

Microsoft Cloud Strength Highlights Second Quarter Results

Commercial cloud annualized revenue run rate exceeds \$9.4 billion; Windows 10 active on over 200 million devices

REDMOND, Wash. — January 28, 2016 — Microsoft Corp. today announced the following results for the quarter ended December 31, 2015:

- Revenue was \$23.8 billion GAAP, and \$25.7 billion non-GAAP
- Operating income was \$6.0 billion GAAP, and \$7.9 billion non-GAAP
- Net income was \$5.0 billion GAAP, and \$6.3 billion non-GAAP
- Earnings per share was \$0.62 GAAP, and \$0.78 non-GAAP

During the quarter, Microsoft returned \$6.5 billion to shareholders in the form of share repurchases and dividends.

"Businesses everywhere are using the Microsoft Cloud as their digital platform to drive their ambitious transformation agendas," said Satya Nadella, chief executive officer at Microsoft. "Businesses are also piloting Windows 10, which will drive deployments beyond 200 million active devices."

The following table reconciles our financial results reported in accordance with generally accepted accounting principles ("GAAP") to non-GAAP financial results. Microsoft has provided this non-GAAP financial information to aid investors in better understanding the company's performance. All growth comparisons relate to the corresponding period in the last fiscal year.

	Three Months Ended December 31,			
(\$ in millions, except per share amounts)	Revenue	Operating Income	Net Income	Earnings per Share
2014 As Reported (GAAP)	\$26,470	\$7,776	\$5,863	\$0.71
Net Impact from Revenue Deferrals	(326)	(326)	(248)	(0.03)
Integration and Restructuring Charges	-	243	175	0.02
2014 As Adjusted (non-GAAP)	\$26,144	\$7,693	\$5,790	\$0.70
2015 As Reported (GAAP)	\$23,796	\$6,026	\$4,998	\$0.62
Net Impact from Revenue Deferrals	1,897	1,897	1,277	0.16
2015 As Adjusted (non-GAAP)	\$25,693	\$7,923	\$6,275	\$0.78
Percentage Change Y/Y (GAAP)	(10)%	(23)%	(15)%	(13)%
Percentage Change Y/Y (non-GAAP)	(2)%	3%	8%	11%
Percentage Change Y/Y (non-GAAP) Constant Currency	3%	13%	20%	23%

"We delivered double-digit operating income growth in non-GAAP constant currency while investing in key strategic areas that position Microsoft for continued long term growth," said Amy Hood, executive vice president and chief financial officer of Microsoft.

Revenue in Productivity and Business Processes declined 2% (up 5% in constant currency) to \$6.7 billion, with the following business highlights:

- Office commercial products and cloud services revenue grew 5% in constant currency driven by Office 365 revenue growth of nearly 70% in constant currency
- Office 365 consumer subscribers increased to 20.6 million
- Dynamics revenue grew 11% in constant currency with Dynamics CRM Online seat adds more than doubling year-over-year for the fifth consecutive quarter

Revenue in Intelligent Cloud grew 5% (up 11% in constant currency) to \$6.3 billion, with the following business highlights:

- Server products and cloud services revenue grew 10% in constant currency
- Azure revenue grew 140% in constant currency with revenue from Azure premium services growing nearly 3x year-over-year
- Over one third of the Fortune 500 have chosen our Enterprise Mobility solutions, up nearly 3x year-over-year

Revenue in More Personal Computing declined 5% (down 2% in constant currency) to \$12.7 billion, with the following business highlights:

- Windows OEM revenue declined 5% in constant currency, outperforming the PC market, driven by higher consumer premium and mid-range device mix
- Surface revenue increased 29% in constant currency driven by the launch of Surface Pro 4 and Surface Book
- Phone revenue declined 49% in constant currency reflecting our strategy change announced in July 2015
- Search advertising revenue excluding traffic acquisition costs grew 21% in constant currency with continued benefit from Windows 10 usage
- Xbox Live monthly active users grew 30% year-over-year to a record 48 million

"It was a strong holiday season for Microsoft highlighted by Surface and Xbox," said Kevin Turner, chief operating officer at Microsoft. "Our commercial business executed well as our sales teams and partners helped customers realize the value of Microsoft's cloud technologies across Azure, Office 365 and CRM Online."

Business Outlook

Microsoft will provide forward-looking guidance in connection with this quarterly earnings announcement on its earnings conference call and webcast.

Webcast Details

Satya Nadella, chief executive officer, Amy Hood, executive vice president and chief financial officer, Frank Brod, chief accounting officer, John Seethoff, deputy general counsel and corporate secretary, and Chris Suh, general manager of Investor Relations, will host a conference call and webcast at 2:30 p.m. Pacific time (5:30 p.m. Eastern time) today to discuss details of the company's performance for the quarter and certain forward-looking information. The session may be accessed at <http://www.microsoft.com/investor>. The webcast will be available for replay through the close of business on January 28, 2017.

Adjusted Financial Results and non-GAAP Measures

During the second quarter of fiscal year 2016, GAAP revenue, operating income, net income, and earnings per share include the net impact from revenue deferrals. For the second quarter of fiscal year 2015, GAAP revenue, operating income, net income, and earnings per share include the recognition of previously deferred net revenue and charges related to integration and restructuring expenses. These items are defined below. In addition to these financial results reported in accordance with GAAP, Microsoft has provided certain non-GAAP financial information to aid investors in better understanding the company's performance. Presenting these non-GAAP measures gives additional insight into operational performance and helps clarify trends affecting the company's business. For comparability of reporting, management considers this information in conjunction with GAAP amounts in evaluating business performance. These non-GAAP financial measures should not be considered as a substitute for, or superior to, the measures of financial performance prepared in accordance with GAAP.

Non-GAAP Definitions

Revenue Deferrals. Microsoft recorded a net \$1.9 billion revenue deferral during the three months ended December 31, 2015, primarily related to Windows 10 and Halo 5.

Microsoft recognized a net \$326 million of previously deferred revenue during the three months ended December 31, 2014, primarily related to sales of bundled products and services.

Integration and Restructuring Charges. Integration and restructuring expenses were \$243 million during the three months ended December 31, 2014. Integration and restructuring expenses include employee severance expenses and costs associated with the consolidation of facilities and manufacturing operations related to restructuring activities, and systems consolidation and other business integration expenses associated with the acquisition of Nokia's Devices and Services business.

Constant Currency

Microsoft presents constant currency information to provide a non-GAAP framework for assessing how our underlying businesses performed excluding the effect of foreign currency rate fluctuations. To present this information, current and comparative prior period non-GAAP results for entities reporting in currencies other than United States dollars are converted into United States dollars using the average exchange rates from the comparative period rather than the actual exchange rates in effect during the respective periods. The non-GAAP financial measures presented below should not be considered as a substitute for, or superior to, the measures of financial performance prepared in accordance with GAAP. All growth comparisons relate to the corresponding period in the last fiscal year.

Financial Performance Constant Currency Reconciliation

	Three Months Ended December 31,			
(\$ in millions, except per share amounts)	Revenue	Operating Income	Net Income	Earnings per Share
2014 As Reported (GAAP)	\$26,470	\$7,776	\$5,863	\$0.71
2014 As Adjusted (non-GAAP)	\$26,144	\$7,693	\$5,790	\$0.70
2015 As Reported (GAAP)	\$23,796	\$6,026	\$4,998	\$0.62
2015 As Reported (non-GAAP)	\$25,693	\$7,923	\$6,275	\$0.78
Percentage Change Y/Y (GAAP)	(10)%	(23)%	(15)%	(13)%
Percentage Change Y/Y (non-GAAP)	(2)%	3%	8%	11%
Constant Currency Impact	\$(1,212)	\$(766)	\$(676)	\$(0.08)
Percentage Change Y/Y (non-GAAP) Constant Currency	3%	13%	20%	23%

Segment Revenue Constant Currency Reconciliation

	Three Months Ended December 31,		
(\$ in millions)	Productivity and Business Processes	Intelligent Cloud	More Personal Computing
2014 As Reported (GAAP)	\$6,822	\$6,041	\$13,282
2015 As Reported (GAAP)	\$6,690	\$6,343	\$12,660
Percentage Change Y/Y (GAAP)	(2)%	5%	(5)%
Constant Currency Impact	\$(439)	\$(369)	\$(404)
Percentage Change Y/Y (GAAP) Constant Currency	5%	11%	(2)%

About Microsoft

Microsoft (Nasdaq "MSFT" @microsoft) is the leading platform and productivity company for the mobile-first, cloud-first world and its mission is to empower every person and every organization on the planet to achieve more.

Forward-Looking Statements

Statements in this release that are "forward-looking statements" are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could differ materially because of factors such as:

- intense competition in all of Microsoft's markets;
- increasing focus on services presents execution and competitive risks;
- significant investments in new products and services that may not be profitable;
- acquisitions, joint ventures, and strategic alliances may have an adverse effect on our business;
- impairment of goodwill or amortizable intangible assets causing a significant charge to earnings;
- Microsoft's continued ability to protect and earn revenues from its intellectual property rights;
- claims that Microsoft has infringed the intellectual property rights of others;
- the possibility of unauthorized disclosure of significant portions of Microsoft's source code;
- cyber-attacks and security vulnerabilities in Microsoft products and services that could reduce revenue or lead to liability;
- disclosure of personal data that could cause liability and harm to Microsoft's reputation;
- outages, data losses, and disruptions of our online services if we fail to maintain an adequate operations infrastructure;
- government litigation and regulation that may limit how Microsoft designs and markets its products;
- potential liability under trade protection and anti-corruption laws resulting from our international operations;
- laws and regulations relating to the handling of personal data may impede the adoption of our services or result in increased costs, legal claims or fines against us;
- Microsoft's ability to attract and retain talented employees;
- adverse results in legal disputes;
- unanticipated tax liabilities;
- Microsoft's hardware and software products may experience quality or supply problems;
- exposure to increased economic and operational uncertainties from operating a global business;
- catastrophic events or geo-political conditions may disrupt our business; and
- adverse economic or market conditions may harm our business.

For more information about risks and uncertainties associated with Microsoft's business, please refer to the "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Risk Factors" sections of Microsoft's SEC filings, including, but not limited to, its annual report on Form 10-K and quarterly reports on Form 10-Q, copies of which may be obtained by contacting Microsoft's Investor

Relations department at (800) 285-7772 or at Microsoft's Investor Relations website at <http://www.microsoft.com/investor>.

All information in this release is as of January 28, 2016. The company undertakes no duty to update any forward-looking statement to conform the statement to actual results or changes in the company's expectations.

For more information, press only:

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Note to editors: For more information, news and perspectives from Microsoft, please visit the Microsoft News Center at <http://www.microsoft.com/news/>. Web links, telephone numbers, and titles were correct at time of publication, but may since have changed. Shareholder and financial information, as well as today's 2:30 p.m. Pacific time conference call with investors and analysts, is available at <http://www.microsoft.com/investor>.

MICROSOFT CORPORATION

INCOME STATEMENTS

(In millions, except per share amounts)(Unaudited)

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2015	2014	2015	2014
Revenue	\$ 23,796	\$26,470	\$ 44,175	\$49,671
Cost of revenue	9,872	10,136	17,079	18,409
Gross margin	13,924	16,334	27,096	31,262
Research and development	2,900	2,903	5,862	5,968
Sales and marketing	3,960	4,315	7,293	8,043
General and administrative	1,038	1,097	2,122	2,248
Impairment, integration, and restructuring	0	243	0	1,383
Operating income	6,026	7,776	11,819	13,620
Other income (expense), net	(171)	74	(451)	126
Income before income taxes	5,855	7,850	11,368	13,746
Provision for income taxes	857	1,987	1,750	3,343
Net income	\$ 4,998	\$ 5,863	\$ 9,618	\$10,403
Earnings per share:				
Basic	\$ 0.63	\$ 0.71	\$ 1.21	\$ 1.26
Diluted	\$ 0.62	\$ 0.71	\$ 1.20	\$ 1.25
Weighted average shares outstanding:				
Basic	7,964	8,228	7,980	8,238
Diluted	8,028	8,297	8,047	8,321
Cash dividends declared per common share	\$ 0.36	\$ 0.31	\$ 0.72	\$ 0.62

MICROSOFT CORPORATION

COMPREHENSIVE INCOME STATEMENTS

(In millions)(Unaudited)

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2015	2014	2015	2014
Net income	<u>\$ 4,998</u>	<u>\$ 5,863</u>	<u>\$ 9,618</u>	<u>\$10,403</u>
Other comprehensive income (loss):				
Net unrealized gains (losses) on derivatives (net of tax effects of \$5, \$6, \$28, and \$10)	(49)	247	8	566
Net unrealized gains (losses) on investments (net of tax effects of \$86, \$(124), \$(222), and \$(226))	160	(231)	(411)	(420)
Translation adjustments and other (net of tax effects of \$(9), \$(211), \$(21), and \$(258))	(76)	(390)	(346)	(471)
Other comprehensive income (loss)	<u>35</u>	<u>(374)</u>	<u>(749)</u>	<u>(325)</u>
Comprehensive income	<u>\$ 5,033</u>	<u>\$ 5,489</u>	<u>\$ 8,869</u>	<u>\$10,078</u>

MICROSOFT CORPORATION

BALANCE SHEETS
(In millions)(Unaudited)

	December 31, 2015	June 30, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 7,185	\$ 5,595
Short-term investments (including securities loaned of \$360 and \$75)	95,455	90,931
Total cash, cash equivalents, and short-term investments	102,640	96,526
Accounts receivable, net of allowance for doubtful accounts of \$384 and \$335	14,507	17,908
Inventories	2,702	2,902
Deferred income taxes	1,618	1,915
Other	6,345	5,461
Total current assets	127,812	124,712
Property and equipment, net of accumulated depreciation of \$18,008 and \$17,606	15,789	14,731
Equity and other investments	11,514	12,053
Goodwill	17,436	16,939
Intangible assets, net	4,619	4,835
Other long-term assets	2,928	2,953
Total assets	\$ 180,098	\$ 176,223
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 6,936	\$ 6,591
Short-term debt	3,000	4,985
Current portion of long-term debt	750	2,499
Accrued compensation	3,649	5,096
Income taxes	493	606
Short-term unearned revenue	20,929	23,223
Securities lending payable	439	92
Other	6,447	6,766
Total current liabilities	42,643	49,858
Long-term debt	40,679	27,808
Long-term unearned revenue	4,102	2,095
Deferred income taxes	2,194	2,835
Other long-term liabilities	13,700	13,544
Total liabilities	103,318	96,140
Commitments and contingencies		
Stockholders' equity:		

Common stock and paid-in capital - shares authorized 24,000; outstanding 7,925 and 8,027	68,279	68,465
Retained earnings	6,728	9,096
Accumulated other comprehensive income	1,773	2,522
<hr/> Total stockholders' equity	<hr/> 76,780	<hr/> 80,083
Total liabilities and stockholders' equity	<u>\$ 180,098</u>	<u>\$ 176,223</u>

MICROSOFT CORPORATION
CASH FLOWS STATEMENTS

(In millions)(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2015	2014	2015	2014
Operations				
Net income	\$ 4,998	\$ 5,863	\$ 9,618	\$10,403
Adjustments to reconcile net income to net cash from operations:				
Depreciation, amortization, and other	1,544	1,521	3,005	2,949
Stock-based compensation expense	658	633	1,332	1,279
Net recognized losses (gains) on investments and derivatives	50	(179)	151	(124)
Excess tax benefits from stock-based compensation	(20)	(22)	(302)	(524)
Deferred income taxes	(247)	314	(174)	615
Deferral of unearned revenue	12,570	10,200	22,993	18,222
Recognition of unearned revenue	(11,929)	(11,495)	(23,284)	(22,138)
Changes in operating assets and liabilities:				
Accounts receivable	(3,118)	(3,378)	3,258	3,249
Inventories	1,104	1,070	167	587
Other current assets	(912)	(159)	(1,192)	(439)
Other long-term assets	56	170	51	449
Accounts payable	369	137	234	(522)
Other current liabilities	105	(986)	(1,919)	(2,152)
Other long-term liabilities	370	651	254	840
Net cash from operations	5,598	4,340	14,192	12,694
Financing				
Proceeds from issuance (repayments) of short-term debt, maturities of 90 days or less, net	(7,031)	4,798	(2,141)	7,797
Proceeds from issuance of debt	13,128	0	13,249	0
Repayments of debt	(121)	0	(1,871)	(1,500)
Common stock issued	117	121	336	337
Common stock repurchased	(3,678)	(2,145)	(8,435)	(5,033)
Common stock cash dividends paid	(2,868)	(2,547)	(5,343)	(4,854)
Excess tax benefits from stock-based compensation	20	22	302	524
Other	(65)	285	(243)	285

Net cash from (used in) financing	(498)	534	(4,146)	(2,444)
Investing				
Additions to property and equipment	(2,024)	(1,490)	(3,380)	(2,772)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	(381)	(2,794)	(771)	(2,935)
Purchases of investments	(34,750)	(19,167)	(72,320)	(43,252)
Maturities of investments	5,351	2,389	11,037	4,082
Sales of investments	28,191	16,108	56,693	32,553
Securities lending payable	285	238	347	(129)
Net cash used in investing	(3,328)	(4,716)	(8,394)	(12,453)
Effect of exchange rates on cash and cash equivalents	(18)	(34)	(62)	(40)
Net change in cash and cash equivalents	1,754	124	1,590	(2,243)
Cash and cash equivalents, beginning of period	5,431	6,302	5,595	8,669
Cash and cash equivalents, end of period	\$ 7,185	\$ 6,426	\$ 7,185	\$ 6,426

MICROSOFT CORPORATIONSEGMENT REVENUE AND OPERATING INCOME
(In millions)(Unaudited)

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2015	2014	2015	2014
Revenue				
Productivity and Business Processes	\$ 6,690	\$ 6,822	\$ 12,990	\$13,312
Intelligent Cloud	6,343	6,041	12,232	11,516
More Personal Computing	12,660	13,282	22,114	24,548
Corporate and Other	(1,897)	325	(3,161)	295
Total revenue	<u>\$ 23,796</u>	<u>\$26,470</u>	<u>\$ 44,175</u>	<u>\$49,671</u>
Operating Income (Loss)				
Productivity and Business Processes	\$ 3,305	\$ 3,587	\$ 6,460	\$ 6,988
Intelligent Cloud	2,580	2,600	4,977	4,705
More Personal Computing	2,038	1,506	3,542	3,014
Corporate and Other	(1,897)	83	(3,160)	(1,087)
Total operating income	<u>\$ 6,026</u>	<u>\$ 7,776</u>	<u>\$ 11,819</u>	<u>\$13,620</u>