

UBS Global Technology Conference

Company Participants

- Christopher C. Capossela, Executive VP of Marketing & Consumer Business and CMO

Other Participants

- Jennifer Alexandra Swanson Lowe, Analyst, UBS Investment Bank, Research Division

Presentation

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Good morning, everyone. I'm Jen Lowe. I cover the U.S. Software Group here at UBS. And with us this morning we have Chris Capossela from Microsoft, CMO and EVP Marketing and Consumer Business is your title. But may be before you jump in, you could just give us a quick overview of your areas of responsibility at Microsoft and then we can jump off from there.

Christopher C. Capossela {BIO 6054036 <GO>}

Yes, Great. Well. Good morning, everyone. Thanks for being here. So my name is Chris Capossela. And I essentially have 2 kind of hats. I get to look after marketing for Microsoft. And so that means our pricing and packaging and naming and positioning and messaging and advertising and communications, all of the classic things we think of when you think about marketing, including pricing which often isn't in marketing. I do that across the company. Then I also look after a few sales organizations at Microsoft one -- mostly having to do with consumer or in small business-oriented products. So our Microsoft retail stores and our store -- our online store, which is quite large. The sales teams that call on are OEM partners like HP, Dell and Lenovo. And then our large retail partners around the world like a Best Buy and an Amazon and a Walmart. And also a sales team that looks after competing with Google selling Bing Advertising to marketers like myself. So a marketing hat for the company and then a few of the sales teams that have particular areas of focus.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Okay. Great. And even though it's a good place to start because they think one of the things that's really impressed people over the last few years is the brand transformation at Microsoft and just -- investor perceptions but also market perceptions have shifted fairly dramatically, can you talk a little bit, because we've seen other companies try and make that shift from being a successful client server company, PC era company to being a successful brand in the cloud? And most have

really struggled to do that. Microsoft is certainly the shiny example of success. So can you just talk a little bit about how that happened and what the mindset was?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. It's interesting. It doesn't always feel like the shiny example if successful, while I'll take it. But it's a journey. Every day, we're trying to make progress and there's a lot more room to go, I would say. I think there's a couple of things that have helped us transition from the sort of old Microsoft to the new. One is certainly product. I'd love to take credit for it as the marketer. But having real product truth when it comes to a cloud platform that does things that the other major cloud platforms don't do, obviously, helps tremendously, because when customers see what they can do, in our case, the hybrid cloud is really an incredible structural advantage that we have in its true differentiation for us. So now the marketing job is relatively easy and telling a differentiated story. When you have product truth and people can say "Wow, Azure can really do things that others can't," then that helps tremendously and changes people's perceptions of the company. So that's one awesome asset. When we take a business like Office and move it from a licensed device-based business and make it a cloud subscription that we update monthly, that is -- that just changes people's perceptions. So it's incredible. More than half of our Office revenue is now done as a subscription product, not as a transactional device-oriented license sale anymore. So business model changes, product truth, they help tremendously. I would say that Satya has really made Microsoft a mission-driven company. We have this simple mission of trying to empower every person and every organization on the planet to achieve more. And I think that we've embraced that more deeply than anyone felt we would. And we operate more as a single company than we ever have in the past. And it sounds trite or easy. But to live that mission actually takes real work. And one of the most fundamental things that I don't think people yet understand about Microsoft is we make that mission come true in the business model we've moved to, which is a consumption-based business model. We used to be a licensing machine. Now we are driven by consumption. And what I mean by consumption is, a customer, the more they use, the more they pay. They're only going to use our stuff if they like what it does for them, not surprisingly. People have this amazing clarity. If this isn't working for you, I'm going to stop using it. And the way we've designed the Azure business model and really the subscription business model, it's very based on customer satisfaction with the product and with Microsoft being a good partner to the company. And the more we -- the only way we succeed is when our customers succeed. And that's just simply not true of some of our biggest cloud competitors. And I think customers really value that. And it feels like a different company because of that. We feel more like a partner to our customers and less like a licensing machine. And I think that's subtle. I don't think most people deeply understand it yet. But I think it has deep structural advantages that have helped us on the perception side of the company.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Okay. And maybe before we sort of dig into the business a little more, I thought -- one of the questions that people ask is, Microsoft spends so much money on sales and marketing. And it has been a bit more efficient than in years past. But it's still a very big number. So as you look at your own budget and look at where investments

are happening, where you see the greatest return on that incremental marketing dollar, what do you see as sort of the best opportunities to continue and advance the story?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. I mean, I think we're obviously blessed to be a big believer in spending on R&D and a big believer in spending in sales and marketing to grow. And we're thrilled that we had incredible growth in Q1. I think it was in the 17%, 18%, 19% range. I think 19%. And it's fantastic. We're very blessed to see those results. We have to be smart about the way we spend. Microsoft's marketing spend as a % of revenue has come down dramatically over the past six years. And yet even though that's the case, we've been able to fund important, new marketing initiatives inside of the company that have reaped really nice reward. For us, the way I think about it is we are going to spend more and more of our marketing dollars on what we would consider performance-based marketing. Because we've gotten our act together as it relates to our data estate, we have very good line of sight to how much money it takes us to acquire a new Azure customer direct on our website or a new Office customer or a new Xbox customer or a new Surface customer. We have good data now on customer acquisition costs by SKU, by channel. And we have very good data now on the lifetime value of an Azure customer to Microsoft or the lifetime value of a Surface customer to Microsoft. And so putting that math together and be able to say, "Hi. I want to spend as much money as I possibly can as long as my customer acquisition cost is within a particular range and my lifetime value stays where we think it is. I want that budget to feel somewhat infinite to the teams who are responsible for spending the media dollars to acquire that next customer." And that's been an excellent engine for us to invest in. And interestingly, even though we've said it's sort of an infinite budget, the reality is there's only so much media you can buy before the media stops being as efficient and your customer acquisition cost starts to go up. Then the media teams will come to me and say, "Okay, we need to ratchet that down because it's just not as efficient as we need it to be," and that's a wonderful sort of self-fulfilling motion to have created, though I still do love spending marketing on perception. It is important, I think, to tell the world that you're going to be a leader in AI, to tell the world you're going to be a leader in cloud. Those are much harder to draw a direct line to the customer acquisition costs. But we know in our customers' eyes that if we're not seen as an innovative company and if we're not seen as a trustworthy company. And those for us are the 2 perceptions that probably matter most, then that spells problems for us long term. And so I have to constantly balance performance-based marketing with a hard TAC and LTV ratio with perception-based marketing to make sure people understand some of the new innovations that we have and what we're doing around trust and privacy.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And it's interesting because it's a little bit -- as we talk about digital transformation, you have a pretty concrete example of how data is driving value in your own organization. But maybe taking that up a little higher. I mean, digital transformation is just broadly one of the big talking points within the investment community and within your customer base. And as you think about -- going back to what you were saying, the truth in the message and making sure that you're able to deliver on what

you promise. As you think about digital marketing, what's sort of the right message that you should have in the marketplace now around digital transformation? How do you balance having a visionary point of view around things like AI that may be a little bit forward-leaning versus what's sort of grounded and what the technology's capable of today?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. So we're lucky to be in tech because the total addressable market is exploding. Everything is becoming digitized. So every company is becoming a tech company. And that allows Microsoft to be a great partner to them on their own tech journey. And I think while a lot of people use the term, there's real truth to it. We see it happening industry by industry, company by company. And so that puts Microsoft in a wonderful position of being able to be a trusted partner to these companies who are trying to figure out, how do I hire 1,000 engineers? How do I create an engineering culture to help me transform my products and empower my employees, et cetera, et cetera? From a marketing perspective, one of the things we found is truest to our own culture that we want to live, we really want to be an empowerment company. We're never going to be the cool kids. We're never going to be the things that a lot of people associate with tech. We're always going to want to be the company that empowers others. So that means the customer has to be cool. You celebrate what the customer does. You don't celebrate what your products do. And that's why if you look at most of our marketing, we're showcasing customers who have used our technology in some interesting way and allowing them to tell their own story. It's rare that you'll see an ad that's all about our product. It's much more common that our storytelling puts a real customer on stage and has them talk about the trials and tribulations of the transformation that they went through. And once you go there and you say most of your storytelling is going to be based on real customers, then you don't really have much of an issue in terms of it being fake because customers just won't go up on stage at an event and tell you about how they're doing unless they really believe. They won't let you do a TV ad, even if you pay for the media on their brand, unless they really believe. And so 98% of our marketing is based on stuff we're doing right now, that customers are doing right now, that you can go and buy our products and make them work for you. Then a tiny bit of what we do, we'll talk about quantum computing, which is an area that we're taking a real leadership position in. We'll do a 20-minute session of a Satya keynote at one of our big developer events. And he'll bring computer scientists on stage and talk for 20 minutes about quantum computing. And people will take notice of that. They'll say, "Wow! Satya took half of his keynote to talk about quantum. Even though there's no tech that can use it right this second, it must be important to Microsoft." But it's really a 95%-5% split on here-and-now versus putting a stake in the ground and saying, "We're doing things to invent the platforms that'll be important 10 years from now or five years from now."

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And if you think about sort of that continuum, because it's great when you have customers that have long tenure with Microsoft using some of the more innovative things that you're doing these days. But it might take time for a big Fortune 500 customer. So is there sort of a middle area where things like quantum computing are

still very much largely in the realm of academia versus the -- I mean, UBS isn't the best example. But a company that's fully embraced Azure and has great experiences. And they can talk about that. But what happens with the things in the middle, where you have some adoption, it's getting some momentum but maybe isn't mainstream and you don't have those big, strong reference points? How do you sort of manage that?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. We typically don't talk about them. You really don't -- we're lucky that we're in a broad set of markets. You really want to nurture those relationships. You want to help a customer realize their transformation. You take a partnership like the one we have with Real Madrid. And that took years in the making before they felt like they had really used our technology in a way that they were proud of. And so 2 or three years, we're working with them behind the scenes to actually implement things. Then 2 or three years down the road, they're willing to sort of stand up and say, "Hi. we have 450 million fans that follow this one small football team. And we have transformed our fan experience using Microsoft," and you just have to be quiet until the customers are really ready to talk. And so there's a painful pipeline you have to build. It's just like a sales pipeline. It's essentially a marketing -- sort of a marketing storytelling pipeline. And yet you have to go -- I think we've gotten better at resisting the temptation that when a customer says, "Yes. We're all in with you," to not then necessarily overmarket that. Because all that is, is a statement of intent. And perhaps a statement of buying a bunch of our stuff. But until they've actually used it in a powerful way, we'll try to avoid marketing it because it's just not real yet. I noticed that Accenture's going to be speaking later this morning. We've been on an incredible journey with Accenture. Today, they now have more PCs running Windows 10 than Microsoft does. They have more PCs running Windows 10 than Microsoft does. They're a much bigger company, 450,000 employees and associates. But they have more people on Windows 10 than we do. And they can update Windows 10 as fast as Microsoft can update Windows 10 for our own employees. Now that took years of work. That didn't just happen by saying, "We want to do this." And now you hear them talk very frequently about how they run on Microsoft. That was not a short -- that was not a short thing. That took a lot of hard work. So long answer to a simple question.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

It's a good answer. So maybe shifting gears a little bit. You mentioned also that pricing and some of those things fall within your purview. And an area where that is maybe in a bit higher focus is Office 365 and some of the packaging and the bundling happening there. If we look at where we are in that journey, you mentioned the revenues in subscription model. But it's moving fast. And there's a question of, in the next few years, do you reach a point where everybody is converted to Office 365? And what's the next leg of growth? So as you think about the pricing strategy in a business like Office 365, both bundling and also hitting new user groups, what's sort of -- how do you approach that? What's the strategy from a marketing perspective?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. So Microsoft is in a bunch of different businesses that have different sort of economic models, I guess, I would say. Gaming now has a very heavy usage-based model. The more hours people play something like a Fortnite or a Minecraft, you can essentially figure out what that model is. Azure is a consumption-based model. Office is sort of the classic playbook that Microsoft knows so. So well and our sales force knows incredibly well, which is essentially how many new users are you attracting and what's the average revenue per user. And so from a pure economic model perspective, it's probably the -- it's one of the simplest businesses we run. It's not a simple business. The economics behind it are quite easy to understand. There's an interesting notion that Office is somewhat penetrated. And the reality is that there's a huge number of workers that Microsoft has historically underserved with Office. We call these workers the first-line workers. Office has been very good for people who work in carpeted buildings with lots of glass in them. Office has never been great for people who work in buildings that have concrete floors and are 1-story tall or 2-stories tall. Think of a manufacturing shop floor. Think of airline pilots and people who check people into airlines. Think of Starbucks retail employees or Best Buy retail employees. These are people who don't use Word, Excel and PowerPoint as part of their day jobs. And so we put a pretty big investment in building new tools for these first-line workers that are available as an Office subscription. But they're not buying all of the Word, Excel and PowerPoint stuff that the people who work in carpeted buildings typically buy. So first-line workers are one part of our strategy. And that is to reach people that Office has never reached. And there's tons of them in the world. We've done a relatively good job penetrating the relatively small number of people in carpeted buildings. But there's far more human beings who have jobs as first-line workers. And that's a great, great opportunity. We've shipped a bunch of cool technology to let people like, do staff scheduling. So if you have a hair salon. And you have 20 people cutting hair, you need to schedule who's cutting here when. We now have tools in office that people are giving us wonderful feedback on. So first-line worker is new seats. And then what we've done on the existing seats, of course, is to create Office 365, higher value and -- all the way up to this thing that we call Microsoft 365, which includes Office, Windows and Enterprise Mobility and Security. So even when somebody has taken advantage of all of Office 365, there is still a way to move them up the value chain by adding in -- and what's hunting the best right now is security and manageability. And that move from Office 365 to Microsoft 365 represents a big step up in average revenue per user. So the economics are relatively straightforward, can you attract new people you've never attracted before? And for the ones who are doing things today, do you introduce new ways that they want to work that are valued and they're willing to buy? Teams would be an important part of that portfolio for new ways to work. And then a security would be the other important part of that portfolio to sort of move people up that stack.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And given some of the earlier commentary about the granularity you have into things like LTV versus CAC. And as you get into these higher volume, lower price point audiences, are you able to sort of sustain the LTV to CAC? Or maybe some of that data and granularity helps you get comfortable that that's ultimately a profitable

effort? I'd just be curious to get the perspective on the volume versus the higher value type stuff.

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. So for the Office business, it's just not an issue at all. We're very happy to continue to expand to new users. The way we run, we -- given the gross margin on Office is fantastic, including the transition to the cloud, we're very pleased that we have no issue with acquiring a first-line worker who maybe is going to pay us less than a white-collar, knowledge worker. I'd say we have lots of room to grow there. On the other side of the equation, as we move people up this stack, what we're finding is that security is an area where the overbuy from customers is pretty extreme. The number of security vendors that an IT shop will have inside their company is off the charts. And so there's an opportunity there for us to help customers save money. And their outlay overall goes down where, obviously, Microsoft's realization of what their spending goes up. So it's not just -- there's benefit on both sides of the equation, I would say.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And as you think about something like that because there's a huge opportunity for Microsoft from a revenue perspective in areas like security. But the flipside of that is also you've been a great partner in security do a lot of companies and you want to maintain that relationship as well. And that's important. How do you, from a marketing perspective, show all the great things Microsoft can do and advocate for Microsoft's capabilities without potentially stepping on the toes of companies that have been good partners for you in some of those areas traditionally?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. Well the key -- I think the key thing is to make sure that we have a great partnership with those ISVs. So they understand where we're going. We find that when we can do a good job communicating our roadmap to companies that are partners of ours, even as we're going into areas that our customers want us to go that may compete in areas they've gone, if they know we're headed there, then that typically gives them time to innovate on top of what we're doing or understand where our focus is so they can make sure that they continue to add value. At times, you're obviously going to compete head-to-head with somebody. But more often than not, a lot of the verticalized ISVs that we work closely with always feel like they have room to do things on top of what we're doing. And that's important to us to keep those partnerships strong.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Okay. Great. And looking at areas where -- at least there is a perception that Microsoft might compete with itself, things like Azure, where you have a great base of customers who are paying you under annuity contracts. And have been great customers for a long time, making sure that they remain happy and feel good about the product that they have if that's a choice they've made versus trying to get people

excited about Azure and moving to the cloud and that's really where the innovation, at least the perception is that's sort of the innovation center right now. How do you balance those audiences and those different products within the Microsoft portfolio that may have sort of different long-term aspirations attached to them?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. Well for us, there are a couple of things we think of. One is we don't think of the public cloud as the end all, be all. For us, we're -- we think there is a big structural advantage we have around this notion of the hybrid cloud. And being the only partner, the only company, that can take a customer and allow them to build a private cloud, allow them to build a hybrid cloud and allow them to build a public cloud and manage that spectrum of those 3 absolutely seamlessly is a huge, huge differentiator for us versus our cloud competitors who are sort of born in the cloud and cloud-only. And if you want to do your own private data center or if you want to have a hybrid solution, you really have no option without going to a bunch of third-party companies. So rather than me thinking about, "Hi. it's either Windows Server or its Azure," I think of frankly, Windows Server as your private Azure inside your company. In fact, we have a product called Azure Stack, which essentially allows you to take Azure and essentially privatize a lot of it and run it wherever you want to run it. We're the only company that can do that. And so rather than thinking about, "Oh, Windows server is the old thing," instead, we say no, no, no, it's just part of a continuum. We want to be the partner for you if you need to be in your own data center. We want to be the partner for you if you need to be create a portable data center that goes on cruise ships, that connects to the public cloud when it docks. But otherwise it's -- when it's out at sea, it's on its own. And when you, of course, want pure public infrastructure and you don't want to run any of your own servers, we want your applications. So just be able to move from public to hybrid to private. And if we think of it as more of a spectrum and less of a, that's old and bad. And this is new and good, that's an awesome competitive advantage because every customer goes on their own cloud journey. No 2 look the same. If you're starting a company from scratch today, unless you're in a really highly regulated industry, you're probably going to be public cloud from the start because why would you buy your own servers, why would you hire your own people to manage those servers. But if you're not starting today, if you have data centers around the world or you have a data center footprint, you're not just going to flip the switch and move it all to the public cloud. And so understanding that journey is something, I think, we're better positioned to do than our competitors. And that's how we think about it. Marketing, very simple. You market all the new stuff because you need customers to see that you're not holding onto the old world, that you're embracing the new world. You have to market Azure, you have to market Office 365, you have to market the cloud. You don't market Dynamics, you market Dynamics 365. You don't market traditional Office, you market Office 365. But lots of people just want to go to Walmart and buy a copy of Office and they don't want to be a subscription. They just want the disk, they just want Office, for goodness sakes. And we're not going to turn that off. We're not going to say, no, we don't like those customers. But we're going to market the cloud because we need that transformation to be clear in everyone's mind.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And as you think about that marketing audience, the enterprise is an area where you've been strong for a long time, broadly. Consumer is an area where you have a strong brand as well. I think there's sort of a view that developers are increasingly influential in bringing technologies into the enterprise. Microsoft recently acquired GitHub and the large community of developers, which haven't engaged with Microsoft technology traditionally. How do you approach marketing to that population. And in particular those people who may have been resistant to the Microsoft brand traditionally and for a variety of reasons?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. I think one of the things that Satya, our CEO; and Amy, our CFO, one of the things that we -- they've done very, very well is I think understand what we are buying when we buy something. And if you look at the acquisitions that we've done that I think have been the most successful under their time as CEO and CFO, they've been companies that are networks. LinkedIn is a network of hundreds of millions of people. Minecraft is a network. You think of it as a game. People think of Minecraft as a game. It's actually -- it's a massive community of builders. And it happens to be a game. But really as -- the asset is really the network. You look at GitHub. 31 million developers are checking in code or have open-source projects in GitHub. It's a network as much as it is a source code repository. And so we're very bullish on our ability to welcome GitHub to Microsoft to keep the wonderful things about that community. We named a developer inside of Microsoft as the CEO of GitHub. And that's Nat Friedman, somebody who has incredible credibility with the elite developer community around the world, with the open-source community around the world. We joined the Open Invention Network, which is a network dedicated to protecting open-source versus patent sort of trolls, if you will. And that was a quite surprising move. Satya has been on stage multiple times with a slide that says Microsoft loves Linux. Microsoft hearts Linux. Something like 40% of the virtual machines that are created on Azure are Linux virtual machines, 40%. Something like 50% of the Azure workloads are open-source workloads. So Azure has become a cloud for open-source developers. It's taken us a while to get past some old tapes that people have about Microsoft and open source. But we've moved on. We're the #1 contributor to GitHub. Way before we bought GitHub, Microsoft was contributing more to source code to GitHub than anyone else on the planet. And so people have been watching the company. They've seen this change to embrace open source. GitHub is the latest big step that I think a lot of people who would say, "Oh, my gosh. What are they going to do with it?" It's been awesome to see the Microsoft followers respond to those people who would say, "Oh, no. This is terrible. Microsoft hates open source. What's going to happen?" A lot of them has come out and said, "No, no, no. That's old tape. You haven't seen the new Microsoft. This is a completely different place. They love open source. And it's going to be a very, very good future." So I think courting developers is unbelievably important to us. Embracing open source is clearly, incredibly important to making that happen. Making Windows an incredible developer machine is another important thing for us to do. And we've done a lot of technical things to do that, including bringing the Linux command shell to Windows. So on your Windows box, you can actually work with Linux. Those are -- there are these many, many small things that we've done that are adding up to people saying, "Oh, I see Microsoft caring a lot more about us than we thought." And like I said earlier, there's not a big company I meet with that isn't trying to hire

more developers than they can hire. They want more developers than they can possibly find. And if you look at the #1 tool that developers use, what is the line of business system that developers use? If salespeople use CRM as their #1 line-of-business system, GitHub is the #1 LOB app for the world's developers. And if you see the number of developers going up, they become more important to every company, it's pretty obvious that that's an important tool set for us to love and care about. And that's a big reason why we embraced it.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And looking at sort of that third population, I guess, the consumers and maybe taking a step up. So I think historically, there's been this view that companies are either good at selling to consumers or they're good at selling to enterprises. But it's rare to do both well. And there's different examples on both sides. But I think Microsoft is the rare company that has strong brand equity in both those domains. How -- from a marketing standpoint, do you treat those separately? Do you see opportunities to showcase the Microsoft brand? And how do you want that brand to either be the same or different between those populations?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. So there's only one product that we have at the whole company -- or one family of products that's only for consumers. And that's gaming. The funny thing, of course, is that every device you can imagine, the #1 activity on that device is gaming. If you look at PCs, what's #1 thing people do with PCs? They play games. If you look at phones, what's the #1 thing they do on their phone? They play games. If you look at tablets, it's literally every single device. So gaming is sort of this incredible business. But every other business that we're in, the products that we make for end users, we want those to be successful at home and in schools as well as we want them to be successful in the enterprise. Windows is this way. Office is this way. Skype is this way. Surface would be one of the best examples. Is Surface a consumer business? Or is Surface a commercial business? Well revenue-wise, it's almost perfectly split for us as a company. I market it like a consumer product. If you look at how we do the TV ads and the video storytelling, we tell individual stories about how people use their Surface. But if you look closely, a lot of them are using Surface to pursue their business passions. We have an ad right now that's about a person who loves robots. And he builds robots using a Surface. It looks like a consumer ad. He feels like a consumer person. He's name is Adam. But if you look at the scenario, he's running a company. Is he a small company? Is he a big company? You don't really know. It's got a consumer vibe to it. But if you actually look at what he's doing, he's making money using his Surface to run his company. And so I think we don't actually think at Microsoft we have a consumer business and we have a commercial business. We actually think we have -- we go after gamers. We love gamers. We love developers. We love end users. And the end users are people like you and me. We use a device at home. And then if we love it, we hope our work allows us to bring that device or they're going to buy us -- buy one for us that's just like it. It's funny, the rest of the world or maybe investors like to think about commercial and consumer. Well we actually don't. We think about gamers. We think about IT pros. We think about developers. We think about end users. We know we have to appeal to end users. We know we have to win end users in small business, in education, at home. And if we

do a good job there, we know that that's going to carry over into the workplace, too, if that makes any sense.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Yes. It does. And actually, I'm going to take one off the (bolus). But I think it's related to this. I sort of simplify and say, consumers, enterprises, developers as audiences. But you have also potential future hires at Microsoft, you also have people like us. How does that factor into what you view as your domain in marketing versus either Investor Relations or HR or other groups? How do you sort of -- those populations like investors and potential hires, how do you think about those in your world view?

Christopher C. Capossela {BIO 6054036 <GO>}

I see. I see. So we have -- I'd say we look at it broadly and say the company has many stakeholders. Investor is an incredibly important stakeholder. Employees are stakeholders. Our own employees who already work at the company are stakeholders. Potential employees who may be thinking about joining the high-tech world is another set of stakeholders we need to think about. The press and analysts, not investor analysts but industry analysts like a Gartner or Forrester, that's another set of stakeholders. So broadly, across the company, one of the nice things about one Microsoft is the finance team, the marketing team, the HR team, we can all line up and say we all have the same stakeholders. Maybe Amy spends more of her time on the investor stakeholder. But she's counting on me to have great marketing that's going to appeal and that everyone's going to see. And I might take more responsibility for the industry analysts. The HR team might take more responsibility for hiring. But they're counting on me to create pull for young people to care about Microsoft and know what Microsoft's up to. And that is, I think, the wonderful way that one Microsoft works. I don't just put the blinders on and say, "Oh, Amy has to worry about investors." Otherwise, I wouldn't be here at the UBS tech conference, right? I mean, obviously, it's a team sport at Microsoft now. It wasn't always a team sport. Now it's a team sport. Everybody has to care. And everybody has a role to play. I do think deeply about how are we attracting the next generation of employees at the company. And that's something that maybe other companies would say, "Oh, that's HR's job." And it's not. It's the senior leadership team's job because the engineering leaders want to hire them. The HR leader wants to hire them. The marketing person wants to hire them. We all have to be pulling together there.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Great. And let me just come back. And so you talked about Surface. And going through your responses about the marketing and also within the consumer division, I think there's always a question of, what's considered a win for Surface? Because it's a product that's successful in its own right. But at least at the outset, it was positioned as inspiration for your partner ecosystem and what -- how much of that you want to do versus really just inspire. For you, what's a win? Is it creating a big Surface business? Or is it seeing a lot of other people come in with their Surface-like devices and taking the lead?

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. I think there's 2 things that we look at as a leadership team in terms of what is success for Surface. The first is Surface should be the very best experience for Windows and Office and gaming of any device made by anybody. If we can't do the work between the Surface design team, the Windows team, the Xbox team, the Office team, et cetera, to make Surface the highest product satisfaction laptop or 2-in-1 or pick a category on the planet, then we haven't succeeded. And today, from Surface Pro to Surface Laptop to every Surface we make, in its category, we're seeing higher product satisfaction scores using third-party data, not Microsoft data, that compares it to the MacBook, that compares it to any device in its category. So job 1, we better make these the most highly satisfied products because we're making all the pieces. And if we can't make those work, how would you expect our important OEM partners to build fantastic devices? So one is just make incredibly high-quality product that then makes Windows better for Dell, Windows better for HP, Windows better for Lenovo, et cetera, et cetera, et cetera. The second and probably even more important one is we have to create new categories. We have the P&L that can support us investing in new hardware categories that our traditional OEM partners may not be able to invest in. And so you look at the 2-in-1 category, Surface Pro was really the product that created the 2-in-1. And now, who makes more 2-in-1s than anybody? It's not us. It's Dell. It's HP and Lenovo. They're selling more 2-in-1s than certainly anybody else. You even see one of our big competitors who said they would never create a 2-in-1 because they were too odd. You either should have a tablet or you should have a laptop. And now of course, they've created 2-in-1. And they've got ads talking about their 2-in-1 because we created an absolutely new hardware category. That new hardware category is growing faster than all the traditional categories. And it has higher ASPs than all of the traditional categories. So when we can show our OEM partners that there's a new type of hardware category that customers want, they will then build it. And we give them the reference architecture. And we say Windows already does all these things really well. Look, here's the proof. They're going to then scale it out. They have points of distribution we'll never have. They have geo coverage we'll never have. And so that's how we think about it, best-quality devices across our games, our operating system and our productivity stack, best quality. And then we better create new categories. And we're working. We're hard at work. We love Surface Pro. I walked around the room. It's awesome for me to see all these Surface books and these Surface Pros. I think three years ago, I might've seen none in this room. And now I've seen a whole bunch of them. It's because of the quality. And it's because of the category creation. But we love that Dell and HP and Lenovo are selling far more than we are. We've created a category that they can then scale out, which is great for Windows, which is great for Office, et cetera.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

And maybe just a final question. And it's one that came in from a few people in the audience as well, is if you think about the layers of success within a hardware business, some of it's the form factor and having one that's appealing. But some of it's also the breadth of applications. And at this point in time, Surface is a smaller installed base than some of the alternatives out there. So how do you think about getting the applications that you need? And is there sort of a long tail where there's

a few that matter and a lot that are less relevant? How do you think about building out the app community given a relatively smaller footprint of installed advices?

Christopher C. Capossela {BIO 6054036 <GO>}

Hi. is that Surface statement or maybe a Windows?

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Yes, yes, I mean, yes, because I have Windows. It looks very different. But I'm thinking more just in the tablet form factor.

Christopher C. Capossela {BIO 6054036 <GO>}

Oh, yes. So for us, I think we excel in -- Windows really excels in the 9-inch-and-above screen size. Once you get to 9 inches, productivity becomes something you can really do. You could spend hours on the device being productive, not just consuming. But actually creating. And that's where I think Windows really shines. Introducing new technology like the pen and the dials, that takes some time for our ISVs to latch onto and to sort of say, "Okay, I'm going to actually dedicate resources to making the pen fantastic." We have to do the work in Windows first to make it very easy for them to then pick that up and implement it into their apps. But when we introduced the pen, I don't know, five years ago, people sort of were very cynical that it wouldn't be something that would really take off. And now you have -- everybody has a pen. Just about every device manufacturer, whether they're Windows or not, has embraced the pen, which then means the developers have to follow because you're seeing people sort of demand a better experience. So for us, it starts with the hardware and the form factor. We have to build the support into the operating system. So it's why we do Surface. So that we can actually do it ourselves end to end. But we're always looking to just push that reference out to the broader community because it's just first party. It's not going to work if it's not going to be broad enough. But we're not really wedded to Surface-specific apps. That's not interesting to us. Windows apps are far more what we're trying to do. Surface will always push the envelope on the form factor, on the hardware. But we want everyone else to pick that up as well.

Jennifer Alexandra Swanson Lowe {BIO 6926228 <GO>}

Okay. Great. I think we're out of time. So thank you for being here today.

Christopher C. Capossela {BIO 6054036 <GO>}

Yes. It's my pleasure. Thanks so much. My e-mail is very simple. It's chriscap@microsoft.com. If you had a question that we didn't get to, feel free to just shoot me an e-mail. And I'll be happy to respond. Thanks, everyone.

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