BERNSTEIN
SOCIETE GENERALE GROUP

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Mark L. Moerdler, Ph.D.
+1 917 344 8506
mark.moerdler@bernsteinsg.com


Firoz Valliji, CFA
+1 917 344 8316
firoz.valliji@bernsteinsg.com


Shelly Tang, CFA
+1 917 344 8342
shelly.tang@bernsteinsg.com

Global Software

Microsoft Corp

Rating

Outperform

Price Target

MSFT **646.00 USD** (641.00 *OLD*)

Microsoft 3Q26: a good quarter, but the debate continues

While this was a solid quarter beating consensus on every major metric, this was not the definitive Azure acceleration qtr we had hoped for. At a high level Azure was in-line; CAPEX was slightly lower; while Copilot significantly beat. Q4 guide was similar with CAPEX in-line, Azure slightly above; and Copilot growing strong. It was a solid quarter but not enough to make those sitting on the sidelines to return to Microsoft.

But one must look a bit deeper to see that the global Gen AI disruption cycle is good for Microsoft: 1) AI is a driver of growth for Microsoft and not a headwind; 2) Copilot strength shows AI is not eating Microsoft's apps/ SaaS business; 3) Operating margins are increasing when AI worries point to deceleration; and 4) The Azure growth acceleration is not off the table, it layers in over time.

The company is spending aggressively on CAPEX and more specifically on datacenter hardware to meet demand which of course will give many investors pause, but we would argue that for a stock that was trading at >30x future EPS and now at 23x, Microsoft delivers the combination of AI resilience / upside plus strong GAAP EPS growth and software exposure. Will everyone flock back into the stock over the next few days? We doubt it, but for those ready to add to software exposure this is a solid / safe place to add that exposure at very good valuation.

Investment Implications

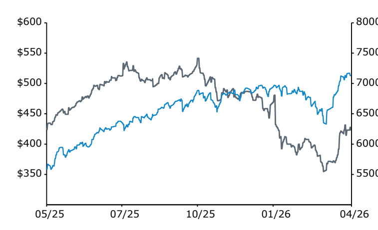
Microsoft (MSFT, $646 TP, Outperform) delivered a quarter with solid Azure growth and strong Copilot momentum. Combine that with 1) ability to deliver stable GAAP margins in the mid 40s and 2) downside risk protection even if we see some bubble like behavior in parts of AI, this is a stock that every investor should have significantly in their portfolio. We raised our price target from $641 to $646 as we roll forward our estimates and lower our valuation multiple from 29.5x to 29x, to reflect peer step-down in peer group valuation.

Close Date	29 Apr 2026
MSFT Close Price (USD)	424.46
Price Target (USD)	646.00
Upside/(Downside)	52%
52-Week Range	555.45/356.28
SPX	7,135.95
FYE	Jun
Div Yield	0.9%
Market Cap (USD) (B)	3,153.07
EV (USD) (B)	3,186.89

Performance	YTD	1M	6M	12M
Absolute (%)	(12.2)	19.0	(21.6)	7.7
SPX (%)	4.2	12.0	3.6	28.3
Relative (%)	(16.5)	6.9	(25.2)	(20.6)

Source: Bloomberg, Bernstein estimates and analysis.

Price Performance, 1YR



Adjusted EPS	F25A	F26E	F27E
MSFT (USD)	13.64	**16.85**	**19.16**
OLD	--	16.84	19.39

Financials	F25A	F26E	F27E	CAGR
Revenues (M)	281,724	330,125	391,739	17.9%
Operating Earnings (M)	128,528	154,362	177,626	17.6%
Net Earnings (M)	101,832	125,599	142,905	18.5%
Revenue/Share	37.74	44.28	52.51	18.0%
Operating Margin (%)	45.6	46.8	45.3	--
Net Income Margin (%)	36.1	38.0	36.5	--
EPS Growth (%)	15.6	23.5	13.7	--

Valuation Metrics	F25A	F26E	F27E
Adjusted P/E (x)	31.1	25.2	22.2
PEG Adjusted (x)	2.0	1.1	1.6
EV/Sales (x)	11.3	9.7	8.1
P/Sales (x)	11.2	9.6	8.1
PEG Reported (x)	2.0	1.1	1.6
EV/EBIT (x)	24.8	20.6	17.9
Div Yield (%)	0.8	0.8	0.9

Source: Bloomberg, Bernstein estimates and analysis.

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VALUATION COMPS TABLE

	4/29/2026		Net Cash Per Share		Free Cash Flow (LTM)		Revenue Growth	Valuation Multiples			
	Company	Share Price	$	% of Share Price	Per Share ($)	% Yield	NTM (%)	EV / NTM Revenue	P / FE	Price / FCF (LTM)	PEG Ratio
Bernstein Coverage	Adobe	$242.91	0.56	0.2%	24.55	10.1%	8.7%	3.7x	10.1x	9.5x	1.0x
	Microsoft	$424.17	(4.53)	(1.1%)	10.37	2.4%	15.3%	9.0x	24.2x	40.7x	1.7x
	Oracle	$163.32	(42.37)	(25.9%)	(8.52)	N/A	28.0%	7.2x	21.5x	N/A	4.2x
	MongoDB	$257.25	28.61	11.1%	6.16	2.4%	17.7%	6.3x	43.9x	41.3x	2.4x
	Salesforce.com	$181.40	(8.52)	(4.7%)	15.06	8.3%	11.1%	3.4x	13.8x	10.3x	2.6x
	HubSpot	$226.79	27.10	11.9%	10.85	4.8%	18.0%	2.8x	18.2x	20.2x	0.6x
	SAP	$170.11	2.15	1.3%	6.98	4.1%	10.5%	5.0x	19.4x	25.6x	1.1x
	Snowflake	$141.31	3.82	2.7%	3.32	2.3%	26.3%	8.0x	78.2x	43.6x	1.8x
	Workday	$121.73	6.09	5.0%	10.36	8.5%	11.5%	2.8x	11.7x	11.3x	0.9x
Other Comps	Autodesk	$234.74	(0.64)	(0.3%)	11.20	4.8%	13.1%	6.1x	18.9x	20.6x	0.9x
	ServiceNow	$88.86	2.63	3.0%	4.43	5.0%	21.2%	5.3x	20.3x	19.8x	1.1x
	Amadeus	$56.59	(6.07)	(10.7%)	4.72	8.3%	5.3%	4.1x	14.3x	12.2x	1.5x
	Datadog	$134.05	8.79	6.6%	2.52	1.9%	19.5%	10.9x	60.9x	52.2x	8.2x

Source: Bloomberg, Bernstein analysis

DETAILS

While Microsoft delivered a solid quarter beating consensus on every major metric (Exhibit 2), this was not the definitive Azure acceleration quarter we had hoped and discussed in our recent note (Microsoft: Could the bear case in fact be the bull case?). At a very high level, Azure was in-line with buy-side expectations; in-quarter CAPEX was slightly lower than expected; while Copilot significantly beat expectations. Q4 guidance was similar with CAPEX roughly line-in with expectations, Azure guidance is likely slightly above expectations and Copilot commentary much stronger than expectations. In other words, a good / solid quarter but not enough to make those sitting on the sidelines return to Microsoft in droves.

But to appreciate the quarter requires looking a bit deeper into the numbers and their implications. There are, we believe, 4 very important data points that really show that the global Gen AI disruption cycle is good for Microsoft:

1. **AI is a driver of growth for Microsoft and not a headwind to Microsoft growth**: The company stated that Microsoft AI ARR was >$37B growing 123% YoY. This means that >11% of Microsoft's total revenue is growing triple digits and if you plug that into your Microsoft model you would have AI, by itself, delivering ~12% revenue growth for all of Microsoft and that is excluding the rest of the business that is doing quite well and overall growing nicely.

    - It is important to call out the size of Microsoft's AI business. $37B makes Microsoft's AI revenue stream much bigger than its hyperscaler peers and in-line with the best in class frontier model business and that $37B does not include the non-GPU revenue that AI at enterprise customers are generating. In fact, as Agentic AI goes mainstream the positive impact on the non-GPU Azure business will be substantial and potentially another leg of growth.

2. **AI is not eating Microsoft's apps/ SaaS business**: We have written extensively about the SaaS Apocalypse concerns impacting software valuations. Office is the largest apps business at Microsoft and Office 365 Copilot, which many investors have been concerned about, grew from 15M paid seats in Q2 to >20M seats in Q3 and management is guiding to more new paid seats in Q4. Note that in May M365 E7 launches which incorporates Copilot and should, we believe help drive this strong adoption.

    - Note that GitHub Copilot is also seeing acceleration and the company is now moving to a hybrid model for both GitHub Copilot and M365 Copilot with subscription plus consumption to assure Microsoft can capture the revenue upside and protect the margin from excess usage.

3. **Operating margins are increasing**: Microsoft delivered another quarter in which operating margins increased. AI is currently negatively impacting gross margins, especially in Azure, but management believes that over time those margins will go up. Meanwhile, the company is driving operating leverage (something they did so successfully during the Cloud transition) and using AI to reduce headcount and operating expenses (even as they invest aggressively in their R&D). The net effect is not simply flat margins but incrementally higher margins even with massively CAPEX investments.

4. **The Azure growth acceleration is not off the table** it just requires a bit more patience. As compared to prior quarters management is now guiding, in fact to acceleration. Q4 guidance is 30-40% CC which at the top end, which they normally beat, is at least 1% above Q3's 39% and then H1FY27 will grow faster than H1 and if capacity constraints abate a bit then we could see and/or further improvement in H2FY27.

The company is spending aggressively on CAPEX and more specifically on datacenter hardware to meet demand which of course will give many investors pause, but we would argue that for a stock that was trading at >30x future EPS and now at 23x Microsoft delivers the combination of AI resilience / upside plus strong GAAP EPS growth and software exposure. Will everyone flock back into the stock over the next few days, we doubt it but for those ready to add to software exposure this is a solid / safe place to add that exposure at very good valuation.

KEY THOUGHTS ON THE QUARTER AND THE GUIDE

Microsoft earnings always have a lot to unpack. But in some ways this quarter there were a lot of interesting data points, beyond those touched above and information that is worth noting.

- **More on M365 Copilot**: As mentioned above we believe that most investors were surprised by the strength of Microsoft Office 365 Copilot adoption. With management expecting to add more Copilot seats in Q4FY26 than in Q3 and what we believe is a solid tailwind just starting from both M365 E7 sales plus incremental revenue from consumption packs the setup is far better than virtually anyone we have recently talked amongst our client base. The general expectation has been that Copilot has had very mixed approval by users and with the recent launches by Anthropic and others of AI plug-ins some have even been concerned that M365 Copilot was doomed. The reality is in fact quite different. Microsoft has always been the software world's equivalent of the turtle to the startup's hares - Microsoft is rarely 1st to market but rather they steadily add functionality and deliver a tightly integrated offering at a very competitive (bundled price). With the inclusion of Copilot Coworks (jointly built with Anthropic), Copilot Council (which allows multiple models to run simultaneously on a single prompt) and Copilot Critique (dual model research tool) Microsoft offers, we believe, a very competitive suite at a price corporate will approve.

- Management stated on the call that Copilot usage has now reached the level of Outlook which is a fascinating data point. It means, we understand, that usage is steady and meaningful and while higher usage could impact Microsoft margins (due to inferencing costs) it increases the stickiness of the solution and the likelihood more seats are procured over time.

- **The hybrid SaaS pricing model**: Everyone in software has been trying to deal with how to price AI. Fixed pricing creates downside risks for the vendor if usage is too high, but pure consumption creates revenue variability for the vendor and a lack of visibility to budgeting for the customer. Microsoft is now shifting from a pure subscription model for some of its Copilots to a hybrid that includes a monthly subscription fee with a built-in allotment of credits (exceeding the allotment generates a consumption fee). This should deliver a cost predictability many companies are interested while projecting Microsoft margins and generating additional revenue for Microsoft.

  - The company is shifting GitHub Copilot to this model in June and M365 E7 also utilizes a similar hybrid approach. Management expects that the hybrid pricing model will increase revenue and improve margins, as the complexity of functionality increases especially due to agents.

- **CAPEX** this quarter was relatively in-line with expectations but next quarter and CY26 were above expectations. In part this is driven by higher component costs ($25B of the $190B for CY26). Management was confident they can 1) procure the components and 2) that they can deliver strong ROIC on those CAPEX investments, even considering the higher component costs.

  - A couple of quarters ago Amy Hood explained that over time CAPEX would grow slower than Cloud revenue and while they have not reached that point due to the disconnect between very strong demand and capacity constraints, they expect to reach that but not until at least FY27.

  - ~2/3 of CAPEX is now for short-lived assets which is predominantly servers.

- **The OpenAI partnership:** We recently wrote a note (Updated Microsoft / OpenAI partnership) that discussed the ramifications of the changes in the OpenAI partnership but two changes we believe are worth repeating here:

  1. Microsoft will not be paying OpenAI royalties for access to OpenAI IP and OpenAI models through 2032. This will have a positive impact on Azure gross margins.

  2. OpenAI is now allowed to offer their models on other hyperscalers. This removes the issues arising between the companies arising out the OpenAI/Amazon agreement relating to Frontier (Link) but it likely will not have a meaningful impact on Microsoft revenue. OpenAI earlier this year committed to an additional $250B (over 6+ years) usage of Azure, and we believe that prior to this change a meaningful portion would have been OpenAI using Azure for OpenAI models procured through OpenAI or others. In other words, OpenAI will be shifting around, we believe where they run what workloads, but overall Microsoft will capture the same revenue over time.

     - Microsoft has been moving to become more 3rd party model agnostic, and they discussed this during call. Microsoft is already partnering with Anthropic (e.g. Office 365 Copilot Coworks was jointly devel Anthropic) and we believe that what drives the selection of where enterprises will run inferencing is w resides and most enterprise data resides at Microsoft rather than exclusivity of models. In fact, over time most IT organizations will not know whose models they are running.

- **Headcount**: The company recently announced a voluntary headcount reduction program which is part of the company's drive to lower their OPEX, drive operational efficiency and streamline the business (especially leveraging AI).

- **Leading indicators of growth** were incredibly strong with RPO growing 29% excluding OpenAI and 99% YoY including the OpenAI $250B+ commitment to reach $627B. Roughly 25% will be recognized over the next 12 months, growing 39%. The remainder is recognized > 12 months and grew 138%.

- **Management is taking a long view**. While investors would have been very happy for Microsoft to deliver faster Azure growth the management is taking a long view on allocation of resources. This is very different from many software companies who are hyper tuned, we believe, to managing and driving the stock price. We know that management was cognizant that last quarter a small miss in Azure growth vs buy side expectations negatively impacted the stock and the company could have fixed that this quarter by focusing most of the new capacity on Azure (the demand is there, but the capacity is not). Instead, they are investing in future technology and supporting the adoption of Copilot, which makes complete sense.

  - Note that even then the 37-38% (CC) Azure revenue growth guidance is very solid, in fact incrementally more solid, considering that 3Q25 was a much tougher comp compared to previous quarters.

The results themselves were solid (Exhibit 2) with all the major metrics nicely beating consensus. As mentioned earlier we believe that the only miss was Azure growth which hit the bottom of the buy side whisper range.

EXHIBIT 2: **Results vs. Consensus Estimates**

3Q26	Consensus vs. Actual		Surprise
Revenue	Consensus	81,370	1.9%
	Actual	**82,886**	
Operating Income	Consensus	36,830	4.3%
	Actual	**38,398**	
Operating Margin	Consensus	45.2%	1.1%
	Actual	**46.3%**	
EPS (GAAP)	Consensus	4.05	5.4%
	Actual	**4.27**	
Cash from Operations	Consensus	42,130	10.8%
	Actual	**46,679**	
Gross Margin	Consensus	67.1%	0.5%
	Actual	**67.6%**	

Source: Company reports, StreetAccount, Bernstein analysis

UNDERSTANDING DEMAND AND WHETHER MICROSOFT COULD BE CAUGHT BY AN AI BUBBLE

As discussed earlier in the note the AI threat concerns, whether AI is a bubble or AI will eat software should at least in part decrease after this quarter as:

- M365 Copilot and GitHub Copilot, Microsoft's 2 largest and most important Copilots are both doing extremely well. M365 Copilot adoption, while still relatively small >20M of 450M commercial office users is growing fast and management expects that trend to continue and we agree. GitHub Copilot is often cited as an AI winning solution and the company feels confident enough to change the pricing to a hybrid for GitHub Copilot which shows how strong they feel about the solution.

    - The other enterprise apps (e.g. Dynamics, LinkedIn, etc.) are much earlier in proving out their AI success but in many cases success with M365 Copilot, we believe, will have a positive effect across products such as Dynamics 365.

- Azure strength continues with growth incrementally accelerating this quarter and expected to accelerate in Q4 and H1FY27.

In general, the AI bubble concern has been a large portion of our in-bound discussions, and it has come up specifically relating to Microsoft given its investments in both AI apps (Copilots) and Azure AI. This concern about the durability of revenue continues to be in question, but we believe that:

- Microsoft is diversified across a wide range of AI apps and in fact we believe that Microsoft's AI enterprise app revenue may be as large or larger than the rest of the market at this time.

- The Azure AI business is across a very broad range of customers and even though they have a meaningful portion of revenue from OpenAI and will even more revenue over time, they are building capacity to meet contracted demand and not in a speculative manner.

- Microsoft AI related revenue is far more than renting bare metal GPUs as many other vendors and their customers are using the broad stack of Azure services including OpenAI.

While there is no certainty that a very large / broad AI bubble pop will not affect Microsoft, the downside risk, we believe, is relatively small even considering our increasing certainty that there are parts of the tech stack that are in fact likely to see some bubble breaking effects.

MARGINS TRENDS CONTINUE

Microsoft very successfully traversed the Cloud transition without negatively impacting margins as many expected (in fact margins increased), but AI is a bit different. Microsoft continues to see a headwind to Cloud and company gross margins from AI which is more than offset by operating leverage. We wrote a note diving into Microsoft AI margins and how the company should be able to deal with most, if not all the operating margin pressure via operating leverage (Microsoft: Azure AI margins, and its implications for next 5 years).

Management guided to Cloud gross margins percentage decreasing to 64% in Q4 FY26 while company operating margins increasing ~1% YoY for the full year FY26.

GUIDANCE

Microsoft supplied guidance for Q4 FY26 (see Exhibit 3), beating consensus on most revenue metrics.

Q426

- **FX**: Microsoft expects FX to increase total 4Q26 revenue growth by less than 1pp. By segment, 1pp positive impact to Productivity and Business Processes, no impact to Intelligent Cloud, and 1pp positive impact to More Personal Computing. At the same time, FX is expected to increase COGS growth by 1pp and have no impact on OPEX.

- Management guided total revenue to be between $86.7B and $87.8B, slightly above consensus expectation of $87.56B. The Productivity and Business Processes segment is guided to be between $37.0B-$37.3B, Intelligent Cloud is expected to be between $37.95B-$38.25B, and More Personal Computing between $11.75B-$12.25B. The company expects COGS to be $29.4B-$29.6B and OPEX to be between $19.3B-$19.4B.

- Productivity and Business Processes is expected to grow 11%-12% in CC, with M365 Commercial Cloud growth expected to be 13-14% in CC (or 15-16% in CC when adjusting for prior year in-period revenue recognition).

- Intelligent Cloud is expected to grow 27%-28% in CC, while **Azure is expected to grow 39%-40% in CC.**

  - Even as Microsoft brings more data center capacity online, demand remains significantly ahead of capacity. As Microsoft balances Azure revenue growth with their first-party growing needs (first-party apps, internal R&D), they expect to remain capacity constrained.

  - Please note that Azure could experience more FX volatility due to more international exposure and consumption based charge.

- More Personal Computing is expected to be decline -14% to -10% in CC.

- Commercial Cloud gross margin is expected to be roughly 64%, down year-over-year driven by continued investments in AI and increased GitHub Copilot usage. Commercial Bookings expects healthy growth in the core business when adjusting for OpenAI contracts. Note that long-term Azure contracts, which are more unpredictable in timing, can drive quarterly volatility in bookings growth rate.

- Management expect Q4 total CAPEX to increase to over $40B as the company continue to bring more capacity online.

- Other income and expense outlook, excluding impact from OpenAI investments, will be roughly $(100) M.

- Q4 effective tax rate is expected to be around 19%, excluding impact from OpenAI investments.

CY26

- Management expects CY26 capital expenditure to be approximately $190B, including roughly $25B from higher component pricing

- Azure revenue growth is expected to show some modest acceleration in 2H CY26 (1H FY27), as compared to 1H CY26.

FY27

- Total revenue is expected to grow double-digits

- Operating expenses expected to grow in mid- to high-single digits

- Operating income is expected to grow double-digits

EXHIBIT 3: **MSFT 4Q26 Guidance vs. Consensus**

4Q26	Guidance Low	Guidance High	Consensus	Guidance vs. Consensus High end
Total Revenue	**86,700**	**87,800**	**87,560**	*0.3%*
Productivity & Business Processes	37,000	37,300	36,650	*1.8%*
Intelligent Cloud	37,950	38,250	37,610	*1.7%*
Azure CC growth%	39%	40%	37%	*3.0%*
More Personal Computing	11,750	12,250	13,340	*(8.2%)*
COGS	29,400	29,600	28,720	*3.1%*
Gross Profit	**57,300**	**58,200**	**58,840**	*(1.1%)*
Gross Margin	*66.1%*	*66.3%*	*67.2%*	*(1.4%)*
Opex	19,300	19,400	19,750	*(1.8%)*
Operating Profit	**38,000**	**38,800**	**39,090**	*(0.7%)*
Operating Margin	*43.8%*	*44.2%*	*44.6%*	*(0.5%)*
Other Income and Expense	-100	-100	--	--
EBT	**37,900**	**38,700**	**--**	**--**
Projected Tax Rate	19.0%	19.0%	--	--
Projected Share Count (Bernstein Est.)	7,460	7,460	--	--
Implied EPS (Non-GAAP)	**4.12**	**4.20**	**4.27**	*(1.6%)*

Source: Company reports, StreetAccount, Bernstein estimates and analysis

TURNING TO THE QUARTER

Results vs. Consensus Expectations (see Exhibit 4):

- Revenue of $82.9B came in 1.9% above consensus estimates.
- Operating income of $38.4B was 4.3% above street estimates
    - Operating margin of 46.3% was 1.1pp ahead of consensus expectations.
- Gross margin was 67.6%, 0.5pp above consensus.
- Diluted GAAP EPS was $4.27, above consensus estimate of $4.05
- Commercial Bookings decreased 4% (6% CC), due to large commitments from OpenAI from the prior year. Excluding the impact from OpenAI, Commercial bookings grew 7%, driven by consistent execution in core annuity sales motions.
- Cash flow from operations was $46.7B, 10.8% above consensus.
- CAPEX including finance leases was $31.9B, up 49% Y/Y. Cash paid for PP&E was $30.9B. Roughly two-thirds of CAPEX was spent on short-lived assets including GPUs and CPUs. (Exhibit 5)
    - Finance leases, primarily for large datacenter sites, was $4.7B. Note the difference between this and total CAPEX minus cash CAPEX is due to the timing of delivery and payment.
- Free cash flow was $15.8B, down 22% Y/Y, reflecting higher CAPEX to support cloud and AI offerings.
- Microsoft returned $10.2B to shareholders this quarter, including $6.8B in dividends and $3.4B in share repurchases.
- Effective tax rate was 19%.

- Microsoft's Commercial Cloud (including LinkedIn) gross margins came in at 66%, down 3 points Y/Y driven by the company's scaling of their AI infrastructure and growing usage of AI product features, partially offset by efficiency gains primarily in Azure and Microsoft 365 Commercial cloud.

EXHIBIT 4: **Results vs. Consensus Estimates**

3Q26	Consensus vs. Actual		Surprise
Revenue	Consensus	81,370	1.9%
	Actual	**82,886**	
Operating Income	Consensus	36,830	4.3%
	Actual	**38,398**	
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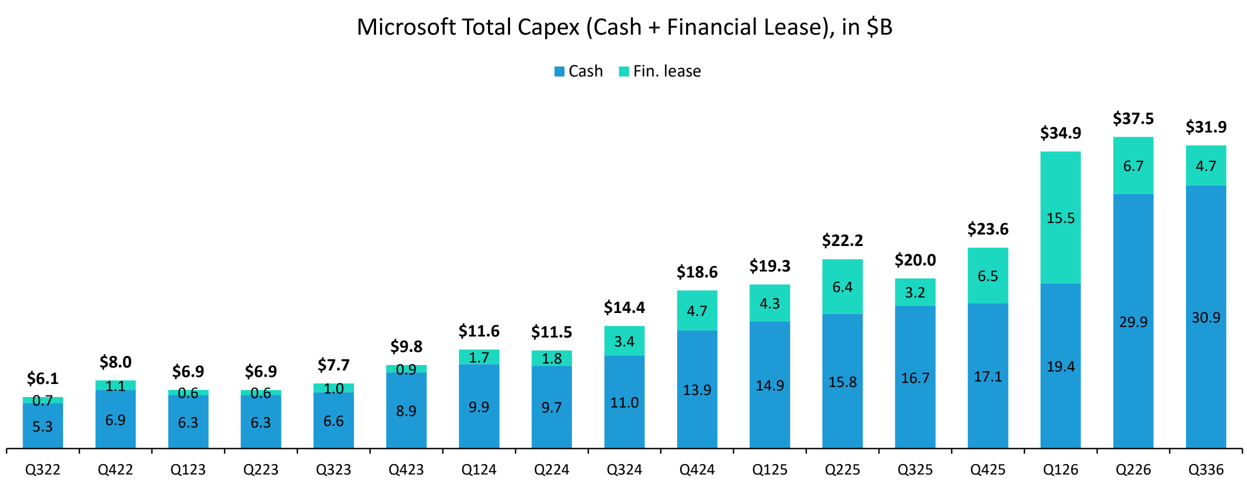
	Actual	**46,679**	
Gross Margin	Consensus	67.1%	0.5%
	Actual	**67.6%**	

Source: Company reports, StreetAccount, Bernstein analysis

EXHIBIT 5: **CAPEX has gone up as Microsoft continues to invest in AI to meet demand**



Note total might differ from sum of the components due to timing of receipt of goods and payment in finance leases.
Source: Company reports, Bernstein analysis

We look at the individual segments in constant currency (see Exhibit 6)

- **Intelligent Cloud** grew 28% CC, above the guidance range of 25%-27% in CC, driven by Azure. This quarter, Azure (now mostly IaaS/PaaS) grew 39% in CC, ahead of the guidance of 37-38% CC, driven by strong demand for Azure's portfolio of services with continued growth across all workloads.
  - Note that the Intelligent Cloud segment no longer includes Azure SaaS components. This segment, although smaller, now focuses on IaaS/PaaS and platform centric software (server & tools) and captures the company's consumption based cloud services (also a bit of revenue from Search).

- **Productivity & Business Process** grew 13% CC, within the guidance range of 12%-14% in CC driven by M365 Commercial cloud. M365 Commercial Cloud revenue grew 15% CC, ahead of guidance range of 13-14% CC, with growth in ARPU driven by E5 and M365 Copilot, which now exceeds 20M paid seats. Seat growth was 6% driven by SMB and frontline worker offerings, which is not surprising given the fact that most enterprises have enough seats for employees and hiring is weak.

- **More Personal Computing** declined 3% CC, which was ahead of guidance range of $ -10% to -6% in CC, due to lower hardware slaves across Device and Gaming, partially offset by Search advertising. Windows OEM and Devices declined 3% driven by Devices, partially offset by growth in Windows OEM. Xbox content and services declined 7% CC and hardware revenue declined 34% CC. Search ex TAC grew 9% in CC, driven by higher search volume and continued benefit from third-party partnerships.

EXHIBIT 6: **Results vs. Consensus Estimates at the Segment Level**

3Q26	Consensus vs. Actual		Surprise
Productivity and Business Processes	Consensus	34,430	1.7%
	Actual	35,013	
Intelligent Cloud	Consensus	34,270	1.2%
	Actual	34,681	
More Personal Computing	Consensus	12,730	3.6%
	Actual	13,192	
Total revenue	Consensus	81,370	1.9%
	Actual	82,886	

Source: Company reports, StreetAccount, Bernstein analysis

WHAT ABOUT AZURE?

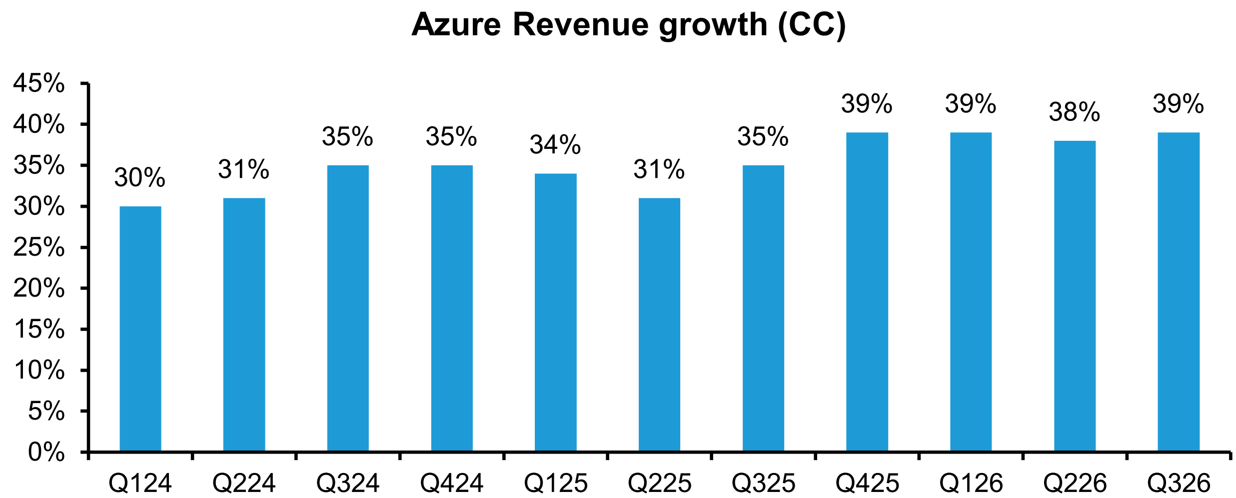
Azure growth this quarter came in at 40% reported and 39% in CC, beating guidance of 37-38% CC, slightly ahead of street consensus and we believe, in line with buyside expectations. Although Microsoft no longer breaks out Azure AI metrics, this quarter they disclosed that total AI ARR (current quarter revenue x 4) surpassed 37B, which includes Azure AI revenue and first-party AI applications. Note that this ARR does not include the CPUs, storage and other services that were required to run AI workloads, outside of frontier model companies.

This quarter, Azure growth is driven by strong demand for the portfolio of services across all workloads. Again, demand continues to exceeded available supply.

On Azure AI, as workloads move from testing of AI to production, one should continue to see both GPU and CPU usage as well as storage and bandwidth usage increase.

As mentioned earlier Azure strength seems to be broad and has been helped by an acceleration in Cloud migrations plus to some extent from digitally native vendors, which historically used Microsoft's hyperscaler peers, are now using Azure which we see as another driver of sustained growth for Azure.

EXHIBIT 7: **Microsoft Azure constant currency growth**



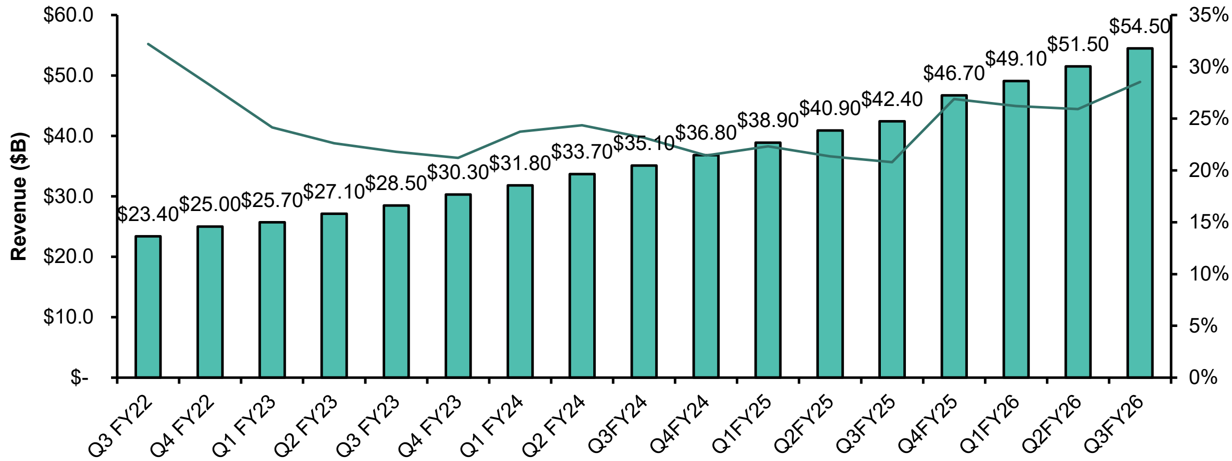
Source: Company disclosures, Bernstein analysis

MICROSOFT COMMERCIAL CLOUD

Commercial Cloud revenue increased to $54.5B and grew 25% Y/Y in CC (see Exhibit 8) showing the strength of Microsoft's transformation to a Cloud-centric company. Commercial Cloud will become a larger and larger portion of the business going forward. While the Cloud story is far from over for Microsoft, especially with Azure, AI has become the next leg of growth for Commercial Cloud and overall Microsoft.

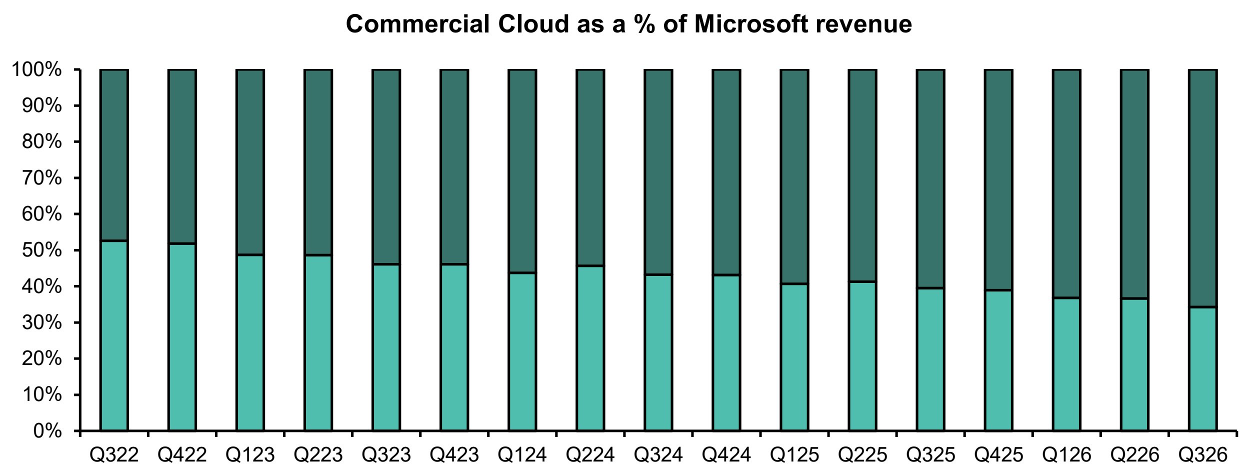
- M365 Commercial Cloud revenue grew 15% CC.
    - Commercial Office 365 seats grew 6% (see Exhibit 16). ARPU growth was primarily driven by upgrade to Office 365 E5 and Copilot for Microsoft 365.
    - The fact that the company is offsetting slowing (due to the law of large numbers / significant market penetration) seat growth by growing ARPU is impressive, especially when the new seats added are from lower ARPU offerings (SMBs and frontline workers). We believe ARPU growth can continue with E5 upgrades and Copilot for Microsoft 365 adoption, and soon E7 upgrades.
- Dynamics 365 continues its strong growth at 17% CC with growth across all workloads.
- Given the faster growth rate of Commercial Cloud, as it becomes a larger portion of Microsoft revenue, we believe we should see the growth rate of the company sustain or even accelerate.
- Azure delivered 39% CC growth, driven by growth across all workloads

EXHIBIT 8: **Microsoft's Commercial Cloud revenue continues to grow**



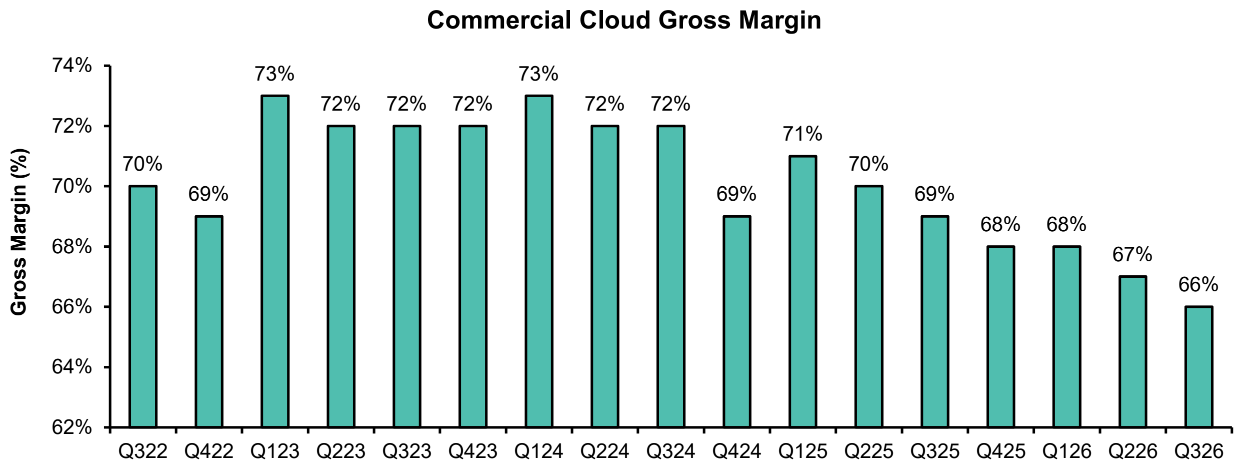
Source: Company reports, Bernstein analysis

EXHIBIT 9: **Commercial Cloud is now well over half of total revenue**



Source: Company reports, Bernstein analysis

EXHIBIT 10: **Microsoft's Commercial Cloud Gross Margin, including LinkedIn Commercial have come down due to the investment in AI**



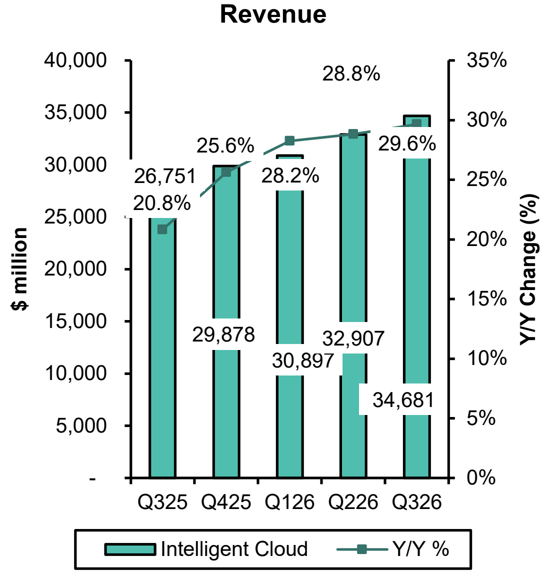
Source: Company reports, Bernstein analysis

INTELLIGENT CLOUD

Intelligent Cloud revenue grew 30% (28% in CC) (see Exhibit 11), with Azure growing 40% (39% in CC). Gross profit grew 19% (18% in CC) Y/Y while the gross margin percentage decreased driven by continued investments in AI infrastructure, partially offset by efficiency gains in Azure. Intelligent Cloud operating expenses grew 9% (7% in CC), driven by continued investments in R&D compute capacity, AI talent, and data to support product development that benefits the entire portfolio. Intelligent Cloud operating income was up 24% Y/Y (23% in CC) (see Exhibit 12).

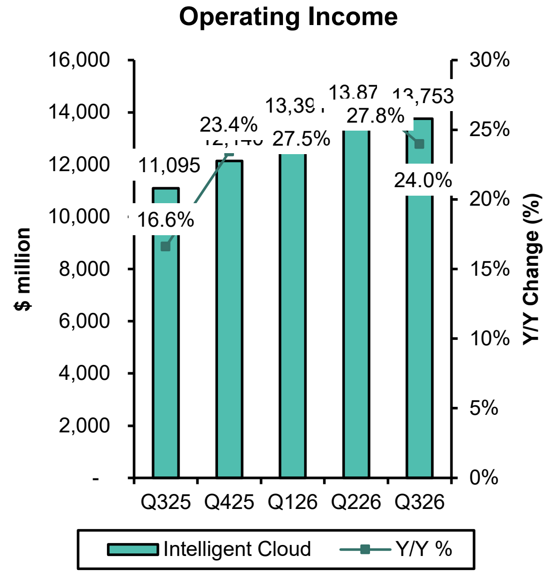
Server products revenue increased slightly (down 3% in CC) driven by higher purchases of licenses running in multi-cloud environments, offset by renewals with lower in-period revenue recognition from the mix of contracts and continued customer shift to cloud. Enterprise and partner services revenue grew 7% (4% in CC) with growth in Enterprise Support Services.

EXHIBIT 11: **Intelligent Cloud revenue was up 30% YoY ...**



Source: Company reports, Bernstein analysis

EXHIBIT 12: **... while Intelligent Cloud operating income was up 24%**



Source: Company reports, Bernstein analysis

PRODUCTIVITY AND BUSINESS PROCESSES

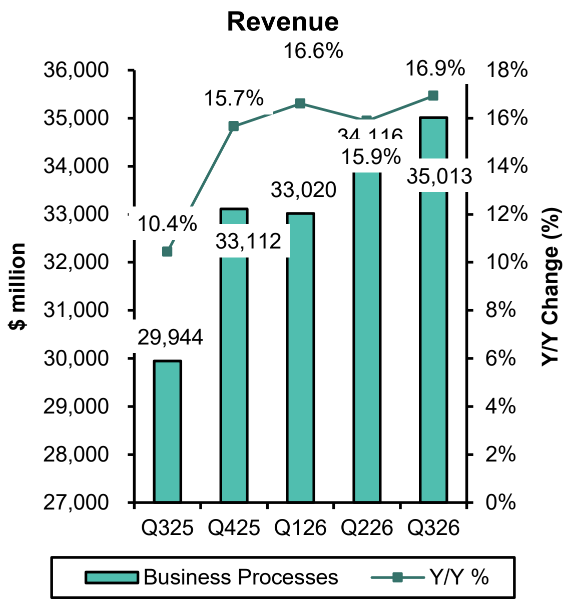
Revenue for the Productivity and Business Process segment (see Exhibit 13) was up 17% (13% in CC), driven by M365 Commercial Cloud.

Gross margin dollars were up 18% (13% in CC) and gross margin increased slightly driven by efficiency gains in Microsoft 365 Commercial cloud, even with continued investments in AI infrastructure and growing AI product usage. Operating expenses grew 11% (9% CC), driven by continued investments in R&D compute capacity, AI talent, and data to support product development that benefits the entire portfolio, as well as higher Copilot advertising spend. Operating income (see Exhibit 14) grew 21% (14% in CC).

Highlights for the quarter:

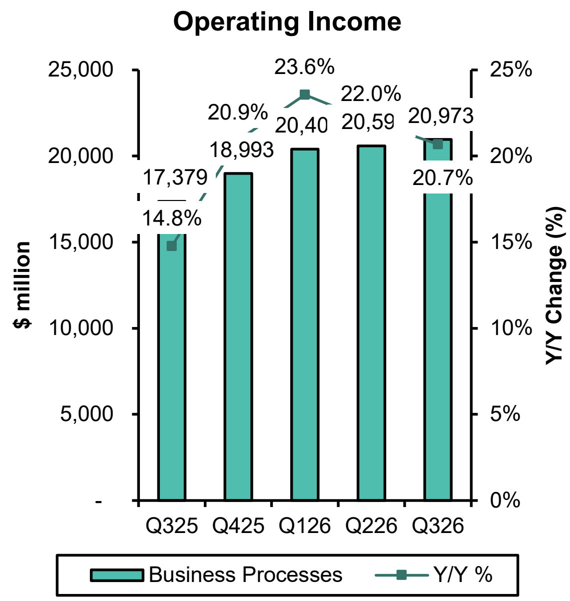
- M365 Commercial Cloud revenue grew 19% (15% CC), driven by growth in ARPU from E5 and M365 Copilot, which now exceeds 20M paid seats, as well as 6% seat growth from SMB and frontline worker offerings. M365 Commercial products' revenue grew 1% (down 3% CC) with continued customer shift to cloud offerings.
    - Note M365 includes Office 365 as well as revenues from Windows, EMS and Power BI.
    - M365 Commercial Cloud represents nearly 90% of the total M365 Commercial products and cloud services.
- M365 Consumer cloud revenue grew 33% (up 29% CC) which was driven by ARPU and M365 Consumer subscribers growth of 7%. Note that Copilot Pro (consumer version of Office Copilot) is no longer reported here and moved to More Personal Computing.
    - M365 Consumer Cloud represents 85% of total M365 Consumer products and cloud services
- Dynamics 365 revenue grew 22% Y/Y (17% in CC).
    - Dynamics 365 represents nearly 90% of total Dynamics revenue
- LinkedIn's revenue grew 12% (9% in CC) driven by growth across all lines of business.

EXHIBIT 13: **PBP revenue grew 17% while ...**



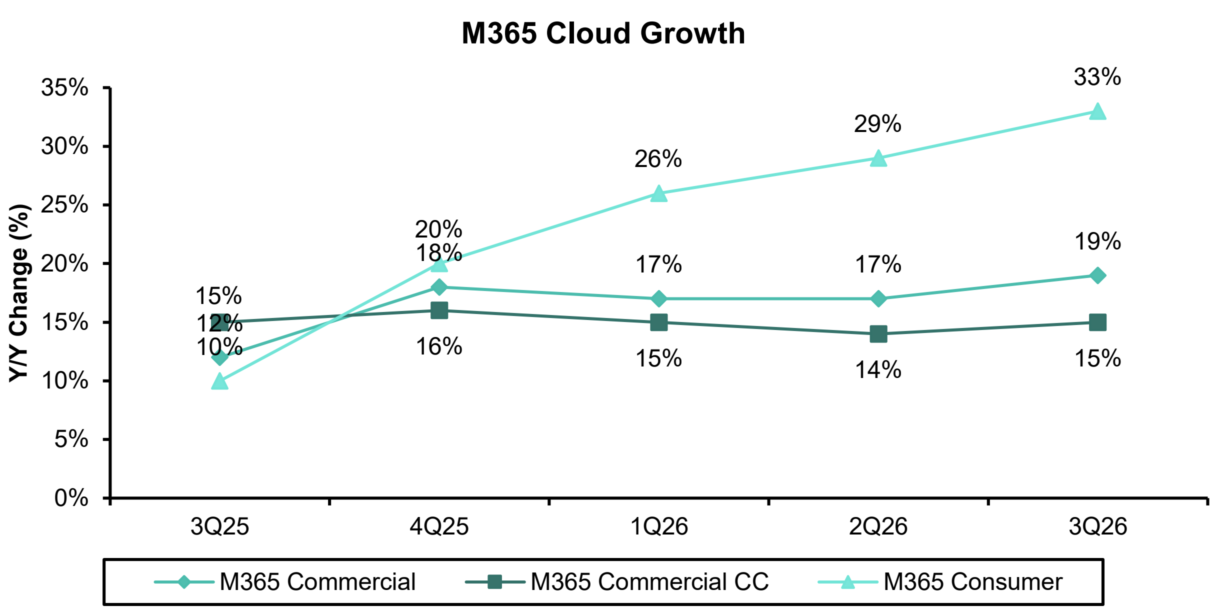
Source: Company reports, Bernstein analysis

EXHIBIT 14: **... PBP Operating Income grew 21%**



Source: Company reports, Bernstein analysis

EXHIBIT 15: **M365 growth was strong**



Source: Company reports, Bernstein analysis

EXHIBIT 16: **M365 Commercial seats grew 6% while M365 Commercial revenue grew 15%CC driven by upsell to E5 and M365 Copilot.**

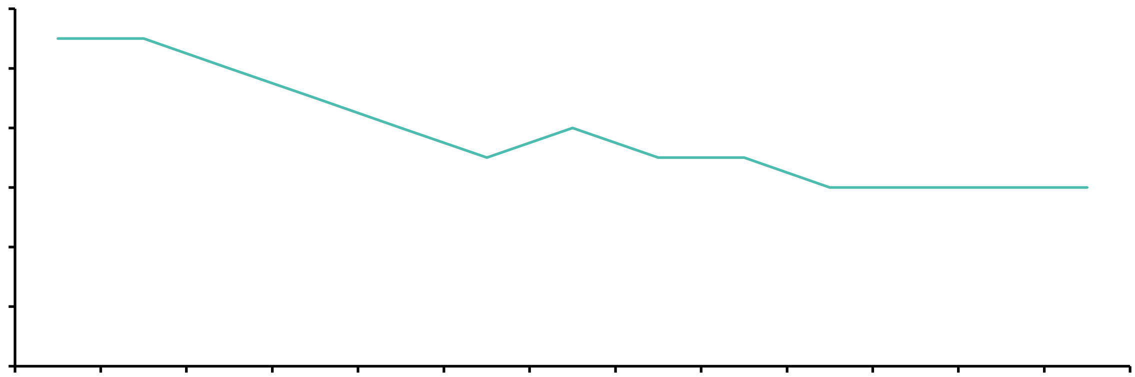
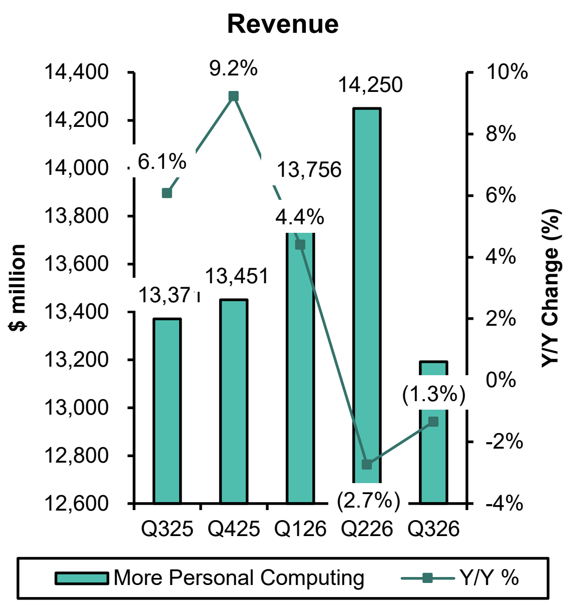
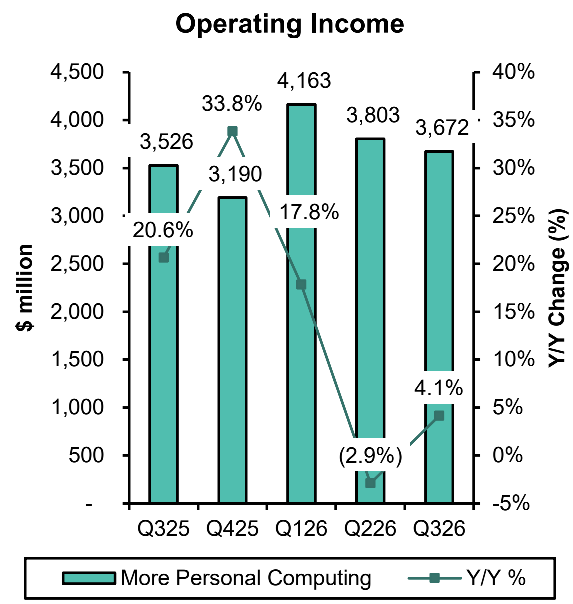


EXHIBIT 17: **MPC revenue declined 1% YoY while ...**



Source: Company reports, Bernstein analysis

EXHIBIT 18: **MPC Operating Income increase 4% YoY**



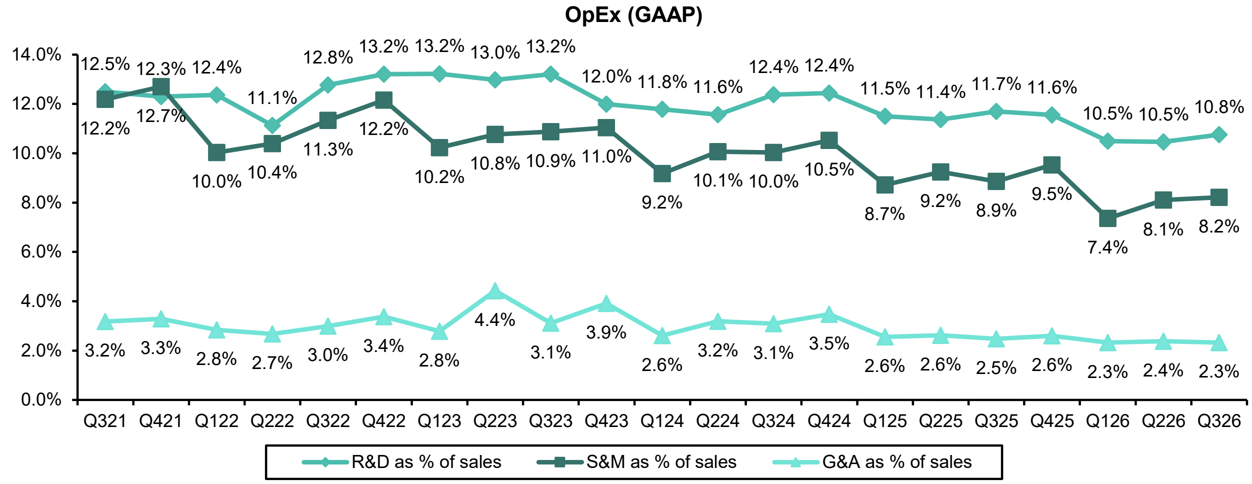
Source: Company reports, Bernstein analysis

MARGINS

Gross margin was 68%, slightly down Y/Y. While Gross margin is trending slightly lower, it is mostly driven by Cloud and AI infrastructure investment, which manifests through higher D&A expense, and growing usage of AI product features but is partially offset by efficiency gains across Microsoft Cloud and sales mix shift to higher margin businesses. The company is also managing to offset through managing OPEX. It is very important to remember that Microsoft is only GAAP (and still GAAP for all lines above operating profit) as compared to all of its software peers who are PF which removes what is often significant costs such as stock-based comp. There are a couple significant factors impacting margins:

- **Microsoft's Commercial Cloud margins were 66%**, a 3pp decrease YoY, driven by investment in Cloud and AI infrastructure and growing AI product usage, partially offset by efficiency gains in Azure and M365 Commercial Cloud.
  - The company is aggressively investing in Cloud and especially AI as seen in the increase of CAPEX. As CAPEX is amortized, it is going to place pressure on Commercial Cloud gross margins. In addition, Generative AI is scaling and could continue to have an impact on margins for a period of time while AI margins improve.
  - We want to note that although Gross Margin is impacted by these infrastructure investments, Azure efficiency, including AI, is improving so the like-for-like gross margin are better.
  - Microsoft will, we believe, continue to offset the GM pressure from AI via managing OPEX.
  - We believe that the longer-term gross margin will improve as Microsoft moves through the investment cycle and keeps improving Cloud and AI efficiency, similar to the Cloud transition period we observed a decade ago. For more detailed information on AI margins and their impact on Microsoft's margins we would recommend one reads: Microsoft: Azure AI margins, and its implications for next 5 years and Microsoft: Could the bear case in fact be the bull case?
  - Microsoft's cloud offerings are all built on the same infrastructure. This is especially true with AI as Microsoft leverages the same reference architecture (the Copilot architecture), and the same infrastructure, and this drives scale and efficiency across all their AI.

EXHIBIT 19: **Microsoft GAAP OpEx as % of Revenue**

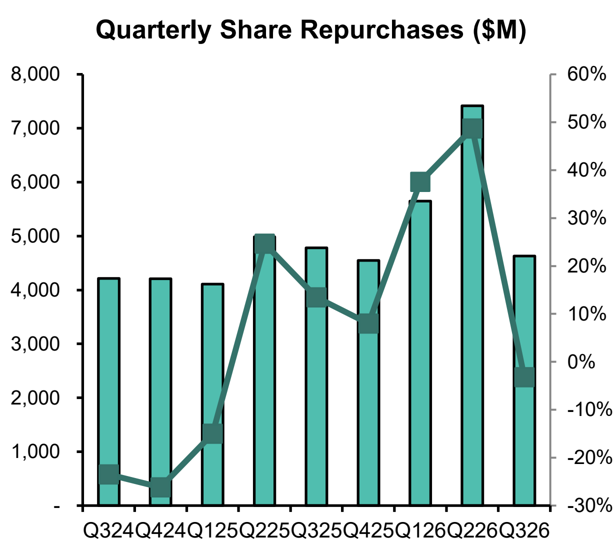


Source: Company reports, Bernstein analysis

CAPITAL RETURN

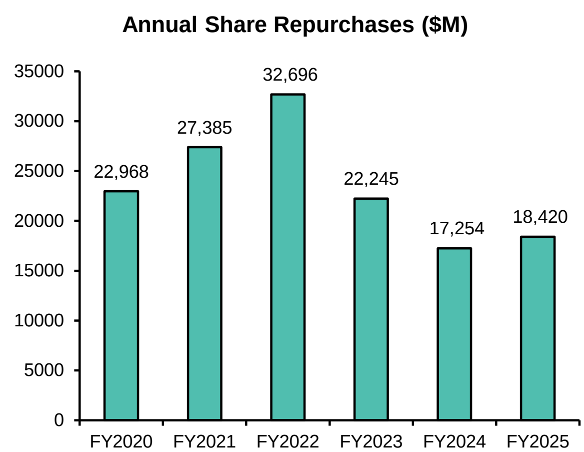
Total capital returned to shareholders was $10.2B. This included $6.8B in dividends and $3.4B in share repurchases.

EXHIBIT 20: **Microsoft cash share purchases**



Source: Company reports, Bernstein analysis

EXHIBIT 21: **...we expect buybacks to continue**



Does not reflect new share issuance.
Source: Company reports, Bernstein analysis

EXHIBIT 22: **Microsoft reporting changes in 1QFY25, highlighting the new reporting metrics and what has moved.**

FY2024 Segments			
PBP			
	Office Products and Cloud Services		
		Office Commercial	
			Commmercial Cloud services
			Commercial Products
		Office Consumer	
			Consumer Cloud services
			(-) Copilot Pro
			Consumer Products
	Dynamics		
		Dynamics 365	
		Dynamics Products	
	LinkedIn		
	Others		
IC			
	Server Products & Cloud Services		
		Azure and Other Cloud services	
			(-) Enterprise Mobility + Security (EMS)
			(-) Power BI per-user revenue
			(-) Nuance Enterprise Cloud
			Nuance Healthcare Cloud
			GitHub
		Server Products	
			(-) Nuance Enterprise Prod
			Nuance Healthcare Prod
	Enterprise and Partner Services		
MPC			
	Windows		
		OEM	
			(-) Comm. Products and Cloud services
		Windows Others	
	Devices		
	Search and News Advertising (gross-TAC)		
			(-) some Search component
	Gaming		

FY2025 Segments			
PBP			
	M365 Commercial Products and Cloud Services		
		M365 Commmercial Cloud *	
			Old Office Commercial. Cloud services
			(+) Enterprise Mobility + Security (EMS)
			(+) Power BI per-user revenue
			(+) Win. Comm. Cloud services
		M365 Commercial Products	
			Old Office Commercial
			(+) Win. Commercial Prods
	M365 Consumer Products and Cloud Services		
		Consumer Cloud services *	
			Remaining Consumer Cloud services
		Consumer Products	
	Dynamics		
		Dynamics 365 *	
			Old Dynamics 365
			(+) Nuance Enterprise Cloud
		Dynamics Products	
			Old Dynamics Prod
			(+) Nuance Enterprise Prod
	LinkedIn		
	Others		
IC			
	Server Products & Cloud Services		
		Azure and Other Cloud services *	
			Remaining Azure (PaaS/IaaS)
			(+) some Search Component
			Nuance Healthcare Cloud
			GitHub
		Server Products	
			Nuance Healthcare Prod
			Other remaining Server Products
	Enterprise and Partner Services		
MPC			
	Windows and Devices		
		OEM & Devices	
		Windows Others	
	Search and News Advertising (gross-TAC)		
		Remaining Search and News Advertising (gross)	
			(+) Copilot Pro
	Gaming		

* New Reporting metrics

Source: Company reports, Bernstein analysis

APPENDIX - FINANCIAL FORECASTS

EXHIBIT 23: **MSFT Income Statement**

$ Millions & Pro Forma, except otherwise noted

Income Statement (PF)	FY2023	FY2024	FY2025	FY2026E	FY2027E	FY2028E	Q126	Q226	Q326	Q426E
Revenue	211,915	245,122	281,724	330,125	391,739	463,939	77,673	81,273	82,886	88,293
Cost of revenue	65,863	74,114	87,831	105,992	136,321	166,015	24,043	25,978	26,828	29,143
Gross Profit	146,052	171,008	193,893	224,133	255,418	297,923	53,630	55,295	56,058	59,150
Research and development	27,195	29,510	32,488	35,189	39,059	43,356	8,146	8,504	8,915	9,624
Sales and marketing	22,759	24,456	25,654	26,764	29,976	33,573	5,717	6,584	6,814	7,649
General and administrative	6,404	7,609	7,223	7,818	8,756	9,807	1,806	1,932	1,931	2,149
Goodwill impairment / Employee severance	-	-	-	-	-	-				
Total opex & COGS	122,221	135,689	153,196	175,763	214,112	252,751	39,712	42,998	44,488	48,565
Operating income	**89,694**	**109,433**	**128,528**	**154,362**	**177,626**	**211,187**	37,961	38,275	38,398	39,728
Other income	788	(1,646)	(4,901)	1,233	(1,200)	(1,200)	401	(29)	961	(100)
EBT	90,482	107,787	123,627	155,595	176,426	209,987	38,362	38,246	39,359	39,628
Taxes	17,175	19,651	21,795	29,996	33,521	39,898	7,529	7,371	7,567	7,529
Net income (PF)	**73,307**	**88,136**	**101,832**	**125,599**	**142,905**	**170,090**	30,833	30,875	31,792	32,099
Basic EPS ($)	9.85	11.86	13.70	16.91	19.22	22.85	4.15	4.15	4.28	4.32
Diluted EPS ($, PF)	**9.81**	**11.80**	**13.64**	**16.85**	**19.16**	**22.77**	**4.13**	**4.14**	**4.27**	**4.31**
Basic share count (M)	7,445	7,431	7,433	7,429	7,434	7,443	7,433	7,431	7,426	7,425
Diluted share count (M)	7,472	7,468	7,465	7,456	7,460	7,469	7,466	7,460	7,445	7,453
Key ratios (PF)										
Gross margin	68.9%	69.8%	68.8%	67.9%	65.2%	64.2%	69.0%	68.0%	67.6%	67.0%
R&D as % of sales	12.8%	12.0%	11.5%	10.7%	10.0%	9.3%	10.5%	10.5%	10.8%	10.9%
S&M as % of sales	10.7%	10.0%	9.1%	8.1%	7.7%	7.2%	7.4%	8.1%	8.2%	8.7%
G&A as % of sales	3.0%	3.1%	2.6%	2.4%	2.2%	2.1%	2.3%	2.4%	2.3%	2.4%
Operating margin	42.3%	44.6%	45.6%	46.8%	45.3%	45.5%	48.9%	47.1%	46.3%	45.0%
Tax rate	19.0%	18.2%	17.6%	19.3%	19.0%	19.0%	19.6%	19.3%	19.2%	19.0%
Net margin	34.6%	36.0%	36.1%	38.0%	36.5%	36.7%	39.7%	38.0%	38.4%	36.4%
YoY change										
Revenue	7%	16%	15%	17%	19%	18%	18.4%	16.7%	18.3%	15.5%
Cost of revenue	5%	13%	19%	21%	29%	22%	19.6%	19.2%	22.4%	21.4%
Gross Profit	8%	17%	13%	16%	14%	17%	17.9%	15.6%	16.4%	12.8%
R&D	11%	9%	10%	8%	11%	11%	8.0%	7.4%	8.7%	9.0%
S&M	4%	7%	5%	4%	12%	12%	0.0%	2.2%	9.7%	5.0%
G&A	9%	19%	-5%	8%	12%	12%	7.9%	6.0%	11.2%	8.0%
Operating income	8%	22%	17%	20%	15%	19%	24.3%	20.9%	20.0%	15.7%
Net income	6%	20%	16%	23%	14%	19%	25.0%	28.1%	23.1%	17.9%
EPS - diluted	7%	20%	16%	23%	14%	19%	25.1%	28.2%	23.4%	18.0%

Source: Company reports, Bernstein estimates and analysisi

EXHIBIT 24: **MSFT Balance Sheet**

$ Millions & GAAP, except otherwise noted

Balance Sheet	FY2023	FY2024	FY2025	FY2026E	FY2027E	FY2028E	Q126	Q226	Q326	Q426E
Assets										
Cash & short-term investments	111,262	75,543	94,565	115,421	115,797	217,975	102,012	89,462	78,272	115,421
Accounts receivable	48,688	56,924	69,905	82,684	98,381	116,024	52,894	56,535	60,041	82,684
Inventories	2,500	1,246	938	818	615	267	1,130	1,059	1,219	818
Other	21,807	26,021	25,723	35,317	47,275	55,752	33,030	33,134	35,797	35,317
Total current assets	**184,257**	**159,734**	**191,131**	**234,241**	**262,068**	**390,018**	**189,066**	**180,190**	**175,329**	**234,241**
Property and equipment	95,641	135,591	204,966	310,780	447,488	514,202	230,861	261,126	283,228	310,780
Goodwill	67,886	119,220	119,509	119,661	119,661	119,661	119,497	119,622	119,661	119,661
Intangible assets, net	9,366	27,597	22,604	18,407	14,992	12,211	21,236	20,289	19,325	18,407
Other	54,826	70,021	80,793	62,544	70,981	75,055	75,691	84,075	96,685	62,544
Total non-current assets	**227,719**	**352,429**	**427,872**	**511,392**	**653,123**	**721,130**	**447,285**	**485,112**	**518,899**	**511,392**
Total Assets	**411,976**	**512,163**	**619,003**	**745,633**	**915,191**	**1,111,147**	**636,351**	**665,302**	**694,228**	**745,633**
Liabilities										
Accounts payable	18,095	21,996	27,724	40,031	43,541	52,877	32,580	37,328	37,513	40,031
Short-term debt & lending payables	5,247	8,942	2,999	8,839	8,839	8,839	7,832	4,837	8,839	8,839
Accrued compensation	11,009	12,564	13,709	12,624	14,077	15,696	9,201	10,103	11,270	12,624
Income taxes	4,152	5,017	7,211	3,848	3,210	2,789	3,655	2,050	3,563	3,848
Short-term unearned revenue	50,901	57,582	64,555	63,598	67,055	69,936	58,987	51,376	50,924	63,598
Other	14,745	19,185	25,020	25,368	24,931	25,685	22,741	24,311	24,552	25,368
Total current liabilities	**104,149**	**125,286**	**141,218**	**154,309**	**161,653**	**175,822**	**134,996**	**130,005**	**136,661**	**154,309**
Long-term debt	41,990	42,688	40,152	31,423	31,423	31,423	35,376	35,425	31,423	31,423
Long-term unearned revenue	2,912	2,602	2,710	9,503	10,020	10,450	2,546	2,668	2,753	9,503
Deferred income taxes	25,993	30,549	28,821	28,360	27,361	24,322	29,421	30,132	30,840	28,360
Other long-term liabilities	17,981	27,064	45,186	65,896	108,970	156,458	53,588	58,852	61,481	65,896
Total long term liabilities	**88,876**	**102,903**	**116,869**	**135,182**	**177,774**	**222,653**	**120,931**	**127,077**	**126,497**	**135,182**
Total Liabilities	**205,753**	**243,686**	**275,524**	**306,194**	**356,129**	**415,178**	**273,275**	**274,427**	**279,861**	**306,194**
Total stockholders' equity	**206,223**	**268,477**	**343,479**	**439,439**	**559,061**	**695,969**	**363,076**	**390,875**	**414,367**	**439,439**
Total liabilities and stockholders' equity	**411,976**	**512,163**	**619,003**	**745,633**	**915,191**	**1,111,147**	**636,351**	**665,302**	**694,228**	**745,633**

Source: Company reports, Bernstein estimates and analysis

EXHIBIT 25: **MSFT Cash Flow Statement**

$ Millions & GAAP, except otherwise noted

Cash Flow Statement	FY2023	FY2024	FY2025	FY2026E	FY2027E	FY2028E	Q126	Q226	Q326	Q426E
Net income	72,361	88,136	101,832	130,082	142,905	170,090	27,747	38,458	31,778	32,099
Adjustments to reconcile net income to net cash from operations:										
Depreciation, amortization, and other noncash items	13,861	22,287	34,153	47,506	80,378	110,795	13,061	9,198	10,167	15,080
Stock-based compensation	9,611	10,734	11,974	12,797	14,150	15,753	2,983	3,219	3,081	3,514
Deferred income taxes	(6,059)	(4,738)	(7,056)	7,344	(1,637)	(3,460)	2,491	4,446	2,602	(2,195)
Deferral of unearned revenue, net	5,535	5,348	5,438	6,358	3,973	3,311	(5,418)	(7,483)	(166)	19,425
Changes in operating assets and liabilities:	(7,923)	(3,524)	(10,788)	(19,074)	(31,307)	(23,482)	5,200	(2,149)	497	(22,622)
Other	196	305	609	(12,218)	-	-	(1,007)	(9,931)	(1,280)	-
Net cash provided by operating activities	**87,582**	**118,548**	**136,162**	**172,794**	**208,463**	**273,007**	**45,057**	**35,758**	**46,679**	**45,300**
Capex	(28,107)	(44,477)	(64,551)	(117,445)	(170,598)	(127,239)	(19,394)	(29,876)	(30,876)	(37,299)
Acquisitions, net of cash	(1,670)	(69,132)	(5,978)	(1,291)	-	-	(578)	(455)	(258)	-
Purchase of securities, net (sale)	44,748	34,371	27,705	35,051	(400)	(71,734)	3,084	17,471	15,735	(1,239)
Securities lending payable	-	-	-	-	-	-	-	-	-	-
Net cash used in investing activities	**(22,680)**	**(96,970)**	**(72,599)**	**(123,207)**	**(170,998)**	**(198,973)**	**(34,559)**	**(22,705)**	**(27,405)**	**(38,538)**
Net borrowing	(2,750)	575	(8,962)	(3,000)	-		-	(3,000)	-	-
Share repurchase	(22,245)	(17,254)	(18,420)	(21,985)	(10,287)	(18,842)	(5,650)	(7,415)	(4,627)	(4,293)
Dividends	(19,800)	(21,771)	(24,082)	(26,444)	(29,089)	(32,037)	(6,169)	(6,762)	(6,756)	(6,757)
Other	860	693	(235)	121	1,943	1,945	20	(440)	32	509
Net cash used in financing	**(43,935)**	**(37,757)**	**(51,699)**	**(51,308)**	**(37,433)**	**(48,934)**	**(11,799)**	**(17,617)**	**(11,351)**	**(10,541)**
Effect of exchange rates on cash and cash equivalents	(194)	(210)	63	(195)	-	-	(92)	11	(114)	-
Net change in cash and cash equivalents	**20,773**	**(16,389)**	**11,927**	**(1,916)**	**32**	**25,099**	**(1,393)**	**(4,553)**	**7,809**	**(3,779)**
Cash and cash equivalents at beginning of period	13,931	34,704	18,315	30,242	28,326	28,358	30,242	28,849	24,296	32,105
Cash and cash equivalents at end of period	34,704	18,315	30,242	28,326	28,358	53,457	28,849	24,296	32,105	28,326

Source: Company reports, Bernstein estimates and analysis

BERNSTEIN TICKER TABLE

			29 Apr 2026		TTM	Adjusted EPS				Adjusted P/E (x)		
			Closing	Price	Rel.							
Ticker	Rating	Cur	Price	Target	Perf.	Cur	2025A	2026E	2027E	2025A	2026E	2027E
MSFT (Microsoft)	O	USD	424.46	**646.00**	(20.6)%	USD	13.64	**16.85**	**19.16**	31.1	25.2	22.2
OLD				641.00				16.84	19.39			
SPX			7,135.95									

PRICE TARGET CHANGE / ESTIMATE CHANGE IN BOLD

O - Outperform, M - Market-Perform, U - Underperform, NR - Not Rated, CS - Coverage Suspended

Source: Bloomberg, Bernstein estimates and analysis.

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VALUATION METHODOLOGY

Microsoft Corp

We value Microsoft shares based on our estimate for 12-month forward NOPLAT per share in 1 year's time ($22.02), and apply a P/FE multiple of 29x. We then add back in the net cash per share, discounted at 15% to account for potential tax costs and other "friction" to repatriate all cash ($7.6 per share), arriving at price target of $646.

RISKS

Microsoft Corp

Risks to our price target for MSFT include: a decreased demand for Azure PaaS/IaaS; increased Cloud cybersecurity concerns that impact Cloud demand; lower than forecast sales of Microsoft SaaS offerings; increased competitive pricing pressure on IaaS; increased competition in the Office market; decreased PC sales; increased pirating of the company's software, especially Windows and Office; increased functionality in the virtualization layer that limits the need for Windows server on VMs; decreased monetization of Microsoft's online offerings especially Bing; failure to increase international market share of Bing; lower than forecast sales for Xbox products and services; decreases in Windows sales.

RATINGS DEFINITIONS, BENCHMARKS AND DISTRIBUTION

EQUITY RATINGS DEFINITIONS

Bernstein brand

The Bernstein brand rates stocks based on forecasts of relative performance for the next 12 months versus the S&P 500 for stocks listed on the U.S. and Canadian exchanges, versus the Bloomberg Europe Developed Markets Large and Mid Cap Price Return Index EUR (EDME) for stocks listed on the European exchanges and emerging markets exchanges outside of the Asia Pacific region, versus the Bloomberg Japan Large and Mid Cap Price Return Index USD (JPL) for stocks listed on the Japanese exchanges, and versus the Bloomberg Asia ex-Japan Large and Mid Cap Price Return Index (ASIAX) for stocks listed on the Asian (ex-Japan) exchanges -unless otherwise specified.

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Bernstein brand stock ratings are based on a 12-month time horizon.

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Those denoted as 'Feature' (e.g., Feature Outperform FOP, Feature Under Outperform FUP) are our core ideas.

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Autonomous brand – preferred stocks

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* These figures represent the percentage of companies within each equity rating category for which affiliates of Bernstein have provided investment banking services within the previous 12 months.
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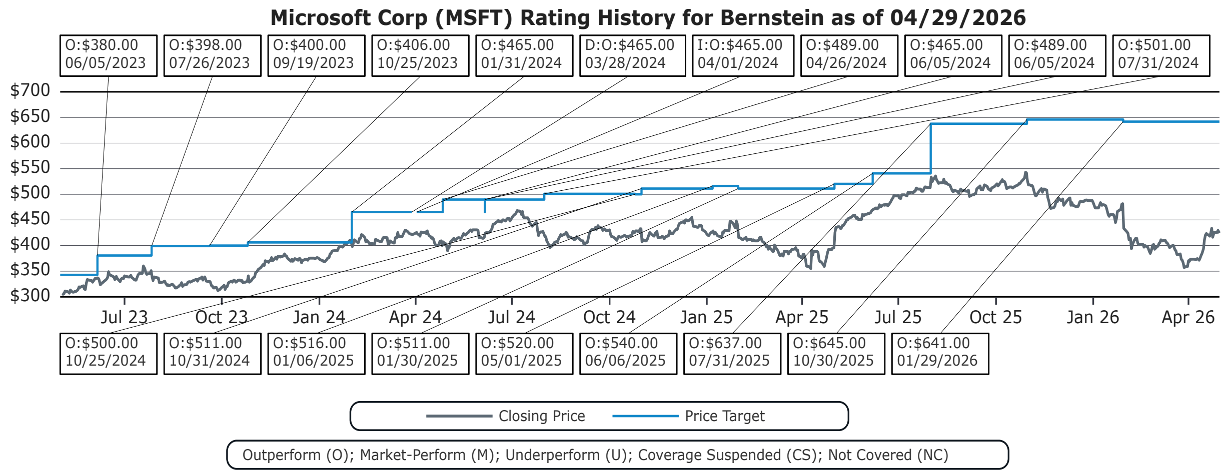

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