

APPENDIX D: Profitability

D.1 This appendix sets out in detail our analysis of the profitability of Microsoft's Business Software Ecosystem, as summarised in Chapter 5 of this report.

Summary

D.2 As part of our investigation, we have undertaken an analysis of the financial performance of Microsoft's Business Software Ecosystem, which can be one indicator of Microsoft's market power, as set out in our guidance.¹

D.3 In this appendix we set out the issues in assessing the profitability of Microsoft's Business Software Ecosystem and our findings on the profitability of Microsoft, having considered Microsoft's responses to our financial information requests and publicly available financial information.

D.4 Since our SMS assessment relates to Microsoft's market position in the UK, we are interested in the profitability of Microsoft's UK Business Software Ecosystem. However, to help inform this assessment we have started with global figures, recognising that the digital activities we are assessing are global in nature, and because [§<].²

D.5 Our analysis is therefore based on global data from Microsoft supplemented by information we obtained from Microsoft to enable more detailed breakdowns and UK-specific analysis where appropriate.

D.6 On the basis of this analysis, our provisional view is that Microsoft is earning profits substantially above its cost of capital.

D.7 We have found the following:

- (a) Microsoft has been highly profitable over the last ten years in absolute terms, and continues to increase its profit margin;
- (b) The return on capital for Microsoft's Business Software Ecosystem (based on Microsoft Corporation overall) has been significantly above its benchmark cost of capital for the last nine years;
- (c) The return on capital for each of the digital activities in Microsoft's Business Software Ecosystem (PSS, PC OS, Server OS, RDBMS, and Security Software) has been above the cost of capital for the last five years, including under all sensitivities tested; and

¹ See CMA194, paragraph 2.55(e) [Digital Markets Competition Regime Guidance](#).

² Microsoft's responses dated [§<] to the section 69 notice dated [§<].

- (d) We estimate that Microsoft's UK Business Software Ecosystem has generated a return on capital employed (ROCE) of over 70% in financial year 2024/25 compared to an estimated weighted average cost of capital (WACC) of 10%-15%, equating to profits in excess of the WACC of £[4-5] billion.

D.8 We have also compared Microsoft's recent financial performance with its financial projections relating to future revenues and profitability and have seen no evidence that these high levels of profitability would not continue.

Contents of this Appendix

D.9 This appendix has the following sections:

- (a) Our approach to profitability analysis;
- (b) Our assessment of Microsoft's publicly available profitability indicators;
- (c) Our analysis of the profitability of Microsoft's Business Software Ecosystem; and
- (d) Our provisional findings.

D.10 We have conducted a profitability analysis to identify whether Microsoft generates profits at a level that indicates it has substantial and entrenched market power from its Business Software Ecosystem.³

D.11 We have focused on a few standard reporting metrics to inform our analysis of Microsoft's revenues, costs, and profits. In particular:

- (a) We have assessed the amount of profit Microsoft has earned in absolute terms and as a proportion of revenues using the metric 'earnings before interest and taxation' (EBIT).
- (b) We have analysed the level of its profits with reference to the 'return on capital employed' (ROCE). This approach compares accounting profit with the size of investment made by firms to achieve those profits.
- (c) We have compared our ROCE findings against Microsoft's WACC, which is a widely used benchmark for returns on an investment. The WACC is essentially the minimum return required on an investment or asset to satisfy the owners and creditors.

³ As identified in CMA194, paragraph 2.55(e), one indicator of a firm with market power would be earnings which are significantly and persistently above normal returns.

- (d) We have also compared Microsoft's recent financial performance with its financial projections relating to future revenues and profitability.

Proposed approach to our profitability analysis

- D.12 In the following section we set out the business activities we consider to be relevant, the time periods over which we propose to assess profitability, and the ROCE-based approach we are applying.

Business activities

- D.13 We are interested in the profitability of Microsoft's Business Software Ecosystem in the UK.
- D.14 We asked Microsoft to provide UK-level financial performance and balance sheet data; however, Microsoft was unable to provide this information for either its business overall or for the specified digital activities. Microsoft explained that it operates its business on a global basis and [§<]. Microsoft said that, consistent with this approach, it [§<].⁴
- D.15 Microsoft also submitted that competition in relation to all of the digital activities takes place primarily on a worldwide basis, rather than on a UK- or EEA-specific basis, and that [§<], so the revenue data Microsoft submitted provides the CMA with a basis for comparing UK performance against global performance for the relevant products.⁵
- D.16 We considered also that Microsoft's global, integrated network for providing its products and services and the way in which products and services are often sold as bundles meant that its global financial data was likely to be reflective of its cost and asset base in markets such as the UK.
- D.17 Our analysis is therefore based primarily on global data due to:
- (a) the integrated nature of the products and services Microsoft provides;
 - (b) the global nature of Microsoft's Business Software Ecosystem and the digital activities this includes;
 - (c) the global nature of Microsoft's financial reporting and monitoring; and
 - (d) the lack of readily available UK-specific profitability data.

⁴ Microsoft's responses dated [§<] and to the section 69 notice dated [§<].

⁵ Microsoft's responses dated [§<] to the section 69 notice dated [§<].

- D.18 We have also supplemented this with information we obtained from Microsoft to enable more detailed segmental breakdowns and UK-specific analysis where appropriate.

Time period under consideration

- D.19 For our SEMP assessment, we are interested in understanding whether Microsoft has been earning consistently high profits in the past and is likely to continue to do so. For that reason, we have aimed to look back over a time period that is sufficiently long to provide a representative picture of profitability and that is not unduly distorted by unusual macroeconomic conditions or one-off events.
- D.20 We have also taken into consideration the length of time that Microsoft has been providing the digital activities in its Business Software Ecosystem and the nature of its past and current investments. As discussed further below, there are indications that Microsoft has entered a new investment cycle in relation to its AI products and services; however, we would expect the profitability of its core non-AI Business Software Ecosystem products and services to otherwise be relatively stable given the length of time Microsoft has been operating in this market.
- D.21 We have therefore focussed on profitability over the last five years but have assessed Microsoft's overall group-level profitability over a longer nine-year period. We have also assessed the profitability of the digital activities in its Business Software Ecosystem over a five-year period.⁶
- D.22 We have also considered the likely profitability of Microsoft's Business Software Ecosystem for the next five years, to the extent that the forecast data provided by Microsoft and our review of Microsoft's internal documents suggests that this may be meaningful.

Overarching conceptual approach

Return on capital employed versus cost of capital

- D.23 The analysis of profitability as an indicator of market power is based on the premise that under effective competition a firm would generally earn no more than a 'normal' rate of profit over the long run.⁷
- D.24 For the purpose of this profitability assessment, we consider a 'normal' level of profit can be defined as the minimum level of profits required to keep the factors of production in their current use in the long run, i.e. the rate of return on capital

⁶ Note, full year results for FY26 were not yet available at the time of our data collection from Microsoft for this analysis.

⁷ As identified in CMA194, paragraph 2.55(e), one indicator of a firm with market power would be earnings which are significantly and persistently above normal returns.

employed for a particular business activity would be equal to the opportunity cost of capital for that activity.⁸

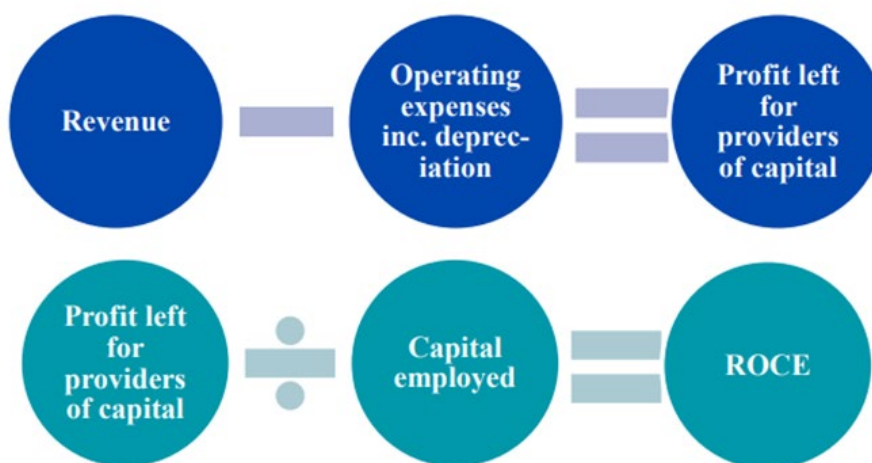
- D.25 The rationale for benchmarking return on capital with the opportunity cost of capital is that, under effective competition, if firms persistently earned in excess of the return required to compensate investors for the risks taken, we would expect these profits to attract entry and/or expansion.⁹ This entry/expansion would serve to compete away profits in excess of the cost of capital up until the point where firms cover their total costs, including a market-based cost of capital, and no more. Where firms persistently earn in excess of a normal return, this signals that there may be limitations in the competitive process.
- D.26 Return on capital can be based on cash flows - internal rate of return (IRR) - or profits (ROCE). These approaches are very similar in substance, with the choice between them determined in part by industry characteristics and in part by data availability.
- D.27 We have considered different approaches to assessing Microsoft's profitability and have taken the approach of comparing its ROCE with the cost of capital. Use of ROCE allows us to calculate annual profitability and thus provides insights into trends over time and the drivers of profits which may exist above the 'normal' level.
- D.28 We consider that the pattern of ongoing variable capital investments (as opposed to large one-off investments) and the lack of any obvious time period to use as investment entry and exit assumptions means that ROCE is more suitable than IRR for measuring profitability. We would not expect an IRR assessment to produce materially different results to a ROCE assessment.¹⁰
- D.29 Figure 1 below illustrates how ROCE is calculated.

⁸ CMA194 does not itself define what constitutes a normal rate of profit. For the purpose of the profitability analysis set out in this appendix, we consider that the CMA's definition of 'normal returns' in the Guidelines for market investigations offers a useful reference point. See CC3, paragraph 116 [CC3 \(Revised\), Guidelines for market investigations: Their role, procedures, assessment and remedies](#).

⁹ The time period over which this process may take place may differ between different sectors due to the time taken for entry and/or expansion of capacity.

¹⁰ Provided that analysis is undertaken carefully, with various adjustments made, ROCE assessment is equivalent to an IRR assessment and is also, therefore, conceptually robust. See *The Economic Analysis of Accounting Profitability* (1987), Jeremy Edwards, J A Kay, Colin P Mayer, for a fuller discussion of the conditions under which the ROCE and IRR approaches are equivalent.

Figure D.1 The components of ROCE



Source: CMA analysis. Note, profit left for providers of capital can be distributed or reinvested in the business.

- D.30 ROCE is the annual return made on the investments needed to run the business and is calculated by dividing EBIT by the value of capital employed in the relevant business. The general principle is that all revenues, costs, assets and liabilities necessarily arising from the operation of the business to supply the relevant activities should be included. In practice this means the following items should be excluded:
- (a) financing costs both of a profit and loss and balance sheet nature (eg cash, interest and sources of finance), regardless of whether they are short- or long-term; and
 - (b) taxation on income and any associated corporation tax or deferred tax assets and liabilities.
- D.31 The ROCE is then benchmarked against the opportunity cost of capital, which is the WACC, over the relevant period(s) of analysis. The WACC is the return on investment that providers of capital– both debt and equity – expect, given the risks associated with the relevant activity.¹¹
- D.32 A finding that ROCE is higher than the WACC is not in itself an indicator of market power. We recognise that profitability could exceed the ‘normal’ level at particular points in time due to a firm earning higher profits as a result of past innovation. However, we would expect the competitive advantage conferred by an innovation to be eroded over time by competition such that a past innovation would not explain sustained profits in excess of the cost of capital over the long term.

¹¹ WACC is therefore expected return on equity and expected return on debt, weighted by gearing – the relevant proportions of debt and equity.

- D.33 For the purpose of our SMS investigation, we do not consider it necessary to define a specific value for the differential between Microsoft's ROCE and WACC that would indicate a level of profits above the 'normal' level. When considering whether the differential is substantial, we will take into consideration the size of this differential and the length of time over which the differential persists.

Economic versus accounting profitability

- D.34 When estimating ROCE, our approach is to start with accounting figures from the profit and loss account and balance sheet of the relevant activities and then make adjustments to arrive at an economically meaningful measure of profitability.
- D.35 An important factor to consider when selecting an appropriate measure of profitability in relation to a business is data availability. Where possible, the CMA will base its calculations on financial data that can be reconciled to audited financial statements, albeit with appropriate adjustments.
- D.36 There is also the need to obtain an appropriate value for capital employed. Obtaining a value for capital employed can present difficulties irrespective of the choice of profitability measurement method; a return on capital approach requires an economically meaningful value for the capital base, which may not accord with the value ascribed in the financial records.
- D.37 We may consider adjustments to accounting data produced in line with UK Generally Accepted Accounting Practice (GAAP) relating to the difference between historical cost and replacement cost, and relating to the inclusion of certain intangible assets where certain criteria are met. We may also consider adjustments to cost or asset allocations on a case-specific basis to account for the activities which are the subject of the investigation, where a firm undertakes other business activities and/or where there are material intercompany transactions.

Limitations of a ROCE versus WACC framework

- D.38 We recognise that economic profitability analysis, based on a ROCE versus WACC framework, requires certain assumptions to be made. The results from economic profitability analysis can be sensitive to ranges around these assumptions, particularly with regard to asset valuations. Where relevant, therefore, we have considered the sensitivity of our analysis to the assumptions we have used.

CMA assessment of Microsoft's publicly available profitability indicators, including in relation to its Business Software Ecosystem

- D.39 In assessing Microsoft's financial performance, we have begun our assessment by considering the profitability of Microsoft and its reporting segments, which can be directly observed from the financial statements.
- D.40 In this section we consider profitability indicators based on publicly available information for Microsoft and its main reporting segments:
- (a) we consider Microsoft's overall size and financial position, based on the consolidated financial statements of the Microsoft Corporation;¹²
 - (e) we consider Microsoft's segmental reporting structures; and
 - (f) we summarise our findings.

Overall size and financial position

- D.41 Microsoft became a publicly listed company in 1986 and has been profitable since at least 1985.¹³ In its most recent full year accounts for the financial year to 30 June 2026 (FY26), Microsoft Corporation generated worldwide revenue of \$332 billion and earnings before interest and tax (EBIT) of \$155 billion.¹⁴
- D.42 Figure 2 below demonstrates Microsoft's total group level revenues and profitability over the last ten years. Microsoft has delivered significant revenue growth alongside substantial EBIT margin expansion over the last ten years, with revenues growing at a compound average growth rate (CAGR) of 15%. Microsoft's EBIT margin has increased from 31% in FY16 to 47% in FY26.¹⁵

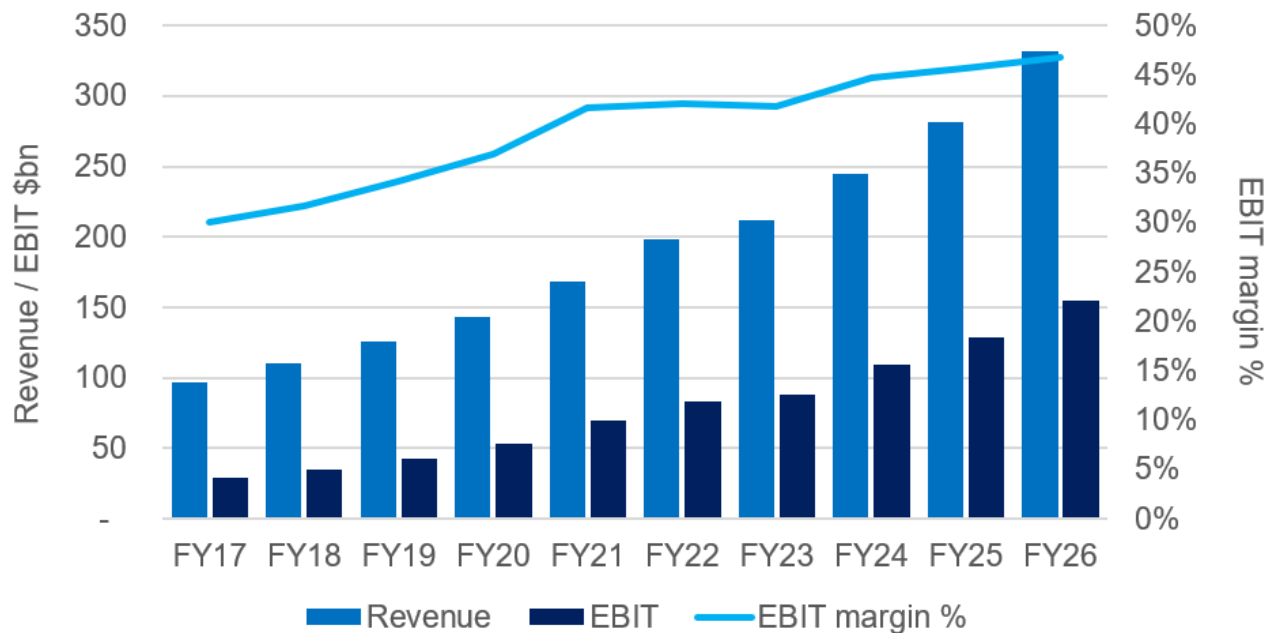
¹² We have considered Microsoft's profitability based on the consolidated financial position of Microsoft Corporation (Microsoft's parent company).

¹³ Microsoft '[Facts About Microsoft - Stories](#)', undated, accessed by the CMA on 3 September 2026; Microsoft, '[Microsoft Form 10-K 1994](#)', 30 June 1994, accessed by the CMA on 3 September 2026, page 131; Microsoft, '[Annual report / Microsoft Corporation 1989 - Northwest Historical Annual Reports Collection - University of Washington Digital Collections](#)', 30 June 1989, accessed by the CMA on 3 September 2026, page 3.

¹⁴ Microsoft, '[Microsoft Form 10-K FY26](#)', 30 June 2026, accessed by the CMA on 3 September 2026, page 37

¹⁵ CMA analysis of Microsoft Form 10-Ks, available at [Microsoft Investor Relations - SEC Filings](#).

Figure D.2. Microsoft Corporation global revenue and EBIT (USD\$bn) and EBIT margin (%), financial years 2016/17 to 2025/25



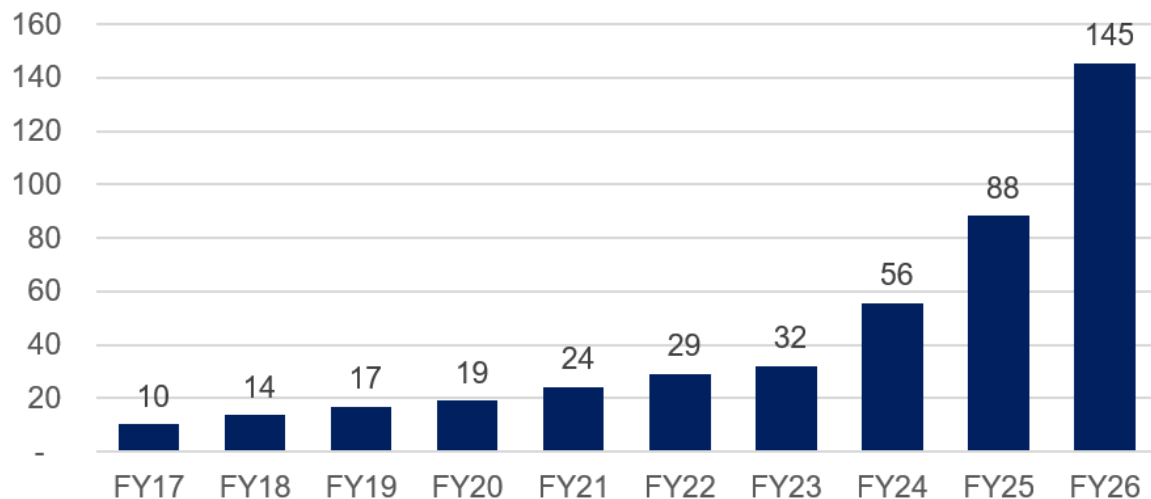
Source: CMA analysis of Microsoft Form 10-Ks.

D.43 Microsoft is not an ‘asset-light’ business. It reported \$682 billion of total assets excluding cash, cash equivalents and short-term investments as of 30 June 2026.¹⁶ Contributing to this is Microsoft’s significant increase in capital expenditure (capex) in recent years as shown in Figure 3 below, primarily in relation to AI and cloud infrastructure investment.¹⁷

¹⁶ Microsoft, ‘[Microsoft Form 10-K FY26](#)’, 30 June 2026, accessed by the CMA on 13 October 2026, page 53.

¹⁷ Microsoft ‘[Q4 FY24 Earnings Call](#)’, 30 July 2024, accessed by the CMA on 14 October 2026; Microsoft ‘[Q2 FY25 Earnings Call](#)’, 29 January 2025, accessed by the CMA on 14 October 2026; Microsoft ‘[Q3 FY26 Earnings Call](#)’, 29 April 2026, accessed by the CMA on 14 October 2026; Microsoft ‘[Q1 FY25 Earnings Presentation](#)’, 30 October 2024, accessed by the CMA on 14 October 2026; Microsoft ‘[Q2 FY25 Earnings Presentation](#)’, 29 January 2025, accessed by the CMA on 14 October 2026; Microsoft ‘[Q3 FY25 Earnings Presentation](#)’, 30 April 2025, accessed by the CMA on 14 October 2026; Microsoft ‘[Q4 FY25 Earnings Presentation](#)’, 30 October 2024, accessed by the CMA on 14 October 2026.

Figure D.3. Microsoft Corporation global capex (USD\$bn), financial years 2016/17 to 2025/26



Source: Capital expenditures as reported in Microsoft Form 10-Ks.

Segmental reporting

D.44 Microsoft is an integrated global firm, providing a range of products and services in addition to the digital activities comprising its Business Software Ecosystem. For segmental reporting purposes, Microsoft's financial statements break down reporting into three main segments:¹⁸

- (a) Productivity and Business Processes is a portfolio of productivity, communication, and information services comprising Microsoft 365 Commercial products and cloud services,¹⁹ Microsoft 365 Consumer products and cloud services, LinkedIn and Dynamics products and cloud services.
- (b) Intelligent Cloud comprises server products and cloud services (including SQL Server, Windows Server, Azure and other cloud services), other on-premises offerings and enterprise and partner services.
- (c) More Personal Computing comprises Windows OEM licensing and devices (Surface and PC accessories), gaming, and search and news advertising.

D.45 Microsoft's accounts note that revenue and costs are generally directly attributed to its segments but due to the integrated structure of its business, certain revenue and costs for one segment may benefit other segments. It notes that revenue from certain contracts is allocated among the segments based on the relative value of

¹⁸ Microsoft, 'Form 10-K FY25' undated, accessed by the CMA on 14 October 2025, pages 82-83. Note, on 2 September 2026 Microsoft announced that it would be restructuring its financial reporting into two segments ('Agents and Infra' and 'Devices and Consumer') for financial year 2026/27.

¹⁹ This includes Microsoft 365 Commercial, Enterprise Mobility + Security, the cloud portion of Windows Commercial, the per-user portion of Power BI, Exchange, SharePoint, Microsoft Teams, Microsoft 365 Security and Compliance, Microsoft 365 Copilot, Windows Commercial on-premises and Office licensed on-premises.

the underlying products and services, and that operating expenses are generally allocated based on relative gross margin or relative headcount.²⁰

- D.46 As shown in Table 1.1 below, Microsoft's Productivity and Business Processes segment has historically contributed the highest share of revenue and has the highest EBIT margin. Intelligent Cloud is the fastest growing segment with revenue growth of 20%-30% in the last three years, compared to 13%-16% revenue growth in the Productivity and Business Processes segment and -1%-13% revenue decline/growth in the More Personal Computing segment.

Table D.1: Microsoft global segmental revenue and EBIT (USD\$bn), share of total revenue (%) and EBIT margin (%),²¹ financial years 2023/24 to 2025/26

	FY24	FY25	FY26	FY24	FY25	FY26
	Revenue \$bn			% of total revenue		
Productivity and Business Processes	107	121	140	44%	43%	42%
Intelligent Cloud	87	106	138	36%	38%	42%
More Personal Computing	51	55	54	21%	19%	16%
	EBIT \$bn			EBIT margin %		
Productivity and Business Processes	60	70	84	56%	58%	60%
Intelligent Cloud	38	45	57	43%	42%	41%
More Personal Computing	12	14	14	24%	26%	27%

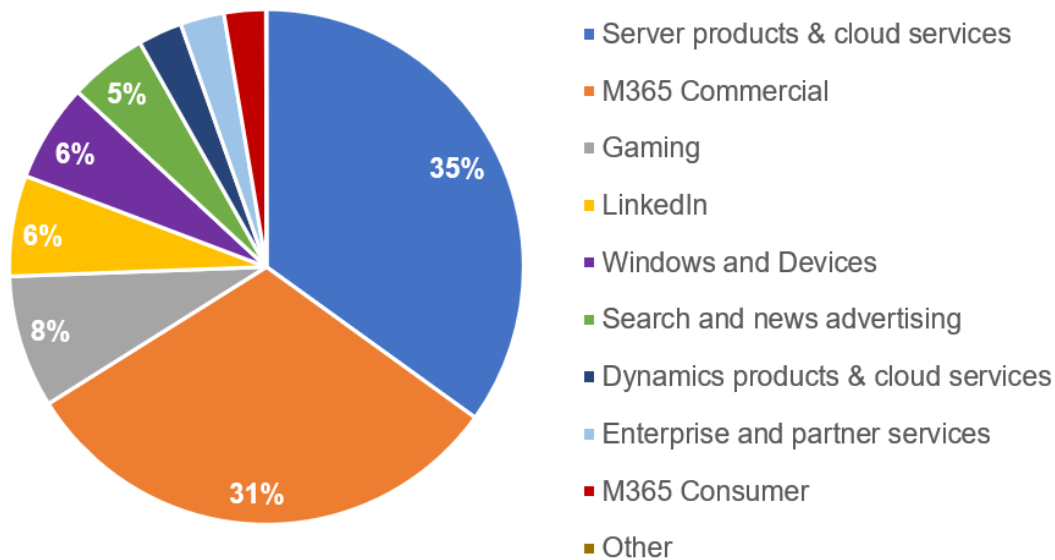
Source: CMA analysis of Microsoft Form 10-Ks. Note, Microsoft restructured its reporting segments in August 2024 (see [SEC Filing | Microsoft Corporation](#)) and as a result, segment financials pre-FY23 on a like-for-like basis are not publicly available.

- D.47 Microsoft publishes some disaggregated segmental revenue data, the breakdown by products and services for which is shown in Figure 4 below.

²⁰ Microsoft, 'Form 10-K FY25' undated, accessed by the CMA on 14 October 2026, page 83.

²¹ EBIT margin is calculated as EBIT (earnings before interest and tax; also referred to as operating income) as a percentage of revenue.

Figure D.4. Microsoft global revenue breakdown by significant product and service offerings, financial year 2024/25



Source: CMA analysis of [Microsoft Form 10-K for FY25](#), p85.

- D.48 Microsoft does not publicly report disaggregated profit data for the products and services comprising its three reporting segments.
- D.49 On a geographic basis, Microsoft splits its revenue reporting between the United States and 'Other countries' and notes that no sales to a country other than the United States accounts for more than 10% of revenue.²²

CMA analysis of the profitability of Microsoft's Business Software Ecosystem

- D.50 In this section, we summarise our analysis of the returns earned by Microsoft in relation to its Business Software Ecosystem and the digital activities included in this (Microsoft's PSS, PC OS, Server OSS, RDBMS and Security Software).²³
- D.51 Ideally, we would assess the profitability of Microsoft's Business Software Ecosystem business specifically, as well as the five digital activities it comprises, taking into account all relevant revenues and costs and an appropriate capital base. Where data is not readily available to do this, we have considered the most appropriate reporting segment(s) or unit(s) to use to assess the digital activity.

²² Microsoft, 'Form 10-K FY25' undated, accessed by the CMA on 14 October 2026 <https://microsoft.gcs-web.com/static-files/9640e86d-a99f-4502-934d-1d3c883fa786>, page 84.

²³ See Chapter 4 of the main report for more detail on the digital activities.

- D.52 We have identified two relevant levels within Microsoft's financial reporting hierarchy for assessing the profitability of Microsoft's Business Software Ecosystem:
- (a) Microsoft Corporation's overall profitability; and
 - (b) Sub-segment level profitability for individual digital activities: we have identified the most relevant sub-segments to assess for the five individual digital activities comprising Microsoft's Business Software Ecosystem. We consider the profitability of the following sub-segments, with our basis for using these sub-segments set out in the section below:
 - (i) Microsoft 365 Commercial products and cloud services ('M365 Commercial') sub-segment is used to assess the profitability of Microsoft's PSS and Security Software;
 - (ii) Server products and cloud services sub-segment is used to assess the profitability of Server OS and RDBMS; and
 - (iii) Device Licensing sub-segment is used to assess the profitability of PC OS.
- D.53 We first summarise our approach to identifying the relevant levels to use in our analysis and determining the corresponding profits, capital base and benchmark cost of capital. We then set out our analysis of:
- (a) Microsoft Corporation ROCE
 - (b) Sub-segment level ROCE
 - (c) Forecast profitability and financial performance
- D.54 Finally, we apply the findings from our global profitability analysis to estimate Microsoft's UK Business Software Ecosystem profitability.

Inputs in assessing the profitability of Microsoft's Business Software Ecosystem

Identifying the relevant segments

- D.55 As described above, Microsoft publicly reports financial results for its three main segments along with some disaggregated revenue data. Microsoft's internal accounts provide a further break down of its three reporting segments with revenue, gross profit and (for larger product and service groupings) EBIT data available at the sub-segment level.²⁴

²⁴ Microsoft's internal document, [§<] to the section 69 notice dated [§<].

- D.56 We asked Microsoft to describe how it monitors the performance of the digital activities and explain the financial data it prepares for these activities. Microsoft said it does not organise or report its financial performance by reference to the digital activities categories, but provided an explanation of how each digital activity maps to Microsoft's reporting segments and sub-segments. Microsoft identified the following internal sub-segments as relevant for the digital activities:²⁵
- (a) For PSS for organisational customers, the M365 Commercial sub-segment within the Productivity & Business Processes segment is relevant as it captures the financial performance of Office (including Word, Excel, PowerPoint, Outlook, Exchange, Teams, SharePoint, OneDrive, and OneNote), Windows, Microsoft 365 Copilot, Enterprise Mobility + Security and Power BI as delivered to organisational and business users, covering both cloud-based and on-premises delivery.
 - (b) For PC OS, the More Personal Computing segment is relevant as it captures the financial performance of Windows 10 and Windows 11. Within the More Personal Computing segment, Microsoft identifies the Windows and Devices sub-segment, and within this Windows OEM Licensing (the 'Device Licensing' sub-segment) in particular, as relevant. Microsoft describes Windows OEM Licensing as Windows Pro and non-Pro licences sold through the OEM channel, though it notes that this includes sales to both organisational customers and consumer end users via the OEM channel.
 - (c) For Server OS, the Server products and cloud services sub-segment within the Intelligent Cloud segment is relevant as it captures the financial performance of Windows Server. Within Server products and cloud services, Microsoft identifies 'Server products' (covering on-premises delivery of Windows Server) in particular as relevant but also notes that, to the extent that Windows Server is consumed through cloud infrastructure, it also falls within the Azure and other cloud services category of the Server products and cloud services sub-segment. Microsoft also notes that this sub-segment covers organisational and enterprise users.
 - (d) RDBMS follows the same the reporting as Server Operating System. The Server products and cloud services sub-segment within the Intelligent Cloud segment is relevant as it captures the financial performance of SQL Server, with on-premises SQL Server included within the Server products category of the sub-segment and Azure SQL included within the Azure and other cloud services category.
 - (e) For Security Software for organisational customers, the M365 Commercial sub-segment within the Productivity & Business Processes segment is

²⁵ Microsoft's responses dated [§<] to the section 69 notice dated [§<].

primarily relevant as it captures security products, including Entra ID, Microsoft Defender and Intune. Microsoft notes that Entra ID and Intune form part of Enterprise Mobility + Security within M365 Commercial, but that as Active Directory is a Windows Server feature delivered on-premises, its financial performance is captured within the Server products and cloud services sub-segment.

- D.57 As shown in Figure 4 above, M365 Commercial, Windows and Devices, Server products and cloud services contributed 72% of Microsoft's total global revenues in financial year 2024/25.
- D.58 Given the integrated nature of Microsoft's business and the products and services in its Business Software Ecosystem, as well as Microsoft's identification of the digital activities as being reported within all three of its main reporting segments, we consider the profitability of Microsoft Corporation overall to be primarily relevant to assessing its Business Software Ecosystem profitability.
- D.59 We estimate that the digital activities in Microsoft's Business Software Ecosystem contribute approximately 40-50% of Microsoft's total global revenues.²⁶ We also calculate that the larger sub-segment groupings identified by Microsoft above which internally report EBIT (M365 Commercial, Windows and Devices, Server products and cloud services) contributed [§<] of Microsoft's total global EBIT in financial years 2023/24 and 2024/25 and [§<].²⁷ This indicates that Microsoft's Business Software Ecosystem business contributes a majority share of Microsoft's profits and earns higher margins than Microsoft overall.
- D.60 To assess the individual digital activities, we have considered the sub-segments identified by Microsoft above and weighed up the availability of internal EBIT data at larger sub-segment grouping levels (M365 Commercial, Windows and Devices, Server products and cloud services) against using the most disaggregated sub-segment levels identified in order to maximise the proportional contribution of the digital activity to the sub-segment.
- D.61 For PSS and Security Software, we consider the M365 Commercial sub-segment to be the appropriate basis to assess the profitability of both activities. Based on Microsoft's description of the products and services included in M365 Commercial, our understanding is that practically all of the sub-segment relates to PSS and Security Software together and reflects sales to organisational customers.²⁸ It does not appear to be possible to further disaggregate financial reporting to

²⁶ [§<]. CMA analysis of Microsoft Form 10-Ks and Microsoft's response dated [§<] to the section 69 notice dated [§<].

²⁷ [§<]. CMA analysis of Microsoft Form 10-Ks and Microsoft's internal document, [§<] to the section 69 notice [§<].

²⁸ As noted above, the M365 Commercial sub-segment does not include Active Directory, which is instead captured within the Server products and cloud services sub-segment.

separately assess each of PSS and Security Software, given the way in which these products and services are often sold as packages.²⁹

- D.62 We estimate that Security Software contributes approximately [§<] of M365 Commercial revenues and that PSS therefore represents the large majority of M365 Commercial.³⁰ The gross margins for the ‘EMS and Power BI per-user’ category (which we understand to reflect in large part Security Software) within M365 Commercial are higher than the overall sub-segment [§<].³¹ We therefore consider that ROCE analysis for M365 Commercial should reflect both PSS and Security Software profitability but may understate Security Software profitability if its margins are higher.
- D.63 For PC OS, we consider the Device Licensing category within the Windows & Devices sub-segment to be appropriate to use to assess profitability. Whilst EBIT data is only available at the Windows & Devices level, Microsoft has identified Device Licensing as particularly relevant and we observe that:³²
- (a) Device Licensing contributes the majority of Windows & Devices revenue [§<]; and
 - (b) The other categories within Windows and Devices (eg Surface devices and mixed reality devices) do not necessarily appear to have revenues directly attributable to, or driven by, the PC OS digital activity³³ and have had declining revenues in financial year 2024/25 along with [§<] gross margins.
- D.64 Given the majority contribution and [§<] of Device Licensing within Windows and Devices, we consider it reasonable to use the Device Licensing category and estimate EBIT using an allocation of Windows and Devices operating costs (explained further below). We estimate that PC OS contributes approximately [§<] of Device Licensing revenue.³⁴
- D.65 We note that both Device Licensing and Windows and Devices are imperfect measures as they include both organisational and consumer customer sales, as well as some proportion of non-digital activity sales. However, given the lack of

²⁹ For example, Microsoft 365 E3 for enterprise customers includes both productivity software and security software. Microsoft, ‘[Microsoft 365 E3 for enterprise](#)’ undated, accessed by the CMA on 30 July 2026.

³⁰ We have used gross revenue data for Entra ID, Intune, Defender, Power BI + M365 Copilot submitted by Microsoft to approximate the Security Software share of revenue. CMA analysis of Microsoft’s responses dated [§<] to section 69 notice dated [§<].

³¹ CMA analysis of Microsoft’s response dated [§<] to the section 69 notice dated [§<].

³² CMA analysis of Microsoft’s response dated [§<] to the section 69 notice dated [§<]; Microsoft’s internal document, [§<] to the section 69 notice dated [§<].

³³ We note that the scope of the PC OS digital activity includes Windows when installed on Surface Pros and Microsoft’s current offer of “all-in-one” Tablet-computers. However, based on the information, available our provisional view is that device sales reported in the Devices sub-segment are unlikely to be directly attributable to installed PC OSs. In contrast, Microsoft’s accounts note that the largest component of its OEM business is the Windows operating system pre-installed on devices. Microsoft, ‘[Form 10-K FY25](#)’ undated, accessed by the CMA on 14 October 2026, page 12.

³⁴ [§<]. CMA analysis of Microsoft’s response dated [§<] to the section 69 notice dated [§<].

available financial reporting for PC OS specifically and with no indication that the profitability for organisational and consumer customers varies materially, we consider Device Licensing ROCE to be indicative of PC OS profitability.

- D.66 For Server OS and RDBMS, Microsoft identified two categories within its Server products and cloud services sub-segment as being relevant (Server products, and Azure and other cloud services). However, Microsoft only internally reports to a gross profit level for these categories, and reports EBIT for Server products and cloud services. Microsoft was not able to provide financial accounts specifically for Windows Server and SQL Server so we do not know exactly how much these products contribute to the sub-segment; however, we estimate that Server OS and RDBMS together contribute approximately [§<] of Server products revenue and [§<] of Azure and other cloud service revenue.³⁵ We also observe that, compared to some other Microsoft segments, the Server products and cloud services sub-segment has had more change in its composition in recent years, with Azure and other cloud services substantially increasing as a share of revenue but also [§<].³⁶
- D.67 Given the availability of EBIT data for the Server products and cloud services sub-segment and potential risks for distortion if estimating EBIT for the categories within the sub-segment that have differing trends and relevance to the Server OS and RDBMS activities, we consider the Server products and cloud services sub-segment to be appropriate to use to assess the profitability of both Server OS and RDBMS. We have not seen any evidence to indicate that profitability would materially differ between these two activities and as noted above, this sub-segment covers organisational customers.
- D.68 We note that the gross margins for the Server products category of the sub-segment, which we estimate to have a materially higher share of Server OS and RDBMS revenues, are substantially higher than for the Azure and other cloud services category (in financial year 2024/25, [§<] gross margin for Server products and [§<] gross margin for Azure and other cloud services).³⁷ This is consistent with a Microsoft internal document identifying that the cost of goods sold is different for software versus cloud services; the document notes that [§<].³⁸
- D.69 We also consider that the fixed asset additions applying to the Server products and cloud services sub-segment in recent years may be of less particular relevance to Windows Server and SQL Server products, given the AI and cloud

³⁵ Microsoft's response dated [§<] to the section 69 notice dated [§<]. We have used Azure and non-Azure gross revenue data for Windows Server and SQL Server submitted by Microsoft to approximate the share of revenue. CMA analysis of Microsoft's responses dated [§<] to the section 69 notice dated [§<].

³⁶ CMA analysis of Microsoft's response to the section 69 notice dated [§<].

³⁷ CMA analysis of Microsoft's responses dated [§<] to the section 69 notice dated [§<].

³⁸ Microsoft's internal document, [§<] to the section 69 notice dated [§<].

focus of investment. The ROCE for Server products and cloud services may therefore understate the profitability of Server OS and RDBMS.

Determining profits

- D.70 Microsoft Corporation publicly reports revenue and operating profit (also known as earnings before interest and tax (EBIT)) data for its entire business. For the relevant sub-segments identified above, Microsoft also internally reports the following:
- (a) M365 Commercial: Revenue, gross profit and EBIT;
 - (b) Server products and cloud services: Revenue, gross profit and EBIT;
 - (c) Device Licensing: Revenue and gross profit.
- D.71 As set out earlier, our understanding is that the gross profit and EBIT data reported by Microsoft includes both direct costs and allocations for shared and common costs such as sales and marketing and research and development costs, as well as internal recharges for the intercompany use of services provided by other businesses within the wider firm.
- D.72 We therefore use reported EBIT for Microsoft Corporation, M365 Commercial and Server products and cloud services. We estimate EBIT for Device Licensing using reported gross profit and an allocation of the operating costs for the Windows and Devices sub-segment it sits within. We allocate operating costs based on the Device Licensing category's proportional revenue contribution to Windows and Devices (averaged over three years, financial years 2022/23 to 2024/25).
- D.73 Microsoft restructured its reporting segments in August 2024, which impacted the relevant sub-segments for our assessment.³⁹ Microsoft provided actual revenue and gross profit data by sub-segment for the last four financial years and EBIT data for the last two financial years on a like-for like reporting basis.⁴⁰ We therefore also adjust historical accounts so that M365 Commercial and Server products and cloud services EBIT and Device Licensing gross profit are on an approximately like-for-like basis with current reporting.⁴¹

³⁹ Microsoft, 'Form 8K', 21 August 2024, accessed by the CMA on 14 October 2026.

⁴⁰ CMA analysis of Microsoft's response dated [§<] to the section 69 notice dated [§<]; Microsoft Internal Document, [§<] to the section 69 notice dated [§<].

⁴¹ To do this we estimate EBIT for Office Commercial, Windows Commercial, EMS + Power BI per-user, Nuance Enterprise for financial years 2020/21 to 2022/23.

Determining capital base

- D.74 Our analysis seeks to reflect the operational capital employed by the businesses. We would generally consider relevant tangible and/or intangible assets used in providing the products and services, including working capital, to determine this.
- D.75 We would expect the capital employed for Microsoft's Business Software Ecosystem business to include working capital and tangible assets such as land, buildings, servers and network equipment. However, any cash and cash equivalents and debt typically represent a means of funding the capital employed by a business, rather than an operational balance, and we do not consider these to be relevant to capital employed for Microsoft's Business Software Ecosystem.
- D.76 Microsoft publicly reports a consolidated balance sheet for the total Microsoft Corporation. The only segmental balance sheet accounts that Microsoft reports are unearned revenue (liabilities) and goodwill (assets).⁴²
- D.77 In response to our request for information on the types of assets used to provide the digital activities, Microsoft referred the CMA to its publicly available financial statements and said the disclosed assets are used across Microsoft's product portfolio and cannot be attributed exclusively to specific digital activities, but that examples of such assets include properties such as office space, datacentres and R&D facilities.⁴³
- D.78 However, in response to our request for the carrying values for each type of asset identified as being used to provide the digital activities, Microsoft said that, at a global level, it maintains the net book value of assets at various internal reporting segments and submitted asset value data for fixed assets [§<], goodwill and intangible assets, with a breakdown of goodwill and intangible asset data by reporting segment. For the fixed assets, Microsoft said that it estimates that approximately [§<] of the asset value is attributable to its cloud business and that the remainder is not allocated to any specific product or business segment.⁴⁴
- D.79 We have considered the data submitted by Microsoft along with the data available from its publicly reported balance sheet.

Working capital and tangible assets

- D.80 Microsoft's submitted fixed assets are clearly identifiable as relevant assets to its provision of Business Software Ecosystem products and services, and we include them in our base case capital employed. However, as Microsoft's response and the AI and cloud focus of its capital expenditures in recent years indicate, there is

⁴² CMA analysis of Microsoft Form 10-Ks.

⁴³ Microsoft's response dated [§<] to section 69 notice dated [§<].

⁴⁴ Microsoft's response dated [§<] to section 69 notice dated [§<].

substantial variation in the extent to which these assets are attributable amongst its reporting segments. We have therefore allocated [~~8~~] of Microsoft's fixed asset balance to the Intelligent Cloud segment based on Microsoft's submission noted above, with the remainder allocated between Microsoft's two other reporting segments based on their share of total costs. We have then allocated fixed assets from the segment level to the relevant sub-segments (M365 Commercial, Server products and cloud services, and Device Licensing) using the segments' proportionate shares of total costs.

- D.81 As noted above, we would expect the capital employed for Microsoft's Business Software Ecosystem business to also include working capital. We calculate Microsoft's working capital as current assets excluding cash, cash equivalents and short-term investments⁴⁵ less current liabilities excluding debt. Using this formula Microsoft has had negative working capital in all years of our analysis.
- D.82 To be conservative and avoid potential distortions to capital employed from allocating Microsoft's negative working capital at the sub-segment level, we do not include working capital in our base capital employed. However, we have tested the sensitivity of our ROCE analysis to the inclusion of working capital. We note that this means that our base case ROCE for Microsoft Corporation and the assessed sub-segments may be understated due to the exclusion of working capital.

Intangible assets

- D.83 We have considered whether we should include intangible assets in our estimate of the capital base. Intangible assets are assets such as goodwill, brand value and in-process research and development assets. In its responses to our information requests, Microsoft submitted data for intangible assets and goodwill, which we consider below.
- D.84 Our approach for considering intangible assets is based on the following set of criteria that we consider intangible assets should meet to be considered for inclusion in capital employed:
- (a) it must comprise a cost that has been incurred primarily to obtain earnings in the future;
 - (b) this cost must be additional to costs necessarily incurred at the time in running the business; and

⁴⁵ We exclude short-term investments as a similar category of cash equivalents as Microsoft's accounts note that these are primarily intended to facilitate liquidity and capital preservation and lists them as a form of funding for Microsoft's operating activities. Microsoft, '[Form 10-K FY26](#)', 30 June 2026, accessed by the CMA on 14 October 2026, pages 42-43.

(c) it must be identifiable as creating such an asset separate from any arising from the general running of the business.

- D.85 Our understanding is that the intangible asset balances submitted by Microsoft are reflective of acquired intangible assets from Microsoft's acquisitions.⁴⁶ On balance, we consider it likely that these assets meet the criteria above and have included these in our base case capital employed.
- D.86 Goodwill can be acquired in a business combination. Acquired goodwill is not a separately identified asset but rather is a balancing figure. It is the remaining, unallocated element of an acquisition price once all tangible assets and certain (although not necessarily all) intangible assets have been fair-valued and set against the price paid. In principle, we consider that, when purchasing a business, goodwill may represent the value of intangible assets not capitalised on the businesses' balance sheets. However, it may also represent capitalised economic profits, which we would not consider to be employed capital.
- D.87 Our approach is to recognise those intangible assets that meet our criteria for recognition, regardless of whether they have been separately identified in the companies' balance sheets or are included in a balancing goodwill figure, but to exclude any remaining goodwill. This approach ensures that only intangible assets that meet our criteria for recognition are included in the estimate of the capital employed by Microsoft in relation to its Business Software Ecosystem. It also avoids the risk of capitalising any economic profit.
- D.88 Based on the information available, we do not consider Microsoft's goodwill balances likely to meet the criteria above.⁴⁷ As Microsoft did not submit any information identifying specific assets that the goodwill balances relate to, and our review of Microsoft's public accounts indicates that most or all of the recorded goodwill represents the balancing figure between price paid and assets acquired for Microsoft's acquisitions, we do not consider its goodwill to meet the criteria of creating a separately identifiable asset.⁴⁸ It is also unlikely to meet the criteria of cost additional to costs necessarily incurred at the time in running the business. We therefore do not include goodwill in our base capital employed; however, we have tested the sensitivity of our ROCE analysis to the inclusion of goodwill.

Weighted average cost of capital

- D.89 As described above, we compare ROCE to the benchmark return of the WACC. We have estimated Microsoft's WACC for its Business Software Ecosystem

⁴⁶ CMA analysis of Microsoft Form 10-Ks and Microsoft's response dated [§<] to the section 69 notice dated [§<].

⁴⁷ We also observe that none of the acquisitions reported in Microsoft's public accounts in the last ten years appear to directly relate to its business software ecosystem. CMA analysis of Microsoft Form 10-Ks.

⁴⁸ For example, Microsoft's Form 10-Ks note that the goodwill for its Nuance and GitHub acquisitions was primarily attributable to anticipated future synergies. Microsoft, '[Form 10-K](#)', 30 June 2023, accessed by the CMA on 14 October 2026, page 70; SEC, '[Microsoft Form 10-K](#)', 30 June 2023, accessed by the CMA on 14 October 2026, page 73.

business and the digital activities to be around 10-15%. This is primarily based on Microsoft's own internal WACC calculations for Microsoft overall and reporting segments.⁴⁹

- D.90 We have also cross-checked this estimate against the WACC calculated for Microsoft's cloud businesses in the CMA's Cloud Market Investigation (taking into consideration the relevance of the inputs used in calculating Microsoft's cloud WACC and potential movement in these inputs if updating the WACC estimate to 2025) and for Alphabet Group (as a competitor) in the CMA's general search and search advertising services SMS investigation.⁵⁰

Microsoft Corporation Return on Capital Employed (ROCE)

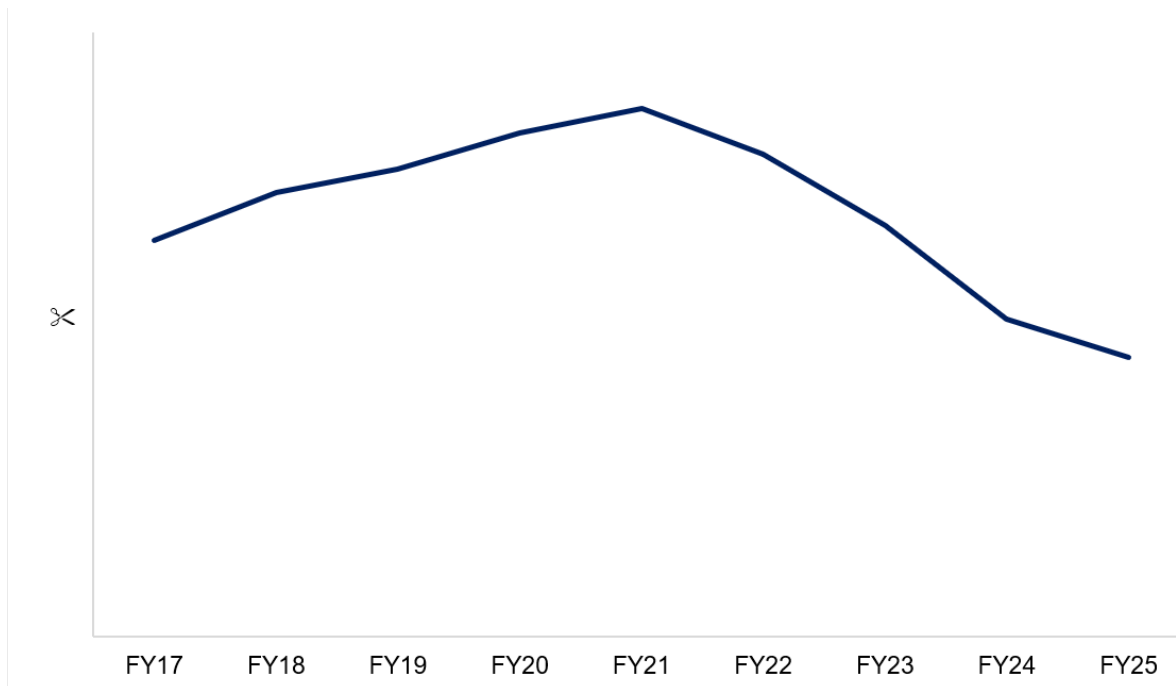
- D.91 We have calculated the ROCE for Microsoft Corporation, using EBIT reported in Microsoft's public accounts⁵¹ divided by capital employed (fixed asset and intangible asset balances as submitted by Microsoft, as explained above). We compare it to the benchmark return of Microsoft's WACC.
- D.92 To take a view on current market trends in profitability, we are primarily interested in the last five years. However, in order to assess Microsoft Corporation profitability over a longer period of up to 10 years we have estimated historical fixed asset values for financial years 2016/17 to 2019/20 using the ratio of the fixed asset data submitted by Microsoft to its reported total property and equipment balance sheet values.
- D.93 Our ROCE calculation for the last nine years is shown below. As noted above, we intend to update this analysis for the latest financial year 2025/26.

⁴⁹ Note, we have analysed Microsoft's average, minimum and maximum WACC estimates over the last five years and adjusted these to a pre-tax basis. CMA analysis of Microsoft's internal document, [8<] to the section 69 notice dated [8<].

⁵⁰ See [Cloud MI Profitability analysis](#) and [Search SMS Profitability analysis](#).

⁵¹ Microsoft's accounts refer to EBIT as Operating income.

Figure D.5. Microsoft Corporation ROCE, financial years 2016/17 to 2024/25



Source: CMA analysis of Microsoft Form 10-Ks, Microsoft's response dated [§<] to section 69 notice dated [§<].

- D.94 Figure 5 above demonstrates that over the last nine years, we estimate that Microsoft Corporation has generated a ROCE in excess of 70%. This is consistently above the estimated WACC of 10-15% for Microsoft.
- D.95 As noted in the previous section, Microsoft has been substantially increasing its capex in AI and cloud infrastructure in recent years. This may indicate a new investment cycle in relation to AI services which may see initial upfront investments that then generate higher returns in the future.
- D.96 Our review of Microsoft's public announcements and internal documents indicates that it is expecting large, accelerating revenue growth from its AI services but that AI is currently contributing to lower margins in Microsoft's business.⁵² Therefore, Microsoft's increased investment in AI and associated costs from this (which would suggest a relatively lower profit contribution from AI services) explains the downward trend in ROCE in recent years, as it increases capital employed at a greater rate than the growth in EBIT.
- D.97 Based on the comments in relation to AI growth in Microsoft's public announcements and internal documents, Microsoft's increased capex appears to

⁵² Microsoft's public accounts in the last three years have regularly noted a downward impact on Microsoft Cloud and/or Microsoft overall gross margin from continued investments in AI infrastructure and, more recently, growing AI product usage. Microsoft, '[Form 10-K FY26](#)', 30 June 2026, accessed by the CMA on 14 October 2026, page 37; Microsoft, '[Form 10-Q Q1](#)', 30 September 2024, accessed by the CMA on 14 October 2026, page 36; Microsoft, '[Form 10-Q Q2 FY23](#)', 31 December 2023, accessed by the CMA on 14 October 2026, page 35; Microsoft, '[Q4 FY26 Earnings call transcript](#)', 29 July 2026, accessed by the CMA on 14 October 2026, pages 7-9, 16, 26-28, 38-39; Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's response dated [§<] to the section 69 notice dated [§<].

represent an upfront investment ahead of developments that would be expected to generate their own returns in the future, and if these returns materialise we would expect Microsoft Corporation ROCE to stabilise or potentially increase in the future. Irrespective of potential future growth from AI services, our analysis shows that Microsoft Corporation ROCE levels have consistently remained substantially above WACC even with this increase in investment.

- D.98 On the basis that Microsoft Corporation profitability is reflective of its Business Software Ecosystem business and Microsoft Corporation ROCE has been in excess of 70% for at least the last nine years. We therefore provisionally find that ROCE for Microsoft's Business Software Ecosystem has been consistently and substantially higher than the benchmark WACC.

Sensitivity analysis

- D.99 We recognise that economic profitability analysis, based on a ROCE versus WACC framework, requires certain assumptions to be made. The results from economic profitability analysis can be sensitive to ranges around these assumptions, particularly with regard to asset valuations.
- D.100 We have conducted sensitivity analysis to test the sensitivity of our ROCE to:
- (a) The inclusion of working capital in capital employed;
 - (b) The inclusion of goodwill in capital employed; and
 - (c) Use of a more conservative approach to estimating capital employed from Microsoft's publicly reported balance sheet, calculated as total assets excluding cash, cash equivalents and short-term investments less current liabilities excluding debt. This approach is equivalent to using net working capital plus total reported non-current assets and means that some assets which we would not consider to be operating assets for Microsoft's Business Software Ecosystem business based on evidence available (for example, equity investments and deferred tax assets, along with goodwill as discussed above) are included and likely to overstate capital employed.
- D.101 We find that Microsoft Corporation ROCE remains well above the benchmark WACC of 10%-15% in each of the above scenarios tested and is materially higher with the inclusion of Microsoft's negative working capital. Even under the most conservative scenario tested (sensitivity (c) above), we calculate ROCE to be between [§<] [30-40]% - [§<] [50-60]% for the last nine years.⁵³

⁵³ CMA analysis of Microsoft Form 10-Ks.

Sub-segment level financial performance and ROCE

- D.102 In this section we consider revenue and margins for the identified relevant Microsoft sub-segments (M365 Commercial, Device Licensing, Server products and cloud services) as an indicator of the scale of relative profitability of the digital activities. We then set out our ROCE analysis for the last five years for these sub-segments.
- D.103 Our approach to calculating ROCE at the sub-segment level is consistent with our approach for Microsoft Corporation ROCE. As detailed below, we have used segment breakdowns for asset and liability balances where available and otherwise made allocations between sub-segments.

PSS and Security Software profitability

- D.104 As explained in the previous section, we have assessed the profitability of the PSS and Security Software digital activities using Microsoft's M365 Commercial sub-segment.
- D.105 Microsoft's internal accounts show that M365 Commercial has [§<] and its EBIT margin is [§<], as show in Table D.2 below. M365 Commercial revenue growth has also been broadly in line with Microsoft Corporation overall.⁵⁴

Table D.2: Microsoft 365 Commercial products and cloud services revenue and profits for financial years 2022/23 to 2024/25

M365 Commercial	FY23	FY24	FY25
Global revenue (\$bn)	66.9	77.0	87.8
Global EBIT (\$bn)	[§<]^	[§<]	[§<]
EBIT margin (%)	[§<]	[§<]	[§<]

Source: CMA analysis of Microsoft Form 10-Ks, Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

^ Estimated FY23 EBIT on a like-for-like basis with current reporting structure has calculated using historical internal accounts.

- D.106 In comparison to the above, Microsoft Corporation's overall EBIT margin was between 42%-46% in financial years 2022/23 to 2024/25.⁵⁵
- D.107 Gross revenue data⁵⁶ submitted by Microsoft indicates that its UK PSS and Security Software revenue was at least \$[§<] (c.£ [§<]) in financial year 2024/25.⁵⁷

⁵⁴ CMA analysis of Microsoft Form 10-Ks.

⁵⁵ CMA analysis of Microsoft Form 10-Ks.

⁵⁶ Note, Microsoft's financial reporting is on a net revenue basis so the gross revenue data submitted may not be perfectly comparable to segment financials.

⁵⁷ CMA analysis of Office 365, on-premise Office suite and other Productivity Software suite revenues and standalone sales of Entra ID, Intune and Defender (individually and in combination) submitted by Microsoft. Note that this data does not capture revenue for Entra ID, Intune, Defender or Active Directory when sold within a suite with other products. Converted to GBP using the Bank of England average exchange rate of 1.2942 for the period from 1 July 2024 to 30 June 2025. Bank of England, 'Our Database', 13 October 2026, accessed by the CMA on 14 October 2026; CMA analysis of Microsoft's responses dated [§<] to the section 69 notice dated [§<].

- D.108 If we assume Microsoft's PSS and Security Software EBIT margins in the UK are the same as its global M365 Commercial margin, then, on the above analysis, this would imply Microsoft's UK EBIT for PSS and Security Software to be at least \$[§<] (c.£[§<]).
- D.109 To calculate ROCE for M365 Commercial, we follow a consistent approach to that set out in the previous section and compare this to the benchmark WACC.
- D.110 Microsoft provided EBIT data for M365 Commercial for financial years 2023/24 and 2024/25. Due to Microsoft's restructure of its reporting segments in August 2024, we have estimated M365 Commercial EBIT for financial years 2020/21 to 2022/23 on a like-for-like basis with current reporting using Microsoft's previous internal accounts breakdown.⁵⁸
- D.111 Our base case estimate of M365 Commercial capital employed includes fixed assets and intangible assets, with sensitivity testing conducted on this estimate. As noted earlier, we have allocated Microsoft's fixed asset balances using a [§<] approximate attribution to Intelligent Cloud and the remainder allocated using proportionate shares of total costs, to reach an estimate of M365 Commercial fixed assets. We have conservatively included the full value of intangible assets allocated to M365 Commercial, and to the 'Productivity' segment in historic years,⁵⁹ from the data submitted by Microsoft.
- D.112 From our ROCE calculation for the last five years, we estimate that Microsoft's M365 Commercial sub-segment has generated a ROCE consistently in excess of [§<].⁶⁰ This is substantially above the estimated WACC of 10-15%.
- D.113 On the basis that M365 Commercial profitability is reflective of PSS and Security Software (see discussion in earlier section), we therefore find that ROCE for Microsoft's Productivity Software Suite and Security Software digital activities has been consistently higher than the benchmark WACC. As set out earlier, we take this global ROCE to be reflective of the UK profitability for these digital activities.

PC OS profitability

- D.114 As explained in the previous section, we have assessed the profitability of the PC OS digital activity using Microsoft's Device Licensing sub-segment.

⁵⁸ We used previously tracked gross profit data for the segment components [§<] and an estimate of 'EMS and Power BI per user' gross profit together with allocations of operating costs based on proportional revenue contribution.

⁵⁹ [§<].

⁶⁰ CMA analysis of Microsoft Form 10-Ks, Microsoft's response dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's internal documents [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

D.115 Microsoft's internal accounts show that Device Licensing has consistently [§<] profitable [§<] and its gross margin is [§<].⁶¹ We also estimate that Device Licensing EBIT margin has been [§<], as show in Table 1.3 below.

Table D.3: Device Licensing revenue and profits for financial years 2022/23 to 2024/25

<i>Device Licensing</i>	<i>FY23</i>	<i>FY24</i>	<i>FY25</i>
Global revenue (\$bn)	[§<]	[§<]	[§<]
Global EBIT estimate (\$bn)	[§<]	[§<]	[§<]
Estimated EBIT margin (%)	[§<]	[§<]	[§<]

Source: CMA analysis of Microsoft Form 10-Ks, Microsoft's response dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's internal document [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

D.116 Gross revenue data submitted by Microsoft indicates that its UK PC OS sales including Service Provider License Agreement ('SPLA') programme but excluding OEM sales were approximately \$[§<] (c.£ [§<]) in financial year 2024/25.⁶²

D.117 If we assume Microsoft's PC OS EBIT margin in the UK is the same as its global Device Licensing margin, then, on the above analysis, this would imply Microsoft's UK EBIT for PC OS to be at least \$[§<] (c.£[§<]).

D.118 To calculate ROCE for Device Licensing, we follow a consistent approach to that set out in the previous section and compare this to the benchmark WACC.

D.119 Microsoft provided gross profit data for Device Licensing for financial years 2020/21 to 2024/25.⁶³ We have estimated Device Licensing EBIT by allocating operating costs from Microsoft's larger encompassing 'Windows and Devices' segment based on proportional revenue contribution.⁶⁴

D.120 Our base case estimate of Device Licensing capital employed includes fixed assets and intangible assets, with sensitivity testing conducted on this estimate. As noted earlier, we have allocated Microsoft's fixed asset balances using a [§<] approximate attribution to Intelligent Cloud and the remainder allocated using proportionate shares of total costs, to reach an estimate of Device Licensing fixed assets. We have conservatively included the full value of intangible assets allocated to the larger Windows and Devices segment, and to the 'Windows' segment in historic years, from the data submitted by Microsoft.

⁶¹ CMA analysis of Microsoft Form 10-Ks and Microsoft's response dated [§<] to the section 69 notice dated [§<].

⁶² Based on the global gross revenue data submitted by Microsoft, we would expect the excluded OEM sales for the UK to potentially be material. CMA analysis of Microsoft's response dated [§<] to the section 69 notice dated [§<]. Converted to GBP using the Bank of England average exchange rate of 1.2942 for the period from 1 July 2024 to 30 June 2025.

⁶³ We note that the Device Licensing sub-segment was not impacted by Microsoft's August 2024 reporting restructure.

⁶⁴ We have estimated Windows and Devices EBIT for financial years 2020/21 to 2022/23 on a like-for-like basis with current reporting using Microsoft's previous internal accounts breakdown of Windows, Windows Commercial and Devices.

- D.121 From our ROCE calculation for the last five years, we estimate that Microsoft's Device Licensing sub-segment has generated a ROCE consistently in excess of [§<].⁶⁵ This is substantially above the estimated WACC of 10-15%.
- D.122 On the basis that Device Licensing profitability is reflective of PC OS (see discussion in earlier section), we therefore find that ROCE for Microsoft's PC OS digital activity has been consistently higher than the benchmark WACC. As set out earlier, we take this global ROCE to be reflective of the UK profitability for these digital activities.

Server OS and RDBMS profitability

- D.123 As explained in the previous section, we have assessed the profitability of the Server OS and RDBMS digital activities using Microsoft's Server products and cloud services sub-segment.
- D.124 Microsoft's internal accounts show that Server products and cloud services [§<] and its EBIT margin is [§<] Microsoft Corporation overall, as shown in Table 1.4 below. Server products and cloud services revenue growth has also been higher than Microsoft Corporation overall.⁶⁶

Table D.4: Server products and cloud services revenue and profits for financial years 2022/23 to 2024/25

Server products and cloud services	FY23	FY24	FY25
Global revenue (\$bn)	65.0	79.8	98.4
Global EBIT (\$bn)	[§<]	[§<]	[§<]
EBIT margin (%)	[§<]	[§<]	[§<]

Source: CMA analysis of Microsoft Form 10-Ks, Microsoft's response dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's internal document [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

[^] Estimated FY23 EBIT on a like-for-like basis with current reporting structure has calculated using historical internal accounts.

- D.125 Gross revenue data submitted by Microsoft indicates that its UK Server OS and RDBMS revenue was approximately \$[§<] (c.£ [§<]) in financial year 2024/25.⁶⁷
- D.126 If we assume Microsoft's Server OS and RDBMS EBIT margins in the UK are the same as its global Server products and cloud services margin, then, on the above analysis, this would imply Microsoft's UK EBIT for Server OS and RDBMS to be approximately \$[§<] (c.£ [§<]).

⁶⁵ CMA analysis of Microsoft Form 10-Ks, Microsoft's responses dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's internal documents [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

⁶⁶ CMA analysis of Microsoft Form 10-Ks.

⁶⁷ [§<]. CMA analysis of Microsoft's responses dated [§<] to the section 69 notice dated [§<]. Converted to GBP using the Bank of England average exchange rate of 1.2942 for the period from 1 July 2024 to 30 June 2025.

- D.127 To calculate ROCE for Server products and cloud services, we follow a consistent approach to that set out in the previous section and compare this to the benchmark WACC.
- D.128 Microsoft provided EBIT data for Server products and cloud services for financial years 2023/24 and 2024/25. Due to Microsoft's restructure of its reporting segments in August 2024, we have estimated Server products and cloud services EBIT for financial years 2020/21 to 2022/23 on a like-for-like basis with current reporting using Microsoft's previous internal accounts breakdown.⁶⁸
- D.129 Our base case estimate of Server products and cloud services capital employed includes fixed assets and intangible assets, with sensitivity testing conducted on this estimate. As noted earlier, we have allocated Microsoft's fixed asset balances using a [§<] approximate attribution to Intelligent Cloud and estimated the Server products and cloud services share of this based on the proportionate share of total costs. We have conservatively included the full value of intangible assets allocated to Server products and cloud services, and to the 'Cloud and Enterprise' segment in historic years, from the data submitted by Microsoft.
- D.130 From our ROCE calculation for the last five years, we estimate that Microsoft's Server products and cloud services sub-segment has generated a ROCE consistently at, or in excess of, [§<].⁶⁹ This is substantially above the estimated WACC of 10-15%.
- D.131 On the basis that Server products and cloud services profitability is reflective of Server OS and RDBMS (see discussion in earlier section), we therefore find that ROCE for Microsoft's Server OS and RDBMS digital activities has been consistently higher than the benchmark WACC. As set out earlier, we take this global ROCE to be reflective of the UK profitability for these digital activities.

Sensitivity analysis

- D.132 Consistent with our approach to Microsoft Corporation ROCE, we have conducted sensitivity analysis to test the sensitivity of each of our sub-segment ROCEs to:
- (a) The inclusion of working capital in capital employed;⁷⁰
 - (b) The inclusion of goodwill in capital employed;⁷¹ and

⁶⁸ We used previously tracked EBIT data for the 'Cloud and Enterprise' segment and estimates of 'EMS and Power BI per user' and 'Nuance Enterprise' EBIT.

⁶⁹ CMA analysis of Microsoft Form 10-Ks, Microsoft's response dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated; Microsoft's internal documents [§<] from Microsoft's response to the section 174 notice dated [§<] under the Enterprise Act 2002, in the context of the CMA's Cloud Market Investigation.

⁷⁰ We have estimated sub-segment working capital by allocating segment unearned revenue and Microsoft Corporation other working capital based on revenue share.

⁷¹ We have conservatively included the full value of goodwill for the sub-segment/segment as submitted by Microsoft.

- (c) The inclusion of both working capital and goodwill in capital employed. Due to the lack of segment breakdowns available for all of Microsoft's publicly reported asset and current liability categories we do not consider it reasonable to test sub-segment sensitivities based on an allocation of Microsoft Corporation total assets excluding cash, cash equivalents and short-term investments less current liabilities excluding debt; however, given the relative materiality of goodwill and working capital to Microsoft's balance sheet we consider a sensitivity including both working capital and goodwill to be reasonable proxy for this.

D.133 We find that ROCE for each of M365 Commercial, Device Licensing and Server products and cloud services remains well above the benchmark WACC of 10%-15% in each of the above scenarios tested. Even under the most conservative scenario tested (sensitivity (c) above), we calculate ROCE to remain above [8%] for M365 Commercial, Device Licensing and Server products and cloud services respectively in the last five years.

Our analysis and provisional findings of Microsoft's overall and sub-segment ROCE in relation to its Business Software Ecosystem

- D.134 Based on the above analysis, we have provisionally found that Microsoft's global Business Software Ecosystem business generated a ROCE substantially above the benchmark WACC and in excess of 70% for the last nine years. Our sub-segment analysis is consistent with this, showing that each of the identified digital activities for Microsoft's Business Software Ecosystem have generated a ROCE substantially above the benchmark WACC for the last five years.
- D.135 As described above, we have considered the sensitivity of our profitability analysis to the assumptions we have made, including in relation to the assets submitted by Microsoft and its reported balance sheet more broadly, and have estimated a range for returns with these assumptions varied, and these do not change our finding that Microsoft's Business Software Ecosystem, and the five digital activities comprising this, is highly profitable.

Our estimate of Microsoft's UK Business Software Ecosystem profits

- D.136 As set out earlier, we consider Microsoft's global financial data likely to be reflective of its UK profitability. For illustrative purposes we have considered how global ROCE would convert into an annual profit number as an estimate of how much profit Microsoft's UK Business Software Ecosystem business earned over and above our estimate of Microsoft's WACC.
- D.137 To calculate our estimate of UK Business Software Ecosystem ROCE above a benchmark level we have:

- (g) First, estimated UK business software ecosystem EBIT using a revenue-based allocation of the estimated global EBIT for each of the digital activities (ie Microsoft's EBIT, as reported or estimated per our above analysis, for each of the following: M365 Commercial, Server products and cloud services, Device Licensing);
- (h) Second, used a revenue-based allocation to estimate a UK share of the global expected investor return based on our estimate of Microsoft's WACC; and
- (i) Third, deducted (b) from (a) to estimate the profit earned by Microsoft's UK Business Software Ecosystem business in excess of WACC.

D.138 Following this approach, we estimate a combined UK EBIT of £[§<]billion in financial year 2024/25 for the three reporting segments identified above which cover each of the digital activities. On the basis that the profitability of these reporting segments should be largely reflective of, and a reasonable proxy for estimating, the scale of Microsoft's Business Software Ecosystem business, we estimate that Microsoft earned £[4-5] billion more profit than a return based on the estimate of WACC.⁷²

Forecast profitability

D.139 As part of the SMS investigation, we have also compared Microsoft's recent financial performance with its financial projections relating to future revenues and profitability, based on available information, in order to assess whether current trends in revenues and profitability are expected to continue into the future.

D.140 As part of this assessment, we have reviewed the forward-looking information in Microsoft's internal documents, including:

(a) [§<].⁷³

(b) [§<].⁷⁴

(c) [§<].⁷⁵

⁷² The sections above set out our basis for considering Microsoft's three reporting segments (M365 Commercial, Server products and cloud services, Device Licensing) to most closely represent the digital activities, but we note that this means that our estimate will include some product and services which are not part of the digital activities. CMA analysis of Microsoft Form 10-Ks, Microsoft's responses dated [§<] to the section 69 notice dated [§<]; Microsoft's internal document, [§<] to the section 69 notice dated [§<]. Converted to GBP using the Bank of England average exchange rate of 1.2942 for the period from 1 July 2024 to 30 June 2025.

⁷³ Microsoft's internal document, [§<] to the section 69 notice dated [§<].

⁷⁴ Microsoft's internal document, [§<] to the section 69 notice dated [§<].

⁷⁵ Microsoft's internal document, [§<] to the section 69 notice dated [§<].

(d) For financial year 2026/27, Microsoft's forecast segment and sub-segment revenue growth, operating margin and capex. This shows [§<].⁷⁶

D.141 Based on our review of Microsoft's financial projections relating to future revenue and profitability, we have seen no evidence that these high levels of profitability would not continue. Our estimate of Microsoft Corporation ROCE for the next five years using high level assumptions from Microsoft's financial projections and recent financial trends is consistent with Microsoft continuing to generate substantial profits from its Business Software Ecosystem which are above the benchmark WACC.

Summary of provisional findings on Microsoft's Business Software Ecosystem profitability

D.142 Our analysis of Microsoft's financial performance illustrates that it has consistently been highly profitable over the last five to ten years, including in relation to its Business Software Ecosystem.

D.143 We have demonstrated this by comparing our estimates of Microsoft's ROCE – its actual profitability – at both an overall and sub-segment level with an estimate of Microsoft's WACC, based primarily on Microsoft's own internal estimates.

D.144 We have also found that over the last five years, the digital activities in Microsoft's Business Software Ecosystem (PSS, PC OS, Server OS, RDBMS and Security Software) have had operating profit margins that are [§<] Microsoft Corporation overall, based on Microsoft's segmental reporting.

D.145 Taking into consideration that Microsoft's operating profit margins for its Business Software Ecosystem activities are [§<], we consider Microsoft's Business Software Ecosystem business to be at least as profitable as Microsoft Corporation. We therefore consider that Microsoft is likely to generate a ROCE in excess of 70% from its Business Software Ecosystem, including for the UK.

D.146 Given the global nature of Microsoft's cost reporting structures, and having seen no evidence that Microsoft's UK Business Software Ecosystem business and the digital activities have materially higher operating costs relative to its global business, we estimate that Microsoft's UK Business Software Ecosystem is generating economic profits substantially higher than our estimate of the WACC.

⁷⁶ Microsoft's internal document, [§<] to the section 69 notice dated [§<]; Microsoft's response dated [§<] to the section 69 notice dated [§<].

- D.147 We estimate that this high return means that Microsoft's UK Business Software Ecosystem earned substantially more profit than a return based on the estimate of WACC.
- D.148 Based on our review of Microsoft's own financial projections relating to future revenues and profitability, we have seen no evidence that these high levels of profitability would not continue.