tandem systems not only for their hardware attributes, but also for advanced functionality, programmability, networking capabilities, maintainability—and the fact that only Tandem systems can cost-effectively process high transaction volumes.

A broad base of prestigious users

Many customers who began by using Tandem systems to automate a single function are now implementing broad-based, mainstream applications. Wells Fargo Bank, for instance, began by basing the largest automated teller machine (ATM) network in California on Tandem systems—over 700 ATMs in a network of 24 Tandem NonStop processors. This leading bank now is implementing its Retail Outlet Automation program entirely with Tandem equipment. NonStop systems will support thousands of ATMs, teller terminals and administrative terminals in over 350 branch locations throughout California.

Other customers base entire businesses on Tandem systems. NonStop systems provide GTE's *SPRINT*™ long distance telephone service with its backbone, internal administrative network. It is currently the largest Tandem customer network—and expected to triple in size by 1985. Tandem systems are also driving emerging applications like the *Viewtron*™ service of Knight-Ridder's Viewdata subsidiary, a leading contender in the market for videotex services. Viewdata had 16 NonStop processors for their 1983 start-up service, and they plan expansion into 18 cities commencing in 1984, 30 cities within ten years. (By 1990, industry sources estimate that 45 million homes may be using videotex.) And Tandem systems are at the heart of other innovative new services like the *Federal Express Satellite Network.* Federal Express, which delivers 250,000 packages daily, in 1984 will launch a vast, electronic delivery service for documents that ultimately will use a network of multiple earth stations at numerous locations, with Tandem NonStop computers at the heart of the business.

These customers did not buy Tandem systems only because of the NonStop system capabilities of fault-tolerance, data integrity and expandability. They based their decisions on other considerations as well:

Customers buy Tandem NonStop systems for many reasons, not only for their unprecedented reliability.

1. *Advanced Programming Tools.* Tandem supplies superior, high-level tools that dramatically reduce the complexities, leadtime and costs of programming on-line applications. Using Tandem's ENCOMPASS distributed relational data base management system, customer applications can be brought up quickly, maintained easily and enhanced cost-effectively. And EXPAND networking software makes writing applications across a network equally productive. Customers regularly report on new applications coming on-line in record time and below budget. Rockwell International, for example, began operating a plant automation program just four months after programming started.

2. *State-of-the-Art Communications.* Powerful local networks of up to 224 NonStop processors can be quickly, inexpensively created with Tandem's FOX fiber optic link—over 300 times faster than conventional communications lines. Using EXPAND software, users can build a worldwide network of up to 4,080 processors without programming changes. Tandem also provides gateways to other networks, including SNA and X.25. And the company's INFOSAT product is the first commercially available, fully integrated satellite communications network. FOX, EXPAND and INFOSAT extend NonStop system reliability and data integrity across networks.

3. *Advanced Functionality.* Backbone networks of the future will integrate and disseminate information from such diverse office equipment as telex, photocopiers, telecopiers, word processors and a range of incompatible computers. Tandem has already provided

Half of the Tandem organization is dedicated to field service, customer service and support activities. The Tandem Executive Institute, for example, conducts 4-day seminars on using technology to gain competitive advantage for customers and prospects in specific industries. The institute and its industry-expert guest speakers have been host to hundreds of senior management people from the world's largest corporations.

the capability for such multi-media transaction processing. TRANSFER moves integrated data from person to person, or program to program, to put the information where it is needed, when it is needed.

4. *Support and Maintainability.* Half of the entire Tandem organization worldwide is composed of marketing and service people. They support customers through activities that include customer education, field service and applications support—a good part of the reason why Tandem ranks first in the industry for customer satisfaction and loyalty. And the Tandem NonStop architecture allows maintenance to be performed without interrupting customer operations because repairs can be made while the system is running.

5. *Price/Performance.* At all transaction volume levels, Tandem systems offer the best price/performance. More importantly, the total cost of NonStop system ownership is extremely attractive. Reliable data, no downtime and low program development costs ensure economy. And the system's flexibility allows the user to reconfigure systems and networks of systems, without replacing equipment or rewriting software.

6. *Demonstrated Leadership.* Customers make major commitments to Tandem because our dedication to quality and innovative product development protects their investments in Tandem systems.

For the first time in the history of its annual "Supplier Superior Performance Award", Hughes Aircraft's Radar Systems Group honored a computer company. In making the 1983 award to Tandem President Jim Treybig (right), Hughes' Dick Bringuel said, "After the product is delivered, it's the service that counts ...the NonStop II system went on-line ahead of schedule and performed perfectly."


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125
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PRODUCT DEVELOPMENT

Tandem is attuned to rapidly changing marketplace requirements. We have unmatched experience in on-line transaction processing and close relationships with users who are developing advanced applications. Over the past five years, the company has invested more than $100 million to develop hardware and software products that make our customers more productive and profitable.

Sustained technological leadership

Tandem's focus on on-line transaction processing since its founding has provided the organization with a vast amount of knowledge about the particular needs of the marketplace. Our experience and understanding enable us to provide products and enhancements specifically designed to allow our customers to do more and more on-line transaction processing applications, and to do them cost-effectively.

Users share the benefits of our unique product development leverage.

Tandem is committed to technological leadership in our marketpace. We have invested more than $100 million in product development activities over the past five years. In the past two years alone, our product development expenditures were more than twice the total amount spent over our entire previous corporate history. This investment is highly leveraged: The modularity and compatibility of our hardware and software products mean that time and dollars directed at product development and enhancement programs benefit our entire family of products. And that means that all users reap the benefits of increased functionality, productivity, ease of use and improved price/performance.

The NonStop TXP system exemplifies the ability of Tandem to develop products that fill the needs of our marketplace. Using our advantages of years of experience in this market and a large customer base, our development team created a technique to model actual applications so they could design the system to maximize transaction processing performance. As a result, the TXP system utilizes a unique combination of 64-bit, 32-bit and 16-bit features that are optimized for on-line transaction processing.

Tandem's software development focus has also been on protecting and leveraging our customers' investments in their Tandem systems—as well as their earlier data processing investments. For example, in 1983 we delivered our SNAX software product that enables EXPAND network users to access IBM SNA networks, devices and applications programs while retaining the reliability and flexibility of NonStop systems. We also delivered the most advanced software products available for distributed relational data base management, networking and communications—all designed to increase our users' programming productivity.

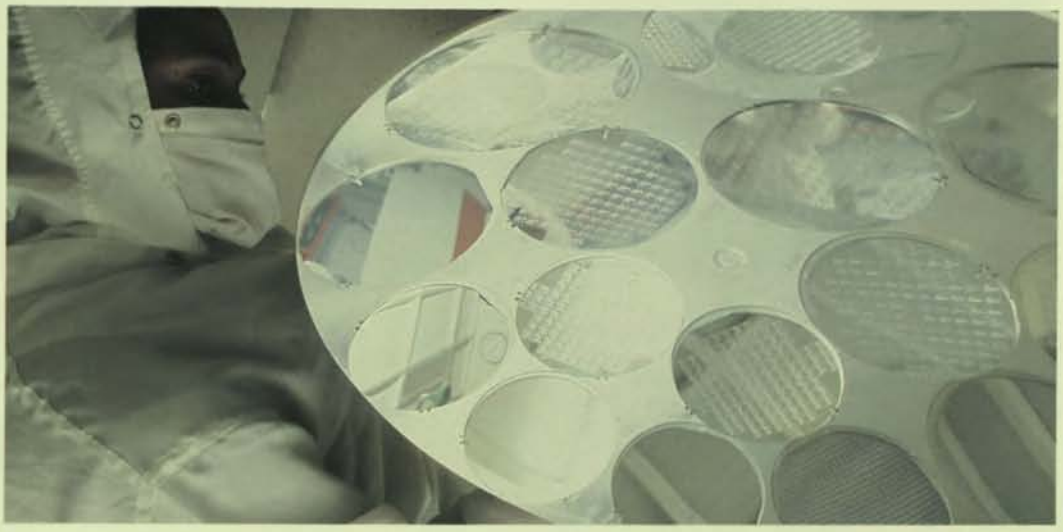
Tandem has invested in technologies and design techniques to further enhance the company's ability to anticipate and meet customers' needs. For example, our engineers extensively used computer-aided techniques to create the NonStop TXP system. We have also built an advanced laboratory where we are designing our next generation of chips and developing techniques to speed the development cycle.

The requirements for on-line transaction processing constantly expand—in part because Tandem has given customers the ability to do more. Tandem will continue to lead the way, capitalizing on our experience and understanding to develop the products for the market of the future.

Tandem Product Development Expenditures

$ Millions

1979	1980	1981	1982	1983
$4.7	$8.9	$17.8	$33.6	$39.2



▲

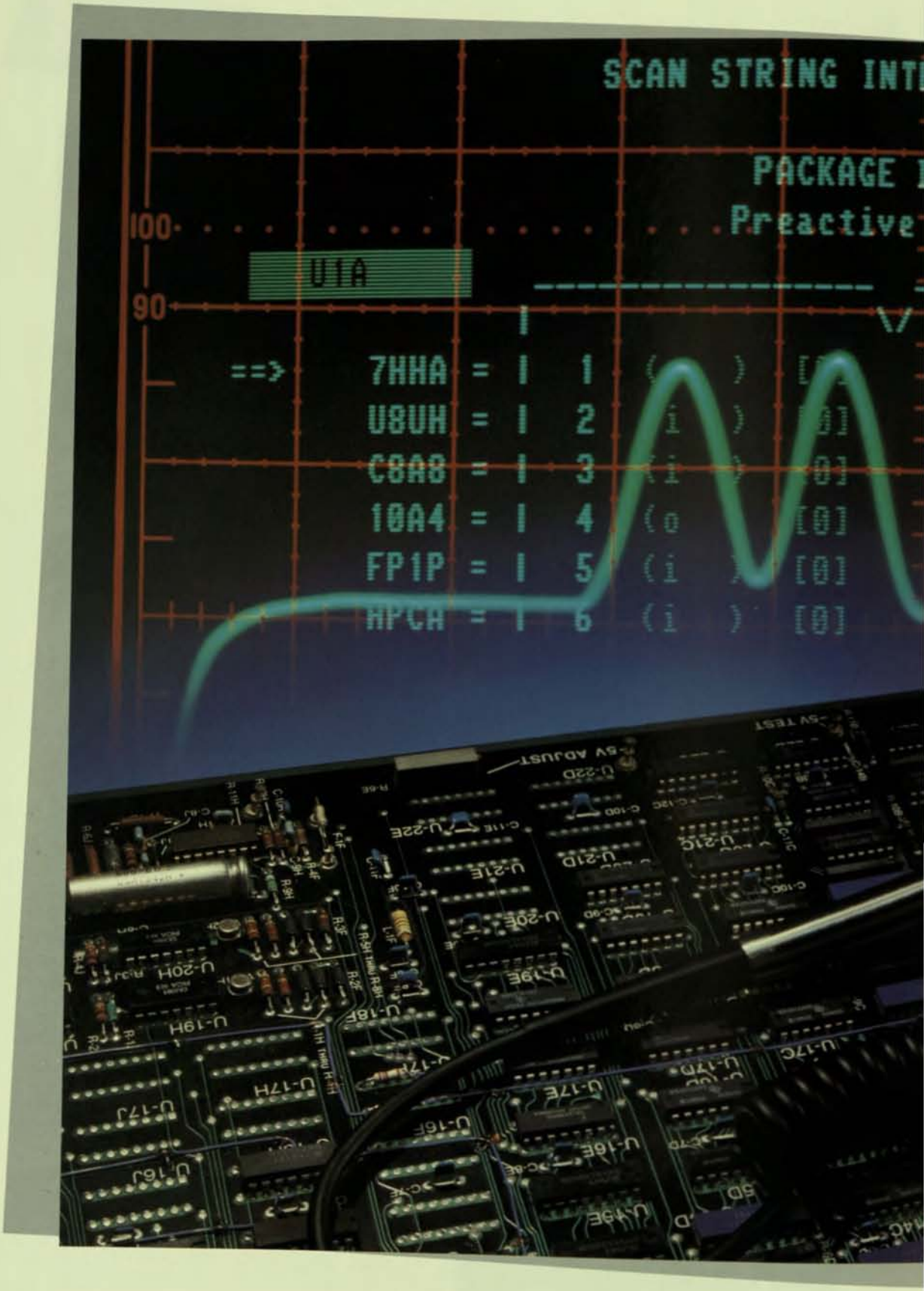
In addition to working on enhancements to disc subsystems, terminals and data base management systems that optimize NonStop system price/performance, functionality, programming ease and user friendliness, Tandem is developing processors for the future.

Tandem's INFOSAT product extends the NonStop system advantages to satellite-based computer networks. INFOSAT's unprecedented reliability is enhanced by a self-diagnostics package, the only one of its kind, that automatically identifies and isolates down to the component level any malfunctions in the dual-path system.

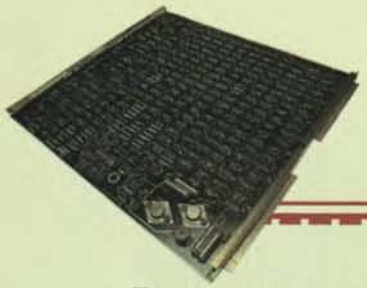
▼

▲

One of Tandem's many product development contributions during 1983 was FOX, Tandem's fiber optic link that quickly and inexpensively ties together up to 224 NonStop processors in a high-speed local network, creating a system more powerful than the largest conventional mainframe computer.


SCAN STRING INTE
PACKAGE
Preactive
100
90
U1A
==>
7HHA = I 1
U8UH = I 2
C8A8 = I 3
10A4 = I 4
FP1P = I 5
HPCH = I 6

Advanced automation technologies and participative management techniques introduced at Tandem manufacturing facilities have significantly increased productivity and product quality. They play an important part in sustaining Tandem's aggressive price/performance position in the marketplace.



Advanced techniques to achieve high productivity

Tandem manufacturing facilities, which are among the most advanced in the world, contribute to the company's competitiveness in the marketplace.

The integration of technology and participative management techniques at our plants has substantially enhanced productivity and product quality. They are key factors in our ability to deliver products with attractive price/performance ratings while maintaining acceptable product margins.

New techniques and technologies strengthen our ability to meet constantly increasing demand for our products.

At our computer terminal manufacturing plant in Austin, Texas, for example, the combination of automation and participative management resulted in inventory turn rates and sales per employee in 1983 that are well above the industry average.

The Austin plant has no assembly lines: Each Tandem terminal is completely assembled and tested by one person who personally "signs" the completed unit.

The plant is paperless: Everyone uses terminals tied to a Tandem system as production tools to control the manufacturing process.

Production decisions that were once made only by managers are made by the people who make the products: Everyone participates in weekly plant meetings and daily "focus group" meetings to set and review goals.

The meetings are called and run by the workers: Managers attend and provide open-book information on how the business is progressing.

Quality is a major end result: Virtually every unit produced passes all test procedures the first time.

Our Austin operation is so impressive that scores of executives from major industrial companies—prospects for Tandem systems—toured the facility during 1983. And we are adopting the Austin techniques in other Tandem facilities as well.

We have also automated the assembly operations at our circuit board facility in Watsonville, California. Slow, tedious work that was previously performed manually is now accomplished with greater speed and accuracy using computer-controlled equipment.

Our manufacturing emphasis on quality and productivity has led us to develop our own sophisticated testing equipment for NonStop processor circuitry. Last year we developed an automatic testing system called ORACLE that gave us testing capabilities not previously possible—and reduced the circuit board testing cycle from 30-60 minutes to 3-6 minutes, a tenfold increase in productivity.

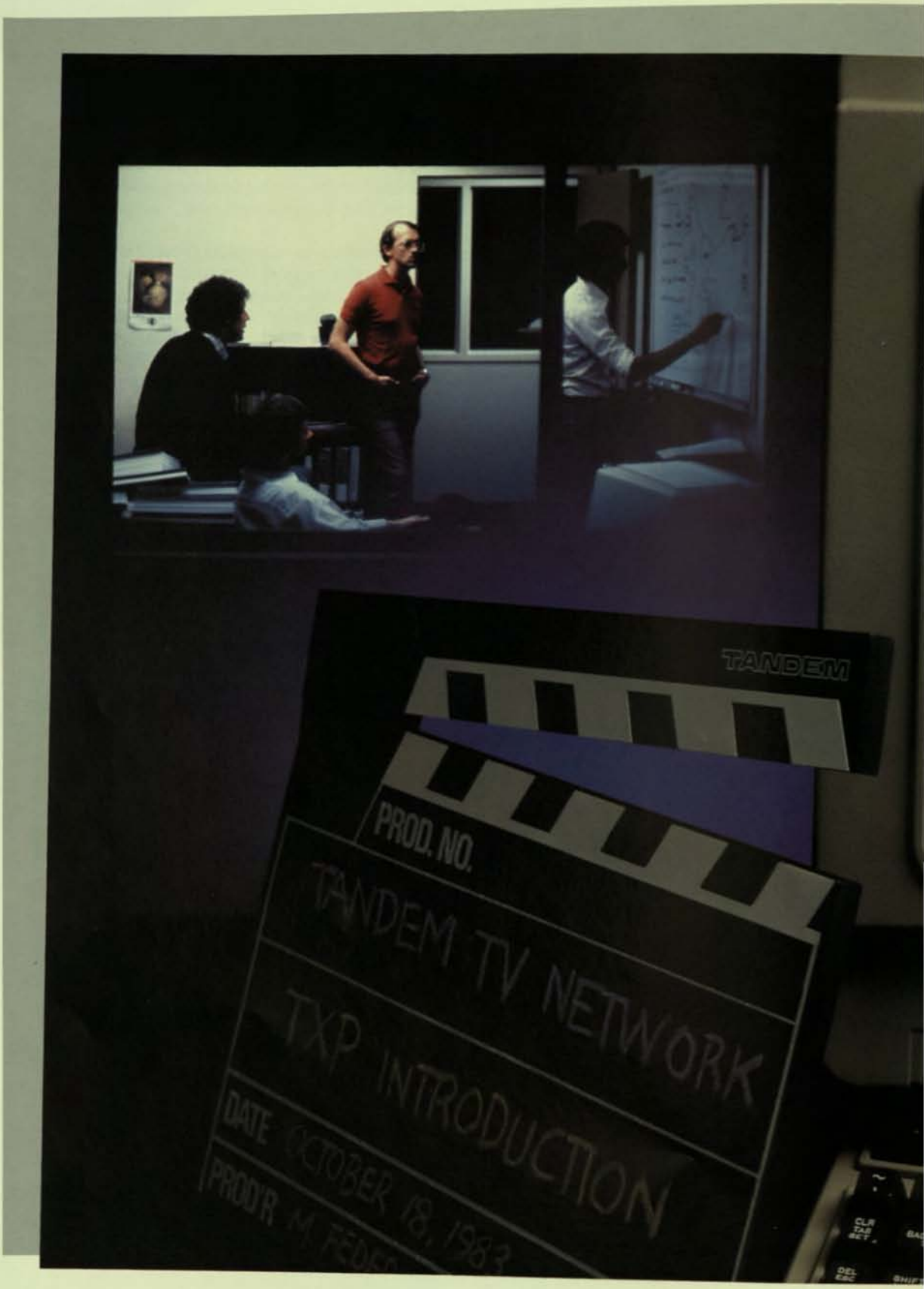
Even as ORACLE was being installed, we were at work on MERLIN, the next generation of automated system diagnostics. To create the new NonStop TXP system, engineers in product development and manufacturing pursued complementary approaches that took advantage of new scan logic design techniques. The result was a system with greatly enhanced testability. Utilizing MERLIN, the need for manual test programming was eliminated.

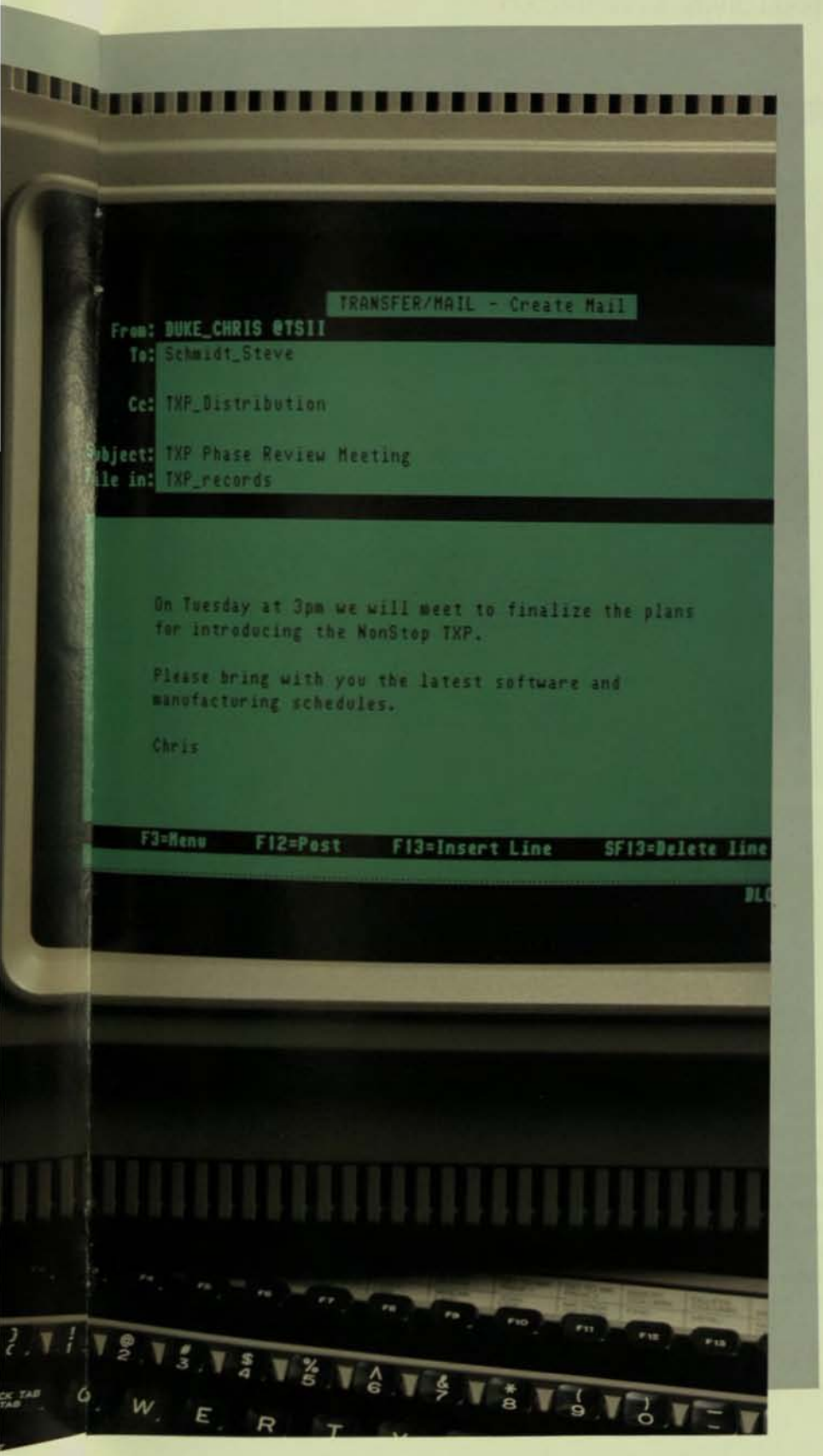
▲ *At Tandem's new paperless plant in Austin, each person builds and tests a complete terminal, and "signs" the finished product.*

MERLIN increases testing productivity by as much as 120 times, completing some test phases that would have taken up to six minutes in as little as three seconds.

Tandem has an outstanding record of meeting production targets. The new techniques and technologies, in addition to enabling us to build quality products at lower cost, strengthen our ability to meet constantly increasing demand for our products.

▲ *Participative management techniques developed at Tandem's Austin plant are being introduced successfully at other Tandem facilities. At Tandem's power supply manufacturing facility in California, workers use such techniques as this "focus group" meeting to improve performance. The result: a three-fold increase in productivity, lower costs, improved inventory management and enhanced product quality.*


TANDEM
PROD. NO.
TANDEM TV NETWORK
TXP INTRODUCTION
DATE OCTOBER 18, 1983



Tandem's effectiveness is due in large part to the cohesiveness that results from widespread individual understanding of company goals and how individual performance affects those goals. Much of the employees' understanding comes from our use of advanced techniques and technologies to foster communication and participation.

Creativity, Productivity, Contribution

Tandem's success results directly from the creativity, productivity and contribution of its people. As the company grows larger, a key challenge is facilitating communication within a multinational organization. Tandem is meeting that challenge by utilizing advanced techniques and technologies to foster communication and participation, and to manage the company.

Democratic management practices tap the creativity of employees at all levels and increase our productivity.

Written and electronic media augment personal contact to communicate information and to share ideas.

Tandem's own technology supports people in their jobs via one of the largest computer networks in the world. Our EXPAND network links more than 150 nodes, bringing applications programs and electronic mail to employees at Tandem's worldwide locations.

Along with our commitment to keep Tandem a good place to work, we also focus on the disciplines necessary to achieve growth while maintaining profitability.

Employee publications, including CENTER magazine, NonStop News and technical and marketing publications, distribute information about the company's activities, products, customers, philosophy and goals throughout the organization. Our electronic classrooms utilize videotape, computer programs and live broadcasts along with personal instruction to train employees. Tandem's management development program helps people and the company grow through course offerings in management skills with particular emphasis on communicating. The Tandem Television Network produces live, interactive broadcasts to 37 Tandem locations, bringing timely information about technical issues, our financial performance, programs and objectives, and other important activities within the company.

Along with striving to keep Tandem a good place to work, we also focus on the disciplines necessary to achieve growth while maintaining profitability. We continue to improve our control systems. Over the past year we have added key managers to emphasize critical planning and control functions. And we have seen the results in tremendously increased organizational strength.

Tandem's philosophy includes enabling all employees to participate in the financial success of the company. In addition to the benefits of a stimulating place to work and opportunities for contribution and recognition, employees have the opportunity to own Tandem stock. In fiscal 1983, through purchases of stock and exercises of stock options, employees contributed $25 million in cash to Tandem. The employees' level of participation in these stock ownership plans attests to the commitment and faith of our employees in the company's future.

Tandem Employee Productivity

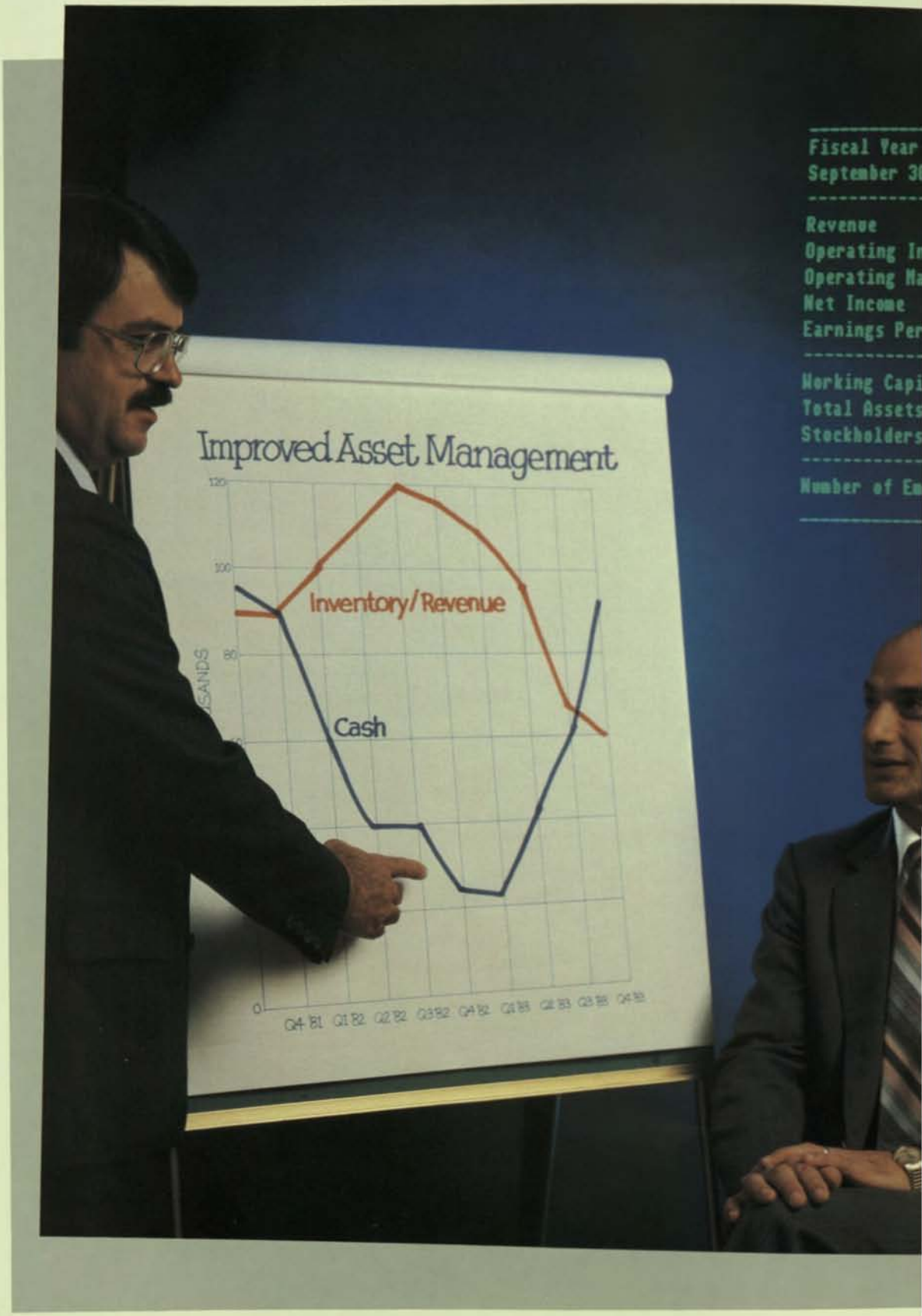
$ Thousands

1979	1980	1981	1982	1983
$87.9	$98.4	$101.2	$95.3	$101.8

Revenue per employee (avg. number of employees)

▲ *Tandem electronic classrooms utilize advanced techniques and technologies to instruct employees in comprehensive courses including sales, manufacturing, technology, professional and management development, and the Tandem philosophy.*

Announcement of an upcoming Tandem Outstanding Performers (TOPS) bonus trip to Hawaii was made during one of the many company-wide Tandem Television Network broadcasts during 1983. TOPS, one way that Tandem recognizes and rewards outstanding contributors, provides an opportunity for exceptional employees from all areas of the company to exchange ideas. ▶


Improved Asset Management
Inventory/Revenue
Cash
Fiscal Year
September 30
Revenue
Operating In
Operating Ma
Net Income
Earnings Per
Working Capi
Total Assets
Stockholders
Number of Em

HIGHLIGHTS

Ended	1983	1982	1981
	$418,282,000	$312,143,000	$208,397,000
ncome	$ 49,771,000	$ 40,708,000	$ 40,391,000
rgin	11.9%	13.0%	19.4%
	$ 30,805,000	$ 29,856,000	$ 26,549,000
Share	$.76	$.76	$.72
ital	$254,145,000	$194,761,000	$179,102,000
	$415,525,000	$337,366,000	$255,971,000
' Investment	$310,993,000	$250,988,000	$204,810,000
ployees	4,396	3,821	2,730

The company made major progress during 1983 in improving asset management through strengthened management systems. Among the results are a $15 million reduction in inventories and a $69 million increase in cash to a year-end cash balance of $94 million. Seen at far left is Lary Evans, vice president of manufacturing, meeting with (from left) Bob Marshall, senior vice president and chief operating officer; Jim Treybig, president and chief executive officer; and Jan Jensen, vice president, human resources.

As we look back in fiscal 1983, we believe that Tandem became a much stronger organization during the course of the year. Despite the fact that the economic recession continued to impact our customers and therefore impact Tandem, our revenues grew 34 percent. More importantly, this was a year when the Company strengthened its management organization, control systems, and asset management, while maintaining our emphasis on product development and marketing.

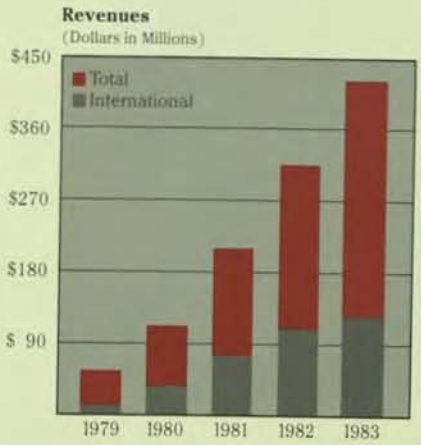
Shortly after the close of the fiscal year, we announced our innovative new computer system, the NonStop TXP. At the time of the announcement, the new machine was already in production and installed at four customer sites. Early customer response has been enthusiastic.

The NonStop TXP system is the most powerful machine in the world for on-line transaction processing. The 32-bit, multiple processor based TXP system provides users with two to three times the processing power of the NonStop II system, and reduces the cost per transaction by up to 50 percent. The TXP system achieves an unprecedented level of hardware and software compatibility. Our customers can even combine NonStop II processors and TXP processors within the same system. They can also run existing application programs on the TXP system.

With this addition to the product line, in 1984 we offer a full range of price-performance to address the complete spectrum of processing needs for our marketplace.

Strengthening our Operations

Our revenue growth rate exceeded that of most computer companies during this recessionary year; however, it was slower growth than Tandem had experienced in prior years. Tandem used this period of relatively slower growth to focus on internal operations, devoting time and effort to strengthening the organization in order to maximize our growth opportunities in the future. We believe that we have made Tandem a much stronger organization. Asset management has improved greatly. Better control of capital spending, inventory, and accounts receivable has contributed to a dramatic increase in our cash balance, which will help us fund our growth in the coming year.



Other internal developments during the year included a continuing emphasis on cost control measures instituted in November of 1982. We have programs in place to control hiring and salaries as well as discretionary spending. We initiated a new internal audit function to further identify ways to improve our systems and controls. In addition, we added David Rynne to our management staff as Vice President and Chief Financial Officer. Prior to joining Tandem, Mr. Rynne was with the Burroughs Corporation for 18 years where he held various finance positions, including most recently vice president and corporate controller.

In the manufacturing area, in addition to improving inventory control, we have also invested in automation and productivity. A new facility in Watsonville, California came on-line this year that is a state-of-the-art, fully automated board assembly and test facility. This plant will allow us to produce the majority of our board needs in a highly efficient facility. Our Austin, Texas terminal manufacturing plant uses a computer-aided manufacturing system that has resulted in a truly paperless factory. Manufacturing productivity was further enhanced by the in-house development of tools that use scan logic to improve product testing and reliability.

Our strong commitment to research and development continues. In product development over the past two years, Tandem has invested more than $70 million, greater than two times the amount invested during our entire previous corporate history. The most visible results of that investment are new products such as SNAX software that enables our EXPAND network users to access IBM SNA networks, devices, and applications programs while retaining the reliability and flexibility of NonStop systems; the FOX fiber optic extension that allows the connection of up to 14 closely proximate NonStop systems into a very high-speed information network; and the top-of-the-line NonStop TXP system.

Tandem invested extensively in technology as well. For example, this year we expanded our computer-aided design capability and opened an LSI lab for prototype chip development. Further, throughout the year, about 50 percent of our development people were working on enhancements to existing products, while the other 50 percent were developing new products that will be introduced in coming years.

We have continued to invest in marketing. In 1983 we inaugurated the Tandem Alliance, a new program to enhance our relationship with software houses. We also furthered our emphasis on major account marketing during the year. In addition to beginning some exciting new projects with existing customers, we increased our customer base by 126, with 47 new customers added in the fourth quarter. This has augmented our established position as a leader in the market for on-line transaction processing.

Financial Performance

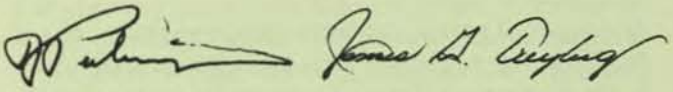
Some challenges remain. While revenue for the fiscal year ended September 30, 1983 grew 34 percent to $418,282,000 from $312,143,000 a year earlier, operating income increased 22.3 percent to $49,771,000 compared to $40,708,000 in fiscal 1982. Operating margins were under pressure this year due to increased cost of revenue. The combination of excess manufacturing capacity and the Company's successful inventory reduction program, which required lower production levels, resulted in substantially higher overhead costs being applied to products shipped. Earnings per share were $.76 in both years. Earnings per share were flat despite the increase in operating income due to lower net interest income and a higher effective tax rate. Although the Company's cash balances grew markedly during the year, much of this cash build-up occurred in the latter half of the year, so most interest-earning funds were only available part of the year. In addition, the prevailing interest rates were substantially lower than in the prior fiscal year.

Outlook

The people at Tandem worked with dedication and sacrifice to improve our operations while launching exciting new products and expanding our marketing efforts. We will continue to work hard to improve margins while emphasizing customer satisfaction and investing for our future growth. We feel we are in an excellent position to capitalize on improvements in the economy. While European operations continue to experience weak economic conditions and the adverse effects of the strong dollar, we believe we have seen a strengthening of the domestic economy. With the combination of outstanding employees, unique and innovative products, a high-potential marketplace, an impressive customer base, and a strengthened internal organization, we feel optimistic that fiscal 1984 will be a year of improved operating results.

Eugene Kleiner

Eugene Kleiner has decided not to stand for reelection as a director. Gene was instrumental in the formation and initial funding of the Company. He has served as a director since the Company's founding and has been a significant factor in its success. We will miss him.



Thomas J. Perkins
Chairman of the Board

James G. Treybig
President and
Chief Executive Officer

December 1, 1983

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

SELECTED FINANCIAL DATA

For the Five Years Ended September 30, 1983

(In thousands except per share amounts)	1983	1982	1981	1980	1979
Revenue	$418,282	$312,143	$208,397	$108,989	$ 55,974
Cost of revenue	168,708	109,305	75,547	40,831	20,786
Product development	39,168	33,642	17,833	8,786	4,654
Marketing, general and administrative	160,635	128,488	74,626	40,049	20,828
Operating Income	49,771	40,708	40,391	19,323	9,706
Interest income, net	730	6,033	10,707	1,759	398
Provision for income taxes	(19,696)	(16,885)	(24,549)	(10,395)	(5,184)
Net Income	$ 30,805	$ 29,856	$ 26,549	$ 10,687	$ 4,920
Earnings Per Share	$ .76	$ .76	$ .72	$ .35	$ .20
Total assets	$415,525	$337,366	$255,971	$ 95,701	$ 45,947
Long term debt and capitalized lease obligations	23,957	21,102	2,054	1,651	1,144
Stockholders' investment	310,993	250,988	204,810	70,294	31,530

Overview

Tandem Computers is committed to being a technological leader in the rapidly growing market for on-line transaction processing systems and networks of on-line systems. Achieving the Company's technological leadership goal involves many factors, including strategic market positioning, an ongoing commitment to product development, and an organizational structure and philosophy that fosters employee productivity and creativity. It is also critical to maintain a financial position and operating record that allow the Company to maximize its performance in an environment of rapid growth.

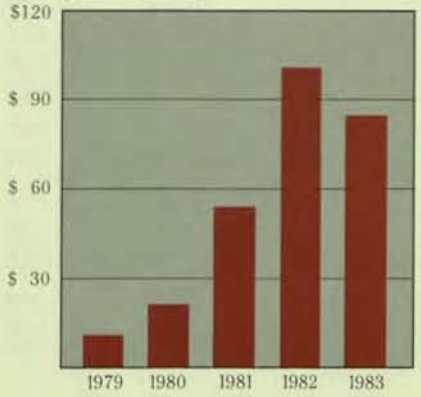
Financial Condition

Maintaining a sound financial position is a high priority within Tandem. The Company's financial condition improved significantly in 1983 as a result of the emphasis placed on asset management. Inventory levels declined, and accounts receivable grew at a rate substantially below that of revenue growth. Capital spending was held to a conservative level. As a consequence of improved asset management, along with employee purchases of stock and funds generated from operations, cash and cash investments increased by $68,685,000, to $93,501,000 as of September 30, 1983.

An important part of Tandem's corporate philosophy is to provide all employees with the opportunity to share in the Company's financial success by means of stock ownership. As a result of employee participation in the employee stock purchase program and exercises of stock options, the Company generated $25,031,000 in cash in fiscal 1983, $12,249,000 in fiscal 1982, and $9,669,000 in fiscal 1981.

The Company's financial strategy also includes maintaining a sound ratio of current assets to current liabilities and a conservative capital structure. At the end of fiscal 1983, the current ratio was 5.5:1, long term debt and capitalized lease obligations were 7.7 percent of total capital, unused revolving lines of credit totaled $67,117,000, and the Company's equity base was $310,993,000. Tandem believes this strategy provides it with maximum near term and long term flexibility to consider the full range of financing alternatives to fund the capital needs of its projected future growth.

Inventories
(Dollars in Millions)



Results of Operations

The table below summarizes the changes in selected operating indicators for the fiscal years presented. The numbers on the left account for the revenue dollar by showing various income and expense items as a percentage of revenue. The numbers on the right measure the yearly percentage increases (decreases) in the same items.

% of Revenues				% Increase (Decrease)		
1983	1982	1981		1983	1982	1981
100	100	100	Revenue	34	50	91
40	35	36	Cost of revenue	54	45	85
9	11	9	Product development	16	89	103
38	41	36	Marketing, general and administrative	25	72	86
12	13	19	Operating income	22	1	109
—	2	5	Interest (net)	(88)	(44)	509
12	15	25	Pretax income	8	(9)	106
5	5	12	Provision for taxes	17	(31)	136
7	10	13	Net income	3	12	148
			Earnings per share	0	6	106
			Weighted average shares outstanding	4	6	22

Numbers may not total due to rounding.

Revenue

Tandem Computers' revenue gains over the last three years have resulted directly from increased shipments of its computer hardware and software products to new and existing customers, and from increases in the number of customers using its support and training services. In both fiscal 1982 and 1983, the Company's revenue growth was affected by economic recession, leading to a slowing of revenue growth in certain geographic regions.

During fiscal 1983, the Company shipped 1,773 processors to 509 customers, compared with 1,542 processors to 483 customers in fiscal 1982, and 1,210 processors to 436 customers in fiscal 1981. The fourth quarter of fiscal 1983 was a particularly strong period for new customer generation, with 47 new customers added. To date, the Company has 5,824 processors installed with 725 customers.

International revenue grew at a slower rate than domestic revenue in fiscal 1983. Foreign revenue accounted for 30.3 percent of total revenue for fiscal 1983, compared to 33.5 percent and 34.3 percent for fiscal 1982 and 1981, respectively.

Operating Income

Operating margins of 12 percent in fiscal 1983 were below the Company's target range of 16 to 20 percent. The principal reason was that cost of revenue as a percent of revenue increased in fiscal 1983, due to higher costs relating to excess capacity, and to the effects of lower production rates resulting from our successful program to reduce inventory levels. Partly offsetting these higher costs was our significant improvement in manufacturing productivity, which enabled the Company to reduce manufacturing employment by six percent.

The Company targets product development expenditures in the range of 9 to 10 percent of revenue. Tandem's product development effort focuses on meeting the needs of computer users who are implementing on-line systems, both at single sites and in geographically distributed on-line information processing networks. The Company believes that the opportunities for technological innovation in this marketplace are enormous. Product development funds are being invested in enhancements to existing products and in important new products that will be introduced in future years.

The Company keys its marketing strategy on selling to users who are implementing major on-line applications. Providing a high level of service and support is essential to meeting the needs of this customer base. To maximize its long-term opportunities in this marketplace, Tandem has built a direct selling and support organization in the United States and, primarily through wholly-owned subsidiaries, in industrial markets throughout the world. The Company's marketing, general and administrative expenditures in fiscal 1983 were lower as a percent of revenue than in fiscal 1982, but were approximately in line on a percentage basis with the pattern of fiscal 1981 and prior years. Looking ahead, the Company believes that it is essential to invest in marketing in order to achieve future growth. A rate of expenditure on marketing and support similar to that experienced in fiscal 1983 and 1981 will be required to compete successfully in its marketplace.

Net Income and Earnings Per Share

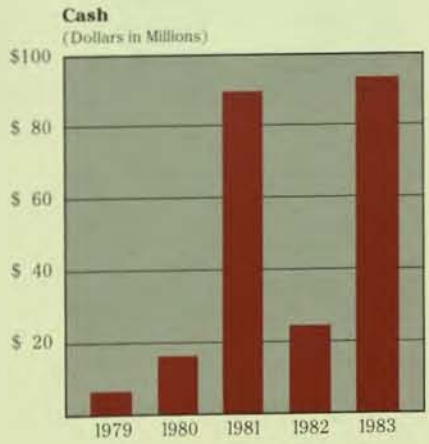
Net income growth has differed from operating income growth over the past three fiscal years because of substantial changes in the Company's net interest income and effective tax rate. Operating income grew faster than net income in fiscal 1983 due to a substantial decline in net interest income and a higher tax rate, compared with fiscal 1982. Over the course of fiscal 1983, the Company has increased its cash balances from $24,816,000 at the end of fiscal 1982 to $93,501,000 at the end of the current fiscal year. Interest income has been earned on these balances. Because the majority of the increase in cash and cash investment balances occurred in the latter part of the fiscal year, and because debt obligations are primarily at higher fixed rates, net interest income was modest. Further, the rate at which interest was earned was lower than in the two previous fiscal years.

The Company's effective tax rate was 39 percent in fiscal 1983, compared with 36 percent in 1982 and 48 percent in 1981. The increase in effective tax rate versus 1982 is largely due to the reduced beneficial impact of tax incentives for investment in capital equipment resulting from the Tax Equity and Fiscal Responsibility Act of 1982. The fiscal 1982 tax rate decrease versus fiscal 1981 was attributable primarily to the tax incentives provided by the Economic Recovery Tax Act of 1981 for research and development expenditures and investment in capital equipment.

Earnings per share were flat versus 1982, while net income grew slightly. The difference is due to increases in weighted average shares outstanding. The Company's public offering of common stock in fiscal 1981, combined with sales of stock to employees under the stock purchase plan and grants under option plans, resulted in increases in weighted average shares outstanding of four percent in 1983, six percent in 1982, and 22 percent in 1981. Proceeds from the sale of these additional shares have been used to finance the capital expansion required to support the Company's growth during this period.

Effect of Inflation

See page 39 of this report for a discussion of the effect of changing prices on the Company's operations.



CONSOLIDATED STATEMENT OF INCOME

For the Three Years Ended September 30, 1983

(In thousands except per share amounts)	1983	1982	1981
Revenue			
Product revenue	$360,133	$272,591	$186,897
Service and other revenue	58,149	39,552	21,500
Total Revenue	418,282	312,143	208,397
Costs and Expenses			
Cost of revenue	168,708	109,305	75,547
Product development	39,168	33,642	17,833
Marketing, general and administrative	160,635	128,488	74,626
Total costs and expenses	368,511	271,435	168,006
Operating Income	49,771	40,708	40,391
Interest expense	(2,806)	(967)	(282)
Interest income	3,536	7,000	10,989
Income Before Income Taxes	50,501	46,741	51,098
Provision for income taxes	(19,696)	(16,885)	(24,549)
Net Income	$ 30,805	$ 29,856	$ 26,549
Earnings Per Share	$ .76	$ .76	$ .72
Weighted average shares outstanding	40,784	39,221	37,025

The accompanying notes are an integral part of this statement.

CONSOLIDATED BALANCE SHEET

As of September 30, 1983 and 1982

(In thousands except per share amounts)	1983	1982
Assets		
Current Assets		
Cash and cash investments	$ 93,501	$ 24,816
Accounts receivable, net of allowances of $2,851 in 1983 and $3,000 in 1982	119,558	98,810
Inventories	85,920	101,335
Prepaid expenses and other	11,775	17,013
Total current assets	310,754	241,974
Property, Plant and Equipment, At Cost		
Land	3,127	4,441
Machinery and equipment	35,162	25,767
Computer equipment and spares	59,836	44,274
Leasehold improvements	27,859	21,788
Construction in process	6,788	11,196
	132,772	107,466
Accumulated depreciation and amortization	(33,991)	(18,080)
Net property and equipment	98,781	89,386
Other Assets	5,990	6,006
Total Assets	$415,525	$337,366

Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of capitalized lease obligations	$ 3,335	$ 2,060
Accounts payable	27,960	22,918
Accrued liabilities:		
Wages, payroll taxes, and employee benefits	14,081	8,913
Income taxes	4,971	7,136
Other accrued liabilities	6,262	6,186
Total current liabilities	56,609	47,213
Capitalized Lease Obligations	15,434	10,378
Long Term Debt	8,523	10,724
Deferred Income Taxes	23,966	18,063
Stockholders' Investment		
Common stock $.025 par value, authorized 60,000,000 shares, outstanding 39,552,963 in 1983 and 37,634,754 in 1982	989	941
Additional paid-in capital	206,911	177,759
Retained earnings	103,093	72,288
Total stockholders' investment	310,993	250,988
Total Liabilities and Stockholders' Investment	$415,525	$337,366

The accompanying notes are an integral part of this balance sheet.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' INVESTMENT

For the Three Years Ended September 30, 1983

(In thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Total
Balance September 30, 1980	30,075	$251	$ 53,555	$ 16,488	$ 70,294
Sale of common stock, net of related expenses	4,500	38	95,995	—	96,033
Sale of common stock under stock option plans	1,692	15	7,381	—	7,396
Sale of common stock under stock purchase plan	143	1	2,272	—	2,273
Capitalization of retained earnings for three-for-one stock split	—	605	—	(605)	—
Tax benefit from employee transactions in common stock	—	—	2,265	—	2,265
Net income	—	—	—	26,549	26,549
Balance September 30, 1981	36,410	910	161,468	42,432	204,810
Sale of common stock under stock option plans	863	22	5,028	—	5,050
Sale of common stock under stock purchase plan	362	9	7,190	—	7,199
Tax benefit from employee transactions in common stock	—	—	4,073	—	4,073
Net income	—	—	—	29,856	29,856
Balance September 30, 1982	37,635	941	177,759	72,288	250,988
Sale of common stock under stock option plans	1,634	41	19,054	—	19,095
Sale of common stock under stock purchase plan	284	7	5,929	—	5,936
Tax benefit from employee transactions in common stock	—	—	4,169	—	4,169
Net income	—	—	—	30,805	30,805
Balance September 30, 1983	39,553	$989	$206,911	$103,093	$310,993

The accompanying notes are an integral part of this statement.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Three Years Ended September 30, 1983

(In thousands)	1983	1982	1981
Funds (Cash and cash investments) at beginning of period	$ 24,816	$ 89,806	$ 16,245
Provided from Operations			
Sources:			
Net income	30,805	29,856	26,549
Depreciation and amortization	18,836	10,196	4,107
Deferred income taxes	5,903	9,920	4,818
Net book value of property, plant and equipment sold or retired	14,408	2,142	1,264
Total sources	69,952	52,114	36,738
Uses:			
Accounts receivable	20,748	28,139	28,119
Inventories	(15,415)	46,792	33,642
Net change in prepaid expenses and non-debt current liabilities	(13,359)	7,096	(17,246)
Investment in property, plant and equipment	42,222	65,819	27,238
Increase in other assets	401	6,006	—
Total uses	34,597	153,852	71,753
Net provided from (used in) operations	35,355	(101,738)	(35,015)
Provided from External Financings			
Net increase in capitalized leases	6,331	9,702	609
Increase (decrease) in long term debt, net	(2,201)	10,724	—
Sale of common stock, net of related expenses	—	—	96,033
Sale of common stock under employee stock option and stock purchase plans	25,031	12,249	9,669
Tax benefit from employee transactions in common stock	4,169	4,073	2,265
Total provided from external financings	33,330	36,748	108,576
Funds (Cash and cash investments) at end of period	$ 93,501	$ 24,816	$ 89,806

The accompanying notes are an integral part of this statement.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Consolidation
The consolidated financial statements include the accounts of Tandem Computers Incorporated and its wholly owned subsidiaries after elimination of intercompany accounts and transactions.

Revenue Recognition
The Company generally recognizes revenue from equipment sales at the time of shipment. Service and other revenue are recognized ratably over the contractual period or as the services are provided.

Exchange Gains and Losses
Foreign exchange and translation gains and losses are not significant and are reflected in the results of operations.

Inventories
Inventories are stated at the lower of cost (first-in, first-out) or market and include materials, labor, and manufacturing overhead. The components of inventories as of September 30 were:

(In Thousands)	1983	1982
Purchased parts and subassemblies	$36,887	$ 56,822
Work-in-process	12,519	13,413
Finished goods	36,514	31,100
Total	$85,920	$101,335

Income Taxes
The Company provides for income taxes on total DISC income and accounts for investment and research and development tax credits as a reduction of the provision for income taxes in the year in which the related credits are realized.

Property, Plant and Equipment
Systems spares ($19,271,000 in 1983 and $15,869,000 in 1982) are depreciated over a five-year period using the double declining balance method. All other property, plant and equipment are depreciated using the straight-line method. The estimated useful lives are:

Machinery and equipment	5-10 years
Computer equipment and spares	5- 7 years
Leasehold improvements	Lease term

Earnings Per Share
Earnings per common share have been computed based upon the weighted average number of common and common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options outstanding that have a dilutive effect when applying the treasury stock method. Fully diluted earnings per share are substantially the same as reported earnings per share.

2. Income Taxes

The provision for income taxes included the following deferred (prepaid) items:

(In thousands)	1983	1982	1981
Current Federal	$ 1,370	$ 5,516	$15,356
Current State	1,532	3,633	3,771
Current Foreign	4,621	2,244	1,401
	7,523	11,393	20,528
Prepaid Federal	4,731	(3,333)	(1,205)
Prepaid State	309	(253)	(180)
Prepaid Foreign	1,230	(842)	588
	6,270	(4,428)	(797)
Deferred Federal	5,843	6,656	4,325
Deferred State	225	239	194
Deferred Foreign	(165)	3,025	299
	5,903	9,920	4,818
Total Provision	$19,696	$16,885	$24,549

Sources of deferred (prepaid) taxes were as follows:

(In thousands)	1983	1982	1981
Installment sale method for income tax reporting	$ 8,572	$ 3,657	$ —
Expenses recognized for financial statements, but not for income tax reporting	810	(1,505)	(897)
Effect of intercompany profit eliminations	(4,143)	(2,654)	(2,522)
Other items	1,031	(3,926)	2,622
Total Prepaid	$ 6,270	$(4,428)	$ (797)
DISC income	$ 3,181	$ 3,918	$ 3,230
Accelerated depreciation	2,628	2,799	1,192
Other items	94	3,203	396
Total Deferred	$ 5,903	$ 9,920	$ 4,818

The provision for income taxes differs from the amount obtained by applying the Federal statutory income tax rate to income before taxes as follows:

	1983	1982	1981
Federal statutory tax rate	46%	46%	46%
State taxes, net of Federal income tax benefit	4	4	4
Investment tax credits	(4)	(8)	(3)
Research and development tax credits	(7)	(8)	(1)
Other	—	2	2
Effective Tax Rate	39%	36%	48%

3. Lease and Other Commitments

The Company leases its headquarters, operating facilities, field offices, and automobiles under operating lease agreements. The Company also has capitalized leases for certain equipment. Future lease payments as of September 30, 1983 are as follows:

(In thousands)	Leases	
Fiscal Year	Operating	Capital
1984	$ 29,856	$ 5,764
1985	27,325	5,632
1986	25,448	5,391
1987	22,815	5,140
1988	21,135	3,915
Thereafter	130,840	—
Total minimum lease payments	$257,419	25,842
Less: Amount representing interest (4%-17%)		7,073
Present value of minimum lease payments		$18,769

Capitalized leases totaling $22,038,000 and $12,999,000 are included in the machinery and equipment and computer equipment and spares classification on the Balance Sheet at September 30, 1983 and 1982, respectively.

Rent expenses were $30,458,000 in 1983, $20,895,000 in 1982, and $8,908,000 in 1981.

4. Long Term Debt

Long term debt as of September 30 consists of the following:

(In thousands)	1983	1982
Construction financing	$ 4,203	$ 8,724
Industrial revenue bonds bearing interest of 12% to 12-3/8%, due 1992, collateralized by equipment in Austin, Texas	2,000	2,000
15% promissory note payable in annual installments through 1986	1,640	—
Other, bearing average interest of 8.6%	680	—
	$ 8,523	$10,724

Construction financing at September 30, 1983 is related to a facility in Austin, Texas. During June 1983, the Company retired $7,125,000 of construction financing relating to a facility in Watsonville, California pursuant to a sales/leaseback transaction. The associated lease has been accounted for as an operating lease. Interest costs of $644,000 and $508,000 relating to these construction projects were capitalized during fiscal 1983 and 1982, respectively.

The Company has entered into unsecured credit agreements totaling $72,000,000 with several banks. The agreements provide for revolving borrowings through various dates in 1984 and 1985, at which time outstanding amounts may be converted into term loans repayable in equal quarterly installments through 1987. Domestic borrowings bear interest at or below the banks' prime rates during the revolving period and approximately 1/4% above these rates during the term period. The Company is required to pay a commitment fee of 3/8% per annum. Of these facilities, $22,000,000 have been earmarked by Tandem for the construction referred to above. The remaining $50,000,000 are for working capital purposes and contain provisions for Eurocurrency and foreign local currency borrowings at interest rates prevailing in these markets. There are no compensating balances required under any of these arrangements.

Certain financial covenants and restrictions are included in the loan agreements, including a restriction on payment of cash dividends. The Company was in compliance with all such covenants and restrictions at September 30, 1983.

5. Preferred and Common Stock

Preferred Stock
The Company has 2,400,000 shares of preferred stock authorized.

Stock Option Plans
The Company has employee stock option plans under which permanent employees may be granted options to purchase shares at 100% of fair market value at the time of the grant. Options generally become exercisable six months after the effective date and expire no later than seven years after the effective date. At the discretion of the Company, options granted under the stock option plans may qualify for Incentive Stock Option treatment under the Economic Recovery Tax Act of 1981.

As of September 30, 1983 options for 4,516,866 shares were outstanding at prices ranging from $3.92 to $29.13, with an average price of $19.75. Options for 4,169,216 shares were exercisable as of September 30, 1983. Options for 4,521,639 shares are available for future grant. Options were exercised at prices ranging from $.58 to $26.88 in 1983, $.17 to $26.88 in 1982, and $.08 to $22.88 in 1981.

Employee Stock Purchase Plan

As of September 30, 1983 the Company has reserved 2,608,040 shares for future issuance under its employee stock purchase plan. Under the plan, the Company may offer shares to employees by two methods. Under one method, eligible employees may elect to purchase shares of common stock at 85% of fair market value as of the beginning or end of a three-month offering period. Under the second method, the Company may grant to employees the option to purchase common stock at not less than 85% of fair market value at the grant date. As of September 30, 1983 options to purchase 30,800 common shares at $26.90 and 204,500 common shares at $12.43 were outstanding under the second method. Such options are exercisable through January 29, 1984 and through November 15, 1984, respectively.

6. Geographic Segment Information

The following table sets forth information about the Company's operations in different geographic regions for the three years ended September 30, 1983.

	Geographic Area			Adjustments	
(In thousands)	United States	Europe	Other	and Eliminations	Consolidated
1983					
Revenue-Customer	$297,722	$91,100	$29,460	$ –	$418,282
Revenue-Intercompany	68,001	–	–	(68,001)	–
Revenue-Total	365,723	91,100	29,460	(68,001)	418,282
Pre-Tax Income	49,084	11,546	(1,127)	(9,002)	50,501
Identifiable Assets	336,193	73,923	26,058	(20,649)	415,525
1982					
Revenue-Customer	$215,154	$74,958	$22,031	$ –	$312,143
Revenue-Intercompany	60,126	–	–	(60,126)	–
Revenue-Total	275,280	74,958	22,031	(60,126)	312,143
Pre-Tax Income	43,949	9,267	22	(6,497)	46,741
Identifiable Assets	276,886	56,685	15,863	(12,068)	337,366
1981					
Revenue-Customer	$144,392	$47,294	$16,711	$ –	$208,397
Revenue-Intercompany	37,580	–	–	(37,580)	–
Revenue-Total	181,972	47,294	16,711	(37,580)	208,397
Pre-Tax Income	50,297	4,145	2,139	(5,483)	51,098
Identifiable Assets	213,693	34,592	12,471	(4,785)	255,971

Intercompany transfers are made at approximately arm's length prices, which include manufacturing profits attributable to United States operations. Identifiable assets are those assets of the Company that are identified with the operations of the corresponding geographic area. United States customer revenue includes export sales of $6,400,000 in 1983; $7,687,000 in 1982; and $7,397,000 in 1981.

7. Unaudited Quarterly Financial Data

(In thousands except per share amounts)	Quarters Ended Dec. 31	Mar. 31	June 30	Sept. 30
Year ended September 30, 1983:				
Revenue	$94,135	$96,006	$110,291	$117,850
Costs and Expenses				
Cost of revenue	37,955	37,856	45,117	47,780
Product development	8,997	9,805	9,961	10,405
Marketing, general and administrative	35,548	37,945	41,561	45,581
Total costs and expenses	82,500	85,606	96,639	103,766
Operating Income	11,635	10,400	13,652	14,084
Interest income, net	47	(184)	251	616
Income Before Income Taxes	11,682	10,216	13,903	14,700
Provision for income taxes	4,556	3,765	5,462	5,913
Net Income	$ 7,126	$ 6,451	$ 8,441	$ 8,787
Earnings Per Share	$ .18	$ .16	$ .21	$ .21
Year ended September 30, 1982:				
Revenue	$70,985	$74,101	$ 79,823	$ 87,234
Costs and Expenses				
Cost of revenue	25,181	26,657	26,968	30,499
Product development	6,816	7,733	9,200	9,893
Marketing, general and administrative	27,636	31,277	33,162	36,413
Total costs and expenses	59,633	65,667	69,330	76,805
Operating Income	11,352	8,434	10,493	10,429
Interest income, net	2,302	1,306	1,489	936
Income Before Income Taxes	13,654	9,740	11,982	11,365
Provision for income taxes	5,866	3,518	4,469	3,032
Net Income	$ 7,788	$ 6,222	$ 7,513	$ 8,333
Earnings Per Share	$ .20	$ .16	$ .19	$ .21

8. Information on the Effects of Inflation
(Unaudited)

The Company has provided an adjusted summary of operations and selected financial data in accordance with the Financial Accounting Standards Board in its Statement No. 33 concerning "Financial Reporting and Changing Prices." This guideline requires that inflation-adjusted information be computed using two methods, "constant dollar" and "current cost." This disclosure requirement is experimental and involves considerably more judgment than traditional financial statements, and therefore should be reviewed with caution.

Under the "constant dollar" method, historical results are restated into dollars having the same purchasing power as measured by the Consumer Price Index for All Urban Consumers (CPI-U). The "current cost" method requires the Company to adjust asset values based on specific indices and appraisals.

Neither method allows for inflation adjustments to operating expenses, revenue or net interest income, nor an adjustment to the tax provision, despite the decrease in pretax income which results from the inflation adjustments of the two methods. Only the cost of revenue and depreciation expense related to assets, which are restated for inflation effects, are adjusted.

For both methods, depreciation is computed on a straight-line basis, rather than the accelerated basis that is used for some assets in the Company's historical financial statements, because the accelerated method already recognizes some of the effects of inflation.

Net income for fiscal 1983 was lower under both methods because of higher depreciation and amortization expense. As a result of higher asset values under the inflation-adjusted methods, depreciation and amortization expenses were also higher. Companies who hold monetary assets during a period of inflation lose purchasing power. Tandem held net monetary assets during the period, and their purchasing power declined.

Of the two methods, the Company believes that the current cost method more accurately reflects the impact of inflation on Tandem. The CPI-U used in the constant dollar method contains items unrelated to the nature of the Company's business, and also does not attempt to measure the impact of inflation on its foreign operations.

CONSOLIDATED STATEMENT OF INCOME ADJUSTED FOR INFLATION
FOR THE YEAR ENDED SEPTEMBER 30, 1983

(In thousands except per share amounts)	In Average 1983 Dollars		
	Historic Cost	Constant Dollar	Current Cost
Total Revenue	$418,282	$418,282	$418,282
Cost of revenue, excluding depreciation and amortization	165,352	169,555	165,352
Other costs and expenses, excluding depreciation and amortization	184,323	184,323	184,323
Depreciation and amortization	18,836	20,852	20,305
Interest (income), net	(730)	(730)	(730)
Provision for income taxes	19,696	19,696	19,696
Net income	$ 30,805	$ 24,586	$ 29,336
Earnings Per Share	$ .76	$ .60	$ .72
Net Assets at Year-end	$310,993	$312,887	$312,434
Decrease in purchasing power of net monetary items		$ 2,816	$ 2,816
Increase in value of inventories, property, plant and equipment held during the year:			
Measured in general prices			$ 5,040
Measured in specific prices			3,889
Excess of increase in general price level (constant dollars) over increase in specific prices			$ 1,151

At September 30, 1983, current cost of inventory was $85,968 and current cost of property, plant and equipment net of accumulated depreciation was $105,628.

FIVE YEAR COMPARISON OF SELECTED FINANCIAL DATA ADJUSTED FOR INFLATION
(Revenue dollars in thousands)

	In Average 1983 Dollars				
	1983	1982	1981	1980	1979
Total revenue Constant dollars	$418,282	$322,948	$231,648	$134,543	$78,496
Market price per share at end of period Constant dollar	$ 34.77	$ 22.95	$ 29.13	$ 20.67	$ 7.50
Average CPI (1967=100)	295.9	286.0	266.2	239.7	211.0

AUDITORS' REPORT

To Tandem Computers Incorporated:

We have examined the consolidated balance sheet of Tandem Computers Incorporated (a Delaware corporation) and subsidiaries as of September 30, 1983 and 1982, and the related consolidated statements of income, stockholders' investment, and changes in financial position for each of the three years in the period ended September 30, 1983. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Tandem Computers Incorporated and subsidiaries as of September 30, 1983 and 1982, and the results of their operations and the changes in their financial position for each of the three years in the period ended September 30, 1983, all in conformity with generally accepted accounting principles applied on a consistent basis.

San Jose, California
November 9, 1983

Arthur Andersen & Co.

TANDEM STOCK PRICE

Calendar Quarter Price	High	Low
1983 3rd Quarter	36-1/2	26
2nd Quarter	34	25-1/2
1st Quarter	30-1/2	23-5/8
1982 4th Quarter	32-3/4	21-3/4
3rd Quarter	25-3/8	14-1/2
2nd Quarter	29	22
1st Quarter	28-1/2	21
1981 4th Quarter	34	27-1/4
3rd Quarter	32	24
2nd Quarter	34-5/8	24-3/4
1st Quarter	25-1/2	20-1/2

Tandem Computers Incorporated has been traded via the NASDAQ National Market System under the trading symbol TNDM since the second calendar quarter of 1982. Beginning in the second quarter of 1982, the quotations represent the high and low sales prices. Quotations that pertain to earlier periods represent prices between dealers without adjustment for mark-up, markdown, or commissions and may not represent actual transactions. All prices have been adjusted for stock splits. No dividends have been declared on the common stock.

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Board of Directors

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Chairman of the Board; Partner,
Kleiner, Perkins, Caufield & Byers

Morton Collins,
Partner, DSV Partners III

Thomas J. Davis, Jr.,
Partner, Mayfield II

Franklin P. Johnson, Jr.,
Chairman, Asset Management
Capital Company

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& Byers

Robert C. Marshall,
Senior Vice President and Chief
Operating Officer, Tandem
Computers Incorporated

John B.M. Place,
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Chief Executive Officer,
Crocker National Corporation

Robert G. Stone, Jr.,
Chairman of the Board,
Kirby Exploration Company

James G. Treybig,
President and Chief Executive Officer,
Tandem Computers Incorporated

Auditors

Arthur Andersen & Co.,
San Jose, California

Registrar and Transfer Agent

Bank of America N.T. & S.A.,
San Francisco, California

Form 10-K

A copy of the company's Form 10-K,
as filed with the Securities and
Exchange Commission, is available
on written request. Please direct
request to:

Treasurer's Office
Tandem Computers Incorporated
19333 Vallco Parkway
Cupertino, California 95014-2599

Annual Meeting

The annual meeting of stockholders
will be held at 10:00 a.m. on Friday,
February 10, 1984, at the corporation's
headquarters.

Tandem

Corporate Headquarters
19333 Vallco Parkway
Cupertino, California 95014-2599
(408) 725-6000

Trademark

Tandem, NonStop, NonStop II,
NonStop TXP, ENCOMPASS, ENFORM,
EXPAND, TRANSFER and TXP are trade-
marks and service marks of Tandem
Computers Incorporated. INFOSAT is
a joint trademark of Tandem and
American Satellite Company.

Officers

James G. Treybig,
President and Chief Executive Officer

Robert C. Marshall,
Senior Vice President and
Chief Operating Officer

Michael K. Bateman,
Vice President and Division Manager

Thomas A. Bechler,
Vice President and Division Manager

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European Division

George Eckert,
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Vice President, Manufacturing

Jan E. Jensen,
Vice President, Human Resources

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Vice President, Hardware Development

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Vice President,
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Vice President, MIS

David J. Rynne,
Vice President and
Chief Financial Officer

Stephen C. Schmidt,
Vice President, Strategic Planning and
Product Management

Jeanne D. Wohlers,
Vice President-Finance,
Treasurer, and Assistant Secretary

Charles J. Yazel,
Vice President and Division Manager

Domestic Sales and Service Offices

ARIZONA, Phoenix

ARKANSAS, Little Rock

CALIFORNIA, Culver City, Irvine,
Long Beach, Los Angeles, Orinda,
Riverside, Sacramento, San Diego,
San Francisco, Santa Clara,
Universal City

COLORADO, Englewood

CONNECTICUT, Hartford, Stamford

FLORIDA, Jacksonville, Miami,
Tampa, Winter Park

GEORGIA, Atlanta

HAWAII, Honolulu

ILLINOIS, Chicago, Itasca, Oakbrook,
Schaumburg

INDIANA, Indianapolis

IOWA, Cedar Rapids, Des Moines

KANSAS, Overland Park

LOUISIANA, Metairie

MARYLAND, Linthicum

MASSACHUSETTS, Newton

MICHIGAN, Ann Arbor, Grand Rapids,
Livonia

MINNESOTA, Minneapolis

MISSOURI, Maryland Heights

NEBRASKA, Omaha

NEVADA, Las Vegas

NEW JERSEY, Cardiff City, Hasbrouck
Heights

NEW MEXICO, Albuquerque

NEW YORK, Jericho, New York City,
Pittsford

NORTH CAROLINA, Charlotte,
Greensboro

OHIO, Cincinnati, Cleveland,
Columbus

OKLAHOMA, Oklahoma City, Tulsa

OREGON, Portland

PENNSYLVANIA, Horsham, Pittsburgh

TENNESSEE, Memphis

TEXAS, Austin, Dallas, Fort Worth,
Houston

UTAH, Salt Lake City

VIRGINIA, Falls Church, Reston,
Richmond

WASHINGTON, Bellevue

WEST VIRGINIA, Charleston

WISCONSIN, Brookfield

International Subsidiaries

AUSTRALIA
Tandem NonStop Pty, Ltd
Adelaide, Brisbane, Melbourne,
Perth, Sydney

BELGIUM
Tandem Computers SA/NV
Brussels

CANADA
Tandem Computers Canada LTD
Montreal, Ottawa, Toronto,
Vancouver

DENMARK
Tandem Computers A/S
Taastrup

FRANCE
Tandem Computers S.A.
Rungis-Cedex

GERMANY
Tandem Computers GMBH
Dortmund, Duesseldorf, Frankfurt,
Hamburg, Mannheim, Munich,
Stuttgart

HONG KONG
Tandem Computers Hong Kong LTD.
Kowloon

ITALY
Tandem Computers Italia S.P.A.
Milan, Rome

JAPAN
Tandem Computers Japan LTD
Nagoya, Osaka, Tokyo

THE NETHERLANDS
Tandem Computers BV
The Hague

NEW ZEALAND
Tandem NONSTOP Pty. Ltd.
Wellington

NORWAY
Tandem Computers A/S
Hovik

SINGAPORE
Tandem Computers Int'l Inc.
Singapore

SWEDEN
Tandem Computers AB
Malmoe, Solna

SWITZERLAND
Tandem Computers A.G.
Zurich

UNITED KINGDOM
Tandem Computers LTD
Birmingham, High Wycombe, London,
Northolt, Rochdale

International Distributors

ARGENTINA

BAHRAIN

FINLAND

GREECE

ISRAEL

KOREA

KUWAIT

MEXICO

PHILIPPINES

SAUDI ARABIA

TAIWAN

UNITED ARAB EMIRATES

VENEZUELA

TANDEM COMPUTERS ANNUAL REPORT 1984

Tandem Computers Incorporated designs, develops, manufactures, markets and supports a family of unique computer systems for on-line transaction processing. The Tandem NonStop system concept provides the first on-line, distributed computer architecture for mainstream business applications. Customers' systems are supported from over 100 locations throughout North America, Europe, Asia and the Pacific. The Company operates five manufacturing facilities in the United States and one in Germany.

THE YEAR

Nineteen Eighty-Four was a year of significant accomplishments at Tandem. Our revenues grew 27%. Earnings, with a one-time tax benefit, increased 39%. And we ended the year with a strong balance sheet – including $107 million in cash, the highest level in our history.

Since our first product shipment in 1976, our annual revenues have grown to over a half billion dollars. During 1984 we joined the ranks of the *Fortune* 500 largest U.S. industrial corporations.

We significantly expanded our customer base and our installed base of processors during the year. The addition of the new high-performance TXP system to our family of NonStop systems made a major contribution to this expansion. Introduced in the first month of the fiscal year, TXP processors accounted for over half of all shipments for the full year.

We took action to improve our business. In the fourth quarter we laid the foundation for increasing profits and continuing growth. *Our first priority is increased profitability.* ▶

HIGHLIGHTS

Fiscal Year Ended September 30	1984	1983	1982
Revenue	$532,620,000	$418,282,000	$312,143,000
Operating income	$ 51,101,000	$ 49,771,000	$ 40,708,000
Operating margin	9.6%	11.9%	13.0%
Net income	$ 42,908,000	$ 30,805,000	$ 29,856,000
Earnings per share	$1.04	$.76	$.76
Working capital	$263,403,000	$254,145,000	$194,761,000
Total assets	$501,873,000	$415,525,000	$337,366,000
Stockholders' investment	$375,122,000	$310,993,000	$250,988,000
Number of employees	5,223	4,396	3,821

Toward that end we are emphasizing:

☐ Managing our growth of personnel in line with revenue growth.

☐ Maintaining tight control over our cost structure.

☐ Continuing our successful asset management program.

To help our growth continue, we are:

☐ Aggressively pursuing third-party relationships to enhance the marketability of our products in target industries. During the year we increased by nearly 80% the number of software houses writing application programs to run on NonStop systems. We expect these joint-marketing arrangements to significantly leverage our marketing productivity.

☐ Augmenting our emphasis on software house relationships through new alliances with select equipment remarketers. These companies, which independently market value-added Tandem systems, will expand our presence in market segments where we do not concentrate our own marketing resources.

☐ Enlarging our sales force and bringing in salespeople experienced in providing total business solutions.

☐ Emphasizing low-end products to complement the high-performance TXP system, thereby extending our ability to penetrate new accounts and expand existing accounts. As a first step, we repriced the NonStop 1+ and NonStop II systems at aggressive levels. In 1985 new products will strengthen our low-end offerings further.

☐ Introducing a series of new products designed to widen our lead in high-performance transaction processing and to open new opportunities in the area of professional support products. ■

The market for on-line, distributed data processing systems is the fastest growing segment of the commercial computer industry.

**FEDERAL EXPRESS INTRODUCES ZAPMAIL.
THE TWO-HOUR DOOR-TO-DOOR DUPLICATE.**

Federal Express introduced its ZapMail℠ service based on Tandem systems with this advertisement in 1984.

The market for on-line systems is huge and rapidly growing. It spans all industries and a vast array of applications.

A number of business needs drive this growth. To remain competitive in dynamic markets, businesses are moving on-line to:

☐ Offer new and better services to attract and retain customers.

☐ Improve profitability by lowering the cost of delivering services and producing products.

☐ Gain greater control over business information to make better business decisions, and make them more rapidly.

To achieve these critical objectives, businesses are converting from batch to on-line information processing. As a result, the marketplace for commercial computers is in rapid transition.

Entirely new applications are also fueling market growth. The combination of less costly, better-performing hardware and the growing availability of on-line applications software opens up new business opportunities for users.

And success breeds success. Successful applications in one area of a business can create potential in other operational areas. Half of our revenue comes from new applications – not only from new customers, but from new applications with existing customers. The remainder of our revenue comes from customers ▶

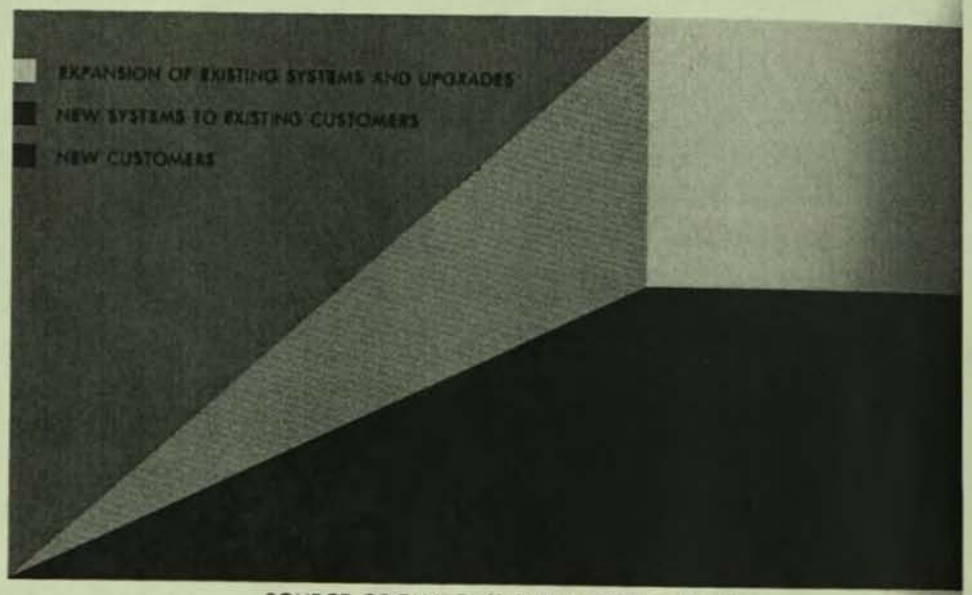
who are expanding existing applications or upgrading their systems.

Users evaluate on-line systems in a markedly different way from that of batch-processing systems. Tandem is a major supplier of systems to the on-line marketplace because we designed our system architecture to meet the new criteria:

Adaptability to constantly changing requirements. By definition, the user's on-line environment is more volatile, more unpredictable, than that of batch processing. The expandability of our NonStop systems makes it easy and economical for customers to enlarge existing applications, add new ones, and link them all together.

Competitive price/performance. The new on-line applications are either central to business operations or to customer services. In both cases, the cost per transaction directly affects profitability. The Tandem family of compatible systems brings price/performance leadership to a full range of application sizes.

Quality systems and applications software. On-line users are demanding innovative and often complex on-line applications. We provide advanced programming tools that simplify program development. In addition, our customers have access to a library of proven, economical application programs developed by Tandem Alliance software houses.



SOURCE OF TANDEM'S 1984 PRODUCT SALES

High-performance data base. Many of today's applications require on-line data bases that will support hundreds of transactions per second. Tandem's unique distributed data base architecture allows growth to very high transaction rates with manageable communication costs and assured data integrity.

Networking and communications capabilities. In order to exploit their new on-line applications efficiently, large organizations often need to distribute data bases and application processing, and to integrate existing information resources. Our architecture and systems software offer outstanding data communications and networking capabilities.

Reliable and available systems. Companies using computers to run their businesses cannot afford system failures or lost data. Tandem's fault-tolerant features are a fundamental strength that assures that all the other product benefits are constantly productive. ■

Tandem is widely recognized as the originator and premier supplier of general-purpose, fault-tolerant systems. But fault tolerance is only the beginning.

We designed our system architecture specifically for on-line applications and distributed data processing. It is singularly well suited to the on-line environment because it is based on independent, parallel processors with separate memory and high-speed interconnections, running a unique message-based operating system that optimizes the movement of transaction-like events throughout the system.

What this means for users is:

Fault tolerance is only part of the Tandem architectural contribution, and only the beginning of user benefits.

Easy, economical application growth
Tandem users can expand a system incrementally from the power of a large minicomputer to many times that of IBM's largest mainframe. Users with growing applications can enlarge each Tandem system modularly from 2 to 16 processors, or to as many as 224 processors in a local cluster using FOX, Tandem's fiber optic link. NonStop systems economically address application demands ranging from a few transactions per second to hundreds of transactions per second. As a result, Tandem users can:

Increase power linearly. When users double the number of Tandem processors, they get double the power.

Buy only as much capacity as they need. With conventional systems, ▶

users must purchase excess capacity to accommodate change.

Add incremental capacity when needed without reprogramming, thereby protecting their investments in hardware and software.

Maintain consistent cost per transaction as the application grows and capacity is added.

High performance

The Tandem multiple-processor architecture and high-performance data base products provide users with fast and accurate information. And our distributed relational data base capabilities let customers put information where it is most needed and used.

Whether customers' data bases are large or small, simple or complex, Tandem systems provide outstanding performance at economical cost. We deliver high performance using our standard, general-purpose software.

Even in the most demanding environments, customers achieve high performance. Our users can:

☐ Accommodate large numbers of users simultaneously accessing a data base.

☐ Handle the largest data bases with fast transaction rates and short response time.

In a benchmark test conducted by a major U.S. business during 1984, for example, a TXP system – configured to only *one-seventh* of the maximum system size – outperformed one of the industry's most powerful mainframes.

Tandem systems are price/performance leaders across a broad performance range.

Networking and communications

The growing trend toward distributed data bases and application processing, and the proliferation of information-generating devices within a single organization, have clearly created a need for integration of all this information into a cohesive resource.

Tandem's network-oriented architecture is ideally suited to the integration task. Even a basic two-processor system operates like a network within a system. Using our EXPAND software and sophisticated communications offerings, customers can:

☐ Establish networks of up to 4,080 Tandem processors without rewriting applications software. And they can easily reconfigure the network as needs change.

☐ Distribute the data base to the points of greatest use, without increasing programming complexity.

☐ Leverage investments in other technologies. We provide highly functional links to other systems and devices, and to networks such as IBM System Network Architecture (SNA). According to industry analysts, Tandem's SNAX software is the most powerful SNA interface in the industry.

Tandem multifunction networks bring the highest level of flexibility, performance, functionality and economy to our customers' applications. ■

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THE

FROM

MPUTER FAT.

CAUSE AND THE CURE

HE LEADER IN ON-LINE TRANSACTION PROCESSING.

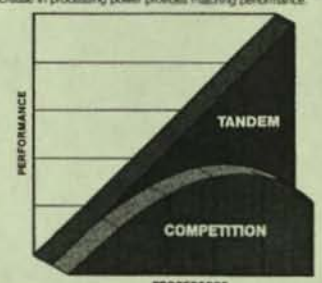
WHAT COMPUTER FAT IS.

Computer fat is created when you buy more computer than you need. With conventional computer architecture, you have no other choice. You buy the closest fit available and "grow into it." So there is always waste and inefficiency. And you pay dearly for it.

WHAT IT COSTS.

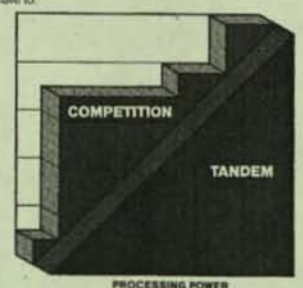
THE PERFORMANCE COST.

With conventional computer architecture, doubling your processors does not double your performance. With Tandem, each incremental increase in processing power provides matching performance.



THE DOLLAR COST.

With conventional computer architecture, growth is convulsive. You must continually over-invest to assure sufficient processing power. With Tandem, growth matches need. You never invest more than you have to.



HOW TO AVOID IT.

Tandem Computers has developed the ultimate system for on-line transaction-processing. It is a fault-tolerant system that can grow as your needs grow, expanding at any increment you choose. You can start with two processors and grow to 16 processors in a system. You can put in a fiber-optic link and grow to a local network of 14 systems. With a combination of land lines and a satellite link, you can expand to 255 systems (4,080 processors) worldwide. With Tandem, your software expands, too. All systems work like one system, and you'll never have to rewrite a line of applications code.

TANDEM'S NON-FAT ARCHITECTURE.

A Tandem NonStop® system stays on-line without using idle backup components. Instead, each component has at least one identical twin with which it shares the workload. The system is also enhanced by a high-performance, relational data base that can be geographically distributed to wherever it's needed. And no single component failure can shut you down.

In a Tandem system, there are no idle backup components. All share the workload, and no single failure can shut you down.

LET'S CHEW THE FAT.

Tandem systems are already at work for Fortune 500 companies in banking, telecommunications, manufacturing, transportation, retailing and energy, as well as several branches of the U.S. Government. To find out what we can do for you, call (800) 482-6336. Or write for our annual report. Corporate Headquarters: 19191 Vallco Parkway, Dept. 762, Cupertino, California 95014.

TANDEMCOMPUTERS
NonStop. NonFat.

Tandem launched a new advertising campaign in the first quarter of fiscal 1985 to create greater awareness of NonStop systems' unique linear expandability.

HOW TANDEM SYSTEMS ARE USED

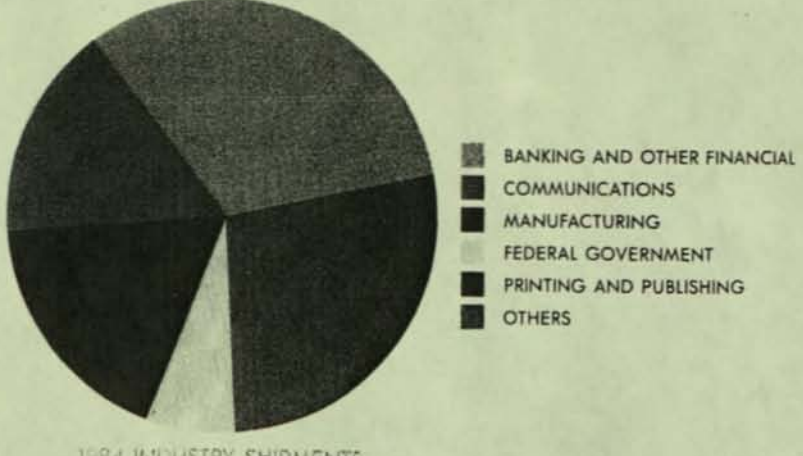
Our customer list spans many industries and reflects a rich variety of applications. Tandem systems are used in large and small applications, both centralized and decentralized, from the more classical to the most innovative.

Chances are you used a Tandem system today. You may have used a Tandem system if you purchased securities traded on one of the world's major stock exchanges; used an automated teller machine; made a long distance telephone call; used a debit card at a gasoline pump; read a newspaper; filed a medical insurance claim; telegraphed a money order; checked into a hospital; shopped or banked at home using home information services; purchased merchandise from a number of large retail establishments; or had a credit card purchase authorized.

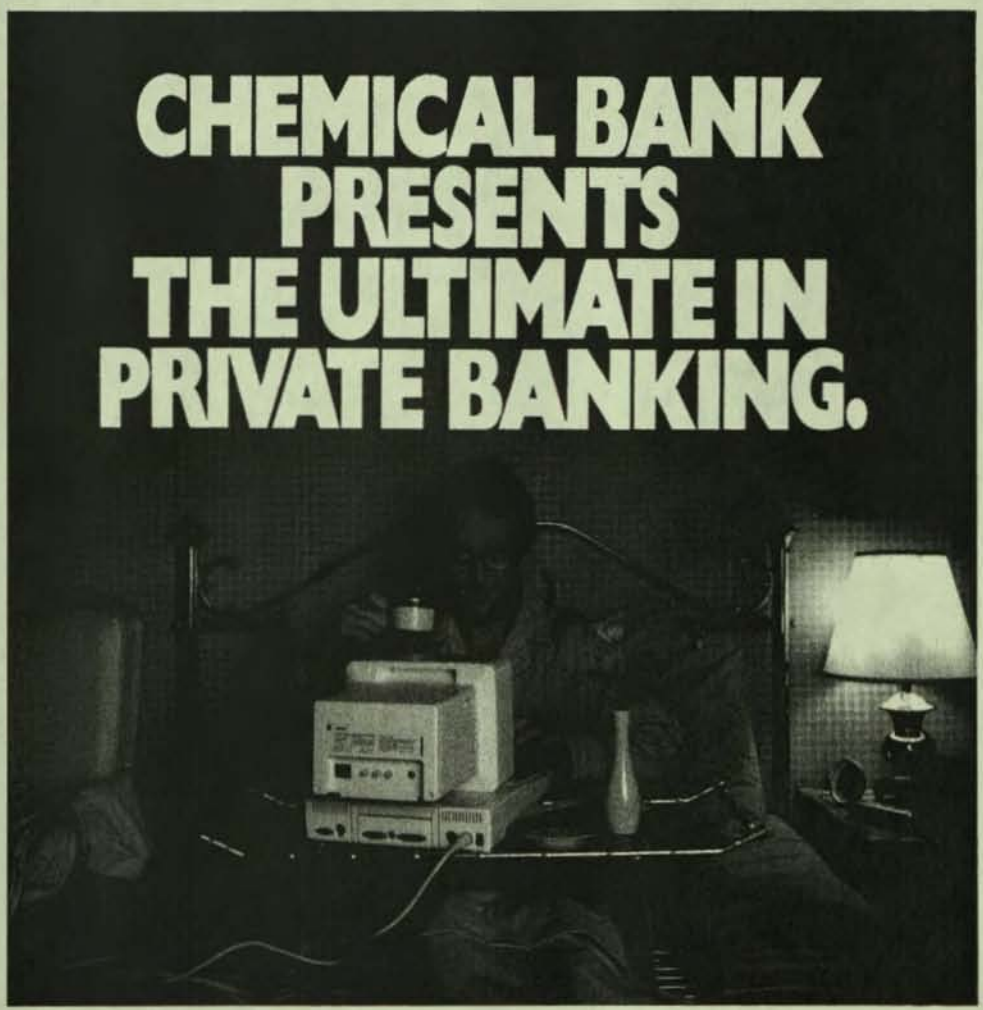
Because of the flexibility of the Tandem architecture and our broad-based price/performance competitiveness, Tandem systems are used in a wide variety of application types:

Beecham Cosmetics, whose product labels include such names as Jōvan, Yardley of London and

The modularity and performance continuum of our systems provides users with ideally sized products for all their needs.



1984 INDUSTRY SHIPMENTS



Chemical Bank used this and other advertisements to announce its PRONTO® home banking and information system in 1984, and by the end of the year had over 10,000 PRONTO customers in the metropolitan New York area. PRONTO is based on Tandem systems.

Vitabath, went from *batch* to *on-line* in 1979 to automate order processing and distribution for their rapidly growing business. NonStop system expandability has enabled Beecham to add major new applications easily.

Thyssen, Germany's multibillion-dollar steel producer, is an example of a *stand-alone application* that has grown into a *network*. Thyssen ordered its first Tandem system in 1977 to automate its factories, and now runs its dispersed plants with a 10-node network of Tandem systems.

According to Thyssen, modular expandability of Tandem systems was a key reason for selecting Tandem: "With Tandem it has not been necessary to define the entire, complex distributed data processing problem before taking action. We are doing it one area at a time, and then integrating that system into the EXPAND network."

Union Bank of Finland has an *expanded system* of 50 processors linked by Tandem's FOX fiber optic extension to handle all of its retail banking services on-line with over 2,300 teller terminals and 140 ATMs at 560 locations throughout Finland.

The May Department Stores Company, one of the largest U.S. retailers, has a *large distributed data base* with more than 35 billion bytes of business information shared in a 12-node Tandem *network*.

The reservation system of Deutsche Bundesbahn, the German national railroad, is a *high-performance data base* application managing ▶

all train seats in six European countries. The yearly reservation volume is about 20 million seats—as many as 100,000 in a single day—booked via 3,500 terminals in Germany and 11 other European countries. FOX linked systems also handle the *communications switching*.

On-line users, as evident in the above examples, commonly need a spectrum of applications. Tandem systems are often used for many different applications within the same organization.

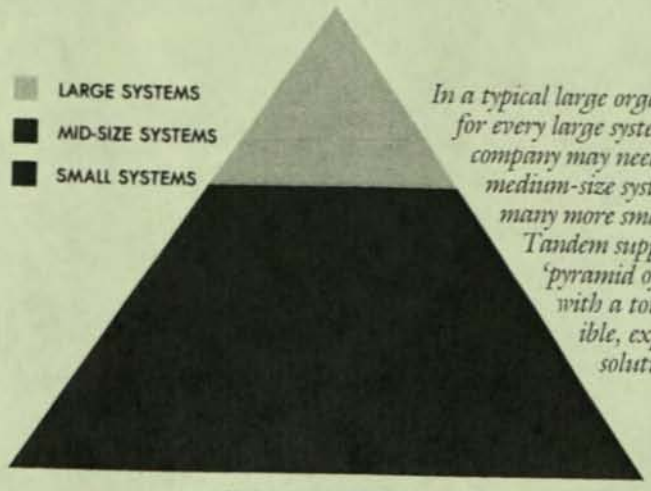
GTE, for example, uses Tandem systems in their separate SPRINT™ long distance telephone and TELEMAIL™ electronic message services.

A large organization also requires systems of varying capacity, often within the same application. It is not uncommon for a single large corporation to use the full range of Tandem system sizes to achieve optimum efficiency.

Extending the GTE example, that company administers its SPRINT subsidiary with a nationwide, 43-node network of low cost, small Tandem systems. Larger Tandem systems are used elsewhere in the SPRINT organization for such applications as on-line unit message billing. And an even larger Tandem system is used at SPRINT headquarters to integrate information from those and other related applications.

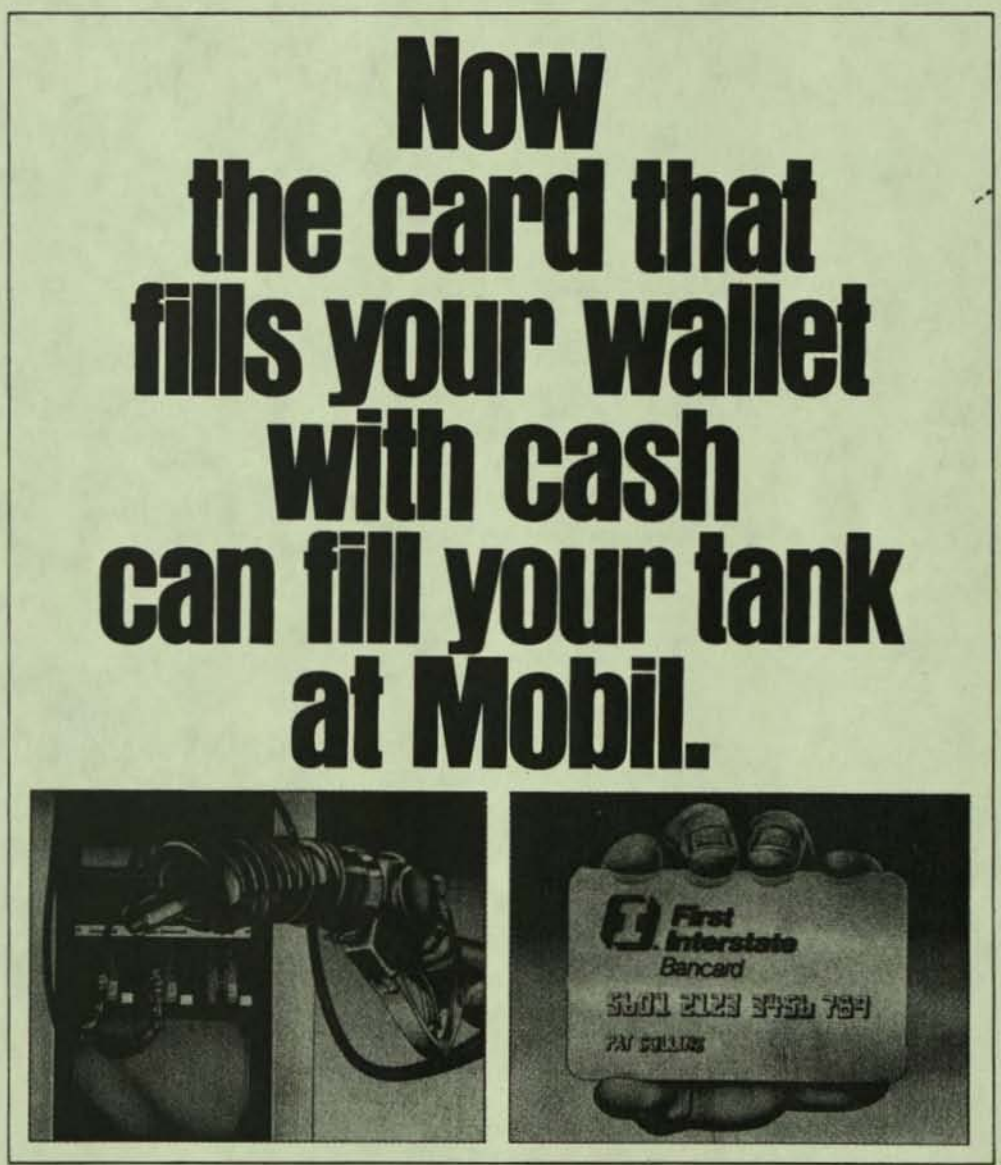
In a typical large organization, for every large system, a company may need several medium-size systems and many more small systems.

The modularity and performance continuum of our systems provides users with ideally sized offerings for all their needs. Tandem supplies this 'pyramid of needs' with a totally compatible, expandable solution. We benefit, too, because we can penetrate an account at the low, middle or high end of the user's performance and price needs. We can then share in the success of the application by expanding it, winning other applications, and extending our presence to other of the user's locations. ■



PYRAMID OF NEEDS

In a typical large organization, for every large system, a company may need several medium-size systems and many more small systems. Tandem supplies this 'pyramid of needs' with a totally compatible, expandable solution.



With advertisements such as this one, Mobil Oil and a number of U.S. banks began jointly promoting an automated system for using credit cards and ATM (automated teller machine) cards at Mobil stations. The Mobil application runs on Tandem systems.

TANDEM ALLIANCE

A top marketing priority at Tandem is to expand the availability of quality applications software designed for NonStop systems.

We created the Tandem Alliance program in late 1983 to develop relationships with key software houses and expand the presence of our existing software houses in order to broaden our marketing opportunities and effectiveness. By joining forces with applications software developers, we can:

- ☐ Provide total business solutions to attract new customers and create opportunities for additional business within existing accounts.
- ☐ Enhance the productivity of our sales force and accelerate the stream of revenues.
- ☐ Benefit customers by speeding their application development.

Software houses that joined the Tandem Alliance in 1984 will develop or adapt applications software in target industries that include manufacturing, telecommunications, transportation, and finance, as well as for the Federal government. We have also targeted point-of-sale for cross-industry applications. When these applications programs are completed, we and our Alliance members will jointly market powerful solutions for our customers' business needs.

Our approach is not limited to traditional software houses. Our customers, too, develop applications with significant commercial value. We have begun to form alliances with some of them to cooperatively market their proven applications to others in their industries.

As an example, we have joined with Michigan Bell, formerly an operating company within the ATT/Bell system and now a member of the Ameritech telephone companies. Together, we are marketing their application for collecting delinquent bills to other, newly independent telephone companies. Similarly, we and Indiana Bell will jointly market its on-line service order entry package.

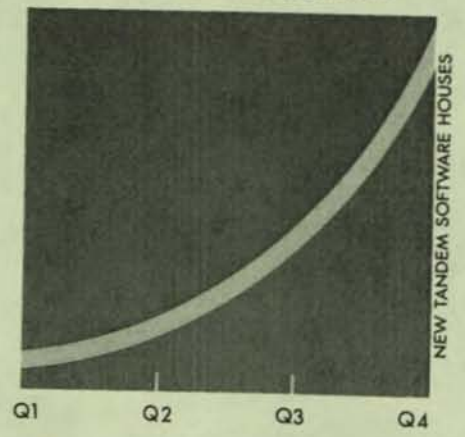
We have also joined with two Scandinavian Airlines System subsidiaries, Linjeflyg AB and Scanator AB, and with U.S.-based Bedford Associates to market an airline reservation system and a series of advanced software packages for airline management.

In the first full year of the program, our Alliance software developers participated in nearly half of our new account sales. During the year, we added 23 new Alliance software houses, expanding the total by nearly 80%. In the fourth quarter of 1984, more software houses committed to Tandem solutions than in any quarter in our history.

The Tandem Alliance attracts software houses because:

Our strong product features and price/performance advantage make their software more attractive to customers.

ALLIANCE PROGRAM GROWTH



A top marketing priority at Tandem is to increase sales through alliances with key applications software firms.

Scandinavian Airlines System (SAS) uses Tandem systems for a variety of applications, and is also a team member in a Tandem Alliance project that will market to the airline industry a reservation system and a series of advanced software packages for airline management.

Our systems' compatibility and modular growth capability let software houses develop an application only once and it will run on small, medium or large systems.

Our extensive program of support includes representatives in all sales regions dedicated to software houses. These Tandem employees communicate the strengths of our software houses and foster relationships with the rest of the Tandem sales force.

Alliance software houses also have access to many Tandem resources.

☐ Our worldwide sales organization expands Alliance members' marketing opportunities.

☐ Alliance software houses participate in some of Tandem's closed-circuit satellite television programs to make marketing presentations to our sales force and customers.

☐ Alliance software houses can take advantage of our training programs – both as student and teacher.

We also join in cooperative promotional activities.

In 1985 we will broaden the Tandem Alliance program to include new types of equipment remarketers. A select group of remarketers will contribute products or expertise to help us address specialized market opportunities. ■

Tandem serves a rapidly growing market with leading edge, much-needed products. We have a large base of prestigious, satisfied customers who count on our products to help make them more competitive. We are confident in the future of the marketplace and in our ability to share in its growth.

Every time Tandem sells to a new customer, you can expect to see the initial sale yield a stream of revenues over the years because of the ease and economy of Tandem system expandability. The unique modular expandability and linear performance continuum of our systems also serves us in developing new business, as well as expanding applications within existing accounts.

We are investing in the future of our marketplace. In the past two years alone, we have invested over $90 million in product development programs. Our development efforts have a magnified impact because our flexible architecture spreads the enhancements over our entire product line. In all of our programs, we maintain our commitment to our architecture, which provides the only computer systems offering fault tolerance as well as linear expandability.

In 1985 we have focused our new product programs on these areas:

High-performance data base. In 1985 we intend to widen our already strong leadership in delivering capabilities for high-performance, distributed data bases. We will introduce software and hardware products that provide significant improvements in price/performance, reliability and serviceability for on-line data base applications.

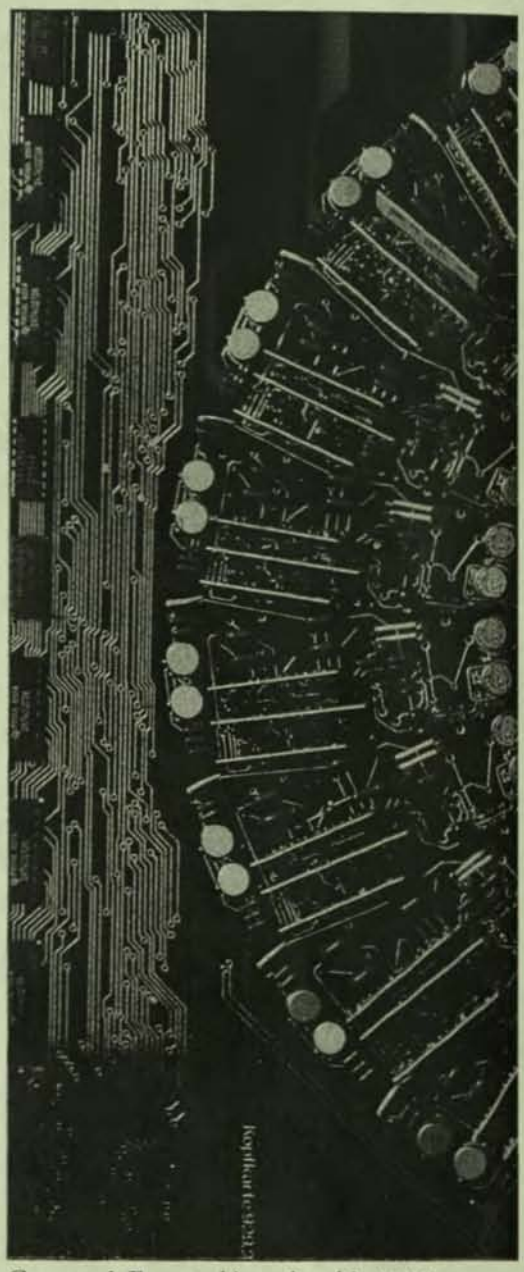
Low-end systems. Tandem's strategy is to provide a family of compatible systems to serve a wider range of capacity needs with greater functionality than any other vendor. In 1984 we moved into very high performance applications with the TXP system. In 1985 we will wage a new offensive at the low end.

We are in the right market with leading edge products, and we are investing in the future of our marketplace.

Networking and communications. We will build on our strength in this technology. In the first quarter of fiscal 1985, we added a major programming productivity enhancement to our SNAX product, already considered the premier SNA interface capability in the industry.

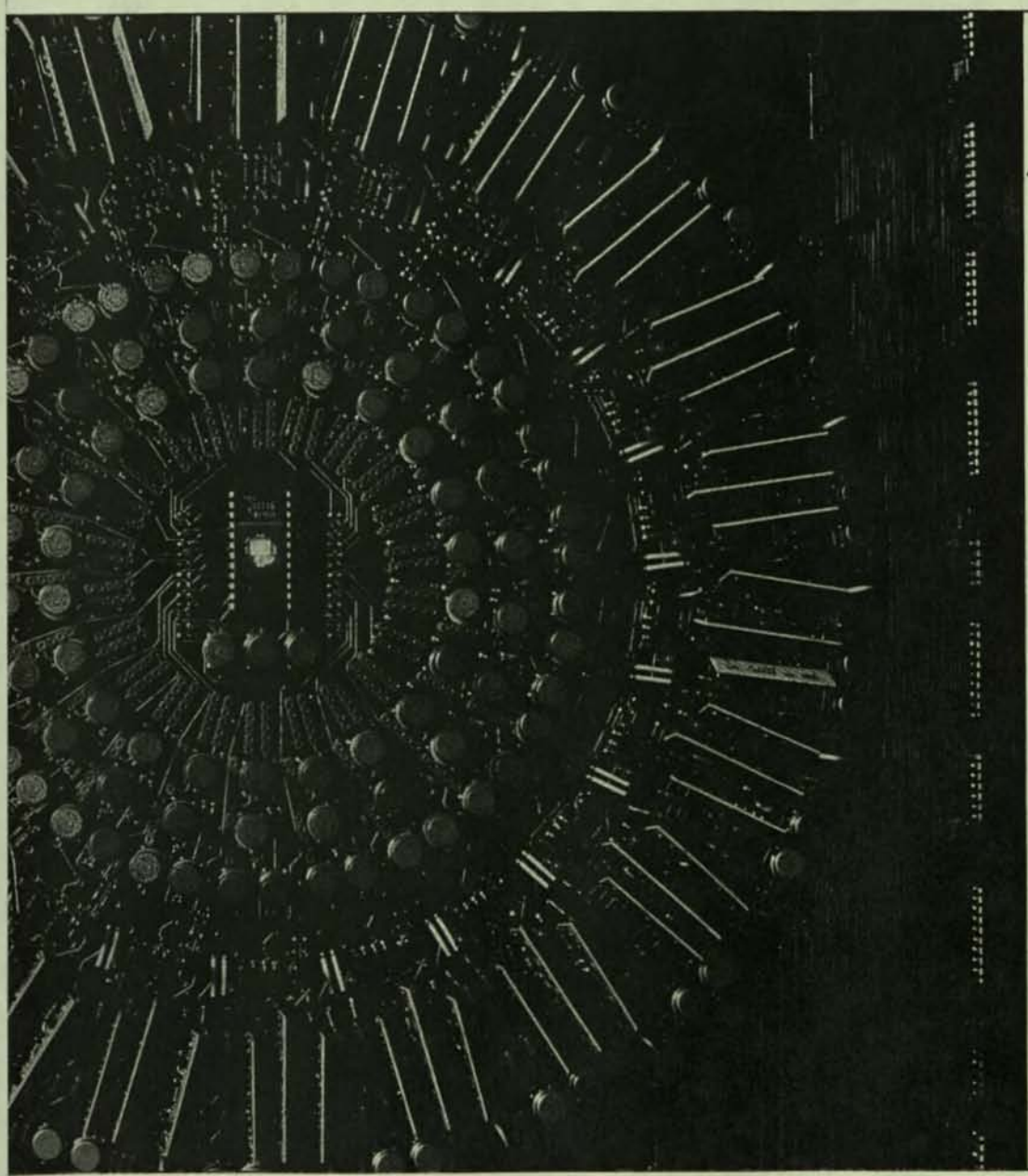
Professional support products. In 1985 Tandem will introduce products aimed at increasing business productivity across our entire customer base. In the first month of the 1985 fiscal year, we introduced our DYNAMITE multifunction workstation. DYNAMITE provides the flexibility of a personal computer with the functionality of a Tandem terminal in a single desk-top device. DYNAMITE gives users access to a wealth of decision support tools while accessing their company's data base on-line.

The new product introductions planned for 1985 are designed to provide more solutions to our customers' business needs, thereby enhancing our competitiveness and ability to grow. ■



Germany's Eurocard introduced in 1984 a pilot program to authorize credit card purchases automatically at point-of-sale locations. The Eurocard organization, comprising a pool of banks, runs its business on Tandem systems.

F U T U R E



TO OUR STOCKHOLDERS:

Tandem has just marked its tenth anniversary. Since its founding in November, 1974, the Company has grown to more than a half billion dollars in revenue. Our customer list includes more than 850 outstanding corporations and government agencies throughout the world. Our own organization has expanded from the first site in California to over 80 locations in the United States and to 18 other countries, employing more than 5,000 people. And, during this tenth anniversary year, Tandem joined the ranks of the *Fortune* 500 largest U.S. industrial concerns.

Developments

Early in the fiscal year, Tandem introduced the high-performance NonStop TXP system. TXP processor shipments ramped up rapidly during the year, so that the TXP product accounted for the majority of our fiscal 1984 revenue. We believe this result demonstrates the strong customer acceptance of the powerful TXP system. This system should be a major contributor to our financial performance in 1985.

Tandem continues to place high priority on product development. In addition to the TXP system, we introduced a new, sophisticated 6100 communications subsystem. A new 264 megabyte Winchester disc drive brings even better mean-time-between-failure and price/performance to our line of disc drives. The 6530 terminal product was enhanced with the inclusion of two smaller, modular terminals as well as additional functions. The 653X family of terminals offers IBM 3270 emulation and can use a variety of alternate input methods including voice. In 1985 we plan to have an active schedule of new product introductions.

There were a number of developments in our marketing programs this year. Tandem identified the newly deregulated telephone companies as an area of opportunity. In 1984 we established a telecommunications industry marketing program to further penetrate that rapidly growing marketing sector. Telecommunications proved to be Tandem's fastest growing market this year. In addition, through the Tandem Alliance program, we signed Michigan Bell and Indiana Bell as new software houses offering applications programs to the telephone companies. The Tandem Alliance, established late last year to attract software houses to develop application programs on Tandem systems, had other successes as well. For example, to help us in the recently deregulated airline market, we added new Alliance members that are developing application packages for this industry.

We implemented programs to enhance our competitive position across our entire product line. By repositioning the NonStop 1+ and NonStop II systems with pricing that is extremely attractive for the lower end of our marketplace, we believe that our entire family of NonStop systems offers the best price/performance for on-line transaction processing in the industry.

We are very pleased to have a new member on our Board of Directors this year. Mr. Andrew Knight, editor of *The Economist,* was elected to Tandem's Board at the annual meeting of stockholders last February.

Financial Performance

Revenues grew 27%, reaching $532,620,000 at the end of fiscal 1984. Earnings per share grew nearly 37% to $1.04, which included a one-time tax benefit amounting to $.24 per share. Our financial performance improved in the second half of the year compared with the first half. However, we are not satisfied with our level of profitability. The Company's first priority for fiscal 1985 is increasing profitability while meeting our product and marketing objectives. We have taken a number of steps to lay the groundwork for improved profitability in 1985.

Tandem is working hard to improve our cost structure through conservative spending and very limited hiring. Through much of 1984, the growth in employment exceeded the growth in revenue. To counter that trend, we have implemented a program designed to hold employment approximately level. Despite this plan, we intend to continue to add salespeople. We achieved this goal in the fourth quarter of fiscal 1984: Total employment declined slightly while the number of salespeople grew by nine percent.

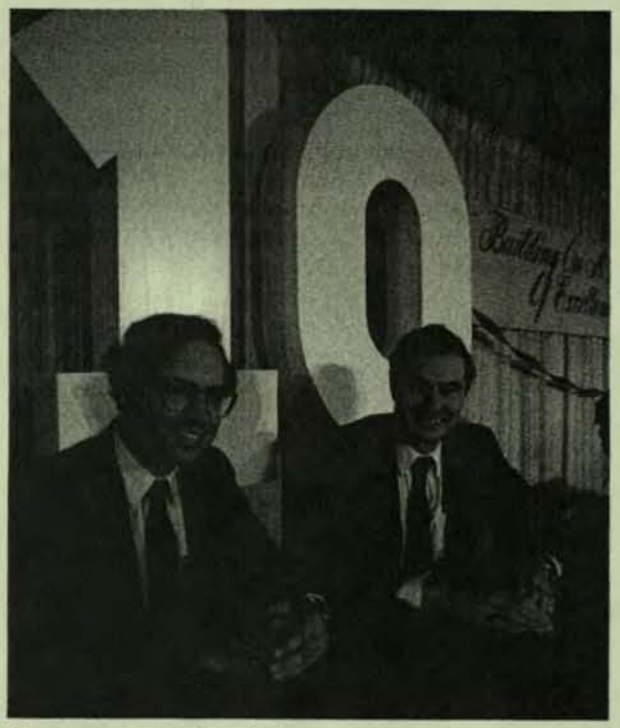
Asset management continued to improve this year. As a result, Tandem's balance sheet is the strongest it has ever been. This year ended with the highest

level of cash in our history, nearly $107 million. In addition, inventory turns increased and receivables collections improved.

Litigation
Just after the close of the fiscal year, Tandem reached an agreement with the Securities and Exchange Commission (SEC) that terminated an investigation relating to Tandem's December, 1982 restatement of revenue and earnings. Without admitting or denying the allegations of the complaint filed by the SEC, which related to the second, third and fourth quarters of fiscal 1982, we consented to the entry of a judgment enjoining the Company against any future violations of the Federal securities laws and requiring Tandem's auditors to conduct annual reviews of certain of the Company's internal controls for this year and an additional two years. Tandem consented to the entry of judgment in order to avoid the extensive commitment of financial resources that would have been required to contest the allegations in court.

Outlook for 1985
As the business section of this annual report notes, Tandem has established several areas of emphasis for 1985. The first priority is better profitability. By improving our cost structure, our goal is to provide a better return to our stockholders while continuing to offer aggressive price/performance for customers. We will continue to form business relationships through the Tandem Alliance. These alliances leverage Tandem's direct selling efforts and give customers the benefit of faster application development. Importantly, our new product program for the year has been designed to provide contributions in three major areas: high-performance data base, low-end systems and personal productivity tools, all key to success in on-line transaction processing.

Nineteen eighty-five is off to a good start. In the first month of the new fiscal year, we announced three new products. DYNAMITE, Tandem's multifunction personal workstation, provides the features of Tandem's 653X family of on-line terminals plus the convenience and local processing capability of a stand-alone personal computer. As a stand-alone workstation, it can run most software written for the IBM PC. Further, using Tandem's micro-mainframe integration software, DYNAMITE users can access the corporate data base and manipulate that information using off-the-shelf software packages. In addition, the Company added a more powerful version of the ENABLE automatic computer program generation



Commemorating Tandem's tenth anniversary, Jim Treybig, at left, and Tom Perkins were among the hosts of a special closed-circuit television broadcast to Tandem facilities in November 1984.

tool, and a major programming productivity enhancement for SNAX, Tandem's System Network Architecture Access Method.

Tandem believes ours is the most attractive market in the computer industry, and that our unique architecture has enabled us to develop the best products for that market. These advantages are leveraged by our foremost asset – our people. Through the continued hard work and commitment of our people, we look forward to achieving our goals for 1985.

James G. Treybig
President and
Chief Executive Officer

Thomas J. Perkins
Chairman of the Board

November 29, 1984

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Tandem Computers is committed to being a technological leader in the rapidly growing market for on-line transaction processing systems and networks of on-line systems. The Company believes that its computer architecture uniquely satisfies the fundamental requirements of fault tolerance and linear power expandability for such applications. Achieving the Company's technological leadership goal involves many factors, including strategic market positioning, a commitment to product development, and an organizational structure and philosophy that foster employee productivity and creativity. It is also critical to maintain a strong financial position and operating record to allow the Company to maximize its performance in an environment of rapid growth.

Financial Condition

Maintaining a sound financial position is a high priority within Tandem. The Company's financial condition further strengthened in fiscal 1984. The year ended with the highest cash and cash investments balance in the Company's history. Cash increased to $106,862,000 at fiscal year end, from $93,501,000 a year earlier, reflecting income from operations, employee purchases of stock, and improved asset management. As a result of Tandem's continuing emphasis on asset management, inventory levels increased modestly, while days of inventory declined. In addition, accounts receivable increased at a rate slower than the rate of growth in revenues, and days of accounts receivable declined. Capital spending increased during the year to $71,519,000. This amount was substantially above the fiscal 1983 capital spending level, and was slightly higher than in fiscal 1982.

An important part of Tandem's corporate philosophy is to provide all employees with the opportunity to share in the Company's financial success by means of stock ownership. As a result of employee participation in the employee stock purchase program and exercises of stock options, the Company generated $16,991,000 in cash in fiscal 1984, $25,031,000 in fiscal 1983, and $12,249,000 in fiscal 1982.

The Company's financial strategy also includes maintaining a sound ratio of current assets to current liabilities and a conservative capital structure. At the end of fiscal 1984, the current ratio was 4:1, long term debt and capitalized lease obligations were 4.4 percent of total capital, and the Company's equity base was $375,122,000. Unused lines of credit total $70,000,000. Tandem believes this strategy provides it with the maximum near-term and long-term flexibility to consider the full range of financing alternatives to fund the capital needs of its projected growth.

Results of Operations

The table below summarizes the changes in selected operating indicators for the fiscal years presented. The numbers on the left account for the revenue dollar by showing various income and expense items as a percentage of revenue. The numbers on the right measure the yearly percentage increases (decreases) in the same items.

% of Revenue				% Increase (Decrease)		
1984	1983	1982		1984	1983	1982
100	100	100	Revenue	27	34	50
41	40	35	Cost of revenue	30	54	45
10	9	11	Product development	34	16	89
39	38	41	Marketing, general and administrative	31	25	72
10	12	13	Operating income	3	22	1
1	–	2	Interest (net)	610	(88)	(44)
11	12	15	Pretax income	11	8	(9)
4	5	5	Current tax provision	17	17	(31)
(2)	–	–	DISC reversal	N/A	–	–
8	7	10	Net income	39	3	12
			Earnings per share	37	–	6
			Weighted average shares outstanding	2	4	6

Numbers may not total due to rounding.

Revenue

Tandem's revenue gains over the last three years have resulted directly from increased shipments of its computer hardware and software products to new and existing customers, and from increases in the number of customers using its support and training services. The Company's revenue increased by $114,338,000 in fiscal 1984 over fiscal 1983. Comparing geographic segments, international sales outside of Europe experienced the highest rate of growth, advancing 97.5 percent over the fiscal 1983 level. Fiscal 1983 revenue increased $106,139,000 over fiscal 1982 revenue. In that year, the United States was the fastest growing geographical area, posting a 38.4 percent rate of revenue growth. During the past two years, the Company's international revenue has been adversely affected by the strength of the U.S. dollar. International revenue accounted for 32.6 percent of total revenue in fiscal 1984, compared to 30.4 percent in fiscal 1983 and 33.5 percent in fiscal 1982.

Operating Income

Operating margins of 10 percent in fiscal 1984 were below the Company's target range. The principal reason was that operating expenses as a percent of revenue increased in fiscal 1984. During the first half of the year, the Company hired people in anticipation of higher rates of revenue growth. As a result, expenses in relation to revenue exceeded plan. The Company reduced its hiring targets sharply beginning in the fourth fiscal quarter of 1984. In response to this program, total employment declined slightly in the final fiscal 1984 period even though people were added in key functions such as sales. The Company anticipates maintaining this limited hiring program in the near term.

In fiscal 1983, operating margins at 12 percent were also below the Company's target range. The principal reason was that cost of revenue as a percent of revenue rose, due to higher costs relating to excess capacity and to the successful program to reduce inventory levels.

Tandem's product development effort focuses on meeting the needs of computer users who are implementing on-line systems, both at single sites and in geographically distributed on-line information processing networks. The Company believes that the opportunities for technological innovation in this marketplace are substantial. Product development funds are being invested in enhancements to existing products and in important new products that will be introduced in future years. Therefore, the Company has increased its investment in product development each year since its founding. The Company targets product development expenditures in the range of 9 to 10 percent of revenue.

The Company keys its marketing strategy on selling to users who are implementing major on-line applications. Providing a high level of service and support is essential to meeting the needs of this customer base. To maximize its long-term opportunities in this marketplace, Tandem has built a direct selling and support organization in the United States and, primarily through wholly owned subsidiaries, in industrial markets throughout the world. The Company's direct selling efforts are complemented by relationships established with third-party software developers and equipment remarketers. The Company's marketing, general and administrative expenditures in fiscal 1984 were higher as a percent of revenue than in fiscal 1983, but lower than in fiscal 1982. Tandem believes that it is essential to invest in marketing in order to achieve future growth. However, a rate of expenditures on marketing and support lower than that experienced in recent years will be sufficient to compete successfully in its marketplace.

Net Income and Earnings Per Share

Net income growth has differed from operating income growth over the past three fiscal years because of substantial changes in the Company's net interest income and effective tax rate. In fiscal 1984 net interest income was significantly above the level of fiscal 1983, although lower than in fiscal 1982. The Company maintained strong cash balances throughout fiscal 1984, thereby earning substantially more interest income compared with fiscal 1983. Fiscal 1982 interest income benefitted from higher prevailing interest rates.

The primary reason net income grew faster than operating income in fiscal 1984 was a one-time reversal of taxes that had been accrued on earnings of the Company's Domestic International Sales Corporation (DISC). The effective tax rate in fiscal 1984 was 24 percent, reflecting a $9,700,000 one-time DISC benefit. In comparison, the effective tax rates in 1983 and 1982 were 39 percent and 36 percent, respectively. In both fiscal 1984 and 1983, relative to fiscal 1982, there were reduced beneficial impacts of tax incentives for investment in capital equipment resulting from the Tax Equity and Fiscal Responsibility Act of 1982. Earnings per share were $1.04 in fiscal 1984. Without the DISC tax reversal, fiscal 1984 earnings per share were $.80, compared with $.76 in each of the two prior fiscal years. Earnings in 1984 were higher because of the DISC tax reversal and because of higher operating earnings.

Effect of Inflation

Please see page 27 of this report for a discussion of the effect of changing prices on the Company's operations.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

SELECTED FINANCIAL DATA *For the Five Years Ended September 30, 1984*

(In thousands except per share amounts)	1984	1983	1982	1981	1980
Revenue	$532,620	$418,282	$312,143	$208,397	$108,989
Cost of revenue	218,810	168,708	109,305	75,547	40,831
Product development	52,514	39,168	33,642	17,833	8,786
Marketing, general and administrative	210,195	160,635	128,488	74,626	40,049
Operating Income	51,101	49,771	40,708	40,391	19,323
Interest income, net	5,183	730	6,033	10,707	1,759
Provision for income taxes					
Current period	(23,076)	(19,696)	(16,885)	(24,549)	(10,395)
Benefit of DISC tax reversal	9,700	–	–	–	–
Net Income	$ 42,908	$ 30,805	$ 29,856	$ 26,549	$ 10,687
Earnings Per Share	$ 1.04	$ .76	$ .76	$ .72	$ .35
Total assets	$501,873	$415,525	$337,366	$255,971	$ 95,701
Long term debt and capitalized lease obligations	17,155	23,957	21,102	2,054	1,651
Stockholders' investment	375,122	310,993	250,988	204,810	70,294

CONSOLIDATED STATEMENT OF INCOME

For the Three Years Ended September 30, 1984

(In thousands except per share amounts)	1984	1983	1982
Revenue			
Product revenue	$448,611	$360,133	$272,591
Service and other revenue	84,009	58,149	39,552
Total revenue	532,620	418,282	312,143
Costs and Expenses			
Cost of revenue	218,810	168,708	109,305
Product development	52,514	39,168	33,642
Marketing, general and administrative	210,195	160,635	128,488
Total costs and expenses	481,519	368,511	271,435
Operating Income	51,101	49,771	40,708
Interest expense	(2,642)	(2,806)	(967)
Interest income	7,825	3,536	7,000
Income Before Income Taxes	56,284	50,501	46,741
Provision for Income Taxes			
Current period	(23,076)	(19,696)	(16,885)
Benefit of DISC tax reversal	9,700	–	–
Total provision for income taxes	(13,376)	(19,696)	(16,885)
Net Income	$ 42,908	$ 30,805	$ 29,856
Earnings Per Share	$ 1.04	$ .76	$ .76
Weighted average shares outstanding	41,399	40,784	39,221

Because of the Company's method of operation, it is not practical or meaningful to report the cost of service and other revenue as a separate line item.

The accompanying notes are an integral part of this statement.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

As of September 30, 1984 and 1983

(In thousands except share data)	1984	1983
Assets		
Current Assets		
Cash and cash investments	$106,862	$ 93,501
Accounts receivable, net of allowances of $1,708 in 1984 and $2,851 in 1983	146,342	119,558
Inventories	92,375	85,920
Prepaid expenses and other	6,998	11,775
Total current assets	352,577	310,754
Property, Plant and Equipment, At Cost		
Land	8,782	3,127
Machinery and equipment	46,642	35,162
Computer equipment and spares	85,002	59,836
Leasehold improvements	31,320	27,859
Construction in process	20,009	6,788
	191,755	132,772
Accumulated depreciation and amortization	(50,253)	(33,991)
Net property, plant and equipment	141,502	98,781
Other Assets	7,794	5,990
Total Assets	$501,873	$415,525

Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 15,025	$ 3,335
Accounts payable	36,350	27,960
Accrued liabilities		
Wages, payroll taxes and employee benefits	22,527	14,081
Income taxes	4,440	4,971
Other accrued liabilities	10,832	6,262
Total current liabilities	89,174	56,609
Capitalized Lease Obligations	11,744	15,434
Long Term Debt	5,411	8,523
Deferred Income Taxes	20,422	23,966
Stockholders' Investment		
Common stock $.025 par value, authorized 60,000,000 shares, outstanding 40,616,638 in 1984 and 39,552,963 in 1983	1,015	989
Additional paid-in capital	228,106	206,911
Retained earnings	146,001	103,093
Total stockholders' investment	375,122	310,993
Total Liabilities and Stockholders' Investment	$501,873	$415,525

The accompanying notes are an integral part of this balance sheet.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' INVESTMENT

For the Three Years Ended September 30, 1984

(In thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Total
Balance September 30, 1981	36,410	$ 910	$161,468	$ 42,432	$204,810
Sale of common stock under stock option plans	863	22	5,028	–	5,050
Sale of common stock under stock purchase plan	362	9	7,190	–	7,199
Tax benefit from employee transactions in common stock	–	–	4,073	–	4,073
Net income	–	–	–	29,856	29,856
Balance September 30, 1982	37,635	941	177,759	72,288	250,988
Sale of common stock under stock option plans	1,634	41	19,054	–	19,095
Sale of common stock under stock purchase plan	284	7	5,929	–	5,936
Tax benefit from employee transactions in common stock	–	–	4,169	–	4,169
Net income	–	–	–	30,805	30,805
Balance September 30, 1983	39,553	989	206,911	103,093	310,993
Sale of common stock under stock option plans	779	19	9,983	–	10,002
Sale of common stock under stock purchase plan	285	7	6,982	–	6,989
Tax benefit from employee transactions in common stock	–	–	4,230	–	4,230
Net income	–	–	–	42,908	42,908
Balance September 30, 1984	40,617	$1,015	$228,106	$146,001	$375,122

The accompanying notes are an integral part of this statement.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Three Years Ended September 30, 1984

(In thousands)	1984	1983	1982
Funds (cash and cash investments) at beginning of period	$ 93,501	$ 24,816	$ 89,806
Provided from Operations			
Sources:			
Net income	42,908	30,805	29,856
Depreciation and amortization	22,741	18,836	10,196
Deferred income taxes	(3,544)	5,903	9,920
Net book value of property, plant and equipment sold or retired	6,614	14,408	2,142
Total sources	68,719	69,952	52,114
Uses:			
Accounts receivable	26,784	20,748	28,139
Inventories	6,455	(15,415)	46,792
Net change in prepaid expenses and non-debt current liabilities	(25,652)	(13,359)	7,096
Investment in property, plant and equipment	71,519	42,222	65,819
Increase in other assets	2,361	401	6,006
Total uses	81,467	34,597	153,852
Net provided from (used in) operations	(12,748)	35,355	(101,738)
Provided from External Financings			
Increase (decrease) in capitalized leases, net	(3,442)	6,331	9,702
Increase (decrease) in long term debt, net	8,330	(2,201)	10,724
Sale of common stock under employee stock option and stock purchase plans	16,991	25,031	12,249
Tax benefit from employee transactions in common stock	4,230	4,169	4,073
Total provided from external financings	26,109	33,330	36,748
Funds (cash and cash investments) at end of period	$106,862	$ 93,501	$ 24,816

The accompanying notes are an integral part of this statement.

1. Summary of Significant Accounting Policies

Consolidation
The consolidated financial statements include the accounts of Tandem Computers Incorporated and its wholly owned subsidiaries after elimination of intercompany accounts and transactions.

Revenue Recognition
The Company generally recognizes revenue from equipment sales at the time of shipment. Service and other revenue are recognized ratably over the contractual period or as the services are provided.

Exchange Gains and Losses
During fiscal year 1984 the Company adopted FASB Statement No. 52 which concerns accounting for foreign currency transactions. Using guidelines established in the Statement, the Company has selected the U.S. dollar as its worldwide functional currency. Adoption of the standard did not have a material effect on the Company's consolidated financial position or results of operations for the three fiscal years ending September 30, 1984.

Inventories
Inventories are stated at the lower of cost (first-in, first-out) or market and include materials, labor and manufacturing overhead. The components of inventories as of September 30 were:

(In thousands)	1984	1983
Purchased parts and subassemblies	$ 45,259	$ 36,887
Work-in-process	12,400	12,519
Finished goods	34,716	36,514
Total	$ 92,375	$ 85,920

Income Taxes
The Company accounts for investment and research and development tax credits as a reduction of the provision for income taxes in the year in which the related credits are realized.

In accordance with the Tax Reduction Act of 1984, the accumulated income taxes provided for the Company's Domestic International Sales Corporation (DISC) have been reflected as a reduction to the provision for income taxes. Through June 30, 1984, the Company provided deferred taxes on total DISC earnings (see Note 2), the reversal of which has been reflected as a reduction in the provision in the fourth quarter of fiscal 1984.

Property, Plant and Equipment
Systems spares ($25,863,000 in 1984 and $19,271,000 in 1983) are depreciated over a five-year period using the double declining balance method. All other property, plant and equipment are depreciated using the straight-line method. The estimated useful lives are:

Machinery and equipment	5-10 years
Computer equipment and spares	5- 7 years
Leasehold improvements	Lease term

Earnings Per Share
Earnings per common share have been computed based on the weighted average number of common and common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options outstanding that have a dilutive effect when applying the treasury stock method. Fully diluted earnings per share are substantially the same as reported earnings per share.

2. Income Taxes

The provision for income taxes included the following deferred (prepaid) items:

(In thousands)	1984	1983	1982
Federal:			
Current	$ 13,882	$ 1,370	$ 5,516
Deferred (prepaid)	(10,550)	10,574	3,323
	3,332	11,944	8,839
State:			
Current	4,800	1,532	3,633
Deferred (prepaid)	(297)	534	(14)
	4,503	2,066	3,619
Foreign:			
Current	6,197	4,621	2,244
Deferred (prepaid)	(656)	1,065	2,183
	5,541	5,686	4,427
Total provision	$ 13,376	$ 19,696	$ 16,885

Sources of deferred (prepaid) taxes were as follows:

(In thousands)	1984	1983	1982
Installment sale method for income tax reporting	$ (1,950)	$ 8,572	$ 3,657
DISC income	(6,084)	3,181	3,918
Accelerated depreciation	2,950	2,628	2,799
Expenses recognized for financial statements, but not for income tax reporting	(4,943)	810	(1,505)
Effect of intercompany profit eliminations	(2,178)	(4,143)	(2,654)
Other items	702	1,125	(723)
Total deferred (prepaid)	$ (11,503)	$ 12,173	$ 5,492

The provision for income taxes differs from the amount obtained by applying the Federal statutory income tax rate to income before taxes as follows:

	1984	1983	1982
Federal statutory tax rate	46%	46%	46%
State taxes, net of Federal income tax benefit	4	4	4
Investment tax credits	(3)	(4)	(8)
Research and development tax credits	(7)	(7)	(8)
Other	1	–	2
	41	39	36
Benefit of DISC tax reversal	(17)	–	–
Effective tax rate	24%	39%	36%

The DISC tax benefit shown above is attributable to the reversal of deferred taxes previously provided on DISC earnings accumulated through June 30, 1984 in accordance with the Tax Reduction Act of 1984, and has been reflected as a reduction in the provision for taxes in the fourth quarter of fiscal 1984. Included in this benefit are $7.4 million attributable to earnings accumulated in years prior to fiscal 1984.

3. Lease and Other Commitments

The Company leases its headquarters, operating facilities, field offices and automobiles under operating lease agreements. The Company also has capitalized leases for certain equipment. Future lease payments as of September 30, 1984 are as follows:

(In thousands)	Leases	
Fiscal year	Operating	Capital
1985	$ 30,637	$ 5,518
1986	28,528	5,377
1987	24,481	5,078
1988	22,258	3,701
1989	21,503	180
Thereafter	112,019	–
Total minimum lease payments	$ 239,426	19,854
Less: Amount representing interest (4%-17%)		4,527
Present value of minimum lease payments		$ 15,327

Assets relating to capitalized leases totaling $21,605,000 and $22,038,000 are included in the machinery and equipment and computer equipment and spares classifications on the Balance Sheet at September 30, 1984 and 1983, respectively.

Rent expenses were $36,726,000 in 1984, $30,458,000 in 1983, and $20,895,000 in 1982.

4. Long Term Debt

Long term debt as of September 30 consists of the following:

(In thousands)	1984	1983
Construction financing	$ 11,250	$ 4,203
Industrial revenue bonds bearing interest of 12% to 12-3/8%, due 1992, collateralized by equipment in Austin, Texas	2,000	2,000
6-7/8% unsecured promissory note payable in Japanese yen, due October 1985	2,327	–
15% promissory note due January 1986	800	1,640
Other	476	680
	16,853	8,523
Less current portion	(11,442)	–
Long term debt	$ 5,411	$ 8,523

Interest costs of $1,606,000, $644,000, and $508,000 relating to construction projects were capitalized during fiscal 1984, 1983 and 1982, respectively.

The Company has entered into unsecured credit agreements totaling $82,000,000 with several banks. The agreements provide for revolving borrowings through 1988, at which time outstanding amounts are to be repaid. Domestic borrowings bear interest at or below the banks' prime rates through 1985 and approximately 1/4% above these rates through 1988. The Company is required to pay a commitment fee of 5/16% per annum. Of these facilities, $12,000,000 have been earmarked by Tandem for construction financing. The remaining $70,000,000 are for working capital purposes and contain provisions for Eurocurrency and foreign local currency borrowings at interest rates prevailing in these markets. There are no compensating balances required under any of these arrangements.

Certain financial covenants and restrictions are included in the loan agreements. The Company was in compliance with all such covenants and restrictions at September 30, 1984.

The Company has guaranteed payment of bank loans made to two officers comprising $550,000 at September 30, 1984.

5. Capital Stock

The Company's authorized capital stock consists of 2,400,000 shares of Preferred Stock and 60,000,000 shares of Common Stock consisting of 56,000,000 shares of "Common Stock" and 4,000,000 shares of "Junior Common Stock." At September 30, 1984, there were no shares of Preferred Stock or Junior Common Stock outstanding.

Stock Option Plans

The Company has employee stock option plans under which permanent employees may be granted options to purchase shares at 100% of fair market value at the time of the grant. Options generally become exercisable six months after the effective date and expire no

8. Commitments and Contingencies

The Company, along with three present or former principal officers, has been named as a defendant in a single class action complaint filed on October 23, 1984 purporting to state claims for alleged violations of Federal securities laws and pendent state claims arising out of the Company's December 1982 restatement of revenue and earnings for fiscal 1982. The action purports to be brought on behalf of all persons who purchased the common stock of the Company from April 28, 1982 through December 8, 1982. The complaint seeks damages in an unspecified amount. No provision has been made in the accompanying financial statements for possible liability because, in the opinion of management, it is unlikely that the ultimate disposition of the suit would have a material effect on the Company's financial position.

9. Information on the Effects of Inflation
(Unaudited)

The Company has provided an adjusted summary of operations and selected financial data in accordance with the Financial Accounting Standards Board in its Statement No. 33 concerning "Financial Reporting and Changing Prices." This disclosure requirement is experimental and involves considerably more judgment than traditional financial statements, and therefore should be reviewed with caution.

Inflation-adjusted information is computed using the "current cost" method, which requires the Company to adjust asset values based on specific indices and appraisals.

The method does not allow for inflation adjustments to operating expenses, revenue or net interest income, nor an adjustment to the tax provision, despite the decrease in pretax income which results from the inflation adjustments. Only the cost of revenue and depreciation expense related to the assets, which are restated for inflation effects, are adjusted.

Depreciation is computed on a straight-line basis, rather than the accelerated basis that is used for some assets in the Company's historical financial statements, because the accelerated method already recognizes some of the effects of inflation.

Net income for fiscal 1984 was lower under the current cost method because of higher depreciation and amortization expense resulting from higher asset values. Companies that hold monetary assets during a period of inflation lose purchasing power. Tandem held net monetary assets during the period, and their purchasing power declined.

Consolidated Statement of Income Adjusted for Inflation
For the Year Ended September 30, 1984
(In thousands except per share amounts)

	In Average 1984 Dollars	
	Historic Cost	Current Cost
Total Revenue	$ 532,620	$532,620
Cost of revenue, excluding depreciation and amortization	214,603	214,603
Other costs and expenses, excluding depreciation and amortization	244,175	244,175
Depreciation and amortization	22,741	23,437
Interest (income), net	(5,183)	(5,183)
Provision for income taxes	13,376	13,376
Net Income	$ 42,908	$ 42,212
Increase in value of inventories, property, plant and equipment held during the year:		
Measured in general prices		$ 8,900
Measured in specific prices		8,118
Excess of increase in general price level (constant dollars) over increase in specific prices		$ 782

At September 30, 1984, current cost of inventory was $92,418 and current cost of property, plant and equipment, net of accumulated depreciation, was $155,776.

Five Year Comparison of Selected Financial Data Adjusted for Inflation
(In thousands except per share amounts)

	In Average 1984 Dollars				
	1984	1983	1982	1981	1980
Total revenue Constant dollars	$532,620	$435,386	$336,154	$241,120	$140,044
Current cost information					
Net income	$ 42,212	$ 30,536			
Earnings per share	$ 1.02	$ .75			
Net assets at year end	$382,305	$319,594			
Excess of increase in general price level (constant dollars) over increase in specific prices	$ 782	$ 1,198			
Other information					
Decrease in purchasing power of net monetary items	$ 5,471	$ 2,931			
Market price per share at end of period	$ 15.83	$ 36.31	$ 23.89	$ 30.33	$ 21.51
Average CPI (1967=100)	308.0	295.9	286.0	266.2	239.7

later than seven years after the effective date. At the discretion of the Company, options granted under the stock option plans may qualify for Incentive Stock Option treatment under the Economic Recovery Tax Act of 1981.

As of September 30, 1984, options for 6,119,873 shares were outstanding at prices ranging from $3.96 to $34.88, with an average price of $22.07. Options for 4,602,047 shares were exercisable as of September 30, 1984. Options for 2,232,619 shares are available for future grant. Options were exercised at prices ranging from $3.92 to $26.88 in 1984, $.58 to $26.88 in 1983, and $.17 to $26.88 in 1982.

Employee Stock Purchase Plan

As of September 30, 1984, the Company has reserved 2,189,328 shares for future issuance under its employee stock purchase plan. Under the plan, the Company may offer shares to employees by two methods. Under one method, eligible employees may elect to purchase shares of common stock at 85% of fair market value as of the beginning or end of a three-month offering period. Under the second method, the Company may grant to employees the option to purchase common stock at not less than 85% of fair market value at the grant date. As of September 30, 1984, options to purchase 94,100 shares at $12.43 and 28,800 shares at $29.00 were outstanding under the second method. Such options are exercisable through November 15, 1984 and through January 20, 1986, respectively.

6. Geographic Segment Information

The following table sets forth information about the Company's operations in different geographic regions for the three years ended September 30, 1984.

(In thousands)	Geographic Area: United States	Europe	Other	Adjustments and Eliminations	Consolidated
1984					
Revenue-Customer	$364,873	$109,562	$58,185	$ –	$532,620
Revenue-Intercompany	90,850	–	–	(90,850)	–
Revenue-Total	455,723	109,562	58,185	(90,850)	532,620
Pretax Income	46,977	10,842	5,261	(6,796)	56,284
Identifiable Assets	421,974	79,747	31,732	(31,580)	501,873
1983					
Revenue-Customer	$297,722	$ 91,100	$29,460	$ –	$418,282
Revenue-Intercompany	68,001	–	–	(68,001)	–
Revenue-Total	365,723	91,100	29,460	(68,001)	418,282
Pretax Income	49,084	11,546	(1,127)	(9,002)	50,501
Identifiable Assets	336,193	73,923	26,058	(20,649)	415,525
1982					
Revenue-Customer	$215,154	$ 74,958	$22,031	$ –	$312,143
Revenue-Intercompany	60,126	–	–	(60,126)	–
Revenue-Total	275,280	74,958	22,031	(60,126)	312,143
Pretax Income	43,949	9,267	22	(6,497)	46,741
Identifiable Assets	276,886	56,685	15,863	(12,068)	337,366

Intercompany transfers are made at arm's length prices, which include manufacturing profits attributable to United States operations. Identifiable assets are those assets of the Company that are identified with the operations of the corresponding geographic area. United States customer revenue includes export sales of $5,989,000 in 1984; $6,400,000 in 1983; and $7,687,000 in 1982.

7. Unaudited Quarterly Financial Data

(In thousands except per share amounts)	Quarters Ended: Dec. 31	March 31	June 30	Sept. 30
Year Ended September 30, 1984:				
Revenue	$126,369	$111,236	$141,925	$153,090
Costs and Expenses				
Cost of revenue	50,437	47,245	57,787	63,341
Product development	10,849	12,853	13,514	15,298
Marketing, general and administrative	48,205	49,132	56,282	56,576
Total costs and expenses	109,491	109,230	127,583	135,215
Operating Income	16,878	2,006	14,342	17,875
Interest income, net	1,076	1,142	1,243	1,722
Income Before Income Taxes	17,954	3,148	15,585	19,597
Provision for income taxes				
Current period	(7,900)	(1,174)	(6,335)	(7,667)
Benefit of DISC tax reversal	–	–	–	9,700
Total provision for income taxes	(7,900)	(1,174)	(6,335)	2,033
Net Income	$ 10,054	$ 1,974	$ 9,250	$ 21,630
Earnings Per Share	$ .24	$ .05	$ .23	$ .53
Year Ended September 30, 1983:				
Revenue	$ 94,135	$ 96,006	$110,291	$117,850
Costs and Expenses				
Cost of revenue	37,955	37,856	45,117	47,780
Product development	8,997	9,805	9,961	10,405
Marketing, general and administrative	35,548	37,945	41,561	45,581
Total costs and expenses	82,500	85,606	96,639	103,766
Operating Income	11,635	10,400	13,652	14,084
Interest income, net	47	(184)	251	616
Income Before Income Taxes	11,682	10,216	13,903	14,700
Provision for income taxes	(4,556)	(3,765)	(5,462)	(5,913)
Net Income	$ 7,126	$ 6,451	$ 8,441	$ 8,787
Earnings Per Share	$ .18	$ .16	$ .21	$ .21

AUDITORS' REPORT

To Tandem Computers Incorporated:

We have examined the consolidated balance sheet of Tandem Computers Incorporated (a Delaware corporation) and subsidiaries as of September 30, 1984 and 1983 and the related consolidated statements of income, stockholders' investment, and changes in financial position for each of the three years in the period ended September 30, 1984. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Tandem Computers Incorporated and subsidiaries as of September 30, 1984 and 1983 and the results of their operations and the changes in their financial position for each of the three years in the period ended September 30, 1984, in conformity with generally accepted accounting principles applied on a consistent basis.

San Jose, California
November 6, 1984

Arthur Andersen & Co.

TANDEM STOCK PRICE

Calendar Quarter Price		High	Low
1984	3rd Quarter	24¾	13
	2nd Quarter	30⅝	16¼
	1st Quarter	40¼	30
1983	4th Quarter	39½	30
	3rd Quarter	36½	26
	2nd Quarter	34	25½
	1st Quarter	30½	23⅝
1982	4th Quarter	32¾	21¾
	3rd Quarter	25⅜	14½
	2nd Quarter	29	22
	1st Quarter	28½	21

Tandem Computers Incorporated has been traded via the NASDAQ National Market System under the trading symbol TNDM since the second calendar quarter of 1982. All quotations shown represent the high and low prices. Quotations that pertain to earlier periods represent prices between dealers without adjustment for mark-up, markdown, or commissions and may not represent actual transactions. No dividends have been declared on the common stock.

Board of Directors

Thomas J. Perkins
Chairman of the Board; Partner, Kleiner, Perkins, Caufield & Byers

Morton Collins,
Partner, DSV Partners III

Thomas J. Davis, Jr.,
Partner, Mayfield Fund

Franklin P. Johnson, Jr.,
Chairman, Asset Management Partners

Andrew Knight
Editor, *The Economist*
Economist Newspaper Ltd

Robert C. Marshall,
Senior Vice President and Chief Operating Officer, Tandem Computers Incorporated

John B.M. Place,
Former Chairman of the Board and Chief Executive Officer, Crocker National Corporation

Robert G. Stone, Jr.,
Chairman of the Board,
Kirby Exploration Company

James G. Treybig,
President and Chief Executive Officer,
Tandem Computers Incorporated

Auditors

Arthur Andersen & Co.
San Jose, California

Registrar and Transfer Agent
Bank of America N.T. & S.A.
San Francisco, California

Form 10-K
A copy of the Company's Report on Form 10-K for the 1984 fiscal year, as filed with the Securities and Exchange Commission, is available on written request. Please direct your request to:

Treasurer's Office
Tandem Computers Incorporated
19333 Vallco Parkway
Cupertino, California 95014-2599

Annual Meeting
The annual meeting of stockholders will be held at 10:00 a.m. on Friday, February 22, 1985, at the Company's headquarters.

Corporate Headquarters
19333 Vallco Parkway
Cupertino, California 95014-2599
(408) 725-6000

Officers

James G. Treybig,
President and Chief Executive Officer

Robert C. Marshall,
Senior Vice President and Chief Operating Officer

Michael K. Bateman,
Vice President and Division Manager

Thomas A. Bechler,
Vice President and Division Manager

Jack W. Chapman,
Vice President and Managing Director, European Division

Thomas L. Chun,
Vice President-Legal Affairs and Secretary

George C. Eckert,
Vice President and Division Manager

Jan E. Jensen,
Vice President-Human Resources

Richard A. Lamb,
Treasurer

Lawrence A. Laurich,
Vice President-Hardware Development

David R. Mackie,
Vice President-U.S. Marketing

Dennis L. McEvoy,
Vice President-Software Development

Lawrence W. McGraw,
Vice President-Marketing and Service Support

Michael C. Moore,
Vice President and Division Manager

Gerald L. Peterson,
Vice President-International Marketing and Product Management

Jerald D. Reaugh,
Vice President-MIS

David J. Rynne,
Vice President and Chief Financial Officer

Stephen C. Schmidt,
Vice President-Operations

Jeanne D. Wohlers,
Vice President and Corporate Controller

Charles J. Yazel,
Vice President and Division Manager

Domestic Sales and Service Offices

ALASKA, Anchorage

ALABAMA, Birmingham

ARIZONA, Phoenix

ARKANSAS, Little Rock

CALIFORNIA, Culver City, Irvine, Long Beach, Los Angeles, Orinda, Riverside, Sacramento, San Diego, San Francisco, Santa Clara, Universal City

COLORADO, Englewood

CONNECTICUT, Hartford, Stamford

FLORIDA, Jacksonville, Miami, Orlando, Tampa

GEORGIA, Atlanta

HAWAII, Honolulu

IDAHO, Coeur D'Alene

ILLINOIS, Arlington Heights, Chicago, Itasca, Oakbrook, Schaumburg

INDIANA, Huntington, Indianapolis

IOWA, Cedar Rapids, Des Moines

KANSAS, Overland Park

LOUISIANA, Metairie

MARYLAND, Linthicum

MASSACHUSETTS, Newton

MICHIGAN, Ann Arbor, Lansing, Livonia

MINNESOTA, Minneapolis

MISSOURI, Creve Coeur, St. Louis

MISSISSIPPI, Jackson

NEBRASKA, Omaha

NEVADA, Las Vegas

NEW JERSEY, Cardiff City, Cherry Heights, Hasbrouck Heights, Mt. Laurell

NEW MEXICO, Albuquerque

NEW YORK, Buffalo, Fairport, Jericho, New York City

NORTH CAROLINA, Charlotte, Greensboro

OHIO, Cincinnati, Cleveland, Columbus, Dayton

OKLAHOMA, Oklahoma City, Tulsa

OREGON, Portland

PENNSYLVANIA, Duncannon, Horsham, Pittsburgh

TENNESSEE, Memphis, Nashville

TEXAS, Austin, Dallas, Fort Worth, Houston, Irving, San Antonio

UTAH, Salt Lake City

VIRGINIA, Falls Church, Reston, Richmond, Virginia Beach

WASHINGTON, Bellevue

WEST VIRGINIA, Charleston

WISCONSIN, Brookfield

International Subsidiaries

AUSTRALIA
Tandem NonStop Pty. Ltd
Adelaide, Brisbane, Melbourne Perth, Sydney

BELGIUM
Tandem Computers SA/NV
Brussels

CANADA
Tandem Computers Canada Ltd
Edmonton, Markham, Ottawa, St. Laurent, Toronto, Vancouver, Victoria, Windsor, Winnipeg

DENMARK
Tandem Computers A/S
Taastrup

FRANCE
Tandem Computers S.A.
Paris

GERMANY
Tandem Computers GMBH
Dortmund, Dusseldorf, Frankfurt, Hamburg, Hilden, Mannheim, Munich, Neufahrn, Stuttgart

HONG KONG
Tandem Computers (Hong Kong) Ltd
Kowloon

ITALY
Tandem Computers Italia S.P.A.
Milan, Rome

JAPAN
Tandem Computers Japan, Ltd
Nagoya, Osaka, Tokyo

THE NETHERLANDS
Tandem Computers BV
The Hague

NEW ZEALAND
Tandem NonStop Pty. Ltd
Wellington

NORWAY
Tandem Computers (Norway) A/S
Hovik

REPUBLIC OF IRELAND
Tandem Computers Ltd
Dublin

SINGAPORE
Tandem Computers Int'l Inc.
Singapore

SPAIN
Tandem Computers Iberica S.A.
Madrid

SWEDEN
Tandem Computers A.B.
Malmo, Stockholm

SWITZERLAND
Tandem Computers A.G.
Zurich

UNITED KINGDOM
Tandem Computers Ltd
Birmingham, Glasgow, High Wycombe, Kirkliston Lothian, London, Northolt, Rochdale

International Distributors

ARGENTINA

BAHRAIN

COLOMBIA

FINLAND

ISRAEL

KUWAIT

MEXICO

PHILIPPINES

REPUBLIC OF CHINA

SAUDI ARABIA

SOUTH KOREA

UNITED ARAB EMIRATES

VENEZUELA

Produced by George E. Browne & Associates Printed in U.S.

TANDEM COMPUTERS

FIRST QUARTER REPORT

DECEMBER 31, 1985

TANDEM COMPUTERS
19333 Vallco Parkway
Cupertino, California
95014-2599

200188

TO OUR STOCKHOLDERS:

Tandem's financial results for the first fiscal quarter of 1986 continued to reflect the trend of comparatively strong demand abroad, but considerable weakness domestically. Total revenue increased 6.5% in the first fiscal quarter to $170,061,000, compared with the fiscal 1985 level of $159,653,000. Our international business contributed 39% of revenue, versus 34% a year ago. This performance was aided in part by a weakening of the U.S. dollar against other currencies during this period.

The company's pretax income was $20,988,000, or 12.3% of revenue, compared with the 1985 first fiscal quarter level of $24,397,000, or 15.3% of revenue. Net income for the first fiscal quarter was $11,648,000, or $.28 per share, versus $14,028,000, or $.34 per share, earned in the same quarter of fiscal 1985. The tax rate in the latest fiscal quarter rose to 44.5% from 42.5% in the same quarter of last year. This increase resulted from the expiration of the federal R&D tax credit program.

While our pretax margins were down from last year's level, they improved over the fiscal 1985 fourth quarter. We are continuing our programs to improve the efficiency of our operations to meet our goal of higher earnings for fiscal 1986.

During this quarter, we made further progress in our product programs that are strategic for our market. For example, we announced leading-edge security products, a capability that is critical for large, network-based applications. The products included our SAFE™ system security family with SAFEGUARD™ software to control access to shared resources in a network and the SAFE-T-NET™ data encryption subsystem.

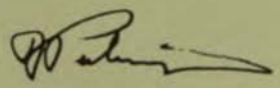
In addition, we announced the XL8™ disc drive, which joins the very successful V8 disc drive introduced in the last fiscal year. Both products employ a unique, proprietary architecture that is optimized for on-line transaction processing applications. The V8 disc drive meets the need for rapid data access, while the complementary XL8 disc drive provides the largest storage capacity per square foot in the industry. We also introduced a state-of-the-art, large capacity tape storage system to allow customers to archive data from discs faster and more efficiently.

Products such as these are designed for outstanding performance and low cost of manufacture. The advantages of our products enable us to win important business, such as a major contract recently awarded to Tandem by GTE Corporation valued at more than $40 million for a telephone equipment facilities management system.

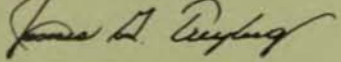
Tandem made gains in our targeted industries this quarter. By adding Continental Illinois National Bank, we now serve 23 of the top 25 U.S. banks. In the securities industry, Morgan Grenfell Securities of the United Kingdom became a customer. Colonial Penn Group joined our growing roster of insurance companies. We continued to widen our lead in point-of-sale applications for petroleum companies with the addition of Dansk Shell and Deutsche Shell. Through our Alliance program, we gained access to a broad library of existing manufacturing applications through a relationship with Ever-On Corporation. Ever-On has become an EXT reseller, offering its PICK-compatible system software on Tandem systems.

We are optimistic about the outlook for fiscal 1986. While we anticipate the normal seasonal pattern in the second quarter with its impact on earnings, we believe the second half of the year will benefit from the continuing success of our marketing and product programs.

Sincereley yours,



Thomas J. Perkins
Chairman



James G. Treybig
President and
Chief Executive Officer

CONSOLIDATED INTERIM STATEMENT OF INCOME (UNAUDITED)

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

(In Thousands, Except Per Share Amounts)	For the Three Months Ended December 31, 1985	December 31, 1984
Revenue		
Product revenue	$137,228	$134,135
Service and other revenue	32,833	25,518
Total revenue	170,061	159,653
Costs and Expenses		
Cost of revenue	58,844	62,021
Research and development	19,817	15,127
Marketing, general and administrative	72,085	59,996
Total costs and expenses	150,746	137,144
Operating Income	19,315	22,509
Interest income, net	1,673	1,888
Income Before Income Taxes	20,988	24,397
Provision for income taxes	(9,340)	(10,369)
Net Income	$ 11,648	$ 14,028
Earnings Per Share	$ 0.28	$ 0.34
Weighted average shares outstanding	42,177	41,384

CONSOLIDATED INTERIM BALANCE SHEET (UNAUDITED)

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

(In Thousands, Except Share Data)	December 31, 1985	December 31, 1984
Assets		
Current Assets		
Cash and cash investments	$134,311	$112,163
Accounts receivable	178,252	152,920
Inventories	75,139	91,836
Prepaid income taxes	1,924	–
Prepaid expenses and other	13,774	9,542
Total current assets	403,400	366,461
Property, Plant and Equipment, at cost	246,915	199,674
Accumulated depreciation and amortization	(88,808)	(57,161)
Net property, plant and equipment	158,107	142,513
Other Assets	8,591	5,101
Total Assets	$570,098	$514,075
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 7,310	$ 6,638
Accounts payable	33,877	34,142
Accrued liabilities	47,773	37,585
Accrued income taxes	–	9,022
Total current liabilities	88,960	87,387
Capitalized Lease Obligations	6,978	10,772
Long Term Debt	4,426	3,237
Deferred Income Taxes	34,684	19,252
Stockholders' Investment		
Common stock, $.025 par value; authorized 60,000,000 shares; outstanding 41,604,711 in 1985 and 40,917,329 in 1984	1,040	1,023
Additional paid-in capital	241,987	232,375
Retained earnings	192,023	160,029
Total stockholders' investment	435,050	393,427
Total Liabilities and Stockholders' Investment	$570,098	$514,075

TO OUR STOCKHOLDERS:

Tandem Computers posted revenue growth of 32% in the second fiscal quarter of 1985, which ended March 31. Revenue for the three-month period was $146,489,000, compared with $111,236,000 for the same period last year. Net income was $6,841,000, or $.16 per share, compared with $1,974,000, or $.05 per share, earned in the second fiscal quarter of 1984.

For the six months ended March 31, 1985, revenue increased 29% to $306,142,000, from $237,605,000 earned in the first six months of fiscal 1984. Year-to-date net income was $20,869,000, or $.50 per share, compared with $12,028,000, or $.29 per share, earned in the same period in fiscal 1984.

Tandem brought two major innovative products to market this quarter – the NonStop EXT™ system and the V8 Disc Storage Facility. The NonStop EXT system was announced in mid-April at press conferences held around the world. The EXT is a self-contained, low-cost and powerful system that is software- and network-compatible with existing Tandem systems. It operates in a copy-room environment and does not require the investment of a computer room. We also implemented a reseller program for the EXT system which we believe will open new markets for our third-party business allies. Consistent with our practice of shipping products before formally announcing them, we produced and shipped several EXT systems this quarter. Early customer feedback has been very positive, and we are optimistic about the product's future.

The V8 Disc Storage Facility is a state-of-the-art, high-performance disc drive that features a unique packaging design. V8 packages up to eight high-speed 168-megabyte Winchester disc drives in a single compact cabinet. The multiple drives speed access to data by allowing up to eight simultaneous disc accesses. We shipped a substantial number of V8's this past quarter, and the market acceptance has been excellent.

During the quarter Tandem continued to be successful in attracting a significant number of new Alliance software houses, which we believe are very important for our continued growth. The quarter was marked by the addition of important new customers as well.

Our financial results were quite positive in the context of a quarter of economic uncertainty in our industry, made more difficult by the continued strength of the dollar. In addition, the second fiscal quarter historically has shown a pattern of seasonal weakness for Tandem, especially pronounced the last two years. While we were pleased with the improvements achieved over last year, our results fell somewhat below plan. Earnings were under additional pressure this past quarter because of the need to increase employment. Tandem had not increased total employment since the end of the third fiscal quarter of 1984. However, since then revenue has increased 21%, creating a need for people to support this level of growth. During the second quarter of fiscal 1985, employment grew 3.5% to 5,367. We expect a lower rate of employment growth in the next two quarters.

Despite the cautious economic environment, we remain positive about the state of our business and our goals for the balance of fiscal 1985. The series of new products already introduced this year and new products that are scheduled for introduction, along with the continued growth and success of our sales force and software alliances, support our belief that we will achieve good growth and profitability this year.

Sincerely yours,

Thomas J. Perkins
Chairman

James G. Treybig
President and Chief
Executive Officer

200186

TANDEM COMPUTERS
19333 Vallco Parkway
Cupertino, California
95014-2599

TANDEM COMPUTERS QUARTERLY REPORT

Second Quarter

March 31, 1985

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED INTERIM STATEMENT OF INCOME (UNAUDITED)

(In Thousands Except Per Share Amounts)	*For the Three Months Ended*		*For the Six Months Ended*	
	March 31, 1985	*March 31, 1984*	*March 31, 1985*	*March 31, 1984*
Revenue				
Product revenue	$120,088	$ 91,223	$254,223	$199,697
Service and other revenue	26,401	20,013	51,919	37,908
Total revenue	146,489	111,236	306,142	237,605
Costs and Expenses				
Cost of revenue	57,713	47,826	119,734	99,186
Product development	17,075	12,853	32,202	23,702
Marketing, general and administrative	61,998	48,551	121,994	95,833
Total costs and expenses	136,786	109,230	273,930	218,721
Operating Income	9,703	2,006	32,212	18,884
Interest income, net	1,573	1,142	3,461	2,218
Income Before Income Taxes	11,276	3,148	35,673	21,102
Provision for income taxes	4,435	1,174	14,804	9,074
Net Income	$ 6,841	$ 1,974	$ 20,869	$ 12,028
Earnings Per Share	$ .16	$ .05	$ .50	$ .29
Weighted average shares outstanding	42,156	41,794	41,770	41,817

Prior period amounts associated with cost of service and other revenue have been reclassified in order to conform to the current period presentation.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED INTERIM BALANCE SHEET (UNAUDITED)

(In Thousands Except Share Data)	*March 31, 1985*	*March 31, 1984*
Assets		
Current Assets		
Cash and cash investments	$107,737	$ 89,354
Accounts receivable	162,927	121,917
Inventories	91,273	108,071
Prepaid expenses and other	7,977	13,316
Total current assets	369,914	332,658
Property, Plant and Equipment, at cost	215,773	158,965
Accumulated depreciation and amortization	(64,554)	(42,829)
Net property, plant and equipment	151,219	116,136
Other Assets	4,882	6,028
Total Assets	$526,015	$454,822
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 6,537	$ 3,534
Accounts payable	39,856	33,764
Accrued liabilities	46,275	25,490
Total current liabilities	92,668	62,788
Capitalized Lease Obligations	9,828	13,840
Long Term Debt	2,672	10,757
Deferred Income Taxes	17,810	29,181
Stockholders' Investment		
Common stock, $.025 par value; authorized 60,000,000 shares; outstanding 41,111,986 in 1985 and 40,242,457 in 1984	1,028	1,006
Additional paid-in capital	235,139	222,129
Retained earnings	166,870	115,121
Total stockholders' investment	403,037	338,256
Total Liabilities and Stockholders' Investment	$526,015	$454,822

TO OUR STOCKHOLDERS:

For the three months ended June 30, 1985, Tandem Computers posted revenue of $144,165,000 compared with $141,925,000 for the same period last year. Net income was $2,388,000, or $.06 per share, compared with $9,250,000, or $.23 per share, in the third fiscal quarter of 1984.

Total revenue for the first three quarters of fiscal 1985 reached $450,307,000, compared to revenue of $379,530,000 for the same period in fiscal 1984. Year-to-date net income was $23,257,000, or $.56 per share, compared with $21,278,000, or $.51 per share, earned in the year-earlier period.

Worldwide revenue for the first nine months of fiscal 1985 grew 19% over the same period of fiscal 1984. However, results in the third fiscal quarter reflected the general slowdown being experienced throughout the computer industry, especially in the United States. The strength of the U.S. dollar compared with year-ago levels also adversely affected both revenue and earnings. As a result, earnings fell significantly below target.

We did see a number of positive developments during the quarter. We continued to achieve good results from our high-priority marketing programs to attract new third-party applications software allies and to develop new customers. In the third quarter, our Alliance program posted its best gains to date, with the addition of 18 software houses and two systems integrators. Also, the number of new customers was up significantly from the second quarter level.

The quarter was marked by a very active schedule of new product introductions. Key among them was the GUARDIAN 90™ operating system software. Tandem significantly boosted the performance of NonStop™ computer systems with the introduction of this new, more powerful version of our GUARDIAN™ operating system. Initial customer experience with GUARDIAN 90 and tests by Tandem, for example, show performance increases of 50–70% for applications using Tandem's Transaction Monitoring Facility (systems software that provides automatic recovery from failure and insures transaction integrity).

The company also announced a multi-vendor system integration strategy that will allow our customers to use their Tandem networks to provide company-wide electronic information sharing between users of a variety of incompatible personal computers, workstations, terminals, facsimile devices and local area networks. Under this Information Management Technology (IMT) strategy, we announced five new products and commitments to support the widest range of industry standards.

We also announced the commitment to support General Motors' Manufacturing Automation Protocol (MAP) specifications for the Computer Integrated Manufacturing market, which is important for our continued growth in this sector of the business.

The new, low-end NonStop EXT™ system was received positively by customers and generated a third of our new customers in the quarter.

These and other new products introduced during the quarter are intended to open new markets, improve performance, facilitate system integration and position us for future growth.

We will maintain our commitment to product programs while tightly managing expenses. We are continuing our program to improve manufacturing productivity and are taking steps to achieve similar efficiencies in marketing and support. We are very optimistic about Tandem's long-term position and are working hard to improve the company's performance during this uncertain economic period.

Sincerely yours,

Thomas J. Perkins
Chairman

James G. Treybig
President and Chief
Executive Officer

TANDEM COMPUTERS
19333 Vallco Parkway
Cupertino, California
95014-2599

TANDEM COMPUTERS QUARTERLY REPORT

Third Quarter

June 30, 1985

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED INTERIM STATEMENT OF INCOME (UNAUDITED)

(In Thousands Except Per Share Amounts)	*For the Three Months Ended*		*For the Nine Months Ended*	
	June 30, 1985	*June 30, 1984*	*June 30, 1985*	*June 30, 1984*
Revenue				
Product revenue	$116,868	$119,064	$371,091	$318,761
Service and other revenue	27,297	22,861	79,216	60,769
Total revenue	144,165	141,925	450,307	379,530
Costs and Expenses				
Cost of revenue	56,116	56,563	175,850	155,749
Product development	18,027	13,514	50,229	37,216
Marketing, general and administrative	69,482	57,506	191,476	153,339
Total costs and expenses	143,625	127,583	417,555	346,304
Operating Income	540	14,342	32,752	33,226
Interest income, net	1,298	1,243	4,759	3,461
Income Before Income Taxes	1,838	15,585	37,511	36,687
Provision for income taxes	(550)	6,335	14,254	15,409
Net Income	$ 2,388	$ 9,250	$ 23,257	$ 21,278
Earnings Per Share	$ .06	$ .23	$ .56	$ .51
Weighted average shares outstanding	41,896	41,039	41,812	41,558

Prior period amounts associated with cost of service and other revenue have been reclassified in order to conform to the current period presentation.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

CONSOLIDATED INTERIM BALANCE SHEET (UNAUDITED)

(In Thousands Except Share Data)	*June 30, 1985*	*June 30, 1984*
Assets		
Current Assets		
Cash and cash investments	$109,022	$ 86,090
Accounts receivable	150,606	135,854
Inventories	94,611	103,475
Prepaid income taxes	19,495	–
Prepaid expenses and other	9,241	10,757
Total current assets	382,975	336,176
Property, Plant and Equipment, at cost	230,817	177,005
Accumulated depreciation and amortization	(72,572)	(48,862)
Net property, plant and equipment	158,245	128,143
Other Assets	3,828	5,590
Total Assets	$545,048	$469,909
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 6,675	$ 3,811
Accounts payable	36,678	28,706
Accrued liabilities	46,678	29,019
Income taxes payable	10,889	11,329
Total current liabilities	100,920	72,865
Capitalized Lease Obligations	8,817	12,640
Long Term Debt	2,719	12,570
Deferred Income Taxes	24,988	20,816
Stockholders' Investment		
Common stock, $.025 par value; authorized 60,000,000 shares; outstanding 41,260,521 in 1985 and 40,448,192 in 1984	1,032	1,011
Additional paid-in capital	237,314	225,636
Retained earnings	169,258	124,371
Total stockholders' investment	407,604	351,018
Total Liabilities and Stockholders' Investment	$545,048	$469,909

TANDEM COMPUTERS ANNUAL REPORT

1985

Leading the Way in On-line Transaction Processing

Tandem Computers Incorporated designs, develops, manufactures, markets and supports a family of unique computer systems for on-line transaction processing. The Tandem NonStop system concept provides the first on-line, distributed computer architecture for mainstream business applications. Customers' systems are supported from over 100 locations throughout North America, Europe, Asia and the Pacific. The Company operates manufacturing facilities in the United States and in West Germany.

Tandem earns the highest marks for customer loyalty.

Outstanding products are a big part of customer satisfaction. But knowing that Tandem will lead the way is equally important.

We delivered our unique computer architecture in 1976 to a data processing community that was just beginning to understand that information technology would create vast changes in business and society.

Businesses began the transition from the first generation of manual handling of transactions to the second generation of centralized, batch-processing computers in the 1950s.

Tandem was founded in response to the need for a third generation, on-line system to fully automate transaction processing. To meet this need, Tandem offered the added values of constant availability through fault tolerance and modular growth with proportional increases in power.

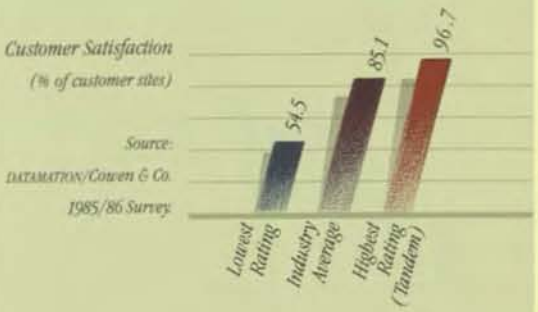
Many of the biggest, most sophisticated organizations in business recognized that Tandem offered the resource they needed to revolutionize the way they did business.

HIGHLIGHTS

Fiscal Year Ended September 30	1985	1984	1983
Revenue	$624,138,000	$532,620,000	$418,282,000
Operating income	$ 50,081,000	$ 51,101,000	$ 49,771,000
Operating margin	8.0%	9.6%	11.9%
Net income	$ 34,374,000	$ 42,908,000	$ 30,805,000
Earnings per share	$.82	$1.04	$.76
Working capital	$298,611,000	$263,403,000	$254,145,000
Total assets	$552,344,000	$501,873,000	$415,525,000
Stockholders' investment	$420,408,000	$375,122,000	$310,993,000
Number of employees	5,494	5,223	4,396

In this decade, the need has developed for a fourth generation of transaction processing, one where business can distribute processing and data where they are needed and can access the information through networks. In this era, advantages of Tandem's architecture and systems software products have become even more important.

And now, we lead the way into the fifth generation with solutions for integrating previously incompatible information resources to give our customers a powerful tool to help take them to the forefront of their industries.



"The potential market is large and growing, with very limited direct competition (for Tandem)."

– Drexel Burnham Lambert

Market direction:

ACCELERATING TRANSACTION RATES

The on-line transaction processing (OLTP) marketplace that Tandem pioneered 11 years ago is still the most attractive segment of the market for commercial data processing systems.

Three major, fundamental sets of forces drive the growth of transaction volumes and the demand for OLTP systems.

Deregulation and competition. The deregulation of industries and worldwide competitive pressures are spawning new, automated procedures and services to control costs or attract new customers. An increasingly automation-dependent world demands computers that can deal with vastly increased transaction rates and volumes.

Technology. Transaction volumes are also increasing as a result of advances in computer processor, memory and communications technologies. Costs of transactions have decreased, inspiring some applications that could not have been considered before. At the same time, business applications are delivering more value for the dollars spent.

Microprocessor technology, too, is feeding transaction volume growth. Microprocessors are bringing intelligence to such devices as automated tellers, retail checkout terminals and wands, facsimile machines, copiers, personal computers, factory data collection terminals, industrial robots and even gasoline pumps. These previously "dumb" devices are now generating transactions at a rapid rate, creating demand for systems to capture and process those transactions.

Integration. As automated procedures multiply, businesses increasingly need to tie together separate batch and on-line applications, usually running on different vendors' systems and networks, into a single information processing resource. This need creates additional demand for systems that can effectively and efficiently perform this integration function.

Most of the growth in OLTP is yet to come. The impact on transaction volumes created by these three forces in the marketplace is just beginning to unfold. Fully 75% of the independent software houses participating in Tandem's Alliance program, according to an independent survey, believe that their Tandem based applications have penetrated less than 10% of their market.

Forces driving up transaction volumes
– Deregulation and competition
– Technology
– Integration

TANDEM LEADS THE WAY:

Dedicated solely to filling the needs of on-line transaction processing for over a decade, Tandem's computer architecture accommodates the full range of OLTP requirements.

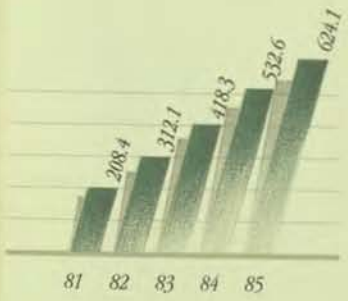
In evidence is the strong Tandem presence among leading-edge applications.

Marketplace innovators look to Tandem for success of new applications, many of which can only be achieved through the unique capabilities and flexibility of the Tandem architecture.

The cornerstone of OLTP requirements and a fundamental benefit of the Tandem architecture is fault tolerance, which significantly increases the productivity of the computer resource. Equally important, however, are programmer productivity, data integrity and security, fast response time, low cost per transaction, ability to distribute data bases, networking and modular system growth from mini to mainframe power without performance degradation and without loss of full functionality.

We believe no other supplier fulfills all of those requirements as well as Tandem. No OLTP application that is subject to growth or modification should be without this critical portfolio of capabilities if it is to enjoy long-term efficiencies and success.

We expect major corporations to continue to rely on Tandem to reduce the risks of automation. Our customers in this rapidly growing, rapidly changing marketplace understand that they can commit to Tandem with confidence. Tandem's technology and focus on OLTP anticipate the direction of the market in the 1990s.



Tandem Revenue ($ Millions)

Industry focus:

POINT-OF-SALE:

Mobil Oil's leading-edge project to automate transactions at the point of sale (POS) is an excellent example of the use of on-line processing to gain cost and competitive advantages, as well as an illustration of microprocessor-based technology accelerating the growth of transaction processing volumes.

The POS application automates authorization and data capture of credit card sales (Mobil or bank cards) and debit card sales at service stations, and dramatically reduces Mobil's cost of carrying those sales.

Microprocessor-equipped on-line terminals at high-volume Mobil stations now automatically and instantly update customers' accounts (at Mobil or a specific bank). This replaces the manual handling of charge receipts that previously delayed account updating and collection by some ten days.

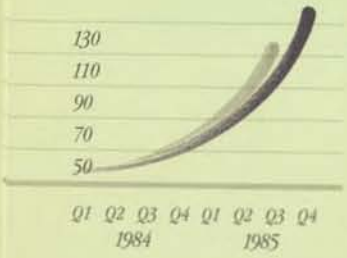
Mobil is also able to negotiate more favorable bank-card discount rates because the on-line, paperless POS system also reduces banks' handling costs. Mobil can pass on to customers the company's discount for cash by allowing them to use bank automated teller cards in lieu of cash.

Mobil began the project in 1983, and the 3,600 highest-volume stations of the company's 12,000 outlets will be POS-automated by early 1986, generating transactions at the rate of approximately 7,000,000 per month.

Tandem is a leading supplier of computer systems for point-of-sale applications in many industries, including some of the largest retailers, banks and petroleum companies. Five of the seven major North American petroleum companies developing POS applications chose Tandem systems.

"Software houses have chosen Tandem as a superior technical solution for their specific applications."

– Prudential-Bache



Alliance Program Growth (Cumulative members)

Alliance software houses that believe markets for their products are less than 10% penetrated.

Source: Prudential-Bache

Market direction:

DEMAND FOR APPLICATION SOFTWARE

Customers are no longer just interested in hardware and systems software. Today they demand total systems solutions to business problems and the ability to pursue business opportunities.

Organizations of all sizes are generating strong demand for proven, readily-available application software packages. These packages help to speed implementation of applications and cost less than custom-developed systems. They enable users to respond quickly to market changes and competitive pressures. And, because these packaged solutions are running and demonstrable, they offer users a low-risk path to automation.

TANDEM LEADS THE WAY:

Through the Tandem Alliance program, the expertise of the independent software house combines with Tandem's knowledge of the needs of industry to deliver powerful hardware and application software solutions.

Our philosophy is to work closely with software houses and other third parties as development partners. Our objective is to do all we can to help our third-party allies be successful.

Advantages of the Tandem hardware and software architecture complement the capabilities of application software produced by independent software houses. Virtually all Alliance software houses, according to an independent survey, consider Tandem systems to be an advantage in developing and marketing their application software. Among major strengths cited are:

☐ Reliability of NonStop systems.

☐ Modularity, compatibility and linear performance growth of Tandem systems, enabling an application to be developed only once to run on small, medium or large systems.

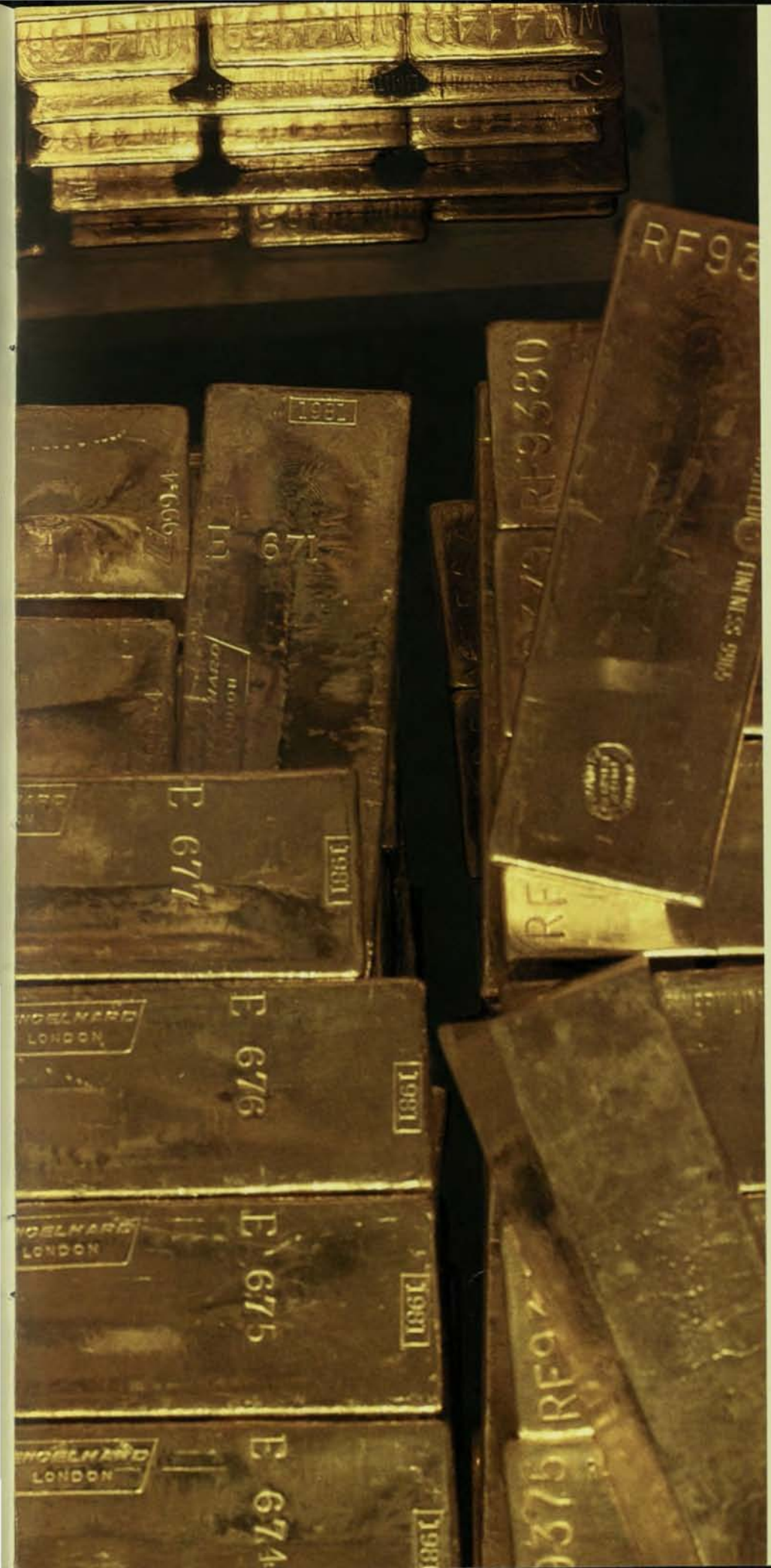
☐ Power and throughput of the NonStop TXP system.

☐ An ideal entry-level system, the self-contained NonStop EXT that needs no specially modified computer room.

☐ Superior networking, communications and distributed data base capabilities.

☐ Growth potential: over 70% of Alliance software houses have products aimed at Fortune 1000 customers where Tandem has a strong market presence.

The Alliance program continues to be extremely successful in establishing new customers for Tandem in target industries, including banking, financial services, manufacturing and telecommunications. During 1985, the number of Alliance members expanded by 80%.



Industry focus:

BANKING

The Tandem Alliance program is successful internationally.

In France, for example, Groupe Francais d'Informatique (GFI) recently helped Tandem win two new accounts in the banking industry. GFI is a major French software house with over 1,000 employees. The company is a subsidiary of SCICON International Limited which is a member of the British Petroleum Group. Other SCICON software houses operate in the United Kingdom, West Germany and the U.S.

The new French banking applications are at Caisse Regionale de Credit Agricole Mutuel (CRCAM) de l'Ile de France and BANQUE SOFINCO. The former, with 800,000 accounts in Paris, is the largest of the CRCAM group which ranks second among French banks ($92 billion in assets). SOFINCO has 80 offices in France and is its second largest provider of consumer credit.

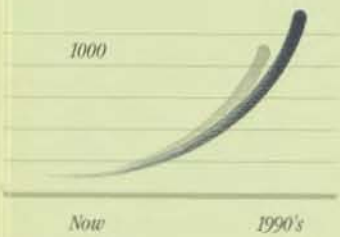
CRCAM de l'Ile de France is using a GFI videotex application for home banking. Its customers can conduct their banking through French MINITEL terminals, distributed free to all telephone subscribers by the French telephone authority.

SOFINCO is also using a GFI videotex application to connect some 2,000 terminals at retailers for instantaneous credit authorization for installment loans.

Tandem has a strong presence in worldwide banking. Over 240 banks use Tandem systems, including 22 of the top 25 U.S. bank holding companies and 15 of Europe's 25 largest banks.

"We expect Tandem to build upon key strengths, including a leadership position in large-scale transaction processing networks and a substantial customer base in over 800 corporations worldwide."

– Merrill Lynch



Performance Trend (Maximum transactions per second)

Alliance software houses that consider Tandem NonStop TXP power and throughput a major strength.

Source: Prudential-Bache

Market direction:

RAPIDLY EXPANDING APPLICATIONS

The forces driving OLTP growth create a dilemma for users: conventional computer architectures force users to choose between higher performance and functionality. But users need both.

As performance requirements grow, applications that run on conventional computers typically trade-off such functions as programming ease, data integrity and the ability to manipulate the data base for analytical queries.

The performance versus functionality impasse will undoubtedly amplify in the near future. Maximum OLTP performance requirements today, with the exception of the largest airline reservation systems, rarely exceed 90 transactions per second (tps). Many are still under five tps. Industry expects tps rates to increase to 200-500 in the next few years. And that in the Nineties users will need systems capable of performing in the 1,000 tps range – over ten times that of most of today's highest performing applications.

TANDEM LEADS THE WAY:

Other vendors may promise full functions at high transaction rates, but Tandem delivers. Tandem users get the same capabilities on large NonStop systems delivering the industry's highest transaction rates that they get on smaller NonStop systems handling lower throughput demands. Functionality is preserved with virtually no degradation of performance.

Tandem can deliver consistent functionality and performance for our systems because of the unique hardware and software architecture of Tandem's product line.

Applications can be implemented on Tandem's entry-level NonStop EXT system and directly moved to a NonStop II or a higher-power TXP system giving increased performance without rewriting application software. In addition, the NonStop II and TXP systems can be expanded modularly to mainframe levels of power – with linear gains in performance while retaining full functions and without reprogramming.

Data bases can be distributed to any size Tandem system using ENCOMPASS software, the industry's only high-performance, distributed relational data base management system. And applications can be linked together transparently with EXPAND networking software, also common to all Tandem systems.

Applications implemented today on Tandem systems will continue to deliver function and value as future transaction rates multiply – even with growth in transaction requirements to 1,000 tps and beyond.

Technical focus:

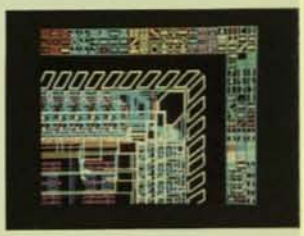
STATE-OF-THE-ART PRODUCTS

Very large-scale integration (VLSI) circuitry applied in Tandem products helps meet the need for reliability, functionality and performance at lower costs. Tandem's strategy is to develop leading-edge VLSI devices jointly with semiconductor manufacturers. Tandem designs its own VLSI prototype devices, then buys production devices from leading semiconductor suppliers, to shorten product development leadtimes and to build the knowledge that enables us to apply the right technology for the right job.

Currently we have established close relationships for the utilization of high-performance bi-polar technology as well as low-power, lower performance CMOS technology.

With the strategic investment that we made in building our own VLSI prototype fabrication laboratory and computer-aided design system, we are able to improve our development engineers' productivity and deliver competitive products rapidly to the market. These resources enable us to produce prototypes three to four times faster than the industry standard.

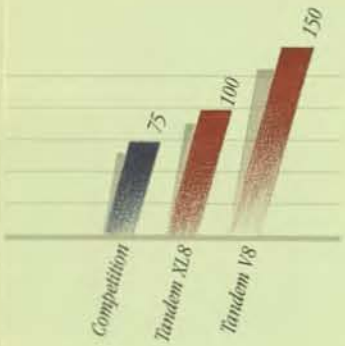
During 1985 we began introducing products that incorporate Tandem designed VLSI gate arrays. For example, subsystems such as our new 3207 tape controller and 5130-31 tape drive employ state-of-the-art, Tandem designed 2,000- and 4,000-gate gate arrays. The 3207 provides significant price and functionality advantages in a single circuit board, compared with competitive devices that are many times larger in size.



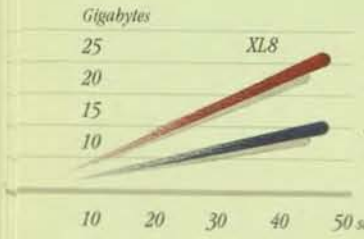
We are now poised for a stream of products at all levels of our system employing VLSI technology.

"Tandem has tremendous value-added in its technology for on-line transaction processing."

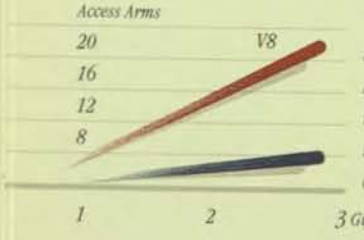
– Prudential-Bache



Accesses per second (per $100,000)



The Tandem XL8 Disc Storage Facility. Storage per square foot vs. leading competitor.



The Tandem V8 Disc Storage Facility. Access arms per megabyte of storage vs. leading competitor.

Market direction:

LOWEST COST PER TRANSACTION

With organizations in all industries becoming dependent on on-line transaction processing to run their businesses, the cost of a transaction has become central to the total cost of doing business. In many cases, the information system *is* the business. The long-term, total cost of delivering OLTP services can be crucial to the profitability of all information-based businesses.

Businesses are, therefore, beginning to make systems purchasing decisions based on total cost per transaction. The many factors that can affect transaction costs over the life of the system must be included in the pre-purchase analysis.

TANDEM LEADS THE WAY:

Tandem focuses on providing products and services that help our customers reduce the total cost of their transaction processing applications. Initial system price and the relationship of price to performance are only part of the total cost picture.

Tandem helps cut programming costs by making the programmer's OLTP task as simple as writing batch processing applications. Tandem users typically implement applications at a fraction of the time and cost – and begin enjoying cost-saving benefits much sooner – than do users of conventional systems.

Users of conventional systems pay for "computer fat" – the over-investment in larger-than-needed systems to accommodate future growth. Tandem eliminates the cost of computer fat. NonStop systems can be appropriately sized to an application environment and then expanded modularly. With each growth increment – all the way to the power of a mainframe – Tandem users get proportional performance gains and retain functionality.

Another major cost of system growth with other vendors is the rewriting of programs and retraining of people at each growth stage. Tandem software is compatible across the widest range of performance in the industry. That means that the Tandem system can grow to a very large distributed environment without reprogramming or retraining.

Using our distributed relational data base management software, Tandem users can cut communications costs by distributing applications and data to remote locations while assuring data integrity.

Tandem systems are easy to use and highly productive. They handle large data bases with large numbers of simultaneous users, yet deliver both high transaction rates and fast response time.

Productivity also comes from the availability of the system provided by the fault-tolerant NonStop architecture.

The ease of networking and of changing network configurations with Tandem systems can yield huge cost savings.

And cost per transaction on Tandem systems is continually improving. A new software product released in 1985, for example, gave Tandem users the ability to reduce transaction cost substantially. GUARDIAN 90XF software, a more powerful version of the Tandem operating system software, increases performance 50-70% for customers using all the facilities of ENCOMPASS data base management software, at no additional cost.

Technical focus:

ADVANCED DISC SYSTEMS

Another major cause of "computer fat" and performance bottlenecks is conventional disc access and storage. Users of conventional devices may waste as much as 70% of disc space to achieve the rapid response rates needed for OLTP applications.

Tandem has radically improved OLTP disc performance and cost through the parallel data access architecture of the new V8 and XL8 Disc Storage Facilities.

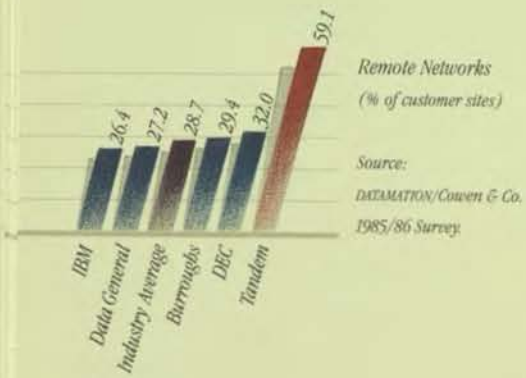
Up to eight drives are packaged in a single, compact cabinet. The V8 facility is designed to be extremely cost-effective for high activity on-line data bases. Response time is the fastest in the industry. And 100% of the disc space is used. The complementary XL8 facility is designed for maximum data storage in the minimum space.

These new Tandem products also dramatically reduce the high cost of computer room space. The V8 and XL8 disc systems concentrate much more capacity per square foot than any conventional disc device: 1.3 and 4.2 gigabytes (billions of bytes), respectively, in just six square feet of floor space. In one large application, five V8 drives provide 700 accesses per second in one-fifth the space and with $100,000 less in equipment than the nearest competitor.

Like the NonStop architecture, the V8 and XL8 Disc Storage Facilities are fault tolerant and expand modularly. Users can start with four drives per cabinet and expand up to eight as applications grow.

"Tandem, through its architectural approach, its GUARDIAN operating system with DYNABUS, its software facilities, and its extensive networking facilities, is a vendor with proven experience that has met and addressed the five basic requirements for on-line transaction processing."

– Yankee Group Research, Inc.



Remote Networks
(% of customer sites)

Source:
DATAMATION/Cowen & Co. 1985/86 Survey

Market direction:

INTERCONNECTION OF APPLICATIONS

With the proliferation of automated applications has come the need to tie together isolated applications into powerful networks. Interconnected applications provide a more complete business picture, reduce costs and increase competitive advantages.

But the networking and communications task can be formidable.

With conventional computers, there are normally long lead times and high costs associated with programming networks.

Performance can deteriorate significantly when linking systems not specifically designed for networking.

Lack of a single communications standard requires complex interfaces.

And businesses in dynamic environments encounter difficulty in forecasting computer size requirements at each of many network nodes. It can be even more difficult, with conventional computers, to alter the network configuration quickly and inexpensively if business is better than expected or if requirements change.

TANDEM LEADS THE WAY:

Tandem's networking and communications offerings are comprehensive, easily implemented and cost effective.

Building a network of Tandem systems is a relatively simple matter because the message-based operating system means that even a single Tandem system operates as a network. Hence, a network is no more complex than a single system.

The integration of EXPAND networking software into the operating system creates a high-performance, fully transparent network of systems. Programming applications across a network is the same as programming a stand-alone application. Users need not know where data resides in the network to complete a transaction. And EXPAND networks provide high performance because the networking software is not grafted on as it is in most systems.

To preserve customers' investments in their various incompatible systems, Tandem got an early start in supporting communications standards to provide the necessary interfaces. Tandem's communications products simplify interconnecting with systems and networks of other vendors.

Tandem's SNAX software, for example, is recognized as the best software for integrating IBM systems and IBM's SNA networks outside of SNA itself. More than 130 Tandem customers have licensed SNAX software.

Tandem was one of the first vendors to support the X.25 European Open Systems Interconnection (OSI) standard, and we continue to work to support emerging OSI standards.

Tandem was the first vendor independently certified for conformance to MAP Level 2.1, the General Motors protocol for interconnection of incompatible devices and systems. MAP is evolving as an important communications standard for manufacturing.

Tandem's communications products add the values of fault tolerance, transparent distribution, data integrity and high performance.

We also lead the way with value-added network security in support of the U.S. National Bureau of Standards Data Encryption Standard. Data is protected from unauthorized access while on the system, in transmission and in storage with Tandem's new SAFEGUARD system protection software and SAFE-T-NET data encryption subsystem.

Industry focus:

FINANCIAL

Bunker Ramo, a major supplier of real-time investment information services, significantly changed its way of doing business and its competitive posture with the introduction in 1985 of its SuperNet™ brokerage network.

SuperNet transforms Bunker Ramo from a terminal manufacturer and information provider to a leading-edge supplier of integrated network services. Bunker Ramo's installed base of over 30,000 brokerage subscribers now can have access to expanded services on either an existing Bunker Ramo terminal, an IBM PC-based brokerage automation system or the broker's own personal computer.

A Tandem 6-node EXPAND backbone network will integrate and transmit up-to-the-second information between previously incompatible terminals and host computers. The new network can reduce broker's communications costs, provide access to a greater volume of timely information and increase productivity.

Tandem's networking architecture is a key part of the SuperNet strategy to preserve customers' investment in Bunker Ramo systems and, at the same time, provide them with the flexibility to access the network with other office equipment.

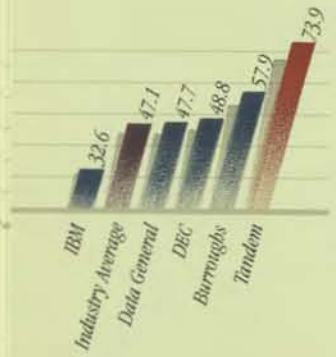
Tandem's corporate network organization will work closely with Bunker Ramo to help assure the success of SuperNet. And Bunker Ramo has joined the Tandem Alliance program to market its proprietary, Tandem driven applications to large financial institutions.

ALLIED Bunker Ramo

The financial services industry is an important part of Tandem's business. Fifteen major stock exchanges worldwide use Tandem systems, as do 17 of the largest brokerage firms.

"Tandem Computers' proven record of user acceptance for the concept of multiprocessing will give strength to the trend of distributing transaction work loads."

–COMPUTERWORLD



Data Base Management Software Users
(% of customer sites)

Source:
DATAMATION/Cowen & Co. 1985/86 Survey.

Market direction:

DISTRIBUTED APPLICATIONS

The success of an application at one location in a large organization provides a great incentive to introduce the application companywide.

To do so, companies typically begin by installing terminals at the remote locations that communicate with the central location's computer. But, as transactions multiply, communicating over long distances can drive costs up sharply.

Long distance communication also slows transaction response times which reduces productivity, further eroding the value of the transaction.

The ideal, therefore, is to distribute all or part of the application's data base to systems located at the sites where the transactions occur, while preserving access by all locations.

TANDEM LEADS THE WAY:

Although for many years there has been a need to distribute data, the capability was rarely implemented until Tandem, five years ago, began delivering the industry's first high-performance, distributed relational data base (DDB) system, ENCOMPASS.

Two fundamental problems of distributing data bases–the distribution itself and data integrity–have been successfully addressed by Tandem.

The distribution task on Tandem systems is relatively simple because the data base management function in a Tandem system is already distributed across all processors. The architecture has no single point of control and no common memory. With the integration of ENCOMPASS relational data base management software, programming and use are no more difficult than with a centralized data base: neither the programmer nor the user need know where the data resides.

Data integrity across a DDB must be assured before an application can be distributed or a user risks contaminating the data base. With Tandem's Transaction Monitoring Facility (TMF), transactions automatically update records in multiple nodes of the DDB. In the event of a communications or system failure anywhere in the DDB, TMF assures that there are no incomplete transactions, assuring the consistency of the information regardless of location. No other computer manufacturer offers this level of logical data integrity across a distributed data base.

TMF also gives Tandem fast data base recovery. In the event of a failure anywhere in the DDB, recovery is automatic.

Industry focus:

MANUFACTURING

Societa Pneumatici Pirelli SpA, one of the largest industrial companies in Italy and maker of the world-respected Pirelli tires, has distributed its manufacturing data bases on Tandem systems throughout Italy.

The data bases are distributed to three plants in northern and central Italy and one in Sicily. They are interconnected by a Tandem EXPAND network that enables users at the four plants to access data transparently from any one of the nodes as well as from a host mainframe in Milan. The network also integrates Tandem terminals and those of other computer suppliers.

Pirelli's Tandem driven applications in Italy, Germany and the United Kingdom are used for production planning and step-by-step manufacturing control, stock control, scheduling of equipment maintenance, attendance records, defect analysis and final inspection.

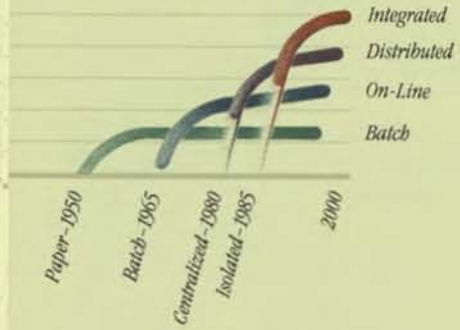
Pirelli has manufacturing facilities in eight countries and began using Tandem systems in 1981. In addition to tires, the company produces electrical cables, fiber optics and automotive rubber components.

Tandem systems are at work at over 200 manufacturing companies worldwide.

"The highest incidence of advanced systems software usage is at Tandem installed sites."

–DATAMATION/Cowen & Co. 1985/1986 Survey

Movement to Integration



Market direction:

INTEGRATED APPLICATIONS & RESOURCES

In almost every industry, the challenge of the Sixties and Seventies was to automate. In the Eighties and Nineties, the challenge expands to integration of multiple applications, systems, devices and networks into a single information resource.

Integration multiplies the cost-effectiveness and competitiveness of the individual information assets. It has become essential to preserve customers' huge investments in an array of incompatible applications, terminals and mainframe computers while distributing information to more users.

The challenge is not limited to organizations integrating their own resources. There are increasing opportunities for interaction with incompatible data bases and networks of other organizations (retail point-of-sale with banks, for example) to accomplish more efficient transactions and provide new, competitive services.

Nor is the challenge limited to integration of computer systems and networks. An evolving need must be met to integrate information from other devices (such as facsimile and copying machines, smart terminals and wands) that are becoming increasingly sophisticated data capturers and transmitters.

TANDEM LEADS THE WAY:

The Tandem architecture suits the integration task. We have invested heavily to produce superior products that are fundamental to integration.

Integration is impossible without networking to interconnect multiple systems at different locations. Broad communications products are essential to tie into a variety of incompatible systems and networks. Distributed data base capabilities are key because applications may be in multiple locations. Fault tolerance is crucial because integration concentrates all of the information needed to run a business into in a single resource. And modular expandability with linear performance is fundamental to handling cost-effectively the increased transaction workloads generated by integration.

Tandem provides all of those integration capabilities. And more.

Tandem has a family of leading-edge integration products collectively called Information Management Technology (IMT). Its foundation is TRANSFER software which merges and moves information between individuals or application programs regardless of the source, format or location of the information.

IMT products, running under TRANSFER software, move combinations of text, data and images from a wide variety of devices through a Tandem network as a single package. Using PS MAIL electronic mail software in combination with FAXLINK and PC LINK facilities, a user can, for example, transmit a drawing with an electronic message and also "attach" a copy of a personal computer file.

The integration function is natural to the Tandem NonStop architecture. Because integration solutions with Tandem systems can be developed with comparative ease–and because Tandem views integration as an extension of on-line transaction processing–Tandem intends to continue to lead the way in this important market direction.

Industry focus:

TELECOMMUNICATIONS

At General Telephone Company of the Northwest (GTNW,) as elsewhere within the GTE organization, integration of various applications, devices, systems and networks is actively underway.

One example is GTNW's 6-node Tandem EXPAND network called LEADS (Line Equipment Assignment and Display System) that links some 1,500 terminals in Oregon, Washington and Idaho. This application, which replaces a manual, paper system to allocate telephone numbers, switch equipment and cable pairs, has cut the previous people-intensive, two or three day process to minutes. The system has also been exported to Canada.

GTNW is a Tandem Alliance member. By leveraging its LEADS experience, GTNW will be able to offer an integrated network management package which consists of facilities management, service order entry, billing, repair and directory assistance packages. These systems, designed to execute on Tandem hardware, are sized and scoped for both telephone companies and private network operations.

Tandem has a growing presence in the telecommunications industry. Forty telecommunications companies in the U.S., Canada, United Kingdom, Europe and Australia use Tandem systems. And many enhanced services, such as Federal Express ZapMail™ and Western Union Easylink,™ are delivered on Tandem systems.

Tandem made major progress this year in the areas critical for long-term success.

TO OUR STOCKHOLDERS

This year Tandem did well strategically and became stronger as a company. By augmenting support and introducing many new products, we maintained a high level of customer satisfaction. Our future position strengthened through the continued commitment to our product programs and through the enhancement of our support of third parties that develop application solutions for Tandem systems. Asset management improved, increasing our financial strength. Tandem made major progress this year in the areas critical for long-term success.

Tandem grew despite the weak demand environment in the United States, yet growth was not equal to the rates of prior years. The strength of the U.S. dollar compared with last year adversely affected both revenue and earnings.

We did not hold expenses as well as we would have liked. We added needed people in customer-related areas and in development. We also invested in third-party relationships essential for future market penetration. Pretax income was slightly ahead of the fiscal 1984 level. Nonetheless, we missed our goal of achieving profitability improvement this year.

The Foundation for 1986

In fiscal 1986, we will continue our focus on strategic areas while we improve expense control so we can grow with very limited increases in employment. We have taken steps to control expenses to position Tandem for improved profitability if capital spending in our market improves. We currently are holding employment levels approximately flat until our marketplace strengthens. Total employment at the end of fiscal 1985 was down slightly from the prior quarter's level. We implemented a number of short-term measures to reduce operating expenses. We also consolidated some manufacturing operations, which should help to continue the improvement in manufacturing efficiency.

We have achieved significant efficiencies in manufacturing over the past two years as a result of major changes we made in our manufacturing operations. Inventory levels have been reduced and the gross profit margin has increased. We believe we can achieve similar efficiencies in marketing.

At the beginning of the 1986 fiscal year, we restructured our marketing organization. Tandem's market is changing, and we saw the opportunity to change our organization in order to build on our successes in this market.

For example, we have made significant penetration of major accounts, and many of these accounts are nationally and internationally distributed. We have defined better ways to support and sell to these accounts throughout their locations. As our customers undertake projects to develop important applications on Tandem systems that are critical to their business operations, Tandem increasingly is asked to participate in the development of the project. We have created a new organization that will provide professional management of such projects.

These two examples represent the ways we intend to leverage our successes and increase efficiency in marketing while maintaining quality. We believe the opportunities are greater than ever, and the new organization will increase our ability to win and win efficiently.

Market Strength

This year we enhanced our strong leadership position in on-line transaction processing, networking, distributed data base and integration of applications and resources in anticipation of emerging competition. The foundation for this leadership is Tandem's multiprocessor architecture.

Tandem has an established position in a number of industries where on-line transaction processing applications are growing rapidly. This year, for example, we strengthened our position in retail point-of-sale and in manufacturing control applications. We increased our penetration of telephone companies, a new target market for Tandem.

We added many important new accounts such as Daimler-Benz and Toshiba in manufacturing; Hoare Govett, Bunker Ramo Information Systems and the Chicago Mercantile Exchange in financial services; Bank of Tokyo, Amro Bank and Standard Chartered Bank in banking; and Shell Canada, J.C. Penney and Ross Stores in point-of-sale retailing.

This past year we offered our customers a wide range of new products, many with strategic importance. The V8 Disc Storage Facility set a new standard for performance in on-line transaction processing applications through a proprietary packaging design. The low-priced EXT system extended Tandem's system family into non-computer room environments. We announced the first products under our Information Management Technology (IMT) strategy. IMT is a multi-vendor system integration strategy to allow our customers to use their Tandem networks to provide company-wide information sharing between users of a variety of incompatible electronic office devices and networks.

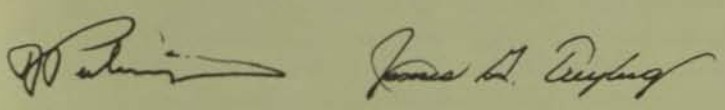
Perhaps most importantly, the new, high-performance GUARDIAN 90 operating system software gives us the foundation for the applications of the 1990s. GUARDIAN 90, which represents a significant revision and extension of the original GUARDIAN operating system, was developed with a view to the requirements of the next decade. We are proud of the significant performance improvements our customers report from using this new operating system software.

Tandem introduced numerous other products as well, such as enhancements to SNAX, our IBM System Network Architecture interface, support for General Motors' Manufacturing Automation Protocol (MAP) standard, programmer productivity tools, workstation products and new languages.

Outlook

Fiscal 1986 will continue the rapid pace of product introductions. In the first weeks of the new fiscal year, Tandem introduced system security tools, three new ergonomic terminals, as well as high-end disc and tape storage subsystems that incorporate the latest in disc, tape and VLSI-based controller technologies.

We are working to make fiscal 1986 a more profitable year as well. Although the weak demand environment may persist for some months, we are taking actions to position the company for stronger performance. We have created a new organization for leverage, efficiency and quality. We will limit hiring and continue expense control so that an improvement in the selling environment will result in better earnings for our stockholders.



Thomas J. Perkins
Chairman of the Board

James G. Treybig
President and
Chief Executive Officer

December 16, 1985

Thomas J. Perkins

James G. Treybig

Overview

Tandem Computers is committed to being a technological leader in the expanding market for on-line transaction processing systems and networks. The Company believes that its computer architecture uniquely satisfies the fundamental requirements for such applications. Achieving this technological leadership goal involves many factors, including strategic market positioning, a commitment to product development and an organizational structure and philosophy that foster employee productivity and creativity. Further, Tandem believes it is essential to maintain a strong financial position and operating record to allow the Company to maximize its opportunities within this dynamic market.

Results of Operations

The following table summarizes the changes in selected operating indicators for the years presented. The percentages on the left show the relationship of the revenue dollar to various income and expense items. The percentages on the right measure the year-to-year percentage increases or decreases.

% of Revenue				% Increase (Decrease)		
1985	1984	1983		1985	1984	1983
100	100	100	Revenue	17	27	34
38	40	42	Cost of revenue	11	23	46
12	10	9	Product development	36	34	16
42	40	37	Marketing, general and administrative	23	39	31
8	10	12	Operating income	(2)	3	22
1	1	–	Interest income, net	21	610	(88)
9	11	12	Pretax income	–	11	8
4	4	5	Current tax provision	(5)	17	17
–	(2)	–	DISC reversal	–	–	–
6	6	7	Net income excluding DISC reversal	4	8	3
6	8	7	Net income	(20)	39	3
			Earnings per share excluding DISC reversal	3	5	–
			Earnings per share	(21)	37	–

Amounts may not total due to rounding.

Revenue

The rate of revenue growth has slowed over the past three years as the Company has undergone a transition to a major supplier in the on-line transaction processing marketplace. The Company's product line has broadened and its customers' needs have expanded, leading to changes in Tandem's market. Further, demand for computers in the U.S. weakened significantly during fiscal 1985, while the strength of the U.S. dollar negatively affected international revenue and profits.

Tandem's revenue gains over the last three years result directly from increased shipments of its hardware and software products to new and existing customers and from increases in the number of customers using its support and training services. The Company's total revenue increased $92 million in fiscal 1985 over fiscal 1984. Nearly three-quarters of the increase came from higher product shipment levels, while the remainder was due to greater service and other revenue. International business, led by Europe, grew more rapidly than domestic, despite the adverse effects of the strong U.S. dollar. International operations contributed 33% of total revenue in fiscal 1985, compared with 31% in the prior year.

In fiscal 1984, revenue increased $114 million over fiscal 1983. Over three-quarters of the increase resulted from higher product shipment levels, while the remainder was due to greater service and other revenue. The growth in international business was considerably stronger than in domestic business. The percentage of total revenue contributed from international operations grew to 31% from 29% in fiscal 1983.

Operating Income

Operating income as a percent of revenue has declined in the past two years because improved gross profit margins were offset by increased product development and marketing, general and administrative expenses. In part, the increase in operating expenses as a percent of revenue resulted from the Company's anticipation of a stronger demand environment than the industry experienced during fiscal 1985.

The Company increased its product development expenditures in fiscal 1985 in support of a more aggressive product introduction schedule. The large number of product introductions in 1985 resulted in increased marketing costs to bring the products to market and to train new and existing sales, service and support personnel.

Tandem's product development effort focuses on meeting the needs of computer users who are implementing on-line systems at single sites and in geographically distributed information processing networks. The Company believes that the opportunities for technological innovation in this marketplace are substantial and, therefore, has increased its investment in product development each year since its founding. The Company expects to increase expenditures on product development in fiscal 1986. However, certain software development expenditures will be capitalized in fiscal 1986, rather than expensed as in the past, due to the implementation of Financial Accounting Standards Board Statement No. 86 which requires capitalization of certain software development expenses. The effect of this accounting change cannot be quantified at this time, however, the Company does expect some positive impact on earnings.

The Company keys its marketing strategy on selling to users who are implementing major on-line transaction processing applications. Providing a high level of service and support is essential to meeting the needs of this customer base. To maximize its long-term opportunities in this marketplace, Tandem has built a direct selling and support organization in industrial markets throughout the world. The Company's direct selling efforts are complemented by relationships established with third-party application software developers, equipment remarketers and distributors.

Marketing, general and administrative expenses have increased as a percent of revenue since fiscal 1983 as the Company has continued to build its marketing organization to meet future needs. In addition to factors noted above, these expenses increased during fiscal 1985 due to further development of Tandem third-party marketing relationships.

In response to the changing needs of the marketplace, the Company slowed the growth in employment during 1985 and has recently restructured the marketing organization with the goal of

improving efficiency and countering the industry trend toward lower operating margins. In addition, cost savings measures were implemented during the year to reduce total payroll, travel and entertainment and energy costs. The Company expects to reduce the employment growth rate further during fiscal 1986.

Cost of revenue as a percent of revenue continued to decline in fiscal 1985. The Company attributes the improvement primarily to the success of its programs to increase efficiency in manufacturing operations. Given a reasonable level of demand, the Company expects to maintain a strong gross profit margin in fiscal 1986.

Net Income and Earnings Per Share

The rate of change in net income has differed from that of operating income over the past three years because of changes in the Company's net interest income and effective tax rate. This year, net interest income was more than $1 million higher than in fiscal 1984 and more than $5 million higher than in fiscal 1983. The effect of lower prevailing interest rates in fiscal 1985 was offset by continuing declines in interest expense and by higher levels of short-term investments throughout the year than in the previous two years.

Net interest income in fiscal 1984 was substantially higher than that of fiscal 1983 because the Company maintained much higher levels of interest-earning short-term investments.

Net income comparisions for the three years are distorted by a one-time tax benefit recorded in fiscal 1984. In that year, there was a reversal of taxes that had been accrued on earnings of the Company's Domestic International Sales Corporation (DISC). The effective tax rate in fiscal 1984 was 24 percent, reflecting a $10 million DISC benefit. In comparison, the effective tax rate was 39 percent in both fiscal 1985 and 1983.

Earnings per share in fiscal 1985 were $.82, compared with earnings per share in 1984 of $.80 (net of the $.24 benefit from the DISC tax reversal) and $.76 in 1983.

Financial Condition

Tandem's financial condition continued to be strong and improved throughout fiscal 1985. For the third consecutive year, the cash and cash investments balance grew. Cash reached an all-time high, rising to $129 million at September 30, 1985, from $107 million at the end of fiscal 1984. Key factors contributing to record cash levels were income from operations, improved asset management and employee purchases of stock. Compared to the prior year, inventories declined by more than $13 million despite an expanded product line and a 15% increase in product shipments. Factors contributing to the decline in inventories were stronger than expected demand in the final fiscal quarter of the year, improved management of the manufacturing process, improved planning of materials purchasing and reductions in component costs.

An important part of Tandem's corporate philosophy is to provide all employees with the opportunity to participate in the Company's ownership through employee stock purchase and option programs. As a result of employee participation in these programs, the Company received $10 million in fiscal 1985 and $17 million in fiscal 1984.

The Company's financial strategy also includes maintaining a sound ratio of current assets to current liabilities and a conservative capital structure. At the end of fiscal 1985, the current ratio was 4.4:1, long term debt and capitalized lease obligations were 2.9% of total capital, unused lines of credit totaled $70 million and the equity base was $420 million. Tandem believes this strategy provides the maximum near-term and long-term flexibility to utilize a full range of financing alternatives to fund the Company's future business needs.

Effect of Inflation

Please see page 27 of this report for a discussion of the effect of changing prices on the Company's operations.

SELECTED FINANCIAL DATA

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

For the Five Years Ended September 30, 1985

(In thousands except per share amounts)	1985	1984	1983	1982	1981
Revenue	$624,138	$532,620	$418,282	$312,143	$208,397
Cost of revenue	240,148	215,692	175,646	120,390	84,868
Product development	71,577	52,514	39,168	33,642	17,833
Marketing, general and administrative	262,332	213,313	153,697	117,403	65,305
Operating Income	50,081	51,101	49,771	40,708	40,391
Interest income, net	6,269	5,183	730	6,033	10,707
Provision for income taxes					
Current period	(21,976)	(23,076)	(19,696)	(16,885)	(24,549)
Benefit of DISC tax reversal	–	9,700	–	–	–
Net Income	$ 34,374	$ 42,908	$ 30,805	$ 29,856	$ 26,549
Earnings Per Share	$ .82	$ 1.04	$ .76	$ .76	$ .72
Total assets	$552,344	$501,873	$415,525	$337,366	$255,971
Long term debt and capitalized lease obligations	$ 12,412	$ 17,155	$ 23,957	$ 21,102	$ 2,054
Stockholders' investment	$420,408	$375,122	$310,993	$250,988	$204,810

CONSOLIDATED STATEMENT OF INCOME

For the Three Years Ended September 30, 1985

(In thousands except per share amounts)	1985	1984	1983
Revenue			
Product revenue	$515,109	$448,611	$360,133
Service and other revenue	109,029	84,009	58,149
Total revenue	624,138	532,620	418,282
Costs and Expenses			
Cost of revenue	240,148	215,692	175,646
Product development	71,577	52,514	39,168
Marketing, general and administrative	262,332	213,313	153,697
Total costs and expenses	574,057	481,519	368,511
Operating Income	50,081	51,101	49,771
Interest expense	(2,407)	(2,642)	(2,806)
Interest income	8,676	7,825	3,536
Income Before Income Taxes	56,350	56,284	50,501
Provision For Income Taxes			
Current period	(21,976)	(23,076)	(19,696)
Benefit of DISC tax reversal	–	9,700	–
Total provision for income taxes	(21,976)	(13,376)	(19,696)
Net Income	$ 34,374	$ 42,908	$ 30,805
Earnings Per Share	$ .82	$ 1.04	$ .76
Weighted average shares outstanding	41,765	41,399	40,784

Because of the Company's method of operation, it is not practical or meaningful to report the cost of service and other revenue as a separate line item.

The accompanying notes are an integral part of this statement.

CONSOLIDATED BALANCE SHEET

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

As of September 30, 1985 and 1984

(In thousands except share amounts)	1985	1984
Assets		
Current Assets		
Cash and cash investments	$128,676	$106,862
Accounts receivable, net of allowances of $3,479 in 1985 and $1,708 in 1984	163,378	146,342
Inventories	78,962	92,375
Prepaid expenses and other	10,746	6,998
Prepaid income taxes	3,655	–
Total current assets	385,417	352,577
Property, Plant and Equipment, at cost		
Land and Building	25,398	8,782
Machinery and equipment	55,669	46,642
Computer equipment and spares	119,982	85,002
Leasehold improvements	32,363	31,320
Construction in process	7,932	20,009
	241,344	191,755
Accumulated depreciation and amortization	(80,746)	(50,253)
Net property, plant and equipment	160,598	141,502
Other Assets	6,329	7,794
Total Assets	$552,344	$501,873
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 7,049	$ 15,025
Accounts payable	33,377	36,350
Accrued liabilities		
Wages, payroll taxes and employee benefits	28,196	22,527
Income taxes	–	4,440
Other accrued liabilities	18,184	10,832
Total current liabilities	86,806	89,174
Capitalized Lease Obligations	7,969	11,744
Long Term Debt	4,443	5,411
Deferred Income Taxes	32,718	20,422
Stockholders' Investment		
Common stock $.025 par value, authorized 60,000,000 shares, outstanding 41,386,572 in 1985 and 40,616,638 in 1984	1,035	1,015
Additional paid-in capital	238,998	228,106
Retained earnings	180,375	146,001
Total stockholders' investment	420,408	375,122
Total Liabilities and Stockholders' Investment	$552,344	$501,873

The accompanying notes are an integral part of this balance sheet.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' INVESTMENT

For the Three Years Ended September 30, 1985

(In thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Total
Balance September 30, 1982	37,635	$ 941	$177,759	$ 72,288	$250,988
Sale of common stock under stock option plans	1,634	41	19,054	–	19,095
Sale of common stock under stock purchase plan	284	7	5,929	–	5,936
Tax benefit from employee transactions in common stock	–	–	4,169	–	4,169
Net income	–	–	–	30,805	30,805
Balance September 30, 1983	39,553	989	206,911	103,093	310,993
Sale of common stock under stock option plans	779	19	9,983	–	10,002
Sale of common stock under stock purchase plan	285	7	6,982	–	6,989
Tax benefit from employee transactions in common stock	–	–	4,230	–	4,230
Net income	–	–	–	42,908	42,908
Balance September 30, 1984	40,617	1,015	228,106	146,001	375,122
Sale of common stock under stock option plans	352	10	3,873	–	3,883
Sale of common stock under stock purchase plan	418	10	6,184	–	6,194
Tax benefit from employee transactions in common stock	–	–	835	–	835
Net income	–	–	–	34,374	34,374
Balance September 30, 1985	41,387	$1,035	$238,998	$180,375	$420,408

The accompanying notes are an integral part of this statement.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Three Years Ended September 30, 1985

(In thousands)	1985	1984	1983
Funds (Cash and cash investments) at beginning of period	$106,862	$ 93,501	$24,816
Provided from (Used in) Operations			
Sources:			
Net income	34,374	42,908	30,805
Depreciation and amortization	35,616	22,741	18,836
Deferred income taxes	12,296	(3,544)	5,903
Net book value of property, plant and equipment sold or retired	13,810	6,614	14,408
Total sources	96,096	68,719	69,952
Uses:			
Increase in accounts receivable	17,036	26,784	20,748
Increase (decrease) in inventories	(13,413)	6,455	(15,415)
Net change in prepaid expenses and non-debt current liabilities	1,795	(25,652)	(13,359)
Investment in property, plant and equipment	67,568	71,519	42,222
Increase (decrease) in other assets, net	(511)	2,361	401
Total uses	72,475	81,467	34,597
Net provided from (used in) operations	23,621	(12,748)	35,355
Provided from (Repayment of) External Financings			
Increase (decrease) in capitalized leases, net	(3,552)	(3,442)	6,331
Increase (decrease) in long term debt, net	(9,167)	8,330	(2,201)
Sale of common stock under employee stock option and stock purchase plans	10,077	16,991	25,031
Tax benefit from employee transactions in common stock	835	4,230	4,169
Total provided from (repayment of) external financings	(1,807)	26,109	33,330
Funds (Cash and cash investments) at end of period	$128,676	$106,862	$93,501

The accompanying notes are an integral part of this statement.

1. Summary of Significant Accounting Policies

Consolidation
The consolidated financial statements include the accounts of Tandem Computers Incorporated and its wholly-owned subsidiaries after elimination of intercompany accounts and transactions.

Revenue Recognition
The Company generally recognizes revenue from equipment sales at the time of shipment. Service and other revenue are recognized ratably over the contractual period or as the services are provided.

Translation of Non-U.S. Currency Amounts
Assets and liabilities of the Company's subsidiaries which are denominated in the local currency of the subsidiary are translated into U.S. dollars (the functional currency) at year-end exchange rates, except for inventories and property, plant and equipment, which are translated at approximate rates prevailing when the assets were acquired. Income and expense items are translated at average rates of exchange prevailing during the year, except that cost of goods sold and depreciation are translated at historical rates. Exchange gains and losses, which are not material for each of the periods presented, are included in earnings currently.

Inventories
Inventories are stated at the lower of cost (first-in, first-out) or market and include materials, labor and manufacturing overhead. The components of inventories as of September 30 were:

(In thousands)	1985	1984
Purchased parts and subassemblies	$41,434	$45,259
Work-in-process	11,176	12,400
Finished goods	26,352	34,716
Total	$78,962	$92,375

Income Taxes
The Company accounts for investment and research and development tax credits as a reduction of the provision for income taxes in the year in which the related credits are generated.

Property, Plant and Equipment
Systems spares ($35,420,000 in 1985 and $25,863,000 in 1984) are depreciated over a five-year period using an accelerated depreciation method. All other property, plant and equipment are depreciated using the straight-line method. The estimated useful lives are:

Buildings	30 years
Machinery and equipment	5-10 years
Computer equipment and spares	5- 7 years
Leasehold improvements	Lease term

Earnings Per Share
Earnings per common share have been computed based upon the weighted average number of common and common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options outstanding that have a dilutive effect when applying the treasury stock method. Fully diluted earnings per share are substantially the same as reported earnings per share.

Reclassifications
Prior period amounts associated with cost of service and other revenue have been reclassified in order to conform to the current period presentation.

2. Income Taxes

The provision for income taxes included the following deferred (prepaid) items:

(In thousands)	1985	1984	1983
Federal:			
Current	$ 2,950	$13,882	$ 1,370
Deferred (Prepaid)	4,610	(10,550)	10,574
	7,560	3,332	11,944
State:			
Current	3,522	4,800	1,532
Deferred (Prepaid)	423	(297)	534
	3,945	4,503	2,066
Foreign:			
Current	12,005	6,197	4,621
Deferred (Prepaid)	(1,534)	(656)	1,065
	10,471	5,541	5,686
Total Provision	$21,976	$13,376	$19,696

Sources of deferred (prepaid) taxes were as follows:

(In thousands)	1985	1984	1983
Installment sale method for income tax reporting	$9,752	$ (1,950)	$ 8,572
DISC income	(6,117)	(6,084)	3,181
Accelerated depreciation	2,586	2,950	2,628
Expenses recognized for financial statements, but not for income tax reporting	(2,632)	(4,943)	810
Effect of intercompany profit eliminations	(90)	(2,178)	(4,143)
Other	–	702	1,125
Total Deferred (Prepaid)	$3,499	$(11,503)	$12,173

The provision for income taxes differs from the amount obtained by applying the federal statutory income tax rate to income before taxes as follows:

	1985	1984	1983
Federal statutory tax rate	46%	46%	46%
State taxes, net of federal income tax benefit	4	4	4
Investment tax credits	(3)	(3)	(4)
Research and development tax credits	(8)	(7)	(7)
Tax exempt DISC and FSC income	(4)	(1)	–
Other	4	2	–
	39	41	39
Benefit of DISC tax reversal	–	(17)	–
Effective Tax Rate	39%	24%	39%

The 1984 benefit of Domestic International Sales Corporation (DISC) tax reversal represents the benefit of deferred taxes previously provided on DISC earnings accumulated prior to the enactment of the Tax Reduction Act of 1984.

The Company established a Foreign Sales Corporation (FSC) effective January 1, 1985.

3. Lease and Other Commitments

The Company leases its headquarters, field offices, certain equipment, automobiles and most of its operating facilities under operating lease agreements. The Company also has capitalized leases for certain equipment. Future minimum lease payments as of September 30, 1985 are as follows:

(In thousands)	Leases	
Fiscal Year	Operating	Capital
1986	$ 29,900	$ 5,349
1987	24,467	5,104
1988	21,280	3,730
1989	19,897	210
1990	18,988	30
Thereafter	79,749	–
Total minimum lease payments	$194,281	14,423
Less amount representing interest (4% – 17%)		2,648
Present value of minimum lease payments		$11,775

The cost of assets held under capitalized leases totaled $20,504,000 and $21,605,000 at September 30, 1985 and 1984, respectively, and are included in the machinery and equipment and computer equipment and spares classifications in the accompanying Balance Sheet. The accumulated depreciation associated with these assets totaled $11,928,000 and $8,686,000 at September 30, 1985 and 1984, respectively.

Rent expenses were $38,213,000 in 1985, $36,726,000 in 1984 and $30,458,000 in 1983.

4. Long Term Debt

Long term debt as of September 30 consists of the following:

(In thousands)	1985	1984
6.9% and 8.2% promissory notes payable to a bank, in Japanese yen, due January 1986 and March 1987	$2,573	$ 2,327
Convertible subordinated debenture, payable to an officer of the Company, bearing interest at 9.5% and due September 1989	1,667	–
Industrial revenue bond, bearing interest at 12%, due July 1992	1,000	1,000
Industrial revenue bond, bearing interest at 12.4%, due July 1992 and collateralized by certain equipment	1,000	1,000
Construction financing	–	11,250
Other	1,446	1,276
	7,686	16,853
Less current portion	3,243	11,442
Long term debt	$4,443	$ 5,411

The $1,667,500 convertible subordinated debenture is convertible into 100,000 shares of Common Stock at a price of $16.675. The debenture becomes convertible as to 25,000 shares each year beginning in September 1986 and is subject to conversion acceleration in the event of certain occurrences.

Interest costs of $594,000, $1,606,000 and $644,000 relating to construction projects were capitalized during fiscal 1985, 1984 and 1983, respectively.

The Company has entered into unsecured credit agreements totaling $70,000,000 with several banks for working capital purposes. The agreements provide for revolving borrowings through December 1985, at which time outstanding amounts may be converted to term loans to be amortized through 1988. Domestic borrowings bear interest at or below the banks' prime rates through December 1985 and approximately 1/4% above these rates through 1988. The Company is required to pay a commitment fee of 5/16% per annum. There are no compensating balances required under any of these arrangements.

Certain financial covenants and restrictions are included in the loan agreements. The Company was in compliance with all such covenants and restrictions at September 30, 1985.

The Company has guaranteed payment of loans made to officers totalling $837,000 at September 30, 1985 under a $2,000,000 bank line of credit. In addition, the Company has a $1,667,500 note receivable from an officer included in Other Assets which matures in September 1989 and bears interest at an annual rate of 10%.

5. Capital Stock

The Company's authorized capital stock consists of 2,400,000 shares of preferred stock, 4,000,000 shares of Junior Common Stock and 56,000,000 shares of Common Stock. At September 30, 1985, 13,794,393 shares of Common Stock were reserved for future issuance under stock option plans, the employee stock purchase plan and a convertible subordinated debenture. There were no shares of preferred stock or Junior Common Stock outstanding at September 30, 1985.

Preferred Stock Rights

During 1985, the Company declared a dividend of one preferred share purchase right for each then outstanding share of Common Stock. In addition, one right will be issued with each share of Common Stock issued by the Company before the date the rights become exercisable, are redeemed by the Company or expire on May 17, 1990. The rights will not be exercisable, or transferable apart from the Common Stock, until 10 days after another person or group of persons acquires 20% of the Common Stock or commences, or announces its intention to commence, a tender or exchange offer for 30% of the Common Stock. Each right entitles its holder to buy one one-hundredth of a share of a newly created series of preferred stock of the Company, par value $.10 per share, designated as Series A Participating Preferred Stock, at an exercise price of $80.00. In certain circumstances, the right will entitle its holder to purchase a larger amount of preferred stock or stock in an acquiring company.

Stock Option Plans

The Company has employee stock option plans under which permanent employees may be granted options to purchase shares of Common Stock at 100% of fair market value at the time of the grant. Options generally become exercisable six months after the effective date and expire no later than seven years after the effective date. At the discretion of the Board of Directors, options granted under the stock option plans may qualify for Incentive Stock Option treatment under the Economic Recovery Tax Act of 1981.

As of September 30, 1985 options for 6,438,989 shares were outstanding at prices ranging from $3.96 to $34.88, with an average price of $21.56. Options for 5,831,459 shares were exercisable as of September 30, 1985. Options for 5,709,069 shares are available for future grant. Options were exercised at prices ranging from $3.96 to $26.88 in 1985, $3.92 to $26.88 in 1984, and $.58 to $26.88 in 1983.

Employee Stock Purchase Plan

As of September 30, 1985 the Company has reserved 1,051,935 shares of Common Stock for future issuance under its employee stock purchase plan. Under the plan, the Company may offer shares to employees by two methods. Under one method, eligible employees may elect to purchase shares of Common Stock at 85% of fair market value as of the last trading day before or the last trading day of the participation period. Under the second method, the Company may grant to all employees the option to purchase the same number of shares of Common Stock at not less than 85% of fair market value at the grant date. As of September 30, 1985 options to purchase 22,400 common shares at $29.00 and 472,000 common shares at $15.73 were outstanding under the second method. Such options are exercisable through January 20, 1986 and through February 28, 1987, respectively.

6. Geographic Segment Information

The following table sets forth information about the Company's operations in different geographic regions for the three years ended September 30, 1985.

	Geographic Area				
(In thousands)	United States	Europe	Other	Eliminations	Consolidated
1985					
Revenue-Customer	$417,460	$136,307	$ 70,371	$ –	$624,138
Revenue-Intercompany	111,742	–	–	(111,742)	–
Revenue-Total	529,202	136,307	70,371	(111,742)	624,138
Pretax Income	34,586	15,496	6,555	(287)	56,350
Identifiable Assets	436,835	101,836	47,386	(33,713)	552,344
1984					
Revenue-Customer	$364,873	$109,562	$ 58,185	$ –	$532,620
Revenue-Intercompany	90,850	–	–	(90,850)	–
Revenue-Total	455,723	109,562	58,185	(90,850)	532,620
Pretax Income	46,977	10,842	5,261	(6,796)	56,284
Identifiable Assets	421,974	79,747	31,732	(31,580)	501,873
1983					
Revenue-Customer	$297,722	$ 91,100	$ 29,460	$ –	$418,282
Revenue-Intercompany	68,001	–	–	(68,001)	–
Revenue-Total	365,723	91,100	29,460	(68,001)	418,282
Pretax Income	49,084	11,546	(1,127)	(9,002)	50,501
Identifiable Assets	336,193	73,923	26,058	(20,649)	415,525

Intercompany transfers are made at arm's length prices, which include manufacturing profits attributable to United States operations. Identifiable assets are those assets of the Company that are identified with the operations of the corresponding geographic area. United States customer revenue includes export sales of $7,053,000 in 1985, $5,989,000 in 1984 and $6,400,000 in 1983.

7. Commitments and Contingencies

The Company, along with three present or former principal officers, was named as a defendant in a class action complaint filed in the United States District Court for the Northern District of California on October 23, 1984 purporting to state claims for alleged violations of federal securities laws and pendent state claims arising out of the Company's December 1982 restatement of revenue and earnings for fiscal 1982. The court dismissed the complaint as to the individual defendants in March 1985 with leave to amend. Subsequently, the court granted the defendant's motion for summary judgment and dismissed the suit in September 1985. The plaintiff filed a notice of appeal in October 1985. No provision has been made in the accompanying financial statements for possible liability because, in the opinion of management, it is unlikely that the ultimate disposition of the suit would have a material effect on the Company's financial position.

In addition, there are various actions or claims which have been brought or asserted against the Company. Management does not consider them to be material to the Company's financial position.

8. Unaudited Quarterly Financial Data

(In thousands except per share amounts)

Quarters Ended	Dec. 31	March 31	June 30	Sept. 30
Year ended September 30, 1985				
Revenue	$159,653	$146,489	$144,165	$173,831
Costs and Expenses				
Cost of revenue	62,021	57,713	56,116	64,298
Product development	15,127	17,075	18,027	21,348
Marketing, general and administrative	59,996	61,998	69,482	70,856
Total costs and expenses	137,144	136,786	143,625	156,502
Operating Income	22,509	9,703	540	17,329
Interest income, net	1,888	1,573	1,298	1,510
Income Before Income Taxes	24,397	11,276	1,838	18,839
Provision for Income Taxes	(10,369)	(4,435)	550	(7,722)
Net Income	$ 14,028	$ 6,841	$ 2,388	$ 11,117
Earnings Per Share	$ .34	$ .16	$ .06	$ .27
Year ended September 30, 1984				
Revenue	$126,369	$111,236	$141,925	$153,090
Costs and Expenses				
Cost of revenue	51,360	47,826	56,563	59,943
Product development	10,849	12,853	13,514	15,298
Marketing, general and administrative	47,282	48,551	57,506	57,974
Total costs and expenses	109,491	109,230	127,583	135,215
Operating Income	16,878	2,006	14,342	17,875
Interest income, net	1,076	1,142	1,243	1,722
Income Before Income Taxes	17,954	3,148	15,585	19,597
Provision for Income Taxes				
Current period	(7,900)	(1,174)	(6,335)	(7,667)
Benefit of DISC tax reversal	–	–	–	9,700
Total provision for income taxes	(7,900)	(1,174)	(6,335)	2,033
Net Income	$ 10,054	$ 1,974	$ 9,250	$ 21,630
Earnings Per Share	$ .24	$ .05	$ .23	$ .53

9. Information on the Effects of Inflation (Unaudited)

The Company has provided an adjusted summary of operations and selected financial data in accordance with the Financial Accounting Standards Board Statement No. 33, as amended, concerning "Financial Reporting and Changing Prices." This disclosure requirement is experimental and involves considerably more judgment than traditional financial statements and, therefore, should be reviewed with caution.

Inflation-adjusted information was completed using the "current cost" method which requires the Company to adjust asset values based on specific indices and appraisals.

The method does not allow for inflation adjustments to operating expenses, revenue or net interest income, nor an adjustment to the tax provision, despite the decrease in pretax income which results from the inflation adjustments. Only the cost of revenue and depreciation expense related to the assets, which are restated for inflation effects, are adjusted.

Depreciation is computed on a straight-line basis, rather than the accelerated basis that is used for some assets in the Company's historical financial statements, because the accelerated method already recognizes some of the effects of inflation.

Net income for fiscal 1985 was lower under the current cost method because of higher depreciation and amortization expense resulting from higher asset values. Companies that hold monetary assets during a period of inflation lose purchasing power. Tandem held net monetary assets during the period, and their purchasing power declined.

CONSOLIDATED STATEMENT OF INCOME ADJUSTED FOR INFLATION

For the Year Ended September 30, 1985

	In Average 1985 Dollars	
(In thousands except per share amounts)	Historic Cost	Current Cost
Total Revenue	$624,138	$624,138
Cost of revenue, excluding depreciation and amortization	225,550	225,550
Other costs and expenses, excluding depreciation and amortization	312,891	312,891
Depreciation and amortization	35,616	38,534
Interest (income), net	(6,269)	(6,269)
Provision for income taxes	21,976	21,976
Net Income	$ 34,374	$ 31,456
Increase in value of inventories, property, plant and equipment held during the year:		
Measured in general prices		$ 8,428
Measured in specific prices		8,367
Excess of increase in general price level (constant dollars) over increase in specific prices		$ 61

At September 30, 1985, current cost of inventory was $79,133,000 and current cost of property, plant and equipment, net of accumulated depreciation, was $180,193,000.

FIVE YEAR COMPARISON OF SELECTED FINANCIAL DATA ADJUSTED FOR INFLATION

(Dollars in thousands except per share amounts)

	In Average 1985 Dollars				
	1985	1984	1983	1982	1981
Total revenue					
Constant dollars	$624,138	$552,234	$451,501	$348,596	$250,045
Current cost information					
Net income	$ 31,456	$ 43,774	$ 31,666		
Earnings per share	$ .75	$ 1.06	$ .78		
Net assets at year-end	$433,546	$396,455	$337,247		
Excess of increase in general price level (constant dollars) over increase in specific prices	$ .61	$ 811	$ 1,242		
Other information					
Decrease in purchasing power of net monetary items	$ 5,334	$ 5,673	$ 3,040		
Market price per share at end of period	$ 14.38	$ 16.72	$ 38.32	$ 25.41	$ 33.00
Average CPI (1967=100)	319.4	308.0	295.9	286.0	266.2

AUDITORS' REPORT

To Tandem Computers Incorporated:

We have examined the consolidated balance sheet of Tandem Computers Incorporated (a Delaware corporation) and subsidiaries as of September 30, 1985 and 1984 and the related consolidated statements of income, stockholders' investment and changes in financial position for each of the three years in the period ended September 30, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Tandem Computers Incorporated and subsidiaries as of September 30, 1985 and 1984, and the results of their operations and the changes in their financial position for each of the three years in the period ended September 30, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

San Jose, California,
November 1, 1985.

Arthur Andersen & Co.

TANDEM STOCK PRICE

Calendar Quarter Price	High	Low
1985 3rd Quarter	18 5/8	13 1/8
2nd Quarter	23 7/8	14 1/2
1st Quarter	28 5/8	17 5/8
1984 4th Quarter	20 1/8	14 3/4
3rd Quarter	24 3/4	13
2nd Quarter	30 5/8	16 1/4
1st Quarter	40 1/4	30
1983 4th Quarter	39 1/2	30
3rd Quarter	36 1/2	26
2nd Quarter	34	25 1/2
1st Quarter	30 1/2	23 5/8

Tandem Computers Incorporated is traded via the NASDAQ National Market System under the trading symbol TNDM. All quotations shown represent the high and low sale prices. No cash dividends have been declared on the Common Stock.

Board of Directors

Thomas J. Perkins,
Chairman of the Board; General Partner,
Kleiner, Perkins, Caufield & Byers

Morton Collins,
General Partner, DSV Associates

Thomas J. Davis, Jr.,
General Partner, Mayfield Fund

Franklin P. Johnson, Jr.,
Chairman, Asset Management Company

Andrew Knight,
Editor, *The Economist*,
Economist Newspaper Ltd.

Robert C. Marshall,
Senior Vice President and Chief
Operating Officer, Tandem
Computers Incorporated

Robert G. Stone, Jr.,
Chairman of the Board,
Kirby Exploration Company

James G. Treybig,
President and Chief Executive Officer,
Tandem Computers Incorporated

Thomas I. Unterberg,
Chairman and Senior Managing Director,
L.F. Rothschild, Unterberg, Towbin

Auditors

Arthur Andersen & Co.
San Jose, California

Registrar and Transfer Agent

Bank of America N.T. & S.A.
San Francisco, California

Form 10-K

A copy of the Company's Report on Form 10-K for the 1985 fiscal year, as filed with the Securities and Exchange Commission, is available on written request. Please direct your request to:

Director of Investor Relations
Tandem Computers Incorporated
19333 Vallco Parkway
Cupertino, California 95014-2599

Annual Meeting

The annual meeting of stockholders will be held at 10:00 a.m. on Monday, February 3, 1986, at the Company's headquarters.

Corporate Headquarters

19333 Vallco Parkway
Cupertino, California 95014-2599
(408) 725-6000

Trademark

Tandem, NonStop, NonStop II, NonStop EXT, NonStop TXP, DYNABUS, ENCOMPASS, EXPAND, FAXLINK, GUARDIAN, GUARDIAN 90, GUARDIAN 90XF, SAFEGUARD, SAFE-T-NET, TRANSFER, TXP and XL8 are trademarks and service marks of Tandem Computers Incorporated.

Officers

James G. Treybig,
President and Chief Executive Officer

Robert C. Marshall,
Senior Vice President and
Chief Operating Officer

Michael K. Bateman,
Vice President – Third Party Marketing

Thomas A. Bechler,
Vice President and Division Manager

Jack W. Chapman,
Vice President and Managing Director,
Europe

Thomas L. Chun,
Vice President – Corporate Projects

George C. Eckert,
Vice President – Major Projects Management

Jan E. Jensen,
Vice President – Human Resources

Thomas J. Klitgaard,
Vice President – Corporate Counsel

Richard A. Lamb,
Treasurer

Lawrence A. Laurich,
Vice President – Engineering

Dennis L. McEvoy,
Vice President – Software

Lawrence W. McGraw,
Vice President – U.S. Sales Operations

Michael C. Moore,
Vice President and General Manager,
Intercontinental Division

Gerald L. Peterson,
Vice President – Marketing

Jerald D. Reaugh,
Vice President – MIS

David J. Rynne,
Vice President and Chief Financial Officer

Stephen C. Schmidt,
Vice President – Operations

Jeanne D. Wohlers,
Vice President and Corporate Controller

Domestic Sales and Service Offices

ALASKA, Anchorage

ARIZONA, Phoenix

ARKANSAS, Little Rock

CALIFORNIA, Culver City, Irvine, Long Beach, Los Angeles, Orinda, Riverside, Sacramento, San Diego, San Francisco, Santa Clara

COLORADO, Englewood

CONNECTICUT, Hartford, Stamford

FLORIDA, Jacksonville, Miami, Orlando, Tampa

GEORGIA, Atlanta

HAWAII, Honolulu

ILLINOIS, Chicago, Oakbrook

INDIANA, Indianapolis

IOWA, Cedar Rapids, Des Moines

KANSAS, Overland Park

LOUISIANA, Metairie

MARYLAND, Linthicum

MASSACHUSETTS, Newton

MICHIGAN, Ann Arbor, Lansing, Livonia

MINNESOTA, Edina

MISSISSIPPI, Jackson

MISSOURI, Creve Coeur, St. Louis

NEBRASKA, Omaha

NEVADA, Las Vegas

NEW JERSEY, Cherry Hill, Hasbrouck Heights

NEW MEXICO, Albuquerque

NEW YORK, Amherst, Fairport, Jericho, New York City

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OHIO, Cincinnati, Cleveland, Columbus, Dayton

OKLAHOMA, Oklahoma City, Tulsa

OREGON, Portland

PENNSYLVANIA, Allentown, Philadelphia, Pittsburgh

SOUTH CAROLINA, North Charleston

TENNESSEE, Memphis, Nashville

TEXAS, Austin, Dallas, Fort Worth, Harrisberg, Houston, Irving, San Antonio

UTAH, Salt Lake City

VIRGINIA, Reston, Richmond, Virginia Beach

WASHINGTON, Bellevue, Bremerton

WISCONSIN, Brookfield

International Subsidiaries

AUSTRALIA
Tandem NonStop Pty. Ltd
Adelaide, Brisbane, Melbourne, Perth, Sydney

AUSTRIA
Tandem Computer Ges.m.b.H.
Vienna

BELGIUM
Tandem Computers SA/NV
Brussels

CANADA
Tandem Computers Canada Ltd
Montreal, Ottawa, Toronto, Vancouver, Winnipeg

DENMARK
Tandem Computers A/S
Copenhagen

FRANCE
Tandem Computers S.A.
Paris

HONG KONG
Tandem Computers Hong Kong Ltd
Kowloon

ITALY
Tandem Computers Italia S.p.A.
Milan

JAPAN
Tandem Computers Japan Ltd
Osaka, Tokyo

THE NETHERLANDS
Tandem Computers BV
Amsterdam

NEW ZEALAND
Tandem NonStop Pty. Ltd
Wellington

NORWAY
Tandem Computers A/S
Oslo

SINGAPORE
Tandem Computers Int'l Inc.
Singapore

SPAIN
Tandem Computers Iberica S.A.
Madrid

SWEDEN
Tandem Computers A.B.
Stockholm

SWITZERLAND
Tandem Computers A.G.
Zurich

UNITED KINGDOM
Tandem Computers Ltd
Birmingham, Glascow, High Wycombe, London, Northolt, Rochdale

WEST GERMANY
Tandem Computers GmbH
Bonn, Dortmund, Duesseldorf, Frankfurt, Hamburg, Mannheim, Munich, Neufahrn, Stuttgart

International Distributors

ARGENTINA

COLOMBIA

FINLAND

MALAYSIA

MEXICO

MIDDLE EAST

SOUTH KOREA

TAIWAN

THAILAND

VENEZUELA

Produced by George E. Browne & Associates Printed in U.S.

Jeffry Canin
August 9, 1985

TANDEM COMPUTERS INCORPORATED (OTC-TNDM) $15 7/8

52-Week Range	Mkt. Val. (mil.)	Year Ends September 30 1984A	1985E	1986E	Calendar P/E 1984	1985	1986	Trend-Line Growth Rate
$13-29	$665	$0.80*	$0.65	$0.95	17	28	16	25%

* Excluding $0.24/share DISC credit

DJIN: 1320.79 **SPIN:** 209.43

- Third quarter reported well below projections.
- Near-term expectations effect neutral investment rating.

	Third Quarter Results				Year to Date: 9 Months		
	6/30/85	6/30/84	% Chg	H&Q Estimate	6/30/85	6/30/84	% Chg
Revenues (mil.)	$144.2	$141.9	2%	$155.0	$450.3	$379.5	19%
Pretax income (mil.)	1.8	15.6	(88)	12.0	37.5	36.7	2
Net income (mil.)	2.4	9.3	(74)	7.0	23.3	21.3	9
Earnings per share	**$0.06**	**$0.23**	**(75)**	**$0.16**	**$0.56**	**$0.51**	**9**
Average shares (mil.)	41.9	41.0	2	42.4	41.8	41.5	1
Gross margin	61.1%	59.3%		60.0%	60.9%	59.0%	
Operating margin	0.4	10.1		6.8	7.3	8.8	
Pretax margin	1.3	11.0		7.7	8.3	9.7	
Tax rate	(29.9)	40.6		42.0	38.0	42.0	
Net margin	1.7	6.5		4.5	5.2	5.6	

Third Quarter Results

Tandem is the originator and leading supplier of fault-tolerant computers, marketing its line of **NonStop** systems for use in on-line transaction processing applications. The company reported disappointing results for its third fiscal quarter, the second quarter of sequentially down revenues, and one in which Tandem barely broke even on operations. Total sales of $144 million were up marginally on a year-to-year basis (sales increased only as a result of higher service income) but fell 2% from the immediately preceding quarter. Gross margins of 61.1% were near record levels but were more than offset by a sharp ramp-up in operating expenses, both in absolute terms and in proportion to revenues, yielding an operating margin of only 0.4%. Tandem's sharp increase in operating expenses stemmed in part from the addition of 148 net new employees in the third quarter (following 181 new hires in the second quarter), bringing Tandem's total headcount to over 5,500. The excessive level is a result of both low manufacturing attrition and hiring in line with an overly ambitious top-line growth objective. The company's cash position at quarter-end was $109 million, up slightly from the second quarter; accounts receivable of $151 million represented 95 days outstanding, while inventory levels of $95 million, or 151 days, were reported (a six-day improvement and seven-day extension, respectively, from the preceding quarter levels). EPS of $0.06 were produced with the aid of a negative effective tax (owing to a partial reversal of first half taxes); a full tax rate of 40% would have yielded EPS of $0.03.

The company attributed poor sales, significantly below levels indicated by management when we visited Tandem only two weeks before quarter end, to the impact of a strong dollar overseas and industrywide weak domestic bookings. Although Tandem

does not release revenue composition by product line, management suggests that the sales shortfall resulted principally from a fairly slow start in deliveries of the low-cost **NonStop EXT** system and from below-plan shipments of high-end **NonStop TXPs.** (However, NonStop II-to-TXP upgrades apparently were marginally ahead of plan.) One bright note in an otherwise lackluster quarter was the significant uptick in the number of new accounts (38) the company added to its installed base. In addition, as part of the **"Tandem Alliance"** program, 21 third-party software houses with industry-specific application packages were added, bringing the cumulative total to nearly 100.

During the quarter, Tandem announced several new products: the low-end, compact **NonStop EXT;** an enhanced performance version of the company's **GUARDIAN** operating system; and a set of networking and office automation software packages. Tandem's **EXT** offers equivalent performance to and compatibility with the company's **NonStop II,** but it doesn't require a computer room environment. Unit priced at $120,000 (roughly 30% below a comparable NonStop II), the EXT will be sold both by Tandem directly and through a newly created vertical market reseller program. **GUARDIAN 90,** representing an estimated 60% rewrite of the Tandem operating system, offers significantly enhanced performance, estimated by management to be a four- to fivefold throughput improvement for batch applications and at least a 50% improvement for on-line programs utilizing Tandem's **Transaction Monitor Facility.** In June, the company announced its **Information Management Technology** offerings, five software packages designed to enable Tandem users to interconnect and network among Tandem host processors and various terminals, personal computers, and facsimile machines. Concurrently, the company announced an OEM and technology licensing agreement with Sytek to offer broadband local area networking to Tandem accounts. Other recent product announcements include color versions of the company's **Dynamite** workstation and reduced-price NonStop memory boards. We expect a series of near-term enhanced peripheral announcements and, more importantly, replacement models (presumably based on CMOS gate array technology) to be introduced over the next twelve months for both the low and high ends of Tandem's processor line.

Financial Expectations and Investment Opinion

In light of its poor third quarter performance, Tandem has taken a number of measures to reign in expenses, including a one-week paid vacation in the fourth quarter for all employees, a hiring freeze, and a three-month deferral on salary increases. Additionally, in response to its historically poor ability to project quarterly business, Tandem will adopt new statistical analysis techniques that it hopes will result in improved forecasting. Although we believe Tandem will retain its position as the predominant vendor of fault-tolerant computers, benefiting from the recent demise of several private would-be contenders and, to an extent, from the IBM/Stratus liaison (which we believe has eliminated the specter of a near-term competitive IBM proprietary offering), we do not envision a business turnaround in the next couple of quarters. We are anticipating flat year-to-year revenues in the fourth quarter (of $153 million), with a 65% decrease in EPS to $0.10; our fiscal 1986 estimates assume only a 20% annual increase in sales and operating margins that will remain below 10% of revenues. Given the company's current operating plan, we expect the fourth quarter to be cash-flow positive; additionally, we anticipate modest improvements in receivables and inventory levels. In 1984, Tandem reported $0.80 in EPS on sales of $533 million. Our revised estimates call for sales of $603 million, yielding EPS of $0.65 in fiscal 1985 (a down bottom line after four relatively flat years) and fiscal 1986 revenues of $725 million and EPS of $0.95. We believe Tandem shares are fully valued at present price levels and advise investors to defer purchase, pending greater business visibility.

NOTE a

Jeffry Canin
November 8, 1985

TANDEM COMPUTERS INCORPORATED (OTC-TNDM) $18 7/8

52-Week Range	Market Val. (mil.)	Fiscal EPS 1984A	Fiscal EPS 1985A	Fiscal EPS 1986E	Calendar P/E 1985	Calendar P/E 1986	Trend-Line Growth Rate
$13-29	$786	$0.80	$0.82	$0.90	29	21	25%

Year Ends: September 30 **DJIN:** 1404.36 **SPIN:** 214.90 **Note:** a

- o Company reports relatively strong fourth fiscal quarter.
- o Significant improvement in balance sheet is demonstrated.
- o Cautious fiscal 1986 outlook and recent share price appreciation effects neutral investment opinion.

	Fourth Quarter Results 9/30/85	9/30/84	% Chg	H&Q Est	Year to Date: 12 Months 9/30/85	9/30/84	% Chg
Revenues (mil.)	$173.8	$153.1	14%	$169.0	$624.1	$532.6	17%
Pretax income (mil.)	18.8	19.6	(4)	16.8	56.4	56.3	0
Net income (mil.)	11.1	11.9	(7)	10.5	34.4	33.2	4
Earnings per share	**$0.27**	**$0.29**	**(8)**	**$0.25**	**$0.82**	**$0.80**	**3**
Average shares (mil.)	41.6	40.9	2	42.0	41.8	41.4	1
Gross margin	63.0%	60.8%		61.5%	61.5%	59.5%	
Operating margin	10.0	11.7		9.1	8.0	9.6	
Pretax margin	10.8	12.8		10.0	9.0	10.6	
Tax rate	41.0	39.1		37.5	39.0	41.0	
Net margin	6.4	7.8		6.2	5.5	6.2	

Fourth Quarter Results

Tandem is the originator and leading supplier of fault-tolerant computers, marketing its line of NonStop systems for use in on-line transaction processing applications. As expected, the company recovered significantly from its exceptionally poor third quarter performance, reporting fourth quarter earnings, in line with projections, on record-level revenues. Quarterly sales of $174 million (of which $144 million represented product sales, and the balance represented service and other) grew 21% sequentially and 13.5% from one year earlier. Gross margins of 63.0%, a 2% improvement over Q3 (and our expectations), represented the highest levels since 1982. Operating expenses, while at record levels in absolute terms, were below either of the previous two quarters in proportion to sales, reflecting the cost-cutting measures imposed during Q4, which included a hiring freeze, a three-month deferral of salary increases and a one-week nonelective companywide vacation. Year-end headcount of 5,494 was effectively unchanged relative to one quarter earlier. For the year, revenues increased 17.2% to $624 million and gross margins improved 2% to 61.5%, countering any speculation on widespread list price discounting to encourage sales. Marketing and development expenses budgeted in line with an overly optimistic growth assumption,

however, effected a contraction in operating margins from the 9.6% reported in fiscal 1984 to 8.0% in fiscal 1985.

The company demonstrated substantial improvement in asset management during Q4. Tandem's cash position increased from three months earlier by nearly $20 million to record levels of $129 million, while accounts receivable of $163 million and inventories of $79 million represented 85 and 110 days-sales outstanding, respectively, impressive 10- and 41-day reductions over corresponding results reported at the end of Q3.

Approximately one third of quarterly revenues represented sales outside the United States, proportionally consistent with results for the last two years. While international sales have held up reasonably well through all of fiscal 1985, management notes a long-awaited pickup in domestic bookings recently. Although disclosing no specific number, the company indicates a relatively high level of new account activity, with significantly more new customers added during Q4 than the incremental 38 resulting from the immediately preceding Q3; the company's customer base now exceeds 1000. During the quarter, high-end TXP system sales were particularly strong, generating approximately 80% of total revenues. Twenty-two new third parties were added in Q4 to the company's Tandem Alliance program, which now includes 132 participants. Last week, a fourth Alliance category—the Independent Software Vendor (ISV) program—was announced, which now joins Tandem's existing roster of OEMs, system integrators, and direct-selling software houses, which together generate approximately one third of corporate revenues. Under the ISV program, Tandem itself will directly sell and support selected third-party software products.

In October, Tandem announced several new products, including a high-performance tape subsystem, ergonomic terminal models, a family of data encryption/security products, and a cost-effective, large-capacity, high-performance disk storage system. We anticipate the introduction of a high-end processor (the replacement for the TXP) during the first half of calendar 1986, with a low-end system announcement scheduled perhaps six months later.

Management is taking a conservative tack regarding 1986 expectations, suggesting that the relatively strong performance of 4Q85 is not indicative of a clear trend in improved business momentum. We are assuming, pending evidence to the contrary, that the current year's top-line growth will, at best, equal 1985's 17% increase relative to 1984 and more likely will fall short by 2-3%—the continuation of the company's as-yet-unbroken trend in decelerating annual revenue growth comparisons. While we expect Tandem to garner substantial continued add-on revenue from its existing customer base and to present a viable alternative to IBM for large-scale transaction-intensive applications, we anticipate an increasingly competitive environment at the low end—particularly represented by the Stratus/32 processor family, sold directly by Stratus or through its recently enhanced joint marketing agreement with IBM. Our estimates for fiscal 1986 remain unchanged—EPS of $0.90 on sales of $715 million. We view the one-month 22% appreciation in Tandem as fully discounting the better-than-expected 4Q85 finish, and, in light of the significant negative bottom-line year-to-year comparisons expected for the first half of 1986 (followed by a strong projected second half), we retain a neutral investment opinion.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED INTERIM BALANCE SHEET
(UNAUDITED)
(In Thousands)

ASSETS

	December 31, 1985	December 31, 1984
CURRENT ASSETS		
Cash and cash investments	$134,311	$112,163
Accounts receivable	178,252	152,920
Inventories	75,139	91,836
Prepaid income taxes	1,924	-
Prepaid expenses and other	13,774	9,542
Total current assets	403,400	366,461
PROPERTY, PLANT & EQUIPMENT, at cost	246,915	199,674
Less accumulated depreciation	(88,808)	(57,161)
Net property, plant & equipment	158,107	142,513
OTHER ASSETS	8,591	5,101
TOTAL ASSETS	$570,098	$514,075

LIABILITIES AND STOCKHOLDERS' INVESTMENT

CURRENT LIABILITIES		
Current portion of long term debt and capitalized lease obligations	$ 7,310	$ 6,638
Accounts payable	33,877	34,142
Accrued liabilities	47,773	37,585
Income taxes payable	-	9,022
Total current liabilities	88,960	87,387
CAPITALIZED LEASE OBLIGATIONS	6,978	10,772
LONG TERM DEBT	4,426	3,237
DEFERRED INCOME TAXES	34,684	19,252
STOCKHOLDERS' INVESTMENT	435,050	393,427
TOTAL LIABILITIES AND STOCKHOLDERS' INVESTMENT	$570,098	$514,075

TANDEMCOMPUTERS

Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-Q

Quarterly Report Under Section 13 or 15(d)
of the Securities Exchange Act of 1934

For Quarter Ended June 30, 1985 Commission File No. 0-9134

TANDEM COMPUTERS INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware (State of incorporation)	94-2266618 (IRS Employer Identification No.)
19333 Vallco Parkway, Cupertino, California (Address of principal executive offices)	95014-2599 (Zip Code)
Registrant's telephone number, with area code	(408)725-6000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No _____

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class:	Common Stock, $.025 par value	Outstanding at August 2, 1985: 41,371,347 shares

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Exhibit index on page 13.

Tandem Computers Incorporated
19191 Vallco Parkway
Cupertino, CA 95014-2599
(408) 725-6000

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

PART I - FINANCIAL INFORMATION

(Unaudited)

The consolidated financial statements included herein have been prepared by the Company, without audit by independent public accountants, according to the rules and regulations of the Securities and Exchange Commission. Consequently, certain information and footnote disclosure normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes the disclosures that are made are adequate to make the information presented not misleading. Further, the consolidated financial statements reflect, in the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position and results of operations as of and for the periods indicated.

It is suggested that these consolidated financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's 1984 Annual Report to Stockholders and the Annual Report on Form 10-K for the year ended September 30, 1984 filed with the Securities and Exchange Commission.

The results of operations for the three-month and nine-month periods ended June 30, 1985 are not necessarily indicative of results to be expected for the entire year ending September 30, 1985.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED INTERIM STATEMENT OF INCOME
(UNAUDITED)
(In thousands except per share amounts)

	For the Three Months Ended	
	June 30, 1985	June 30, 1984
Revenue		
Product revenue	$116,868	$119,064
Service and other revenue	27,297	22,861
Total revenue	144,165	141,925
Costs and Expenses		
Cost of revenue	56,116	56,563
Product development	18,027	13,514
Marketing, general and administrative	69,482	57,506
Total costs and expenses	143,625	127,583
Operating Income	540	14,342
Interest income, net	1,298	1,243
Income Before Income Taxes	1,838	15,585
Provision for income taxes	(550)	6,335
Net Income	$ 2,388	$ 9,250
Earnings Per Share	$ .06	$ .23
Weighted average shares outstanding	41,896	41,039

See accompanying notes to the consolidated condensed interim financial statements.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED INTERIM STATEMENT OF INCOME
(UNAUDITED)
(In thousands except per share amounts)

	For the Nine Months Ended	
	June 30, 1985	June 30, 1984
Revenue		
Product revenue	$371,091	$318,761
Service and other revenue	79,216	60,769
Total revenue	450,307	379,530
Costs and Expenses		
Cost of revenue	175,850	155,749
Product development	50,229	37,216
Marketing, general and administrative	191,476	153,339
Total costs and expenses	417,555	346,304
Operating Income	32,752	33,226
Interest income, net	4,759	3,461
Income Before Income Taxes	37,511	36,687
Provision for income taxes	14,254	15,409
Net Income	$ 23,257	$ 21,278
Earnings Per Share	$ .56	$ .51
Weighted average shares outstanding	41,812	41,558

See accompanying notes to the consolidated condensed interim financial statements.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED INTERIM BALANCE SHEET
(UNAUDITED)
(In thousands except share data)

	June 30, 1985	September 30, 1984
Assets		
Current Assets		
Cash and cash investments	$109,022	$106,862
Accounts receivable	150,606	146,342
Inventories	94,611	92,375
Prepaid income taxes	19,495	-
Prepaid expenses and other	9,241	6,998
Total current assets	382,975	352,577
Property, Plant & Equipment, at cost	230,817	191,755
Accumulated depreciation & amortization	(72,572)	(50,253)
Net property, plant & equipment	158,245	141,502
Other Assets	3,828	7,794
Total Assets	$545,048	$501,873
Liabilities and Stockholders' Investment		
Current Liabilities		
Current portion of long term debt and capitalized lease obligations	$ 6,675	$ 15,025
Accounts payable	36,678	36,350
Accrued liabilities:		
Wages, payroll taxes, and employee benefits	29,917	22,527
Income taxes	10,889	4,440
Other accrued liabilities	16,761	10,832
Total current liabilities	100,920	89,174
Capitalized Lease Obligations	8,817	11,744
Long Term Debt	2,719	5,411
Deferred Income Taxes	24,988	20,422
Stockholders' Investment		
Common stock, $.025 par value; authorized 60,000,000 shares; outstanding 41,260,521 at June 30 and 40,616,638 at September 30	1,032	1,015
Additional paid-in capital	237,314	228,106
Retained earnings	169,258	146,001
Total stockholders' investment	407,604	375,122
Total Liabilities and Stockholders' Investment	$545,048	$501,873

See accompanying notes to the consolidated condensed interim financial statements.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED INTERIM STATEMENT OF CHANGES IN FINANCIAL POSITION
(UNAUDITED)
(In thousands)

	For the Nine Months Ended	
	June 30, 1985	June 30, 1984
Funds (Cash and cash investments) at beginning of period	$106,862	$93,501
Provided from Operations		
Sources:		
Net income	23,257	21,278
Depreciation and amortization	25,078	16,292
Deferred income taxes	4,566	(3,150)
Total sources	52,901	34,420
Uses:		
Increase in accounts receivable	4,264	16,296
Increase in inventories	2,236	17,555
Net change in prepaid expenses and non-debt current liabilities	1,642	(16,798)
Investment in property, plant and equipment, net	41,249	45,237
Increase (decrease) in other assets	(3,394)	17
Total uses	45,997	62,307
Net provided from (used in) operations	6,904	(27,887)
Provided from External Financings		
Net decrease in capitalized leases	(2,761)	(2,318)
Increase in long term debt	1,823	4,047
Retirement of long term debt	(13,031)	-
Sale of common stock under employee stock option and stock purchase plans	8,285	14,453
Tax benefit from employee transactions in common stock	940	4,294
Total provided from external financings	(4,744)	20,476
Funds (Cash and cash investments) at end of period	$109,022	$86,090

See accompanying notes to the consolidated condensed interim financial statements.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED INTERIM FINANCIAL STATEMENTS

1. Reclassifications

Prior period amounts associated with cost of certain service and other revenue have been reclassified in order to conform to the current period presentation.

2. Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market and include material, labor and manufacturing overhead. The components of inventory were:

(In thousands)	June 30 1985	September 30 1984
Purchased parts and subassemblies	$54,024	$45,259
Work-in-process	15,462	12,400
Finished goods	25,125	34,716
Total	$94,611	$92,375

3. Earnings Per Share

Earnings per common share amounts have been computed based upon the weighted average number of common and common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options outstanding that have a dilutive effect when applying the treasury stock method. Fully diluted earnings per share are substantially the same as reported earnings per share.

4. Dividends

The Company has not declared or paid any cash dividends on its common stock. See Item 2 for a discussion of the preferred stock right dividend issued to stockholders during the quarter ended June 30, 1985.

TANDEM COMPUTERS INCORPORATED AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Financial Condition

The Company's financial condition remains strong. Cash and cash investments increased to $109,022,000 from the 1984 year-end level of $106,862,000. At the end of the third fiscal quarter of 1985, unused lines of credit totaled approximately $72,000,000, and the equity base was $407,604,000. The Company had a current ratio of 3.8:1, and long term debt and capitalized lease obligations were 2.8% of total capital (comprising stockholders' investment, long term debt and capitalized lease obligations).

Results of Operations

The following table sets forth items in the Consolidated Condensed Interim Statement of Income as a percentage of revenue for the current quarter, the prior year's quarter and the comparable nine-month periods.

Percent of Revenue

	3 Months Ended June 30		9 Months Ended June 30	
	1985	1984	1985	1984
Revenue	100.0%	100.0%	100.0%	100.0%
Cost of revenue	38.9	39.9	39.1	41.0
Product development	12.5	9.5	11.2	9.8
Marketing, general and administrative	48.2	40.5	42.5	40.4
Operating Income	0.4	10.1	7.3	8.8
Interest, net	0.9	0.9	1.1	0.9
Income Before Income Taxes	1.3	11.0	8.3	9.7
Net Income	1.7	6.5	5.2	5.6

Totals may not add due to rounding.

The table below gives the percentage increase or decrease over the comparable period a year earlier for items from the Consolidated Condensed Interim Statement of Income.

Percent Increase	3 Months Ended June 30, 1985	9 Months Ended June 30, 1985
Revenue	1.6%	18.6%
Cost of revenue	(0.8)	12.9
Product development	33.4	35.0
Marketing, general and administrative	20.8	24.9
Operating Income	(96.2)	(1.4)
Income Before Income Taxes	(88.2)	2.2
Net Income	(74.2)	9.3

Revenue for the quarter ended June 30, 1985 was $144,165,000, 1.6% higher than the corresponding figure of $141,925,000 for the quarter ended one year earlier. For the first nine months of fiscal 1985, revenue was up 18.6% to $450,307,000, compared with $379,530,000 posted in the same period of fiscal 1984.

The 1.8% decline in product revenue for the quarter ended June 30, 1985 compared with the same quarter in the prior year reflected the generally weak business conditions prevalent throughout the computer industry during this time period. The continuing softness in the Company's U.S. business was the major factor in the decline. The growth of 19.4% in service and other revenue accounted for the year-over-year gain in total revenue. Service revenues continued to increase due to a larger installed base of customers. For the nine-month period, both product revenue and service and other revenue remained ahead of the 1984 levels.

Operating income in the third fiscal quarter declined to $540,000 from $14,342,000 posted in the third quarter of fiscal 1984. On a percentage basis, cost of revenue declined versus last year. Both product development and marketing, general and administration increased. The Company's product development expenditures were at the level planned, however, they were higher as a percentage of revenue because realized revenue was below plan. Marketing, general and administrative expenses increased due to such factors as salaries and benefits for additional sales and marketing personnel, and costs associated with hardware and software product introductions.

For the first nine months of fiscal 1985, operating income was $32,752,000, 1.4% lower than the corresponding figure of $33,226,000 in the same period of last year.

Net interest income in the quarter was nearly the same as a year ago, despite significantly higher cash balances. The primary reason net interest income did not grow was that money market interest rates were lower than a year ago.

Net income was $2,388,000, or $.06 per share, for the third fiscal quarter, compared with $9,250,000, or $.23 per share, earned in the prior year's quarter. Nine-month net income was $23,257,000, or $.56 per share, versus $21,278,000, or $.51 per share, earned in the first nine months of fiscal 1984.

The current quarter's net income included a tax credit of $550,000, resulting from an over-accrual of taxes in prior quarters that reflected the Company's anticipation of higher income in the third quarter than was achieved. The effective tax rate for the nine months was 38%, compared with a rate of 42% for the first nine months of fiscal 1984. The single largest factor contributing to the decline in the effective tax rate was a change in the way certain earnings from foreign sales were treated for tax purposes in accordance with the Tax Reform Act of 1984.

PART II - OTHER INFORMATION

Item 2. Changes in Securities.

The description of the change in the Company's securities set forth in the Company's registration statement on Form 8-A filed with the Commission on July 15, 1985 is hereby incorporated by reference.

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits: See Exhibit Index.
(b) Reports on Form 8-K:

A special Report on Form 8-K pursuant to item 5 thereof was filed by the Company on June 5, 1985.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, in the City of Cupertino, State of California.

TANDEM COMPUTERS INCORPORATED
(Registrant)

Date August 13, 1985

By JEANNE D. WOHLERS
Jeanne D. Wohlers
Vice President and
Corporate Controller

Date August 13, 1985

By DAVID J. RYNNE
David J. Rynne
Vice President and
Chief Financial Officer