

(BN) Microsoft Unveils Surface Tablet Computer, Taking on iPad (1)

+-----+

Microsoft Unveils Surface Tablet Computer, Taking on iPad (1)
2012-06-19 07:08:00.858 GMT

(Updates with LG Electronics' plans in 12th paragraph.)

By Dina Bass, Andy Fixmer and Cliff Edwards

June 19 (Bloomberg) -- Microsoft Corp. unveiled its own Windows-powered tablet computer called Surface, altering its strategy of focusing on software and relying on partners to make the machines in a renewed attempt to take on Apple Inc.'s iPad.

The tablet has a 10.6-inch display and will run the new version of Microsoft's operating system, Chief Executive Officer Steve Ballmer said at an event yesterday at Milk Studios in Los Angeles. The device's cover serves as a full keyboard with a track pad. Surface will be available later this year.

The world's largest software maker is stepping up its assault on the tablet market as consumers choose the devices over laptops, weakening the personal-computer market and curbing Windows revenue. The new strategy threatens to sour Microsoft's relationship with some PC makers, many of which have been investing to develop their own Windows 8 tablets and may not want to compete directly with Microsoft.

"What can I say? Hell froze over -- this is totally antithetical to their core business," said Michael Gartenberg, an analyst at Gartner Inc. "They're taking their destiny into their own hands. It's a bold move, but it's a very risky one.

This could turn into Microsoft's next Zune or its next Xbox."

Two Versions

The company wants to release Windows 8, the new version of its software that is optimized for touch-screen tablets, in time for the end-of-year holidays and will have a version for x86 chips from Intel Corp. and for ones based on ARM Holdings Plc's technology, which is also used in the iPad. The Surface tablet will be available in versions running both chip designs.

Microsoft said the Surface's price will be announced closer to when the devices are available and will be "competitive with a comparable ARM tablet or Intel Ultrabook-class PC."

The version for ARM will go on sale when Windows 8 is released. The Intel-based version will be available about 90 days later, Microsoft said in a statement.

The ARM version of Surface weighs less than 1.5 pounds (680 grams), is 9.3 millimeters (0.37 inches) thick, has a magnesium case and will be powered by an Nvidia Corp. Tegra processor, the company said at the event. Surface also has a built-in kickstand.

"The Surface is something new that we think people will absolutely love," Ballmer said.

PC Market

Windows 8 will arrive amid a deteriorating PC market -- research firm Gartner Inc. on June 15 cut its 2012 PC shipment growth forecast to 2.7 percent from 4.4 percent. Tablet shipments, by comparison, are forecast to almost double to 116 million units this year, Gartner estimates.

Microsoft's entry into the tablet market also comes as challengers such as Hewlett-Packard Co. and Research In Motion Ltd. have failed to derail Apple's dominance with their own tablets. The

worldwide tablet market is estimated to reach \$78.7 billion this year, according to research firm DisplaySearch.

LG Electronics Inc., the world's No. 4 mobile-phone maker, will sideline tablet development to focus more on smaller devices rather than compete head-on with Apple Inc.'s iPad, the Seoul-based company said in an e-mail today. LG introduced its second tablet, named Optimus Pad LTE, earlier this year.

Microsoft is also teaming up with PC makers like Acer Inc., Toshiba Corp. and Asustek Computer Inc. to build tablets with Windows 8, which will be called Windows RT for versions running on ARM-based chips.

Working with partners is Microsoft's more traditional way of operating. Apple's success with the iPad may be pushing the company to seek greater control over the hardware design so it works seamlessly with the software, like Apple does.

Apple's Dominance

Still, gaining ground against Apple won't be easy. Even as companies including Amazon.com Inc. and Samsung Electronics Co.

release new tablets running Google Inc.'s Android operating system, Apple's iPad continues to dominate the market.

Researcher IDC predicts the iPad will account for 62.5 percent of global shipments this year, up from 58.2 percent last year.

The last time Microsoft opted to make its own hardware because its partners weren't gaining traction against Apple, the company produced the Zune music player. It didn't fare any better against the iPod, and Microsoft discontinued the product last year.

At the other end of the spectrum, Microsoft's Xbox console is now the top-selling game machine, with 67 million units shipped. The Xbox 360 device, which also streams television and media content, has helped Microsoft stake a claim to customers' living rooms.

'Software Assets'

Sarah Rotman Epps, an analyst at Forrester Research, said Microsoft's focus on trying to best Apple in hardware design could backfire if Surface tablets don't offer software that stands out.

"What they didn't show were Kinect, SmartGlass and other software assets that could be key differentiators against the iPad," she said. "The months are ticking by, and the announcement left more questions than answers about how successful these devices will be."

After seeing early prototypes from its hardware partners, Microsoft probably wanted to show the industry what it thinks is a good implementation of its tablet ambitions, said Ben Bajarin, an analyst at technology consulting firm Creative Strategies.

"A lot of their traditional partners have not really been focused on the tablet market, and were planning early on to go after new designs for traditional notebooks and desktops," Bajarin said. "This is an effort to drive the category in the right direction."

In what may be a concession to PC partners, Microsoft will sell the device only online and in its own retail stores, which will number 20 by the end of the month, Gartenberg said.

Microsoft also could let vendors build their own Surface tablets, which may sell for \$499 to \$699, and pay for marketing the devices, Bajarin said.

Shifting Focus

Since the release of International Business Machines Corp.'s first PC in 1981, Microsoft has focused on software for the machines and left design and branding to hardware makers.

While the company has in the past decade played a larger role in working with some PC makers on design, it has shied away from developing the machines and selling them under the Microsoft brand.

Ballmer's comments at the event indicated that Microsoft no longer wanted to rely on its hardware partners to translate its vision for Windows into compelling devices, said Gartenberg and Rob Enderle, principal analyst at the Enderle Group.

"They clearly want to make sure at least one Windows 8 tablet is seen as a premium product, offering a premium experience to consumers," Enderle said. "Now they need to execute, or they just handed Apple an early Christmas present."

Profit Margins

The addition of a tablet or other hardware device may erode profitability in the Windows business, which now sells just software with operating margins of more than 60 percent. By comparison, computer maker Dell Inc.'s operating margin for the most recent fiscal year was about 7 percent.

"We are certainly running a business," Ballmer said backstage at yesterday's event, though he declined to discuss financial details. "There won't be an advantage from a cost perspective over our OEMs," he said, referring to PC partners.

Sales in Microsoft's Windows division have fallen short of analysts' estimates in four of the past six quarters, partially because consumers are defecting to the iPad.

"Investors will like the device initially and then will go through the question of what does this do to profit margins," said Brendan Barnicle, an analyst at Pacific Crest Securities in Portland, Oregon, who rates the shares "sector perform."

For Related News and Information:

Microsoft company news: [MSFT US <Equity> CN <GO>](#) Microsoft earnings matrix: [MSFT HPQ US <Equity> EM <GO>](#) Microsoft revenue segments: [MSFT HPQ US <Equity> PGEO <GO>](#) Top technology stories: [TTOP <GO>](#)

--With assistance from Ashlee Vance in San Francisco and Jun Yang in Seoul. Editors: Jillian Ward, Ben Livesey

To contact the reporters on this story:

Dina Bass in Seattle at +1-206-913-4543 or dbass2@bloomberg.net; Andy Fixmer in Los Angeles at +1-323-782-4232 or afixmer@bloomberg.net; Cliff Edwards in San Francisco at +1-415-617-7074 or cedwards28@bloomberg.net

To contact the editor responsible for this story:

Jillian Ward at +1-415-617-7261 or jward56@bloomberg.net