

DIGITAL
PRELIMINARY PERSONAL COMPUTER
BUSINESS PLAN

- Intel-Based Product
- Alpha Business Direction
- 1-800-SOFTWARE

April 28, 1993

DIGITAL
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BUSINESS PLAN

● Intel-Based Product

● Alpha Business Direction

● 1-800-SOFTWARE

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Agenda

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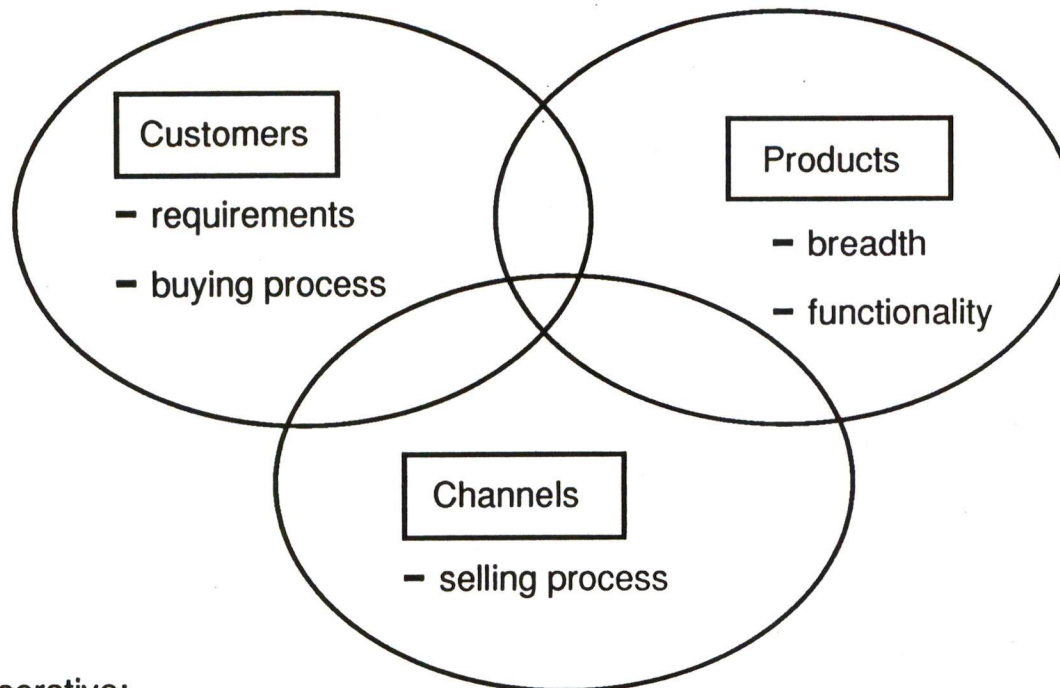
- What Digital must achieve in PC's
 - market and competitive trends and challenges

- How Digital will succeed in PC's
 - critical success factors
 - .products
 - .prices
 - .channels
 - .costs
 - financial summary
 - risks and dependencies

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OVERVIEW

- Digital requirement: To meet the best of competition on quality, price and cost within two years

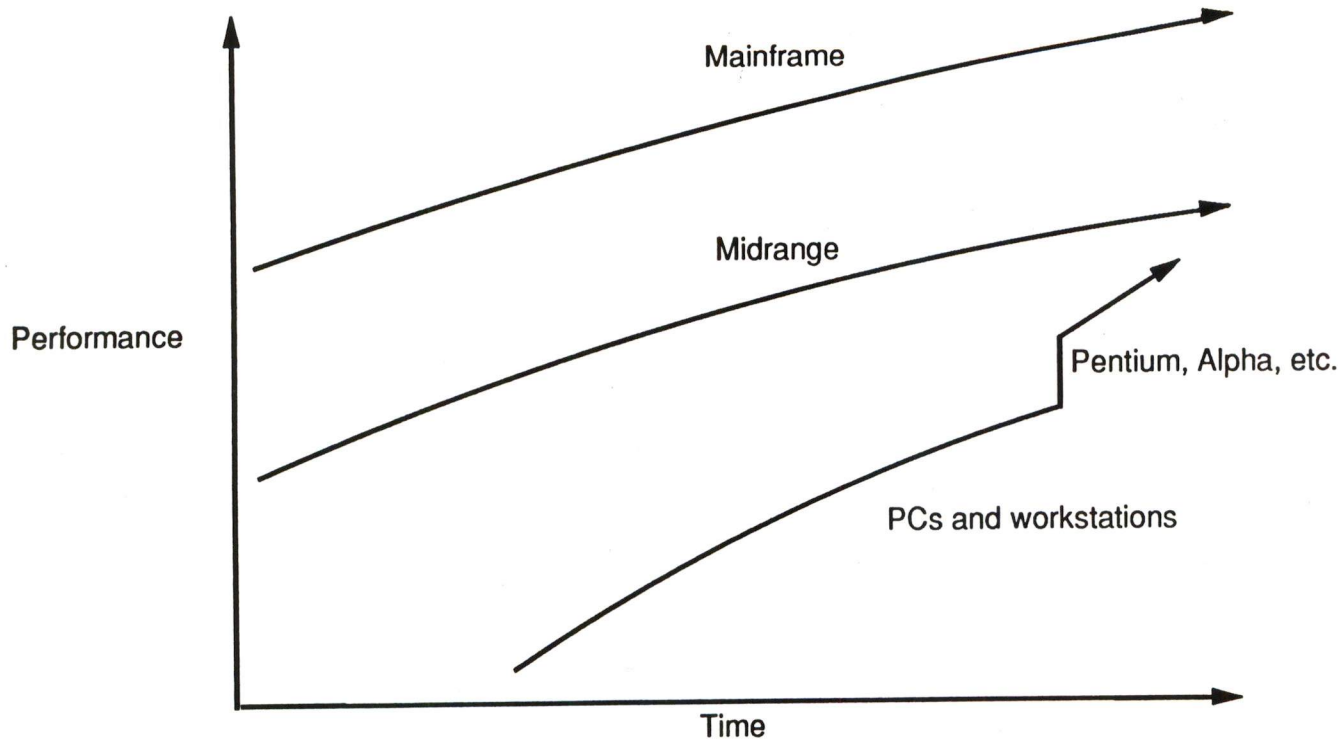


- Key imperative:
 - Digital has grown very rapidly in PCs, but unprofitably
 - Digital must
 - . continue to grow faster than the market leaders to achieve required scale
 - . dramatically reduce total cost to lowest levels achievable for its scale

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WHY SUCCESS IN PCs IS CRITICAL TO DIGITAL

The merging performance of desktops and midrange computers is accelerating customers' shift to PCs and workstations



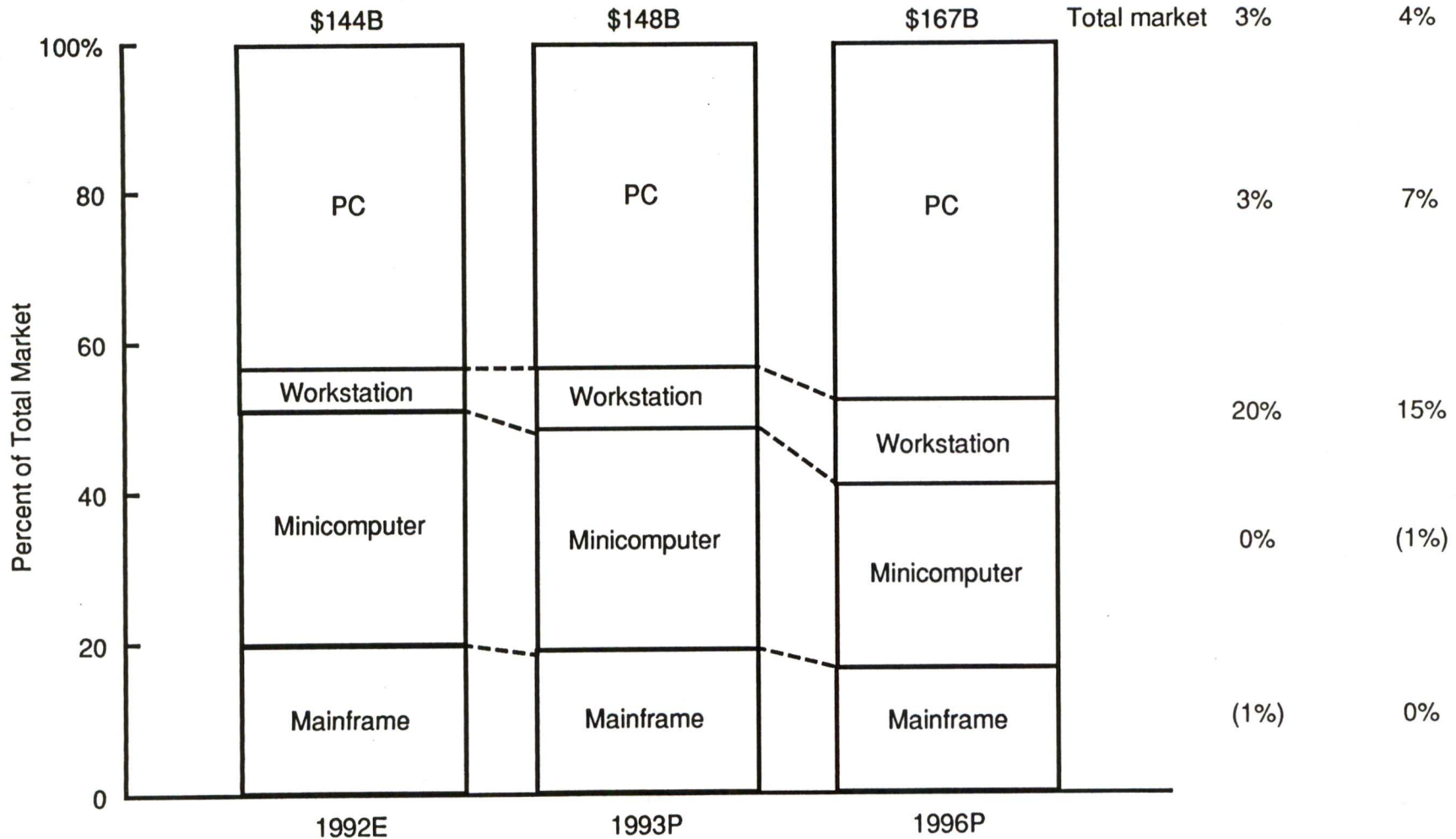
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COMPUTER HARDWARE MARKET

PC hardware sales are nearly half the hardware market today; by 1996 PCs and workstations will be nearly 60% of the market

CAGR

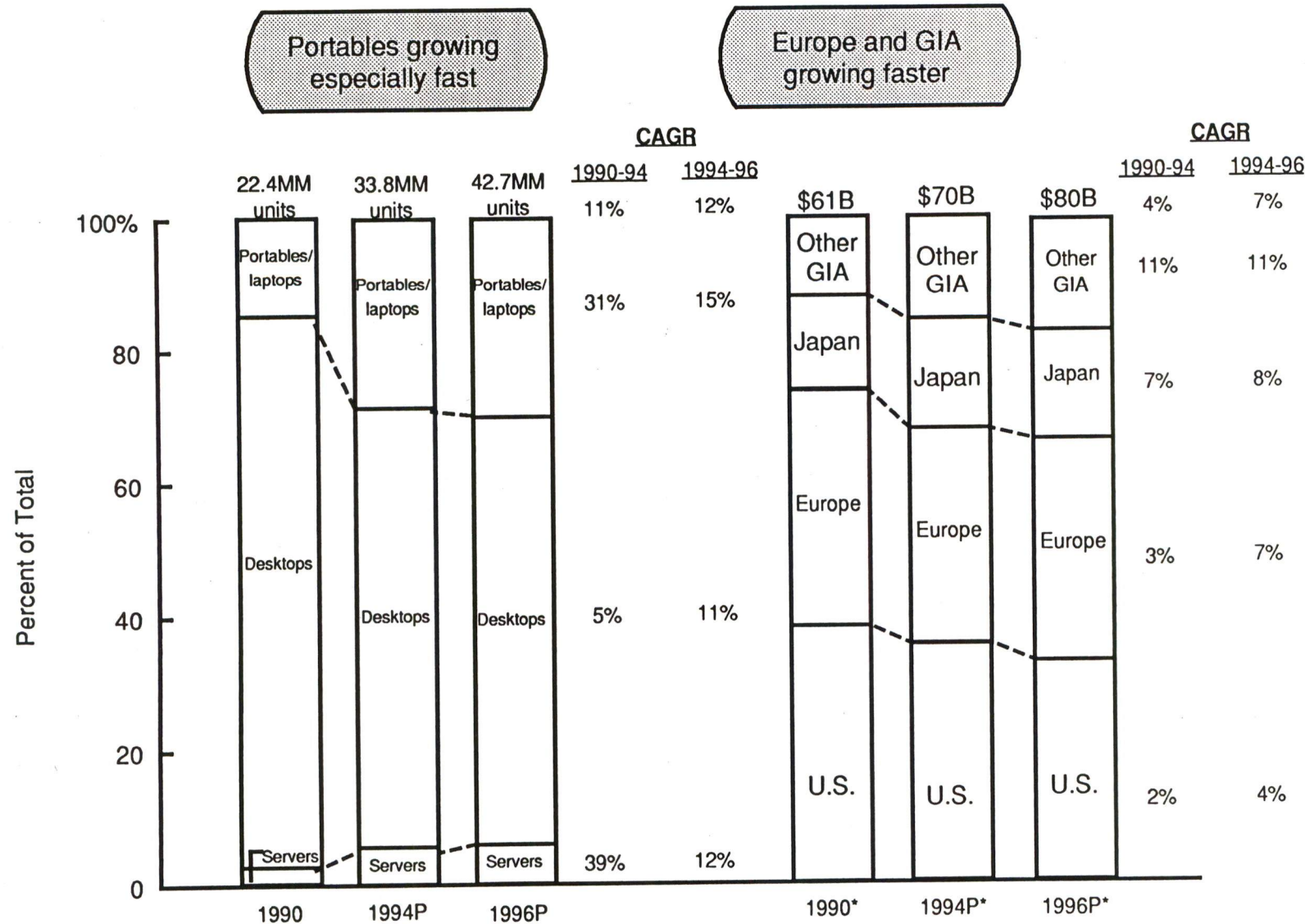
1992-93P 1993-96P



Source: IDC, Gartner Group, PCBU Estimate

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MARKET TRENDS



*Geographic splits are based on PC/single user workstation market
Source: IDC, Dataquest

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MARKET DEVELOPMENT

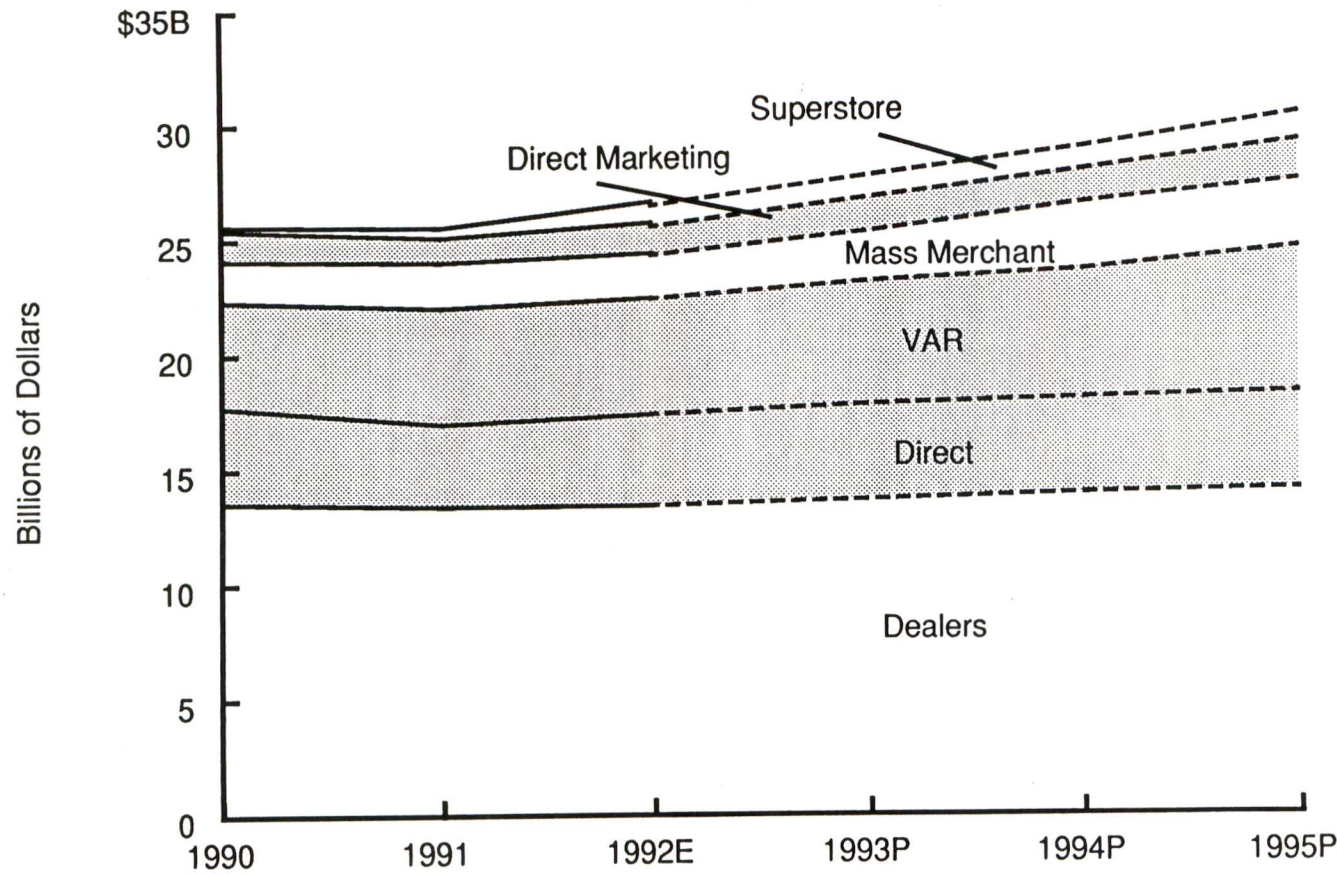
CHANNEL TRENDS (U.S.)

• Digital currently does not participate in retail channels.
 • Lower-cost channels are gaining share.

□ Digital participation

Channel Share and Growth

CAGR
 (1990-92E) (1992E-95P)

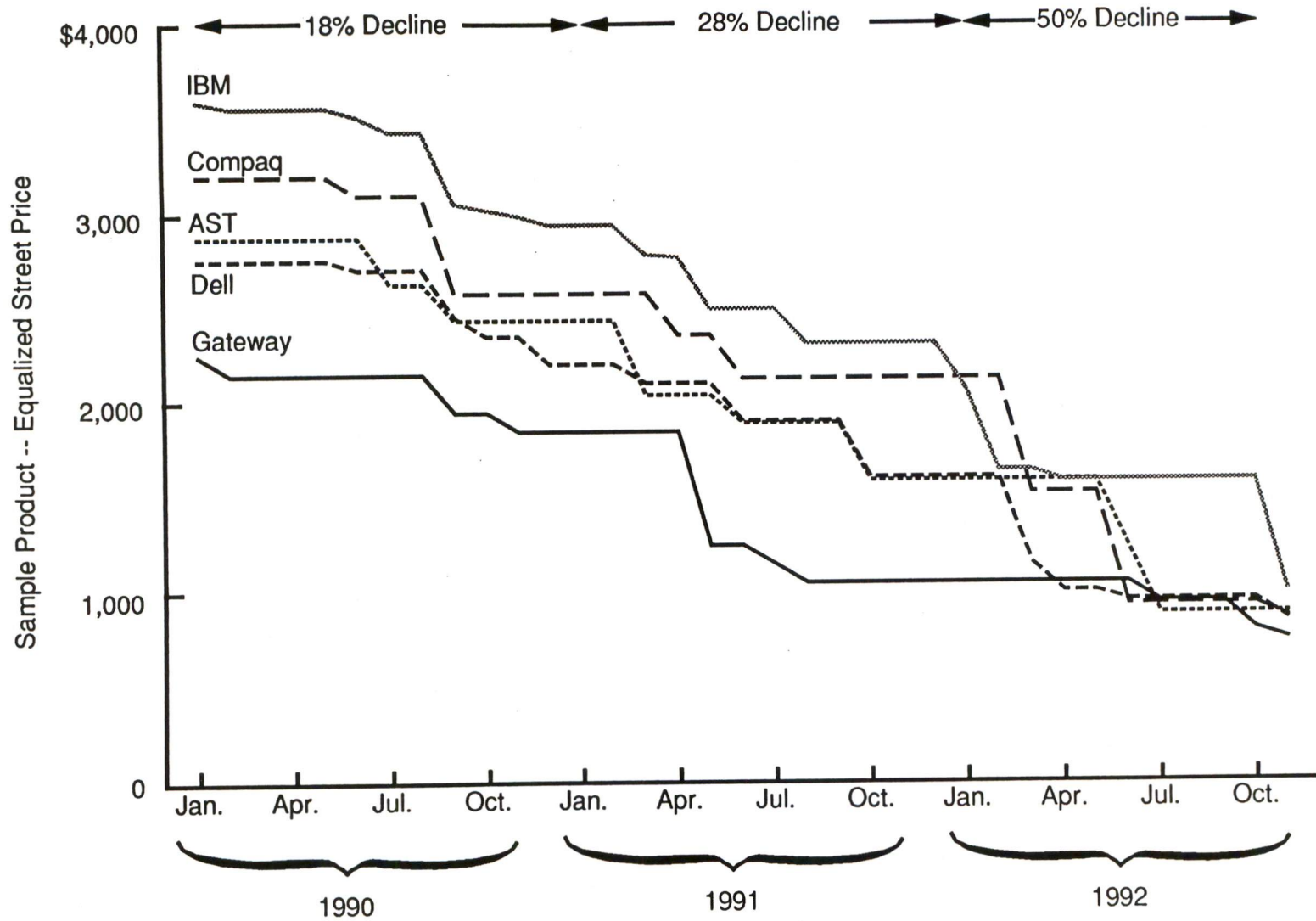


Channel	CAGR (1990-92E)	CAGR (1992E-95P)
Dealers	(1%)	1%
Direct	(2%)	4%
VAR	4%	7%
Mass Merchant	5%	14%
Superstore	1%	7%
Direct Marketing	125%	8%
Digital participation	2%	4%

Source: IDC; Workgroup; Personal Computer Business Unit Estimates

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COMPETITOR PRICE POSITIONING

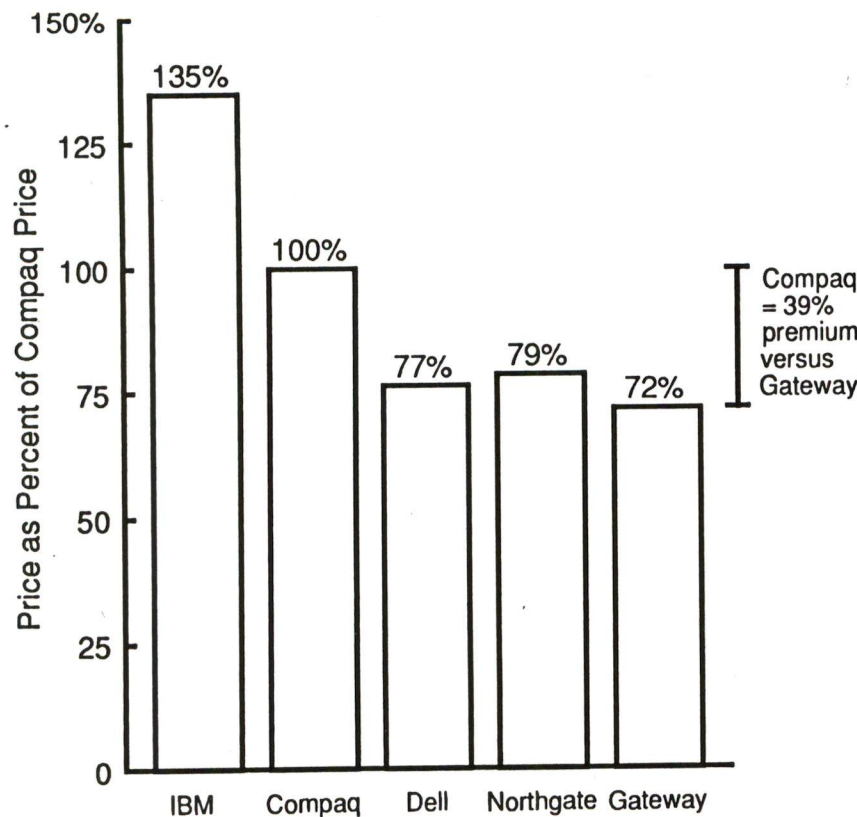


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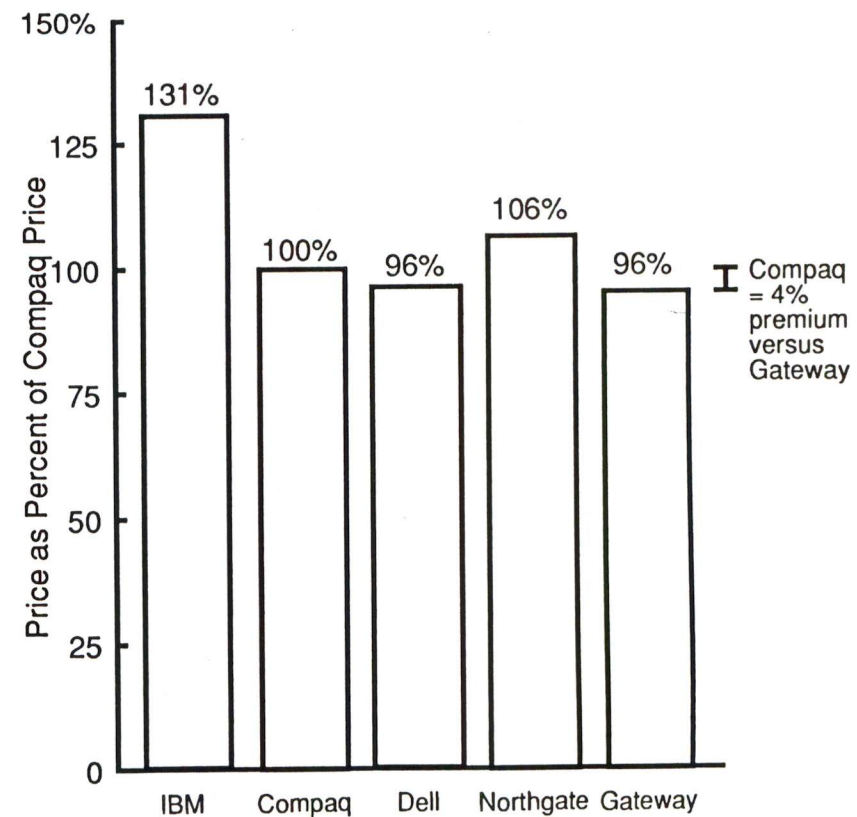
COMPETITOR PRICE TRENDS

In June 1992, Compaq collapsed the price umbrella and has removed most incentive to buy from 2nd or 3rd tier manufacturers

January 1992 (US)
(386/33)



January 1993 (US)
(486/33)



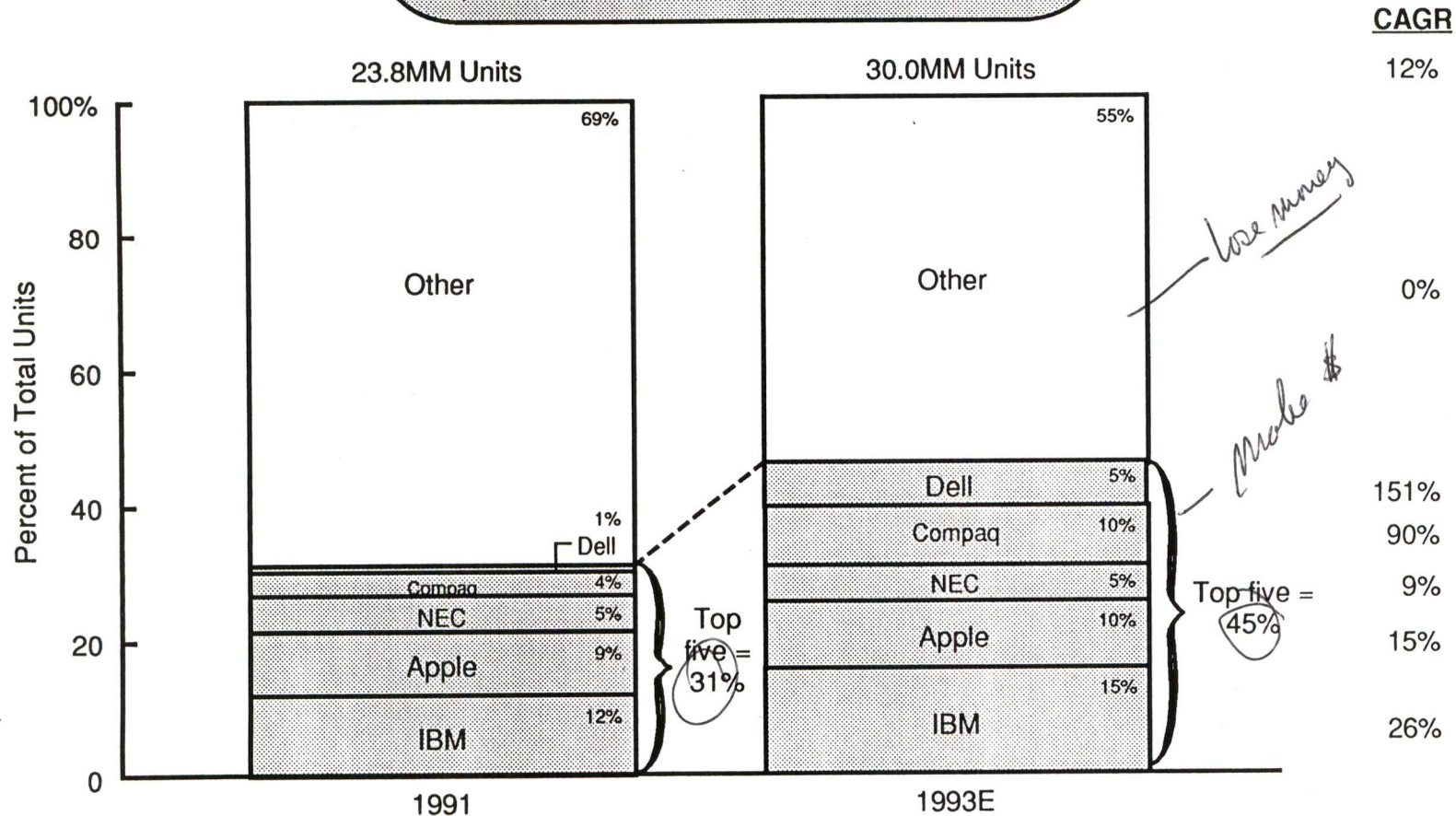
Configuration: 4MB RAM, 120MB HDD, Monitor, DOS, Windows, Mouse
Source: IDC, catalogs, advertisements, Sanford Bernstein

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MARKET DEVELOPMENT

COMPETITOR TRENDS

1992 price collapse led to industry consolidation.
Top five gained approximately 14 points of share



Key Events

- Rapid new product introduction
- Drastic price declines
- Direct marketing channel opens up

Source: IDC; Analyst Reports; Personal Computer Business Unit Estimates

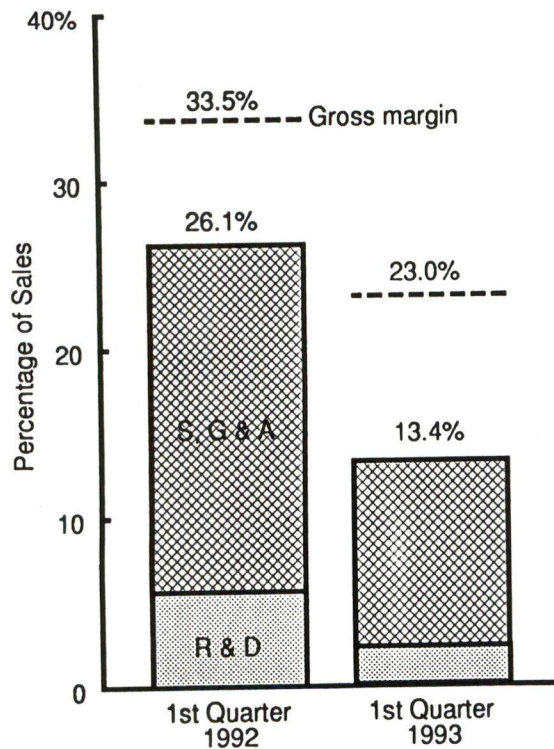
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INDUSTRY STRUCTURE

WINNER COST STRUCTURES

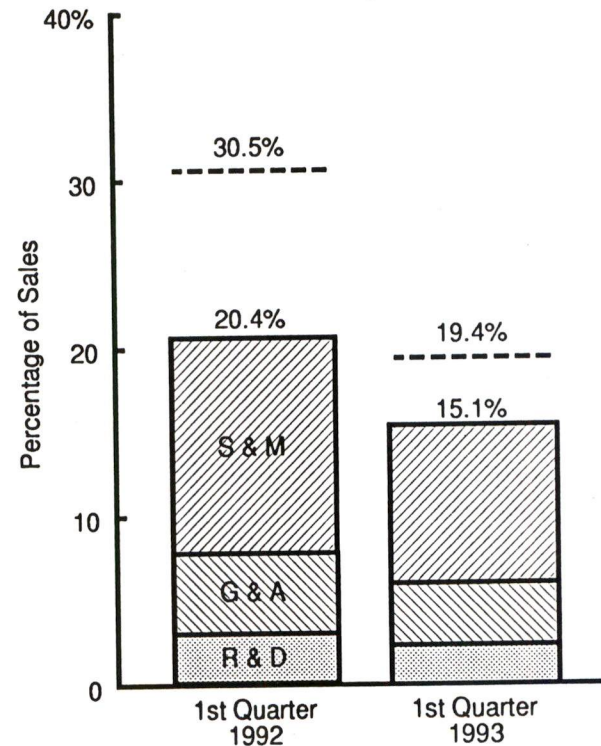
- The combination of pricing and volume changes has had a huge impact on the required financial structures of key competitors
- This process will drive most low-volume players into niches or out of business within 3 years

Compaq



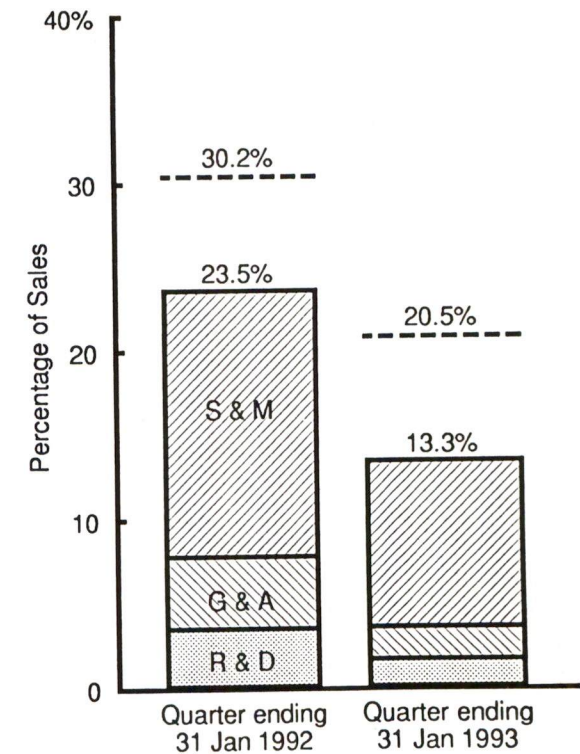
Operating margin:	7.8%	9.6%
Indexed revenue:	1.0	2.06

AST



Operating margin:	10.1%	4.3%
Indexed revenue:	1.0	1.53

Dell



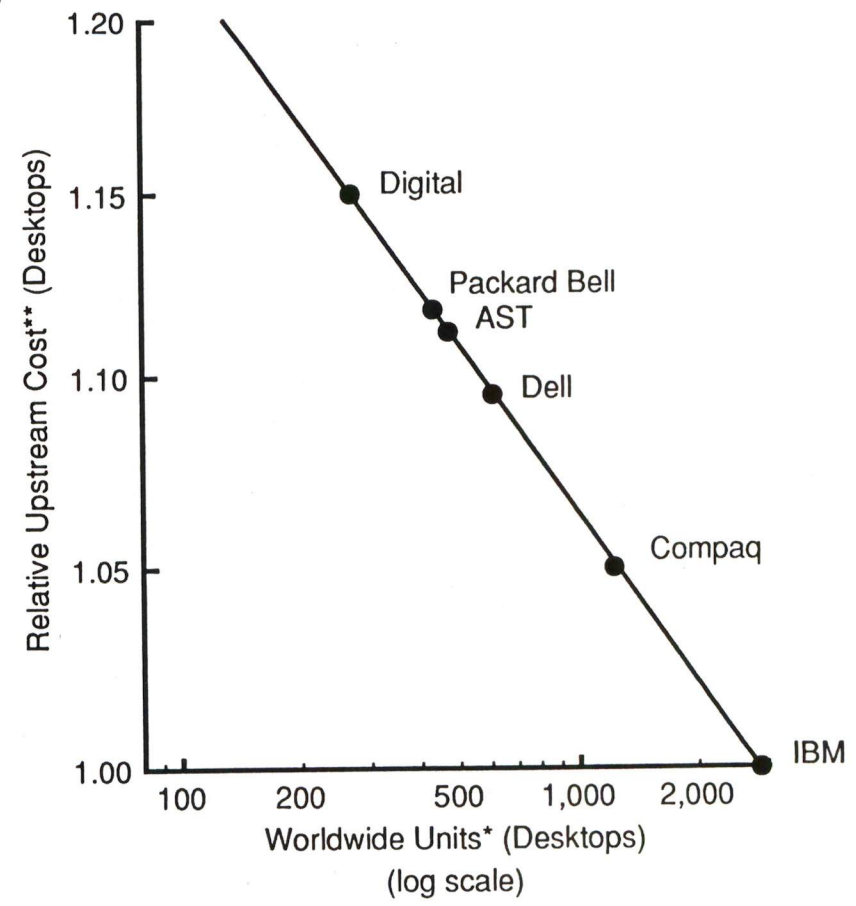
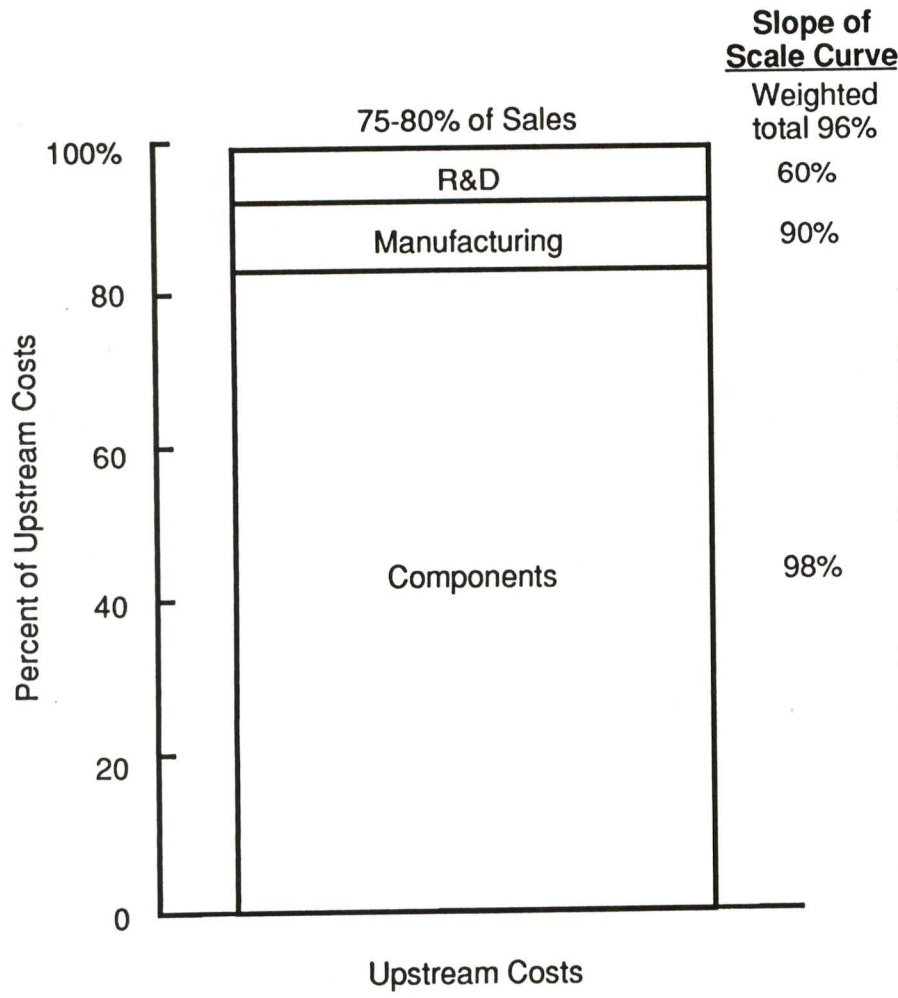
Operating margin:	6.8%	7.2%
Indexed revenue:	1.0	2.17

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INDUSTRY STRUCTURE

PC ECONOMICS

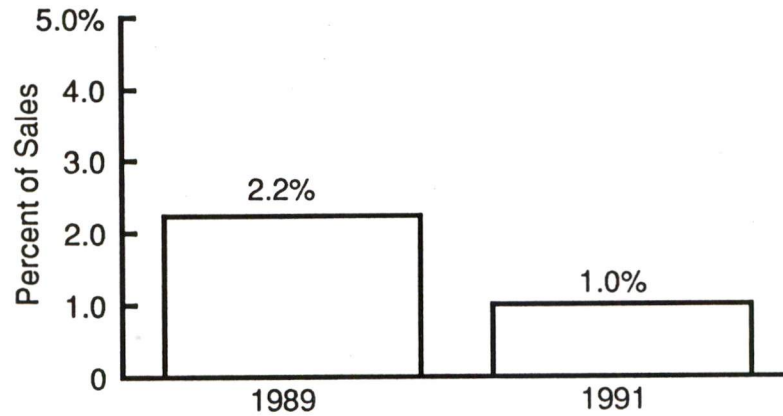
Every doubling of volume yields a 4% upstream cost reduction



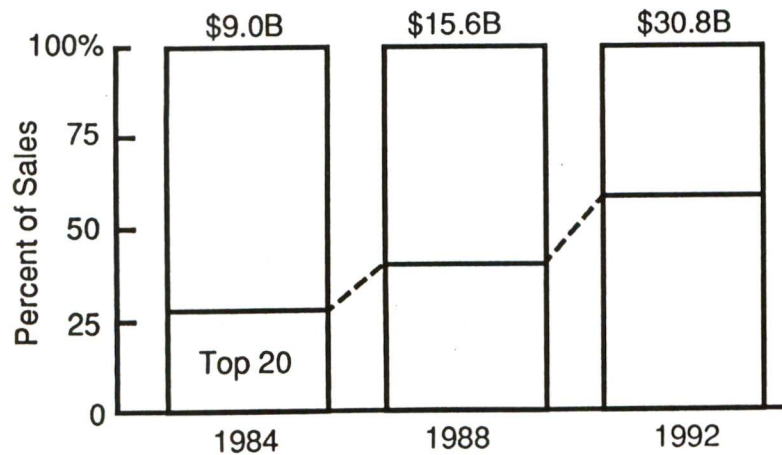
*Units sold worldwide (1992); Digital 1993 unit sales projections
 **Assumes all companies at optimal efficiency level
 Source: PCBU estimates, Analyst reports, IDC

Dealers' ability to support multiple brands has come under increasing pressure

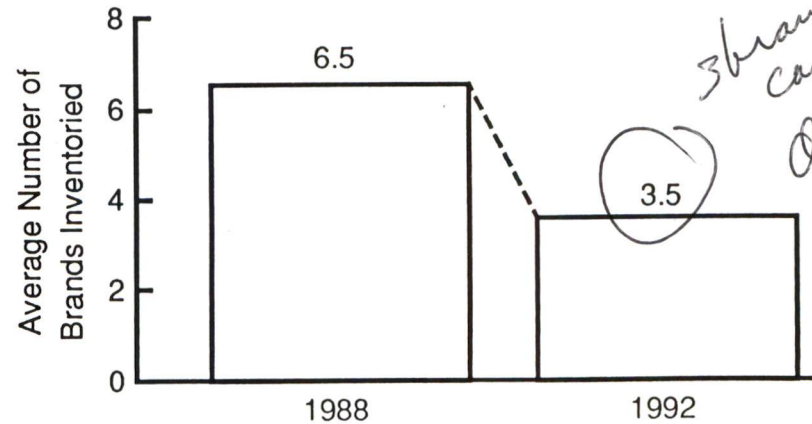
Average Dealer Profitability



Consolidation



Brand Concentration
(Carried in Inventory)

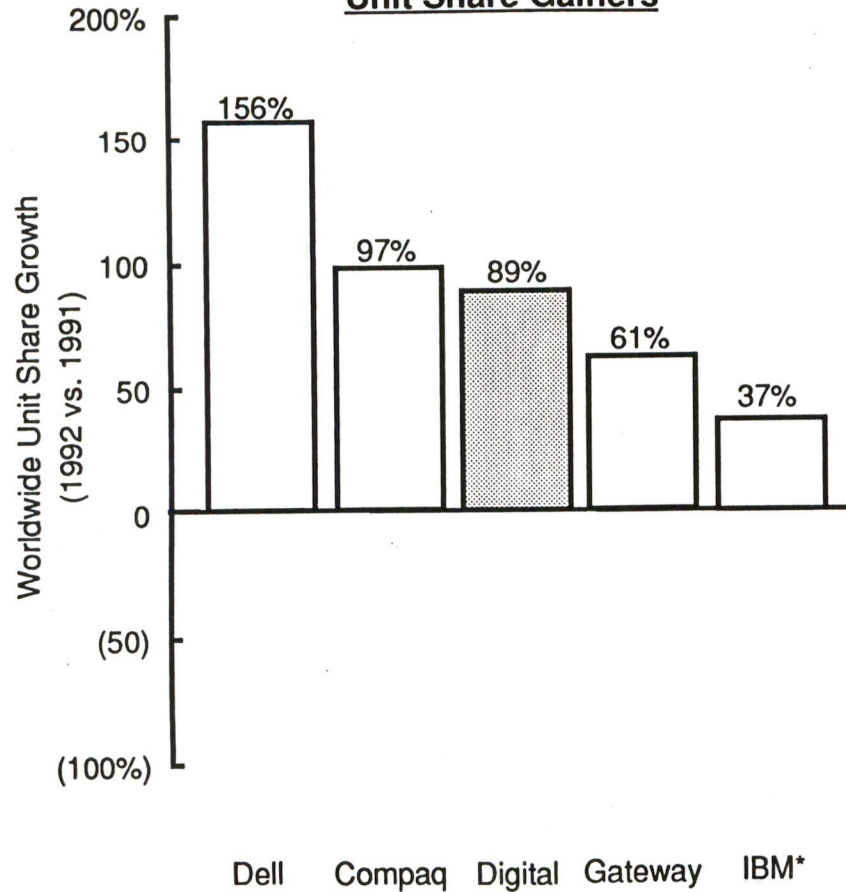


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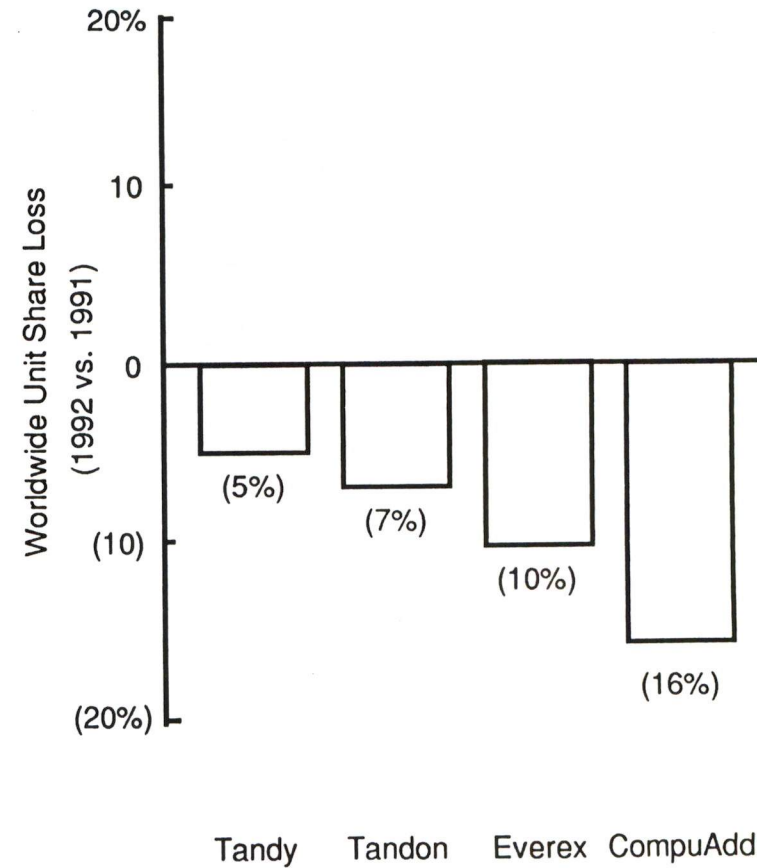
COMPETITIVE SHAKEOUT

So far Digital has been gaining share in the new environment

Unit Share Gainers



Unit Share Losers



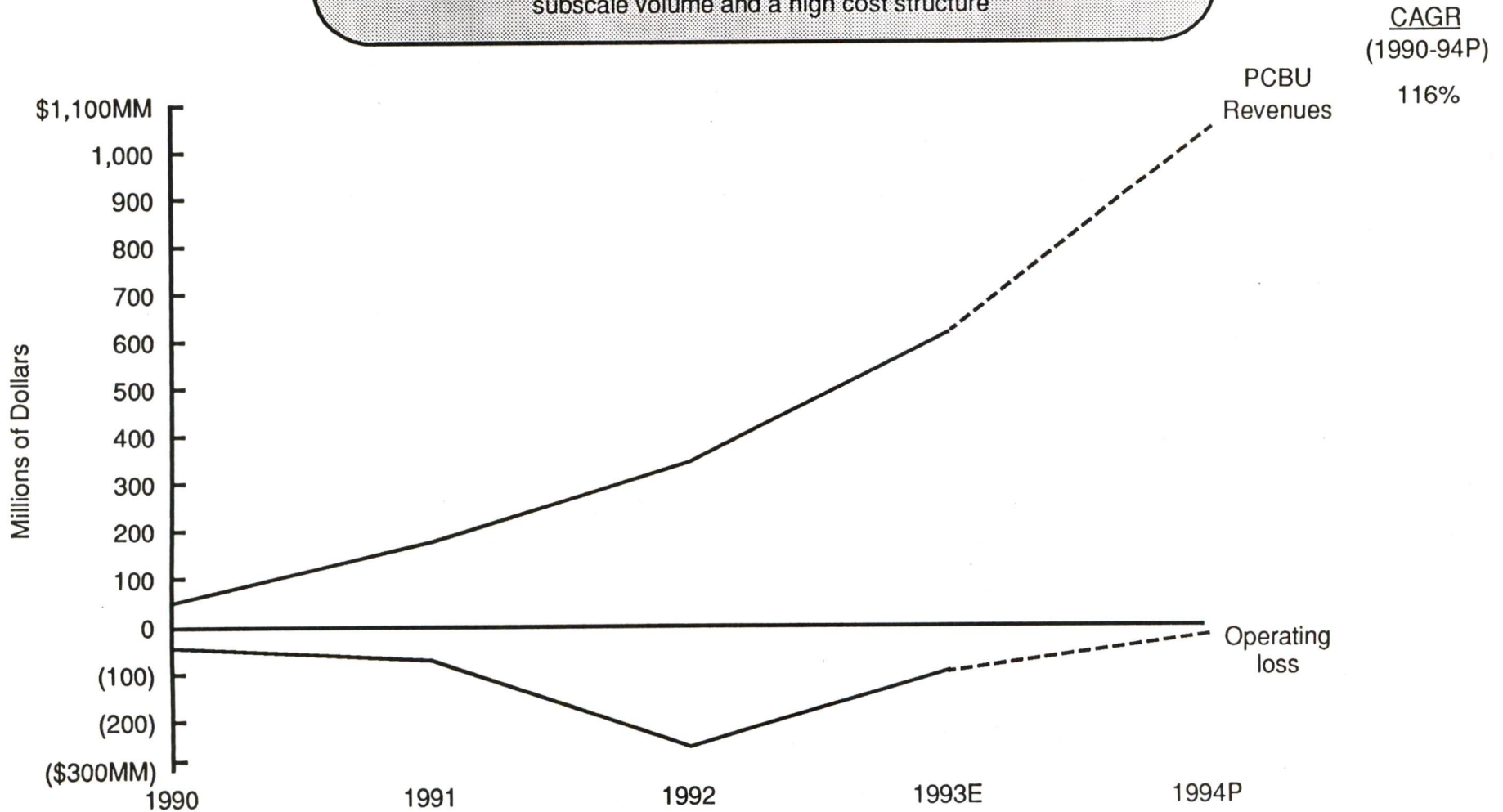
*IBM Q1 1993 vs. 1992
Source: IDC, Analyst Reports

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DIGITAL PC POSITION

HISTORICAL PERFORMANCE

But the challenge is very large - Digital still loses money due to subscale volume and a high cost structure



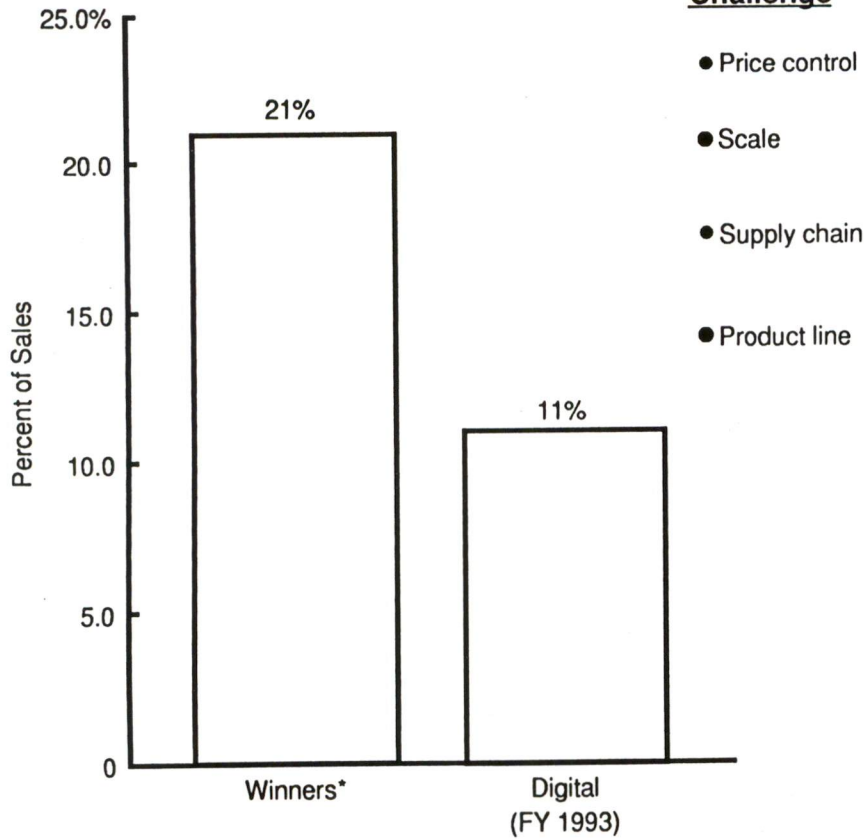
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DIGITAL PC POSITION

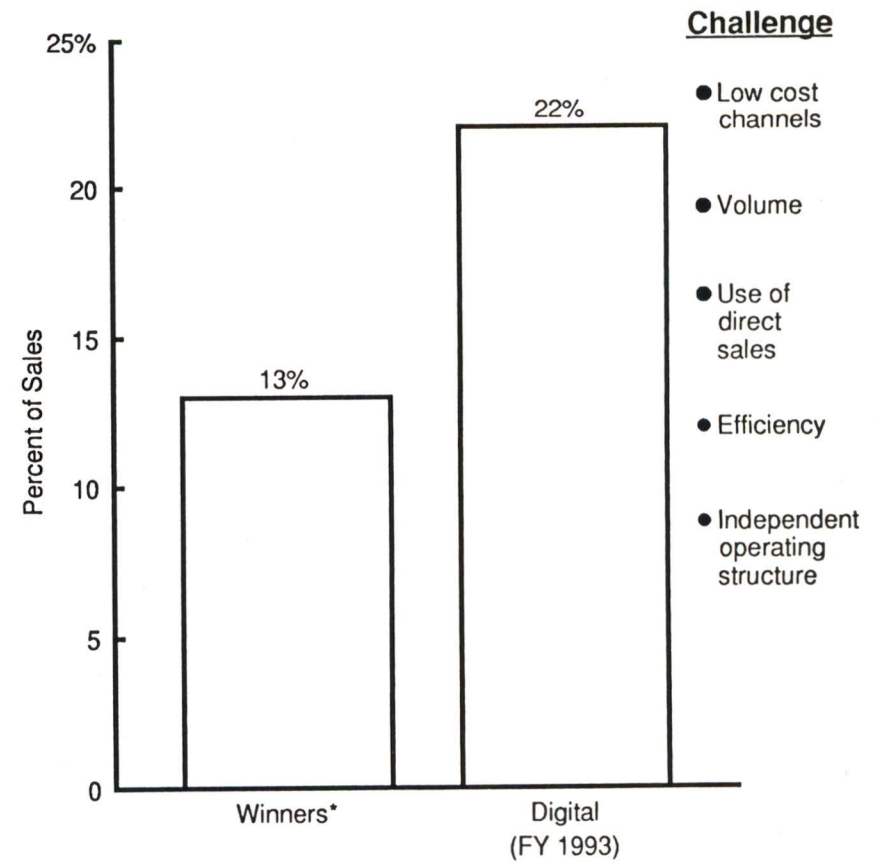
COST CHALLENGE

Digital must surmount a gross margin and S,G&A gap

Gross Margin



S,G&A



*Note: Winners are the average of Dell, Compaq, and AST 93 Q1 performance;
 Digital figures are from "restated financials"
 Source: Competitor Financials, Digital Financials

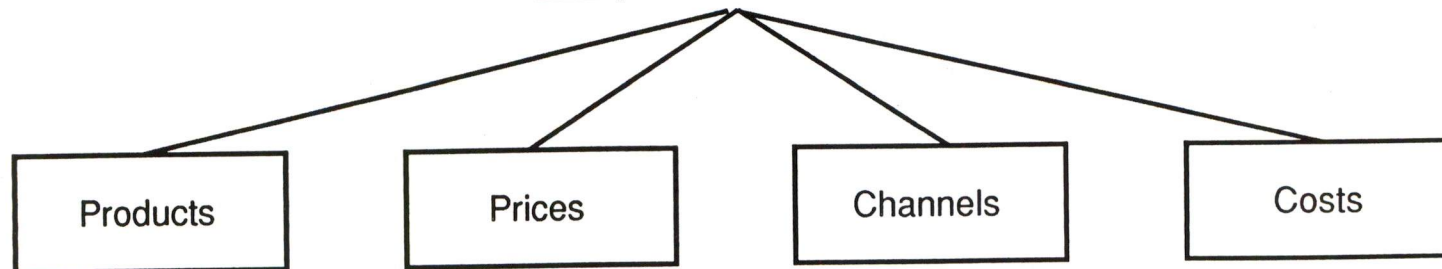
CRITICAL SUCCESS FACTORS

Situation

- Digital has been growing, but unprofitably
- The corporation provides the PCBU with several important assets:
 - Digital name
 - worldwide organization
 - Digital customer base
 - networking/integration capability, etc.
- Over the next two years, Digital must:
 - continue to grow faster than the market leaders to achieve competitive scale
 - dramatically reduce cost to the lowest levels achievable for its scale



Competitive Challenge



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COMPETITOR CHALLENGE

	<u>Competitor Challenge</u>	<u>Digital FY 1993</u>
Products	<ul style="list-style-type: none"> ● Premium and standard families ● Full portable line ● Six month product life cycle 	<ul style="list-style-type: none"> ● One family (premium) ● Limited and outsourced ● Late and limited
Prices	<ul style="list-style-type: none"> ● Steep decline (30-50% in 1992) 	<ul style="list-style-type: none"> ● Competitive with Compaq/Dell, but unprofitable
Channels	<ul style="list-style-type: none"> ● Rapidly expanding to penetrate all major channels 	<ul style="list-style-type: none"> ● Still limited
Costs		
<ul style="list-style-type: none"> ● COGS 	79% - integrated supply chain - "low cost/high speed" mentality	89% - traditional .geographic .functional
<ul style="list-style-type: none"> ● S, G & A 	13% - efficient channel use	22%
<ul style="list-style-type: none"> ● R & D 	3%	4%
Operating margins	5%	(16%)

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COMPETITOR CHALLENGE

	<u>Competitor Challenge</u>	<u>Digital FY 1993</u>	<u>Digital FY 1994 Plan</u>
Products	<ul style="list-style-type: none"> ● Premium and standard families ● Full portable line ● Six month product life cycle 	<ul style="list-style-type: none"> ● One family (premium) ● Limited and outsourced ● Late and limited 	<ul style="list-style-type: none"> ● Premium and standard families ● Internal portable line by mid-1994 ● Becoming competitive
Prices	<ul style="list-style-type: none"> ● Steep decline (30-50% in 1992) 	<ul style="list-style-type: none"> ● Competitive with Compaq/Dell, but unprofitable 	<ul style="list-style-type: none"> ● Improving profitability
Channels	<ul style="list-style-type: none"> ● Rapidly expanding to penetrate all major channels 	<ul style="list-style-type: none"> ● Still limited 	<ul style="list-style-type: none"> ● Expanding
Costs			
● COGS	79% - integrated supply chain - "low cost/high speed" mentality	89% - traditional .geographic .functional	82% - lower production costs - low cost designs - competitive warranty and service costs - grow rapidly
● S, G & A	13% - efficient channel use	22%	16% + 1% - new independent business unit structure - manage down selling cost - shift mix to lower cost channels
● R & D	3%	4%	3%
Operating margins	5%	(16%)	(2%)

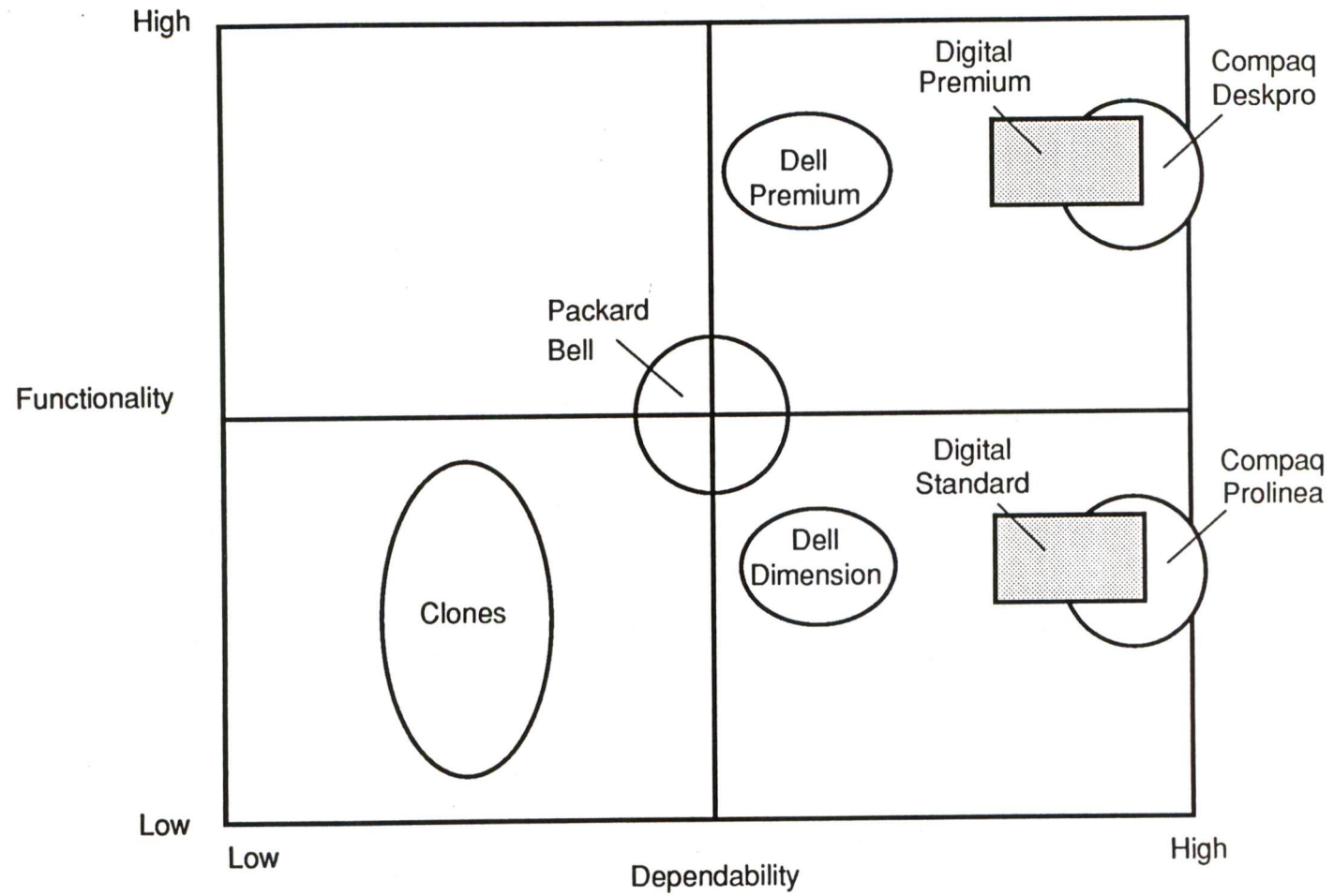
corp allocation

82% - lower production costs
- low cost designs
- competitive warranty and service costs
- grow rapidly

16% + 1% - new independent business unit structure
- manage down selling cost
- shift mix to lower cost channels

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PRODUCT POSITIONING



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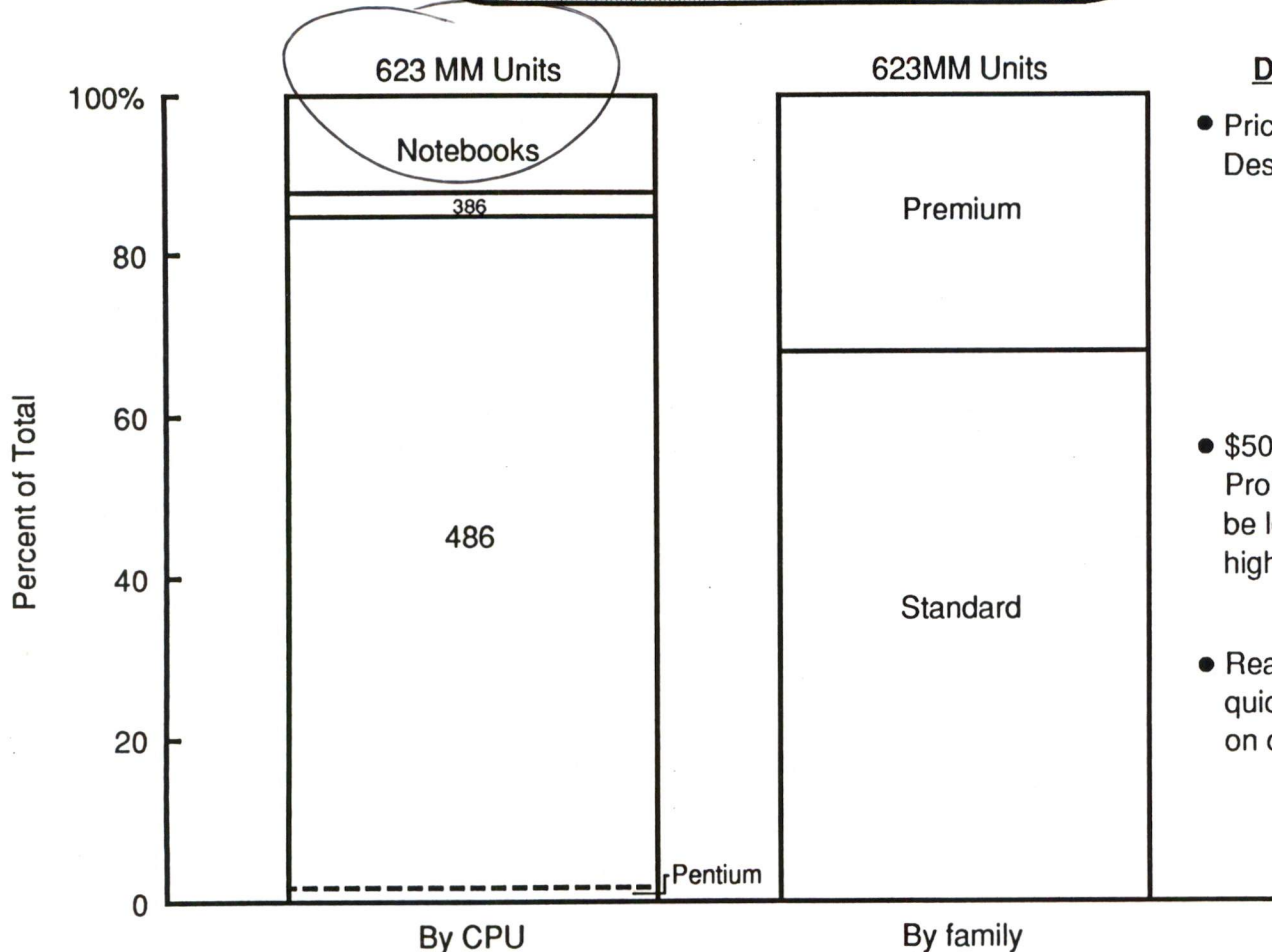
FY 94 PRODUCT STRATEGY

	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>
Portable	486 SL/SLC	486 "S" Mid Range Notebook 486 "S" Low Price Notebook		Digital Family of Notebooks Full Range of 486 Processors	
Server Product Line	xP and 433 MP Products Transition into the New Product Line			Uni & Dual Pentium Servers Alpha Ready	
Premium Desktop/ Deskside Product Line	MT/MTE & ST Products Transition into the New Product Line		Full range of 486 & Pentium deskside		
	LP Line			Desktop Pentium Family of Processors	
			Full range of 486 Plus "Baby Pentium"		
Standard Desktop Product Line	Selected 386 and Full range of Desktop 486 Plus "Baby Pentium"				

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PRICING

• Plan assumes 7% per quarter price declines per machine (market driven)



Digital Pricing Strategy

- Priced equivalent to Compaq Deskpro/ I-M Equivalent
- \$50-\$70 per unit above Compaq Prolinea. (Digital will typically be lower than IBM Valuepoint, higher than Dell Dimension)
- React to Dell or IBM pricing moves quickly, without waiting for Compaq, on case-by-case basis

PCBU FY 1994 Plan

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PRICE EROSION GUIDELINES - FY 1994

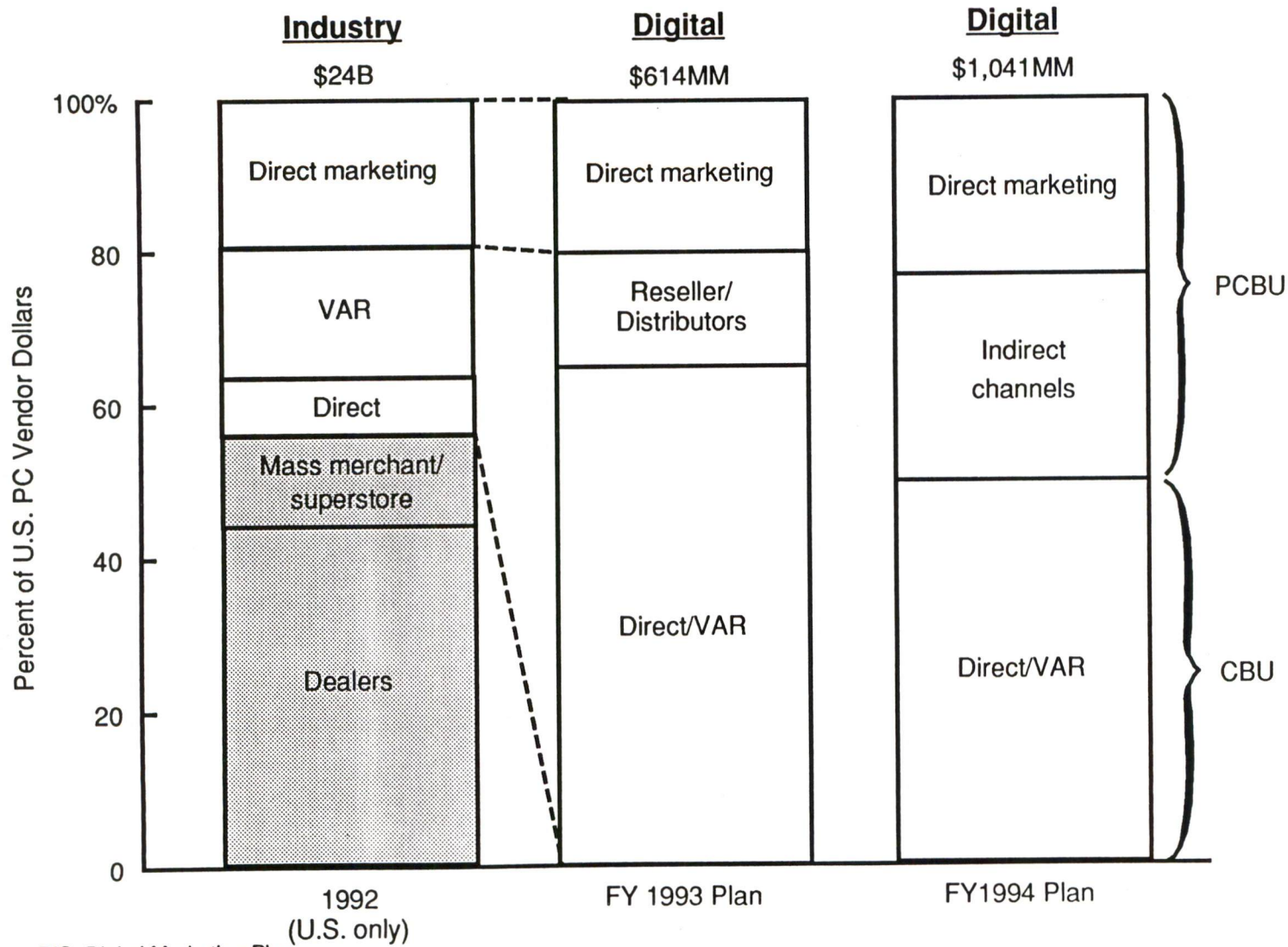
<u>Processor</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>
● 486sx	5%	5%	5%	5%	19%
● 486dx	6%	6%	7%	7%	23%
● 486dx2	7%	7%	8%	8%	27%
● 486dx3	NA	NA	0%	3%	3%
● Pentium	NA	0%	3%	4%	7%

Note: Price erosion is for average systems configured to meet market requirements for those systems

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CHANNEL STRATEGY

Digital will continue to exploit its position in direct marketing and will expand its presence in indirect channels



Source: BIS, Digital Marketing Plan

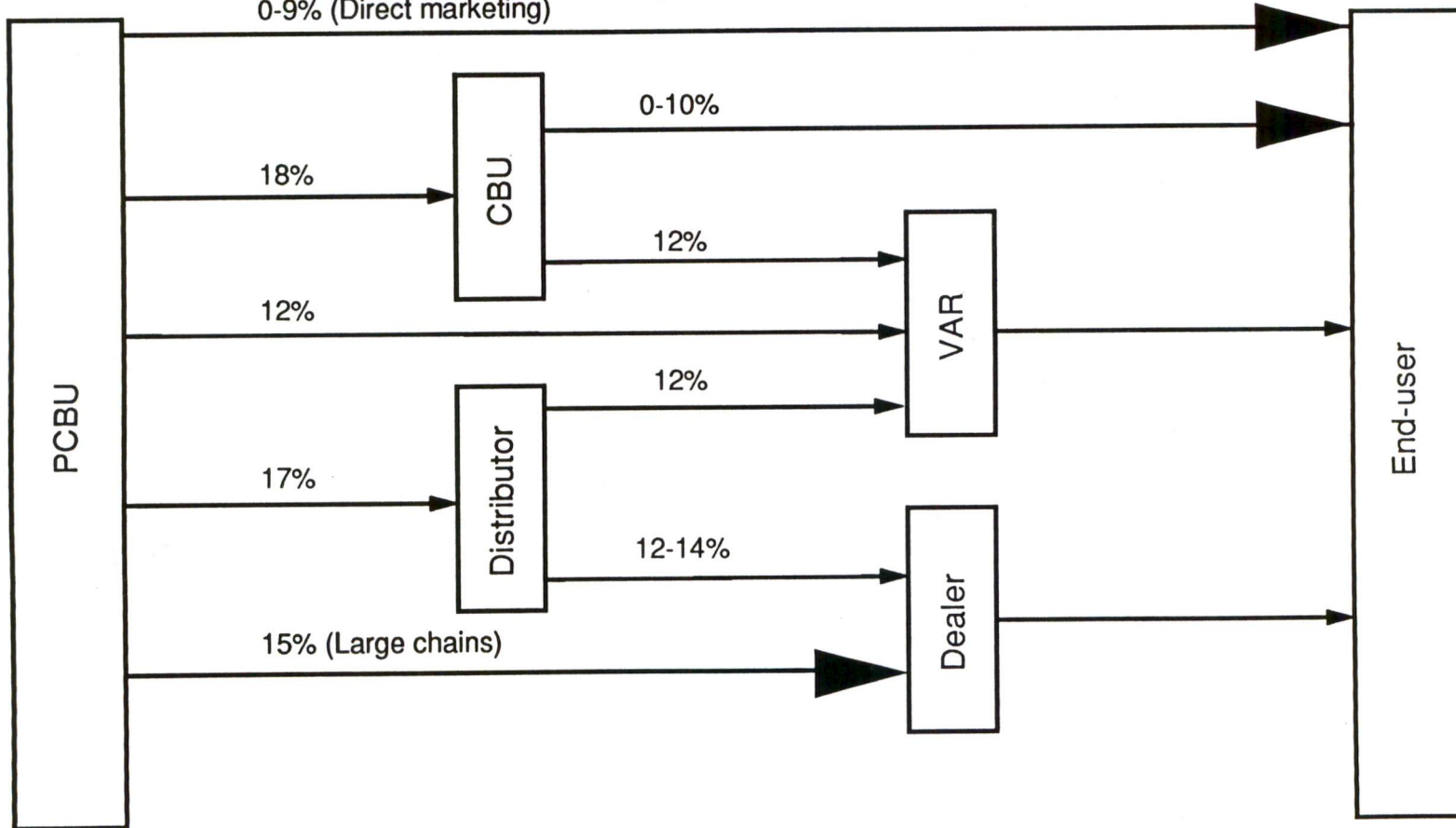
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CHANNELS

DISCOUNT POLICY (1994 PLAN)

Digital to provide balanced pricing across competing channels, minimizing channel conflict

Discounts
0-9% (Direct marketing)



Note: Percent Discount off catalog list price

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CHANNELS

KEY ACTIVITIES FY 1994

United States

- Expand channel presence (indirect)
 - add first tier partner in each new channel e.g.:
 - .MicroAge (dealers)
 - .CompUSA (superstores)
- Direct sales
 - refer all non-integration sales to new force of PC specialists
 - compensate CBU salesforce \$5/box for all referrals
 - fulfill most orders through PC direct
- Enforce Ts and Cs

Europe

- Expand channel presence (indirect) only after reorganization complete (see below)
- Direct sales
 - refer all non-integration sales to force of PC specialists
 - fulfill all orders through 4 PC direct sites (consolidated from 17)
- Enforce Ts and Cs

GIA plan in development

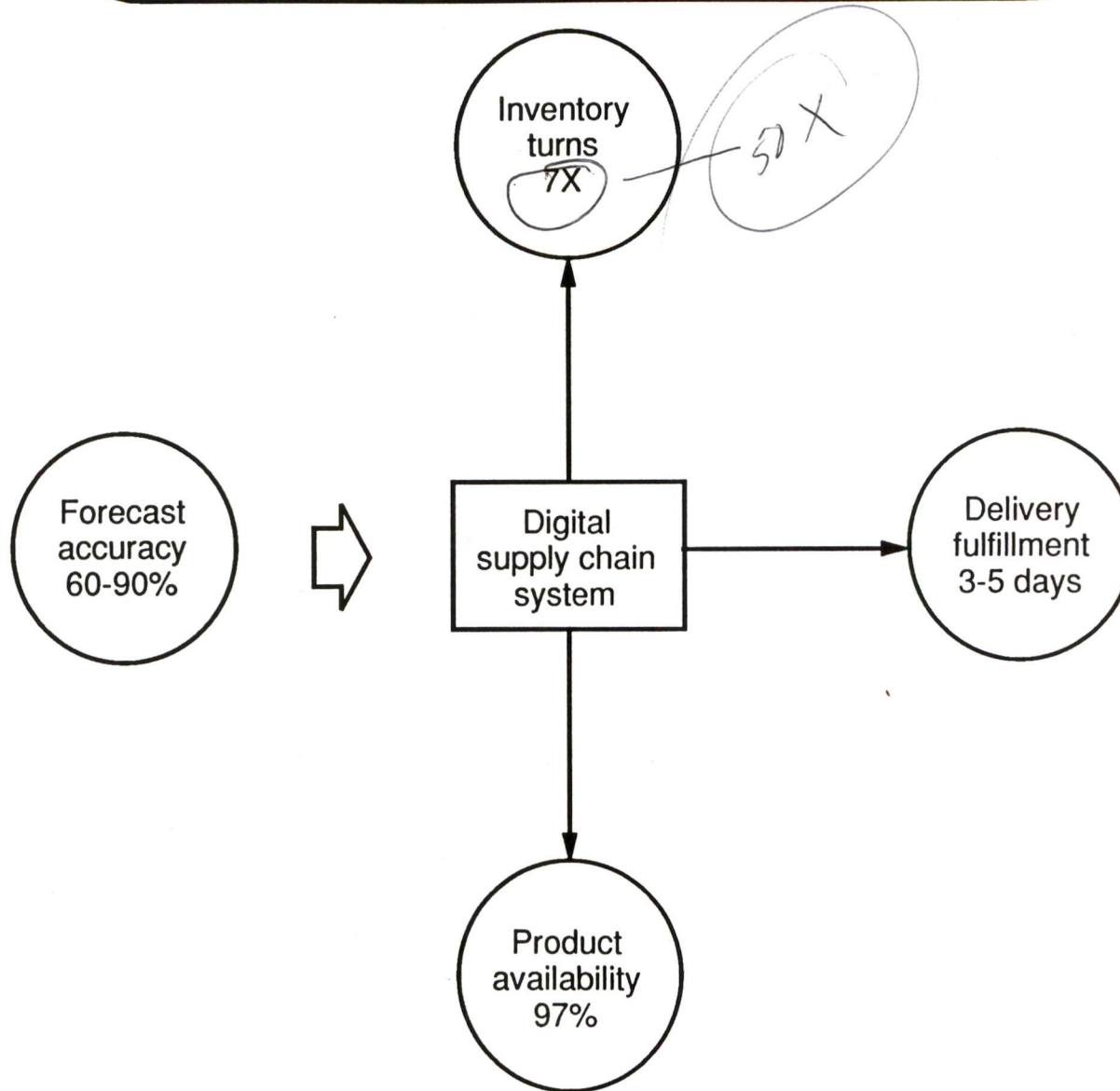
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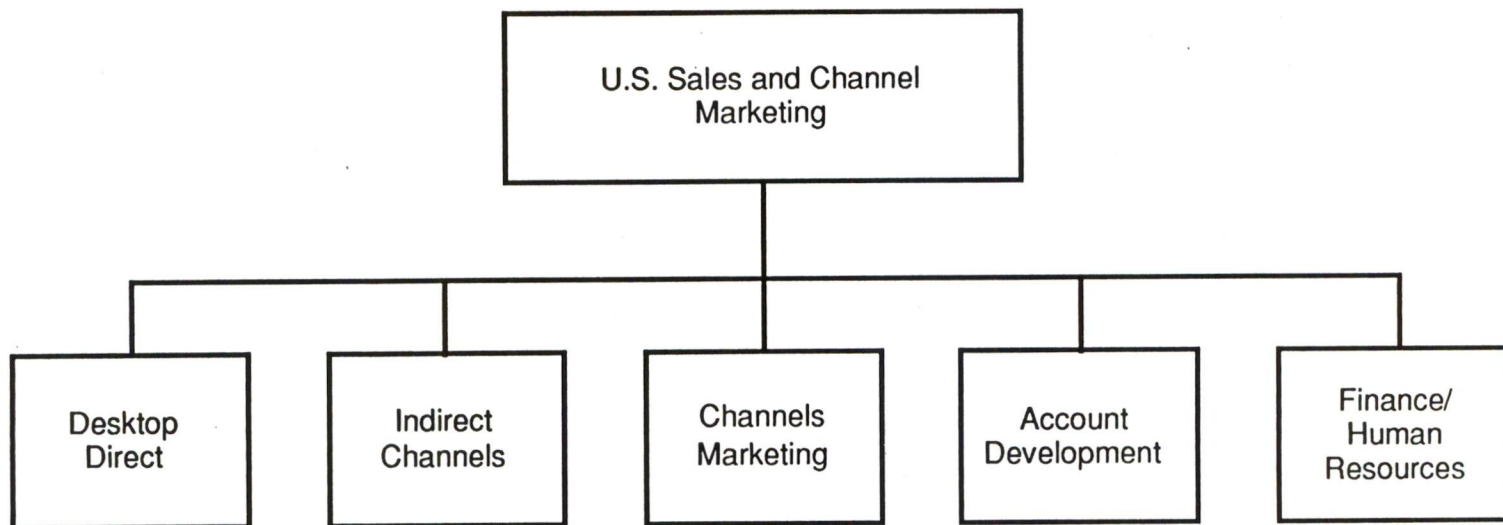
COSTS

	<u>Today</u>	<u>Plan</u>	<u>How</u>	<u>PCBU</u>	<u>Supply chain</u>
Purchased material cost	10% high vs. scale opportunity	Reduce disadvantage by 6 points	<ul style="list-style-type: none"> - MCV (5 of the 6 points) - PCBU purchasing organization/ negotiation strategy change - execute to the new strategy 	<ul style="list-style-type: none"> ✓ 	<ul style="list-style-type: none"> ✓ ✓
Order lead time and delivery consistency	12-60 days 60%	3 days 97%	<ul style="list-style-type: none"> - new system implementation (on demand) - JIT delivery model - manufacturing execution - forecasting model 	<ul style="list-style-type: none"> ✓ 	<ul style="list-style-type: none"> ✓ ✓ ✓ ✓
Inventory (net turns)	6.3 turns \$60MM+ obsolescence	7.0 turns \$36MM est. obsolescence	<ul style="list-style-type: none"> - demand/supply management - fast response to forecast changes - execution and flexibility to plan 	<ul style="list-style-type: none"> ✓ 	<ul style="list-style-type: none"> ✓ ✓

SUPPLY CHAIN REQUIREMENTS

Supply chain system must deliver competitive performance given PC industry forecast variability

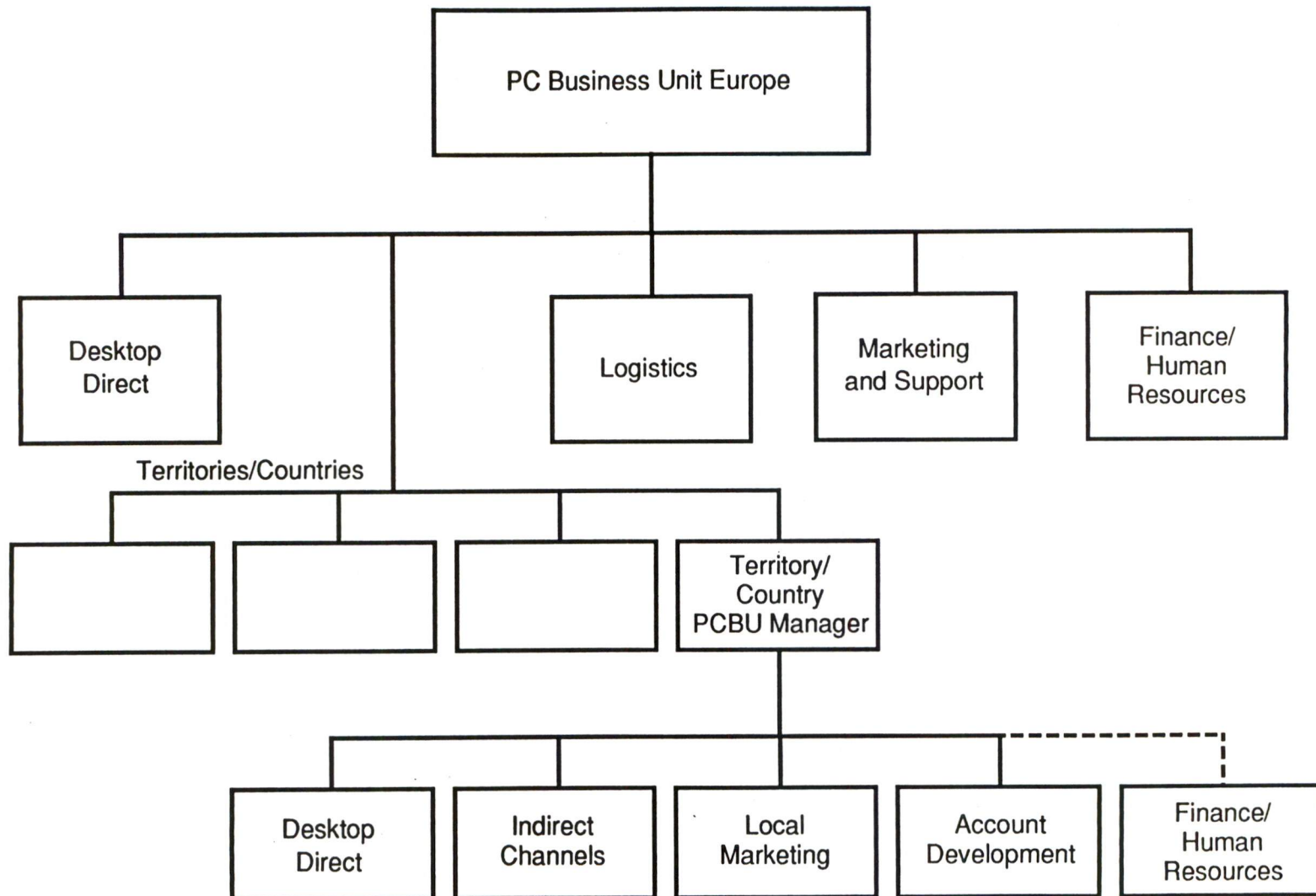




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ORGANIZATION

EUROPE



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FY93-FY95 PROFIT AND LOSS SUMMARY (INTEL ONLY)

	<u>FY1993</u>		<u>FY1994</u>		<u>FY1995</u>		<u>FY93 vs.</u>	<u>FY94 vs.</u>
	(\$MM)	(%)	(\$MM)	(%)	(\$MM)	(%)	FY94	FY95
● PCBU channels revenue	281	46%	500	48%	1,248	75%	2 pts	27 pts
● PCBU to CBU revenue	333	54%	540	52%	420	25%	(2 pts)	(27 pts)
● Total	614	100%	1,040	100%	1,668	100%	0 pts	0 pts
● Gross margin	65	11%	187	18%	317	19%	7 pts	1 pts
● SG&A	135	22%	177	17%	250	15%	5 pts	2 pts
● Research and engineering	27	4%	31	3%	33	2%	1 pts	1 pts
● Operating profit	(97)	(16%)	(21)	(2%)	34	2%	14 pts	4 pts

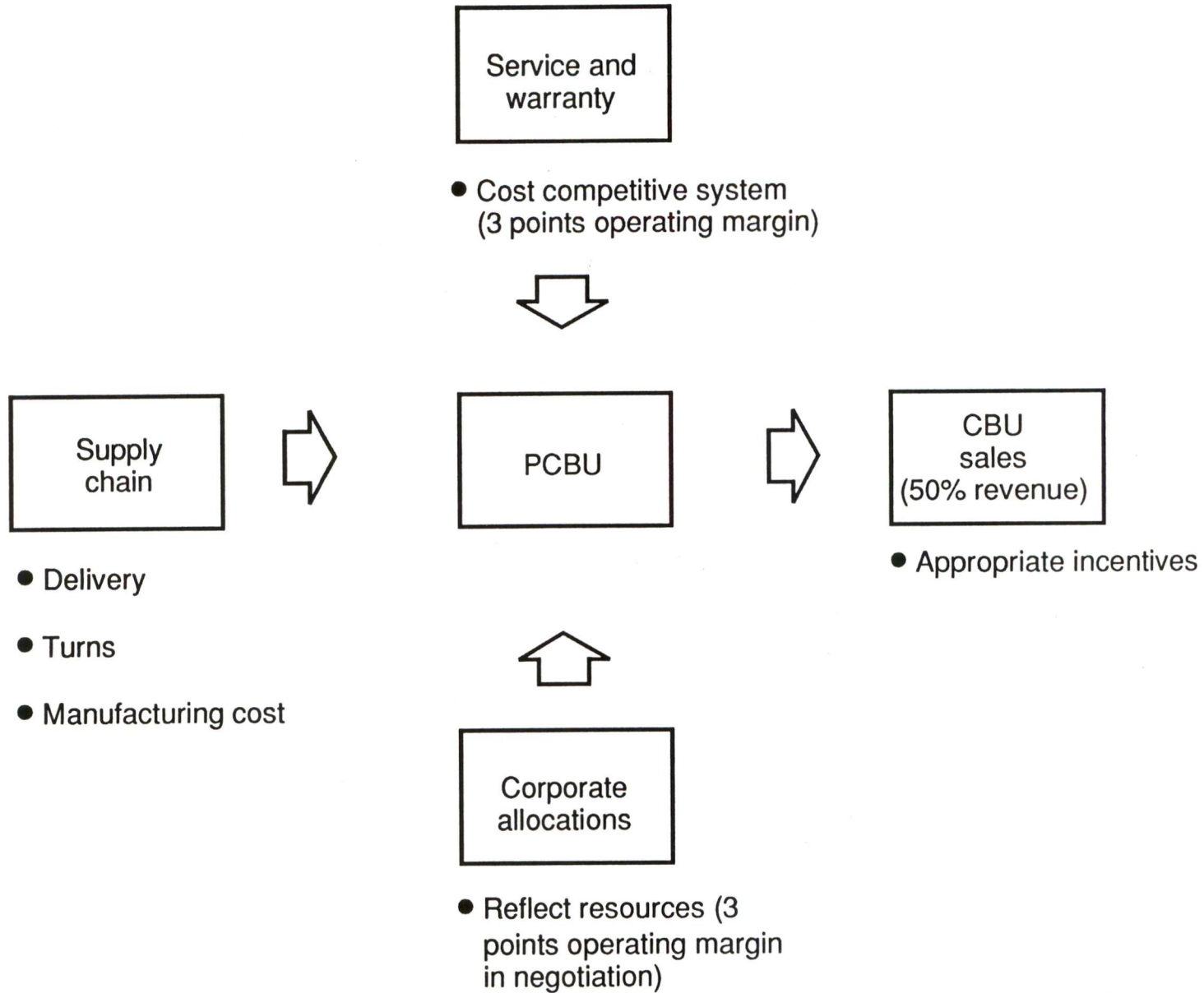
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FY94 PRODUCT MIX

	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Total</u>
● Desktop					
- standard	76%	73%	70%	57%	68%
- premium	3%	3%	8%	16%	8%
- total desktop	79%	76%	78%	73%	76%
● Deskside	10%	10%	10%	16%	12%
● Portable	11%	14%	12%	11%	12%
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
● Total	100%	100%	100%	100%	100%

Key Challenges:

- Put required organization in place, on time
 - Europe
 - U.S.
 - GIA?
 - engineering - starting from zero-base
- Transition from high-cost direct sales model without losing revenue
- Impose rigid control of pricing and T&Cs
 - especially in Europe
- Achieve growth and delivery performance while squeezing out the last unnecessary dollar of cost



- PC industry competitiveness today is driven mostly by manufacturing and logistics performance
 - lead time/delivery
 - flexibility
 - responsiveness
 - cost management
- Major PC players have full control of their manufacturing systems, due to the unique demands of PC logistics
 - IBM
 - Compaq
 - Dell
 - AST
- Digital is pursuing a cross-company manufacturing system to supply PC's, as part of a corporate-wide synergy plan to optimize worldwide manufacturing and logistics. There is no precedent for this logistics model to succeed in the PC industry
- If the Digital supply chain does not deliver substantially improved logistics results in a short period of time, the entire PC business is at serious risk

- The PC business is strategic for Digital, not only for its revenue, but also for the business model it represents
- The corporation must be prepared to respond to the ongoing needs of the PC business. This chiefly implies a flexibility and fast reaction time not characteristic of the historical corporate model
- If Digital can adapt successfully, this can form the basis for significant future growth for the corporation

DIGITAL
PRELIMINARY PERSONAL COMPUTER
BUSINESS PLAN

- Intel-Based Product

- Alpha Business Direction

- 1-800-SOFTWARE

alpha PC
6995

April 28, 1993

PERSONAL COMPUTER BUSINESS UNIT

FY 1994 ALPHA PC BUSINESS DIRECTION (PRELIMINARY)

Agenda

April 28, 1993

- Intel and Alpha PC's - similarities and differences
- Critical success factors
- Preliminary business model
- Issues

SIMILARITIES

- Address common/similar customer requirements for functionality
- Increasingly common customer buying process
- Therefore, reliance on common channels
- NT and standard PC interfaces
- Together, the two product sets meet the full range of customer requirements for PC cost and workstation functionality

- DOS only on Intel; OSF and VMS only on Alpha (NT Windows on both)
- Digital must drive Alpha applications NT
- Initially, Intel covers lower price points and Alpha, high functionality range
- Initially, Alpha has greater reliance on CBU structure (85% of FY 1994 revenue)
- At least initially, workstation discount structure appears necessary for Alpha to create greater channel pull

CRITICAL SUCCESS FACTORS

- Integrate product strategy to optimize PC cost and workstation functionality
- Aggressively drive Alpha cost structure to competitive model
- Convince ourselves, our customers, and our vendors that we intend a truly complementary business strategy

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CRITICAL SUCCESS FACTORS

INTEGRATED PRODUCT STRATEGY

Plans are in place to integrate platforms within 18 months and maximize componentry by next generation

Common Product Plans

- Pre-integrated platforms
- Integrated platforms

Enclosure Style

Tower

○ Hot Pink 165 ○ Ultra 190

○ Flamingo 120 ○ Culzean I 110

Mini-tower

○ Jensen 110 ○ Infinity

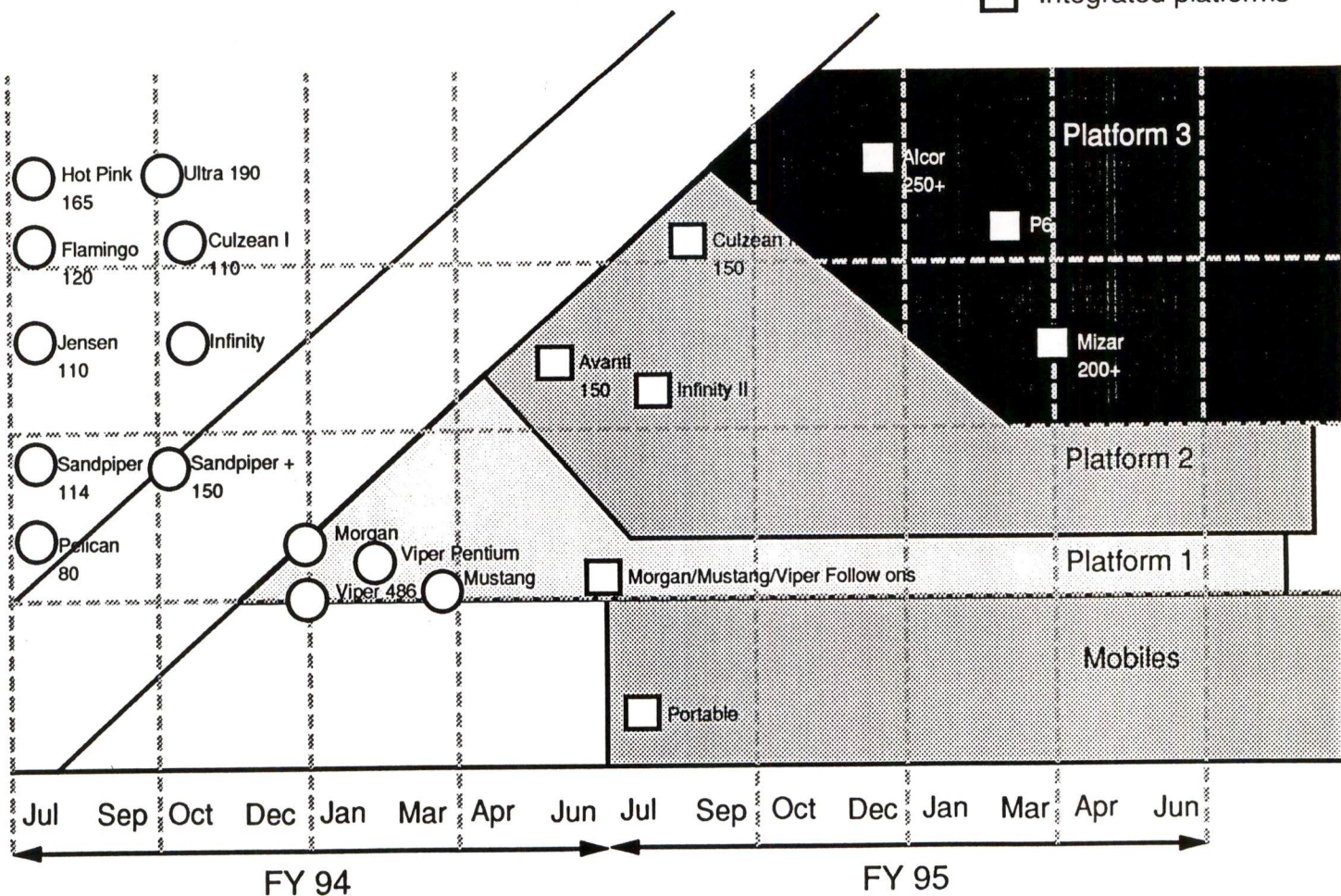
Low profile

○ Sandpiper 114 ○ Sandpiper + 150

○ Pelican 80 ○ Morgan ○ Viper Pentium Mustang
○ Viper 486

Mobile

□ Portable



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ALPHA PC

PRELIMINARY BUSINESS DIRECTION

	PCBU View		
	PC Competitive Model	Preliminary Alpha PC Competitive Model	Memo: FY 1994 Intel PC Model
● Revenue	100%	100%	100%
● Gross margin	23 --> 21	30	18
● Selling/marketing	9	9*	13
● G&A	4	3*	4
● Engineering	3	8	3
● <u>Applications porting</u>	<u>--</u>	<u>3</u>	<u>--</u>
● Operating margin	5%	7%	(2%)
● Memo: first pass submission		(4%)	

*Organizational complexity offset by scale economics

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FIRST PASS ALPHA PC SUBMISSION (KEY ASSUMPTIONS)

7/94

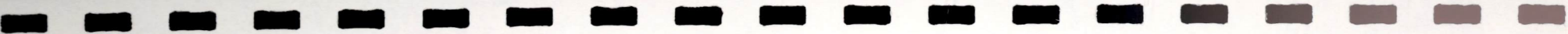
● Revenue	
- millions	\$529
- units	72,000
● Unit sales mix	
- server/single user	12/88
- NT/OSF-VMS	73/27
● Gross Margin	32%
● As a percentage of sales	
- SG&A (including application porting)	26%
- R&D	9
● Preliminary Jensen pricing assumptions	
- base NT entry price	\$6,995
- discount to high-volume resellers	26%
● Operating profit (millions)	(\$22)

(4%)

PERSONAL COMPUTER BUSINESS UNIT

PRELIMINARY ALPHA PC DIRECTION ISSUES

- Market targeting by platform (Intel and Alpha) and operating system (NT and Unix) not yet fully defined
- Price positioning and business practices still to be agreed upon
- Impact of negative reaction by Intel on Digital's base Intel plan and its ability to create channel pull for Alpha
- Upside volume capability if Alpha PC wildly successful



DIGITAL
PRELIMINARY PERSONAL COMPUTER
BUSINESS PLAN

- Intel-Based Product
- Alpha Business Direction

● 1-800-SOFTWARE

April 28, 1993

PERSONAL COMPUTER BUSINESS UNIT

1-800 SOFTWARE

FY 94 PLAN FINANCIALS

	FY 1993	FY 1994	FY 1995
	<u>(\$MM)</u>	<u>(\$MM)</u>	<u>(\$MM)</u>
● NOR			
Product	\$113MM	\$153MM	\$198MM
Service	0	0	0
Total	113	153	198
● Costs of goods sold			
Product	97	133	173
Service	0	0	0
Total	97	133	173
● Gross margin			
Product	16	20	25
Service	0	0	0
Total	16	20	25
● R&E	0	0	0
● SG&A*	<u>17</u>	<u>20</u>	<u>22</u>
● Operating profit	(1)	0	3

*Note: SG&A includes executive bonuses and amortization of acquisition cost memo item (included above)