From: Steven Sinofsky [redacted]
Sent: Thursday, July 18, 2013 9:37 PM
To: Jeffrey Epstein
Subject: FW: Surface sales physics after a week

MS wrote off 900M on inventory...this is a mail thread from November saying this will happen. Kevin Turner is the COO.

Even better--at the last minute this 900M was an increase over the "planned" write off. Classic "well it is bad news so let's bank some of it"....

From: Steven Sinofsky [redacted]
Sent: Monday, November 5, 2012 10:54 PM
To: Kevin Turner; Steve Ballmer
Subject: RE: Surface sales physics after a week

But this is for January. Kevin previously indicated this was already the plan and given that we want to do a good job in January and there is only a little bit of more work time relative to 12/1 it seems like we are on a path not to have time to do what is viewed as a good job in January either.

So I was just going along with what he said was the plan for Q1. I didn't even know about that was a plan as I had previously indicated--I just held them back from everything while we talked about doing something near term. Their view was to roll in the near term with the longer term as you saw in the deck.

Are you saying now that there was not a plan for Q1?

Sent from Windows Mail

From: Steve Ballmer
Sent: November 5, 2012 10:49 PM
To: Steven Sinofsky, Kevin Turner
Subject: RE: Surface sales physics after a week

They cannot do meetings until the plan is approved by me. Please let them know Steven. If I read the deck correctly they want to offer 2-3 year exclusives

Sent from my Windows Phone

From: Steven Sinofsky [redacted]
Sent: 11/6/2012 8:17 AM
To: Steve Ballme[redacted]; Kevin Turner <[redacted]
Subject: RE: Surface sales physics after a week

The group you say below has all been working -- that's the deck they have (which is the suning model).

If you want to meet with them then by all means please do -- set up a call or anything. The deck I sent you is the deck they would use except for the near term part of course. They will focus first on Europe and Oz.

They understand that they are going to meet with folks in order to land January. The timeline for this is equally tight since not much can happen in terms of planning in December (which is partially why they remained optimistic about landing for 12/1).

They are likely booking trips and ready to go is my guess.

Sent from Windows Mail

From: Kevin Turner
Sent: November 5, 2012 6:31 PM
To: Steven Sinofsky, Steve Ballmer
Subject: RE: Surface sales physics after a week

From my side, I remain uncomfortable with Dec 1 jam in outside China. But I am supportive of the unblock for a calendar Q1 approach to mass retail. I would pursue more distribution in China now and we must ensure Sunning is in the loop.

Nick would need to begin the work now on the oem talk track which we would all need to go through and role play. Chris, Stephen S., Jeremy, and Daryl would need to work with Vince on the retailer GTM and I can put cycles on this with them next week. As a reminder, this week in retail is slammed with Halo 4 launch.

I also believe we should do the remaining points i outlined below as well...

Just let me know how you want to proceed as I am in Saudi Arabia today but will do my best on mail.

Kt

Sent from my Windows Phone

From: Steven Sinofsky
Sent: 11/6/2012 1:16 AM
To: Steve Ballmer; Kevin Turner
Subject: RE: Surface sales physics after a week

Jeremy Dale and Alan Bowman in CCG, along with Tami and I if this is about retail execution. Just Tami and I if this is about OEM relationships.

From: Steve Ballmer
Sent: Monday, November 5, 2012 2:10 PM
To: Kevin Turner; Steven Sinofsky
Subject: RE: Surface sales physics after a week

Who should i put with questions about how this work.s kt, Chriscap, steveschueler or. Their repoerts

Sent from Windows Mail

From: Steven Sinofsky
Sent: November 5, 2012 2:05 PM
To: Steve Ballmer, Kevin Turner
Subject: RE: Surface sales physics after a week

The ppt is customized by retailer with the regional account managers in ccg.

The folks who work for Chris are there for delivery and were part of making the decks. They were ready for this. This isn't the Surface team flying solo.

I don't see why the oem relationship is more challenging now than janaury. I get the emotion but that is already there. As a practical matter it isn't a legitimate concern and doesn't change in January.

If we want to sell units this year they need to start now...using the 3week timeline we used for suning. That was in the first mail.

Otherwise they need to start now for a more elaborate plan for January.

But if we don't sell units this year we have to stop the line.

This is really just math.

From: Steve Ballmer
Sent: 11/5/2012 2:01 PM
To: Kevin Turner; Steven Sinofsky
Subject: RE: Surface sales physics after a week

The handling with the retailers and oem's is challenging. what time commitment from Chris, you Steven, kt, and me is required and when. This will take selling is there a proposal or was the ppt for china alne

Sent from Windows Mail

From: Steven Sinofsky
Sent: November 5, 2012 1:56 PM
To: Steve Ballmer, Kevin Turner
Subject: RE: Surface sales physics after a week

What do you want to do? Just tell me how to unblock.

I just went through the math again and the cost of shutting down production is off the scale. And the ability to sell thru what we are making just can't happen if we don't act now. There's a really big financial issue. Even opening the door now doesn't escape the sell thru math but gives us a shot.

lets get folks talking today. We did suning from nothing to a unit run rate equivalent to the us stores in 3 week. We can do something in EC and Oz at least.

From: Steve Ballmer
Sent: 11/5/2012 1:50 PM
To: Steven Sinofsky; Kevin Turner
Subject: RE: Surface sales physics after a week

Does this propose these retailers are exclusive for 2-3 years. Who will make the calls on the partners. Both questions are valid whenever we proceed

From: Steven Sinofsky
Sent: Sunday, November 4, 2012 10:42 PM
To: Kevin Turner; Steve Ballmer
Subject: RE: Surface sales physics after a week

Let's take a step back. The intent was not to surprise, but to act on where we are. I think we're all surprised. I'm surprised at where we are in volumes, and honestly I don't think anyone feels we have "plans" to broaden distribution in January. So let's just assume we all have a bit of surprise and see what we can do to manage what I think is a drastic situation we find ourselves. There's nothing intended other than to get us to a better spot and certainly this is not about the efforts going on everywhere to amplify what is going on in our own stores—we've all spent considerable energy personally and the efforts of those working in the stores are historic.

We can disagree on how Surface will be labeled. Here's the data I am working with. Wall Street analysts have come up with estimates as low as 1 million units and on average in 3-5 million units for 2012. These are not made up. It is clear these are based on sourcing from component providers (likely nvidia but others as well). In other words, it will be pure "spin" to say we are hitting our own targets because in fact we have made about 1.2-1.5 million units this year (the 1.2 number is based on delivery before holiday, so add one more week of production). In addition, we are up against the confusion that got put in place over whether we are committed to Surface or it is a boutique product designed to "push OEMs". Since we will certainly not announce a number, it is likely everyone will conclude whatever we did (and whatever we say) are not meeting even our own expectations. We will be in a spiral very quickly. I've personally talked to several of the analysts who write the reports you send around and I am certain they will look at a lack of a number as a negative and if estimates start to surface (pun intended) that approach reality (250K) we will be in real trouble—that is 1/4th the lowest estimate and not the consensus estimate of 3M. The whole project will be labeled "Zune" and this will be a broad failure. The impact this has on sales in 2013 will be significant just as we saw with Zune—the partners won't carry it, the margins will erode, and pretty soon we'll be in RIM Playbook territory. We need to keep in mind how the Apple favored press will amplify these low numbers and in addition how the OEMs will use this as well. I really struggle with how we can make it through this. The story is out there written just waiting to be told.

Of course we are just comparing our own views of how this can play out in the landscape. If we want to be optimistic we can be. But I don't know how 250K units will meet any views we currently have. But for the purposes of this we can assume the most optimistic scenario. That's because there are real financials and sales velocity we can rely on rather than just predictions about the press.

There are no doubts about the velocity we are selling at—the sales per square foot. We need to have 4x the current sell-thru to be at a steady state. On current path we are going to be sitting on 1M Units of inventory. It is unclear under what plan we can ever burn through these. We can say we planned wrong, but we knew how many we could make and, frankly, we just went in optimistic over how much we could move online. We are currently moving about 28% of units as online. We need to be doing 70% online. But at the same time we more than double our online units we need to increase our total units. It means our online units need to go up by about 8x. It does not seem like that has any chance of happening.

The actions proposed are all excellent. I don't think one could disagree with them. But math says it won't be enough:

1. Take Surface NOW to other retailers in China. Gome, Mall Stores, etc. {Suning has a much larger footprint already so this won't double the runrate}
2. Extend our Holiday stores NOW for next calendar year. {The math on this will be positive, but this all is next calendar year and will not change the velocity we are seeing so this doesn't add to the unit runrate}
3. Start on a plan now to properly take Surface to mass retail in Jan/Feb with the Pro launch,. {We agree we have to plan now. I am suggesting that as we plan this we will find an appetite and capability to do more sooner}
4. Strategize how we tell our OEM's on our plan to take Surface to mass Retail, then we must properly tell the OEM's. {We have to do this no matter what if we follow your recommendation 3.}
5. Accelerate our physical Stores in the US and open physical and pop up stores in the Canada, UK, Australia and China in 2013. {This is a small marginal increase in volume}

We're missing what we would do in Europe, Asia, Pacific. Online and experience centers are not working to move units. With the fulfillment challenges we have had it is not clear we can recover from that—there's a good chance we have a significant SAT issue that will remain for quite some time.

Your issues raised are all real. Let me try to talk about them a bit in terms of the categories of issues:

* OEMs. We are in a tough spot as we operationalize things internally in that when there are differing views one or more folks hold up the possibility of upsetting OEMs. But we're not consistent in what we do or how we do things, so this isn't really something we can model or operationalize. From the outset we've been in a tough spot. When we priced Surface at $499 we sided with "our own" interests. When we included Office we upset the x86 side of things. And so on. I think we can agree, that selling now or later will have the same impact on the dialog. One could argue that OEMs are stocked out for holidays and that there are no tablets or touch screens at volume so we're really not taking "money" as you put it. I'm just pointing out that this is not so cut and dry.

* Retail execution. I've attached a very significant drill down on how this could work. The team that executing on Suning has put this together. It is essentially the deck we would go to Retailers with. It has margin details and an overall approach. We can doubt the ability of the team to execute, but they believe that they can deliver. We will never execute this as well as our stores. We have all done shopping this past week (I went to Northgate and Southcenter) so I'm assuming we all had the same experience of 8 out of 10 PCs "dead", no networking, and poorly trained retailers (I listened to a retailer completely fabricate a Windows 8 phone scenario). It looks really bad for Surface, but frankly unless our plan is store within a store I am not sure what we can ever hope to expect. Yes that makes me sad and is why we bet on our retail.

* SKUS, Online inventory and merchandising. We made a call to price at $499. Given that we can't secure attach very well online we limited this to 10% of the runrate, which is driving the stock out. This was going to have the implications we expected. The color choice was a known tradeoff because we did not want to sell unbundled for margin, value prop, and competitive reasons. While we know enough now on color mix and attach, any change in this (like adding green) will make the complexity of this significant. We've seen the impact of stock out on the blue cover.

We know the demand for coverless 64GB as well. Our margin structure is based on 110% attach. Less than that is problematic. All of this was known in the move to $499 coverless. The retail model we have in place focuses on attach, but is a risky margin proposition and stock out of colors can be a real issue.

* Enterprise. I'm excited to open this up. It is tough to see this as a material impact to the overall model.

* Product quality. I think this is a red herring. We've seen nothing at all to indicate product quality issues. Even twitter is silent on quality issues. The tone of product reviews started off positive and is increasing. The 8% number doesn't match the data we have but even then is close to the modeled number at 6%. Regardless, I don't know what we would do other than merchandising and scripts to change this since the product is what it is.

* Supply chain. I think we've worked this out and know how to scale.

* USA retail. I will defer. In many ways this is the least of our challenges given our footprint in the US. I have a hard time thinking WMT would stock us effectively given the low priced tablets they sell currently.

I'm not trying to be flip and not pay due to these issues. What I want to say is that all of them are being worked on. I think we have three courses of action:

* Plan starting now on how we expand for January. We can call this plan of record. I am not so sure it was. In any event let's do that now. It still involves folks getting rolling now. So we need to get them going.

* With those dialogs happening we can see what we can execute in Europe, Aus now. This is where we have no "see and buy" presence and we can definitely get something going—at least folks think so. We should allow them to have the dialog.

* Decide on a US plan. This seems a separate choice given the footprint we have here.

There is a fourth action which is we essentially do nothing now. I don't think anyone is recommending that.

Arguably there is an option where we just do way more marketing outreach to hope that is a substitute for physically touching the device for Holiday.

What concerns me is that we're not having a dialog about the material issue. 1M units/$500M in inventory on 1/1 is a major problem and that grows by 250K units per week. There are only two ways to fix this. We sell more between now and 1/1 or we stop the manufacturing line. If we stop the line it is a crazy high cost since startup is high. This is just manufacturing management. Even slowing it down means letting workers go. If we don't sell more we're going to need a new building to hold all the inventory. This is the real issue. Everything else feels like tactical issues to address relative to either selling more or making less.

I feel like under any circumstances we should unblock people from going to retailers and having the dialog about January. You indicate we need time to plan this and so we need to start. We can let them do this over the week and based on what we hear we can decide to do more. Absent that, our only option is to reduce manufacturing. I don't see it as feasible to inventory 1M units. And then we'll see how we can manage Wall St expectations.

Related to this is the notion of "Pro in January". I think we should temper expectations. This product is a niche product. It is $1000 and is not "the best tablet and the best laptop". It is a convertible with compromises. It runs x86 software but it does so at a size, weight, and battery life that will not please when compared to the world of 7" tablets. It is a small ultrabook (in 2 of 3 dimensions and weight). It is an ideal PC for a Windows 8 developer or for ruggedized industrial uses. It is not the ideal student PC (battery life) or knowledge worker PC (battery life, weight). It is incredibly nice. But it is not a blockbuster. Our chips are on Surface RT.

I know everything about Surface has been thoughtful. This is just as thoughtful. I've attached the retail deck. This is real work that has been going on for months. The roadshow is what we present to retailers based on the Suning work. Slide 23 has the retailer margin. Slide 26 starts with the gives/gets. Slide 29 has the instore efforts on 12/1. Slide 39 is the RSP strategy.

The GM looks like this:

Open

Max

Suning

32gb Standalone

0%

0%

0%

32gb Bundle

1%

4%

4%

64gb Bundle*

3% ?

6% ?

6%

Covers

20%

25%

25%

Accessories

20%

25%

25%

The following outlines the negotiation scenario financially:

From: Kevin Turner
Sent: Sunday, November 4, 2012 9:06 AM
To: Steven Sinofsky; Steve Ballmer
Subject: RE: Surface sales physics after a week

This is a complete surprise to me.... I had always planned on us bringing Surface to mass retail in the first quarter of 2013 and this is something that requires us to really carefully think through.

Explaining our Surface performance through the Holiday is very positive, simple and straightforward in my view.... It is also the truth.... The gist of our message would be "We are new into pc/tablet hardware business. We purposefully limited our distribution to our own stores and on-line to learn about the product and how it would be received by consumers and to allow us to refine our manufacturing, supply chain and logistics in preparation to bring it to mass retail in 2013. The response from consumers has been incredible, our stores have been over-run with customers wanting to learn more about surface and the selling performance of the devices has exceeded our expectations. We are now in a position to bring this wonderful product to everyone through our retail channel partners in the first quarter of 2013 as we launch our Pro version." I think this is one of the easiest stories we have ever told.

I philosophically disagree that Surface will be labeled a failure if we don't do mass retail distribution by December 1. I actually believe if we try and jam it in and it doesn't land well or perform well at mass retail then it will for sure be labeled a failure. This is why I believe this requires a more thoughtful approach. Also post the Holiday allows the device a better chance to stand on its on at Retail as the noise of competing devices and fixtures between now and the end of the calendar year is and will be deafening.....

Some business concerns I have in jamming this into Dec 1;

1. OEM's would be incensed... Communication that we are doing this before Dec. 1 would be brutal, bloody and further damaging to our trust/relationship. There is no way to spin this as we would be taking money out of our OEM's pocket directly in this holiday selling season. We simply can't do a quality job of this communication in this time frame and it will be viewed as very insincere given the timing.

2. No way to do a quality in store fixture, signage and get it made and get it rolled out in retail stores. Having a dead device in retail would almost be a certainty. Not landing Surface properly at Retail would be very brand damaging.

3. Very difficult to properly train RSP's during the busiest time of the year. So the controlled experience we have in our stores would be compromised. Yes people want to the feel the hardware, but they also want to understand the software, the apps, how you use it, etc. We aren't finding people in our own stores who feel the hardware and want to own it, they want to know what it does and how it works.

4. Quality of the product- is still not known. We are too soon into this to understand what our quality issues are, what our return rates are/will be etc. Note; we are doing a white glove experience and having an 8% plus return rate.

5. Our Supply chain performance and execution has been difficult and bumpy to date. We are shipping units from China direct to our stores today... this isn't scalable for retail stores WW.

6. Our on-line volume has been hampered tremendously because we were told to put on the web-site – "a 1 to 3 week delay in shipping"... We are currently out of the 32 GB tablet on line today.... Note, we just removed the 1 to 3 week delay language last Friday. I do expect our on-line volume to increase as a result.

7. We just launched on Friday the ability to do sales to corporations... Too soon to tell what this will mean but we know we will have increased demand there.

8. I think we need some work on our sku's. Forcing a black touch type key board with the one sku is not what most customers want and it is a customer dis-sat issue.... I think we need to analyze this and consider modifications....

9. In the USA I would not do BBY without doing some number of stores at Wal-Mart. Wal-Mart is the number 2 player in retail pc's in the US and is growing and BBY is shrinking.

10. Everything about Surface has been thoughtful and deliberate and calculated and this goes against that in every way shape and form and I don't get why would even consider this right now.

My recommendations;

1. Take Surface NOW to other retailers in China. Gome, Mall Stores, etc.

2. Extend our Holiday stores NOW for next calendar year.

3. Start on a plan now to properly take Surface to mass retail in Jan/Feb with the Pro launch,.

4. Strategize how we tell our OEM's on our plan to take Surface to mass Retail, then we must properly tell the OEM's.

5. Accelerate our physical Stores in the US and open physical and pop up stores in the Canada, UK, Australia and China in 2013.

From: Steven Sinofsky
Sent: Sunday, November 04, 2012 8:31 AM
To: Steve Ballmer
Cc: Kevin Turner
Subject: RE: Surface sales physics after a week

Jeremy Dale has been involved but I don't know what he has communicated. We are trying to keep this low until we decide given the sensitivities.

Vince Messina on our team is doing the primary driving as he did the Sunning deal in China. Since he does all the hardware assortment already, he worked closely with CCG who supported his lead.

Sent from Windows Mail

From: Steve Ballmer
Sent: November 4, 2012 7:43 AM
To: Steven Sinofsky
CC: Kevin Turner
Subject: RE: Surface sales physics after a week

We all agree we need to expand distribution   How and when have not been discussed amongst the three of us   is chris cap looped in

From: Steven Sinofsky
Sent: Sunday, November 4, 2012 6:51 AM
To: Steve Ballmer
Cc: Kevin Turner
Subject: RE: Surface sales physics after a week

What do you want to learn? What other data can we provide?

Surface is about to catastrophically fail in a very public way. We don't know how to explain selling 1/10th the number of devices as the lowest end of the lowest expectation. Word will get out very soon. There is no long term without this.

From: Steve Ballmer
Sent: 11/4/2012 6:35 AM
To: Steven Sinofsky
Cc: Kevin Turner
Subject: RE: Surface sales physics after a week

This is a huge decision with ramifications on consumers, retailers and oem's   Our OEM's would certainly be upset given their expectations   The timing does not allow care   I think we need a discussion with you KT, me, tami, and chriscap at min to walk through   I do not want to make a mistake on this   the downsize seems large compared to short term upside   What margin are we thinking for the retailers on the various sku's   that was never really worked through to the best of my knowledge   thanks for pushing

I am in Europe all week It will be tough but perhaps we can do a phone call with all relevant parties. I cannot say yes based on what I know   I did call KT on Saturday afternoon and this plan was news to him too

From: Steven Sinofsky
Sent: Saturday, November 3, 2012 3:17 PM
To: Steve Ballmer
Subject: RE: Surface sales physics after a week

Daryl, Vince, and Jeremy and their managers as far as I know. Tons of meetings this week. They are anxious to go.

From: Steve Ballmer
Sent: Saturday, November 3, 2012 3:13 PM
To: Steven Sinofsky
Subject: RE: Surface sales physics after a week

Who on the retail team worked this up

Sent from my Windows Phone

From: Steven Sinofsky [redacted]
Sent: 11/3/2012 2:31 PM
To: Steve Ballmer [redacted]
Subject: Surface sales physics after a week

We're at a point where we have enough data about the velocity and potential velocity for Surface sales to need to make a change. We're really in a very tough spot and I feel like we're on the verge of an unrecoverable situation. This is really just about the physics of how much we can sell through our store presence and online, and the number of units we have and will have. We are going to be sitting a very large inventory very soon and there's no real potential to have sales keep up with inventory growth unless we stop manufacturing, and the implications of that are significant. This is decidedly not a statement of our stores and popups. The traffic is crazy. We are holding steady in terms of traffic and at the limits of sales execution per square foot given traffic, associates, and time with customers (all assuming traffic holds). Here is the San Fran store this morning at an opening:

The only major learning is that we're not selling the units through online that we expected—the physics were such that we had to sell upwards of 70% of the units through online to make the overall sales match inventory/production and we're not even close. While we've had significant problems with the merchandising and selling motion on the site (and fulfillment) and this is likely to taint sales at least in UK and Germany given the breadth or reporting of these issues.

But the core learning and challenge is really that people want to touch Surface—does it type, how does it feel, etc.. Even when available, our experience centers are suffering from a low conversion rate because of frustration that you can't give us money and receive a unit right then and there. So all we can do is look for ways to get the product into people's hands when they can conduct a transaction and receive a PC right away.

The solution is to broaden our retail footprint as fast as possible outside the US, and to extend our retail presence in the US. These are two different choices. Outside the US is much like China and that we just decide to work with partners or not if we want to sell the PCs. Inside the US there are deeper implications. So these are separate choices.

In all cases, we have a plan we can execute on starting Monday that will have a footprint on 12/1 in store and expanding the footprint from a merchandising perspective through the boxing day and sales selling season. It is obviously less than a black Friday presence but it is too late for that. We know retailers are anxious and willing.

My suggestion is to rapidly move on this starting Monday—putting people on planes to make deals. There's not a lot of data beyond the selling data that we can gather. It is about faith we can do something credible. We have structures to maintain margin and pricing, accessory attach, and so on. We will not undermine the pricing and value proposition to land this.

If we don't want to do this right away then we are going to need to do something about production as we will reach an inventory level that cannot be sold through in 2013. I would recommend we stop production and reconsider GTX (which we believe is likely to be low volume at this point).

After reading this if you have any other ideas we should consider them now. We have literally spent the entire week looking at velocity and I really don't see another path.

From my view, this is conservative because it does not add aggressive online distribution which would move units—Amazon and pure play tech online.

Let's look at the specifics of what we want to start on.

Approach:

We will start to engage retailers in each of our current markets starting next week. Each region with a slightly different purpose. The negotiation theme is the same for each- in order to get the best margin possible, we will only offer exclusives to key retailers (list below). We will have walk away points for each retailer and will do so if we can't strike the right deal in margin, placement, and volume (the deal would include a minimum commitment of volume that they own so we don't put a bunch of inventory out there we have to take returns on). We push to hold our margins as best as possible, yet still get assorted (much like the Suning deal we struck).

Background:

The feedback that people believe this is a great product and the desire to touch and feel our device is cool to see. There are many questions about whether the touch cover really works and for a device that people want to carry around with them, understanding the feel of Surface in their hands is very important. Surface is also at a price point where most customers (with the exception of a small group of tech trendsetters) will want to be sure they want this product before they purchase it. We are seeing that today in that all of our Stores are FULL daily with folks that want to see and play with Surface before they purchase. And we're basically selling as fast as we can in the store without sacrificing the whole store experience.

Chart- If we take our current per week sales numbers and assume an increase of 10% growth each week, we would sell about 260K units between now and Jan 1. (These averages remove the peaks of preorder and launch date as well as Black Friday, but have a consistent growth each week). That leaves an inventory of ~1 M units (about $500M plus accessories). It is difficult to model the increase in online—there's a network effect of sorts so 10% a week as a linear growth is likely not the right model for online as there might be a steeper curve that kicks in later.

Physical Stores

US & Canada Online

International Online

Total

3-Nov

13391

4606

868

18865

10-Nov

14730

5067

955

20752

17-Nov

16203

5573

1050

22827

24-Nov

17823

6131

1155

25109

1-Dec

19606

6744

1271

27620

8-Dec

21566

7418

1398

30382

15-Dec

23723

8160

1538

33420

22-Dec

26095

8976

1691

36763

29-Dec

28705

9873

1861

40439

Total (11/30-1/1)

181,843

62,547

11,787

256,177

Based on our manufacturing rate against the current throughput from the stores and online, we believe we will have about 1M units in inventory at the end of the calendar year. While we have opened commercial orders, these will likely take some time before getting to significant volume and that model still must be proven out as we walk a delicate balance with OEMs and manage through an enterprise sales cycle of evaluation, requirements, etc.

The approach is to go to EMEA retailers in the next week, this will enable us to get into stores by 12/1 and still affect the majority of the holiday shopping season. In addition, a meeting with retailers now would help position us more positively when the RSPs are talking to consumers (obviously right now this is fairly ugly as the basic answer from an RSP is "the product is so bad we don't even stock it"). Optimistically, They can then tell customers to come back on 12/1 to buy it, rather than it's not a good product. Over time as our reputation grows among broad consumers and more and more have experience with Surface that they talk about, we hope online will also continue to pick up.

For reference- Suning had an original sell in of 50K with a forecast submitted this week of 225K additional units over the next 3 months (550 stores) as Chinese New Year is their largest selling season. If we go into Europe/Australia Brick and Mortar, we believe we would sell in 200-400K across the four retailers (MSH, FNAC, Dixons, Harvey Norman) with possible upside through holiday. This also is a great time to capitalize on these retailers being excited and the momentum we have in the channel.

The Approach:

* Europe and Australia- Conceptually, here is how we think this can play out. We will engage in Europe and Australia with a target to get assortment by 12/1. We believe this is possible and it will help move the needle before Christmas. This is an opportunity for us to tackle with assortment at MSH, FNAC, Harvey Norman, and Dixons (Each with an exclusive in their primary region of France, Germany, Australia, and UK). It would also increase the amount of countries we are in immediately as they have retail presence are in over 18 Countries throughout EMEA. We are sure that if we start the manufacturing of fixtures today (using a similar footprint we used for Suning), we can have them up and running by 12/1. We also know that we can move product from the DTV and China in time to support a launch in each of these retailers. Naturally, this is aggressive from a timing standpoint, so timing is critical we get started quickly. You can see below, the investment is about $3.8m to make this happen. I am not worried about the cost as much as the need to start executing.

* Japan and Russia- Fairly simple. Engage now, and be ready for the 1/26 launch. This also coincides with the media buy timing we already have in place, so I think this one is reasonably straight forward. I would expect some cultural challenges with Japan retailers as well as some need to find a way to merchandise differently to account for PIPC.

* US and Canada- Start the conversations now with both Best Buy and Staples. We will engage on the exclusive conversation and test the waters. Staples is easier because they are clearly hungry. Best Buy will take some time. The target for assortment in US would coincide nicely with a couple of factors: we target an End of January launch in US retail to coincide with the launch of Pro and it maintains our commitment to stores as the exclusive retailer in the US through holiday. My view is that BestBuy will grind to a halt quickly as the ask for money will be so high and while we would like the potential of ~1000 outlets, many are so sick that it is not likely there is an approach that works other than having a lot of poorly displayed and "dead" units in stores.

* Commercial: Stores started this engagement already, we are supporting through our EPG efforts and Kevin is aligned with this. As of yesterday the pipeline for commercial has opened (Verizon has already purchased 1,800 units). There is work here to make sure that the SA coverage model is clear and we don't inadvertently end up in pricing negotiations or have a mistake on the rights of usage because of Office Home & Student.

This is the details of the plan we want to start on presented in a tabular format:

Region

Approach

Date to Start

EMEA & Australia: in-store presence on 12/1

Retailers and store counts:

FNAC - 75

MSH - 350

Dixons - 500

Harvey Norman - 170

· In-person retailer assortment discussions = wk of 11/4