

## Q4 2020 Earnings Call

### Company Participants

- Luca Maestri, Senior Vice President and Chief Financial Officer
- Tejas Gala, Senior Manager, Corporate Finance, and Investor Relations
- Tim Cook, Chief Executive Officer

### Other Participants

- Amit Daryanani, Analyst
- Chris Caso, Analyst
- Jeriel Ong, Analyst
- Katy Huberty, Analyst
- Krish Sankar, Analyst
- Kyle McNealy, Analyst
- Samik Chatterjee, Analyst
- Shannon Cross, Analyst

### Presentation

#### Operator

Good day, everyone. Welcome to the Apple Incorporated Fourth Quarter Fiscal Year 2020 Earnings Conference Call. Today's call is being recorded.

At this time for opening remarks and introductions, I would like to turn things over to Tejas Gala, Senior Analyst, Corporate Finance and Investor Relations. Please go ahead, sir.

#### Tejas Gala {BIO 20432011 <GO>}

Thank you. Good afternoon and thank you for joining us. Speaking first today is Apple's CEO, Tim Cook and he will be followed by CFO, Luca Maestri. After that, we'll open the call to questions from analysts.

Please note that some of the information you'll hear during the discussion today will consist of forward-looking statements, including, without limitation, those regarding revenue, gross margin, operating expenses, other income and expense, taxes, capital allocation and future business outlook, including the potential impact of COVID-19 on the company's business and results of operations. These statements involve risks and uncertainties that may cause actual results or trends to differ materially from our forecast.

For more information, please refer to the risk factors discussed in Apple's most recently filed annual reports on Form 10-K and the Form 8-K filed with the SEC today, along with the associated press release. Apple assumes no obligation to update any forward-looking statements or information, which speak as of their respective dates.

I'd now like to turn the call over to Tim for introductory remarks.

## **Tim Cook** {BIO 14014370 <GO>}

Thanks, Tejas and good afternoon, and thanks for joining the call today. Back in April, I said we were in the most challenging environment in which Apple as a company has ever operated. That atmosphere of uncertainty, a resolve of making difficult calls with limited information has not only come to define Apple's year, but each of our lives as individuals across this country and around the world. It has been a chapter that none of us will forget. In the face of these challenges, Apple stayed relentlessly focused on what we do best, seeing in every obstacle an opportunity to do something new, something creative, something better on behalf of our customers.

Today, we report a quarter and a fiscal year that reflects that effort. This quarter, Apple achieved revenue of \$64.7 billion, a September quarter record, despite the anticipated absence of new iPhone availability during the quarter and the ongoing impacts of COVID-19, including closures at many of retail locations. We also set a new all-time record for Mac and Services. Outside of iPhone, each of our product category saw strong double-digit year-over-year growth, despite supply constraints in several product categories. Our results for this quarter were ahead of our expectations, driven by stronger than expected iPhone and Services performance. As we anticipated, we launched new iPhone models in October, a few weeks later than last year's mid-September launch. Up to that mid-September point, customer demand for iPhone was very strong and grew double-digits. On services, we saw stronger-than-expected performance across the board. Geographically, we set September quarter records in the Americas, Europe and Rest of Asia Pacific. We also set a September quarter record in India, thanks in part to a very strong reception to this quarter's launch of our online store in the country.

Greater China is the region that was most heavily impacted by the absence of the new iPhones during the September quarter. Still we beat our internal expectations in the region growing non-iPhone revenue strong double-digits and iPhone customer demand grew through mid-September. When you pull back the lens to the entire fiscal year, it's a testament to the team's work and to the resilience of the business in the era of COVID-19. This year, we set an all-time revenue record of \$274.5 billion, growing 6% year-on-year. We grew every quarter, set all-time yearly records in Mac, Wearables, Home and Accessories, and Services and grew by double-digits in every product category outside of iPhone.

When we first began to grapple with COVID-19, I said there are worse things for a company whose business is innovation than having to periodically do just about everything in an entirely new way. This year, we not only launched our most powerful and compelling generation of hardware, software and services ever, we did it in a way that pushed us to re-imagine every part of that innovation process, down to how we share these announcements with the world and how we get new products into our customers'

hands. Working from kitchen tables and bedrooms and distanced office settings and reworked labs and manufacturing facilities, the team rebuilt every part of the plane while it was mid-air and the results speak for themselves.

In a year that has been enormously challenging, our retail teams, contact centers, and all those who work with our customers most closely have gone to creative and dedicated lengths to keep serving our customers, from adapting our stores for contactless pickup to new Apple Express storefronts, to new online customer support options. Amidst store closings, reopenings, and re-imaginings, these teams have been an unfailing source of energy, creativity, and determination.

Innovation isn't just about what you make. It's about how you approach problems. And these teams and every team across Apple have not faced a single question this year that they haven't founded answer to with passion and resolve. Their actions didn't just meet the moment. They will make us a better company moving forward. The pandemic has hit home for all of us. And at Apple, we have seen it as a call to action. We have seen the pain in our communities. Many of us have seen our children work hard to adapt to remote learning. And we all know that the road ahead is uncertain. This quarter and throughout the year, our response to this crisis has been to ask how can we help, in terms of COVID-19 response, that is mid-sourcing and donating millions of face masks, designing and manufacturing millions of face shields, and scaling the production of millions of test kits.

But we have tried to live our values more broadly. We've pledged \$100 million to our new Racial Equity and Justice Initiative. We've committed to be fully carbon-neutral by 2030 across our entire supply chain and device usage as massive wildfires, hurricanes, and floods bring home the consequences of climate change for all of us. And we have deepened our enduring educational partnerships from coding education beginning in elementary school to new efforts with dozens of historically black colleges and universities.

One of the many areas where for COVID-19 continues to have a significant impact is in education. As teachers, students, and parents alike work hard to keep education relevant, creative and effective, our products have helped them meet the moment. In a typical year, the back-to-school season is a bustling time for us. This year, that was true and the biggest way ever. We've helped school districts around the world meet this moment in an unprecedented way, including starting nine of our 10 largest school district deployments ever that alone will support over 1 million students and teachers. We have also supported these deployments and educators and learners everywhere with free tools and training reaching over 150,000 teachers and millions of parents and students around the world.

Looking forward, we feel great optimism about the road in front of us. We're in the midst of our most prolific product introduction period ever. In addition to the announcement of HomePod mini, which achieves unmatched sound quality and Siri and smart home capabilities in a small and affordable format, we just marked the beginning of a new era for iPhone with the arrival of our first 5G-enabled devices. The iPhone 12 and 12 mini, most powerful breakthroughs like an edge-to-edge Super Retina XDR Display, unprecedented durability with the new ceramic shield developed with our partners at Corning, new

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MagSafe charging and accessories, the fastest ever A14 Bionic chip and a new dual camera system driven by computational photography.

The iPhone 12 Pro and 12 Pro Max take all of this to an even higher level, driven by the most powerful photo and video tools ever delivered by a smartphone, including an all-new LiDAR scanner and the ability to shoot in Apple ProRaw and full Dolby video. And of course, all of these devices bringing the 5G experience users have been waiting for with lightning fast downloads and uploads, a new standard in video streaming, more responsive gaming and much more. The early product reviews had been tremendously positive and our customers had been similarly excited to get their hands on this next era of devices. We are very optimistic about what the next few weeks will bring.

We're also seeing a very positive response to our September announcements. The all-new Apple Watch Series 6 boasts powerful new health and wellness features, including a blood oxygen sensor, a next generation altimeter, and a wide variety of new colors and bands. The potential for Apple Watch's powerful health and wellness capabilities continues to grow.

Just yesterday, the government of Singapore and Apple launched LumiHealth, a first of its kind program designed to encourage healthy activity and behaviors using Apple Watch. Created in collaboration with the team of physicians and public health experts, LumiHealth uses technology and behavioral insights to encourage Singaporeans to keep healthy and complete wellness challenges through their Apple Watch and iPhone. Singapore is a trailblazer here and we're proud to be their partner.

Our iPad lineup continues to set the pace for the category, including the new iPad Air now shipping with the A14 Bionic, our most powerful chip ever. We announced Apple Fitness+, which delivers deep personalization and integration across the fitness tools, our users love and depend on. And Apple One, launching tomorrow, is the easiest way for users to enjoy Apple services like Music, TV+, Arcade, iCloud, News+ and Fitness+ on a single plan that is right for them and their family.

Looking across services more broadly, we are really excited about what we see. This was a record quarter for the App Store, AppleCare, cloud services, music and payment services. The App Store in particular continues to play an essential role in helping small businesses, educational institutions, and workplaces adapt to COVID-19. Apple TV+ continues to impress from fan favorites like Ted Lasso, which has won a worldwide audience with its hopeful tone during challenging times to critical and award praise, including a Primetime Emmy for Billy Crudup in 'The Morning Show'.

Luca will speak in greater detail about our expectations for the December quarter. Without giving away too much, I can tell you that this year has a few more exciting things in store.

Before I hand things off, I want to offer one more comment on resilience. Because I think if I had to describe our performance this quarter in a single word, it's resilient. Financial performance aside, I don't think this year will be a time that any of us look back on with great fondness or nostalgia. Those of us who wake up every day, hoping for return to

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normal, can count ourselves fortunate. Others don't have that luxury. There is the great pain of a lost loved one, the uncertainty and fear of a lost job, a deep well of concern for people we care about who we are not able to see. A sense of opportunities missed, the plans delayed, or time lost. Even though we are apart, it's been obvious this year that around the company, teams and colleagues have been leaning on and counting on each other more than in normal times.

I think that instinct, that resilience has been an essential part of how we have navigated this year. Work can't solve for all the things we're missing right now, but a shared sense of purpose goes a long way. I believe that we can do more together than we can alone. The people of goodwill, driven by creativity and passion and that certain itch of a big idea can still do things that help other people in our own small way to teach, to learn, to create or just to relax at a time like this.

Even as the things we make require us to operate at the very cutting-edge of technology in materials, products and ideas that didn't exist just a few years ago, this year has forced us to face plainly the things that make us human, disease, resilience, and hope. You never wish for a year like this one. But I couldn't be prouder of the team, the work we have done and the small role we have played in helping our communities find hope and resilience in this time.

With that, I'll hand things over to Luca.

**Luca Maestri** {BIO 15738533 <GO>}

Thank you, Tim. Good afternoon, everyone. We are very pleased to report today a new September quarter revenue record, which caps a remarkable level of performance for our fiscal year 2020, during which we set new all-time records for revenue, earnings per share, and free cash flow, in spite of an extremely volatile and challenging macro environment. We could not be more proud of the way our team has innovated and executed throughout this unprecedented period of uncertainty.

We reported total revenue of \$64.7 billion for the September quarter, up 1% from a year ago. This is a very impressive level of performance, when we consider that this year we did not launch and ship any new iPhone models during the quarter. Outside of iPhone, we grew 25% in aggregate and had strong double-digit year-over-year revenue growth in each of our product categories. We set all-time records for Mac and services and a September quarter record for Wearables, Home and Accessories.

We also achieved new September quarter records in the vast majorities of countries that we track, including among others, the US, Canada, Brazil, Germany, France, Italy, Spain, Turkey, Russia, India, Korea, Thailand, Malaysia and Vietnam. Products revenue was \$50.1 billion with very strong underlying performance across each product category. Our products, outside of iPhone, grew a combined 30% despite supply constraints on iPad, Mac and Apple Watch throughout the quarter.

For iPhone, through mid-September, customer demand grew double-digits. As a result of this level of sales performance and the unmatched loyalty of our customers, our installed

base of active devices reached an all-time high in aggregate and in each of our major product categories.

Our services set an all-time record of \$14.5 billion, growing 16% year-over-year. We established new all-time records in many services categories and September quarter records in each geographic segment. I'll cover this in more detail later.

Company gross margin was 38.2%. This was up 20 basis points sequentially due to cost savings and a higher mix of services, partially offset by a different mix of products. Products gross margin was 29.8%, growing 10 basis points sequentially driven by cost savings partially offset by a different mix. Services gross margin was 66.9%, decreasing 30 basis points sequentially mainly due to a different mix.

Let me get into more detail for each of our product categories. iPhone revenue was \$26.4 billion, as we did not have availability of new iPhone models during the September quarter this year, which we had mentioned during our call in July. While COVID-19 and social distancing measures impacted store operations in a significant manner, demand for iPhone remained very strong. In fact through mid-September, customer demand for our current product lineup grew double-digits and was well above our expectations.

Our active installed base of iPhones reached a new all-time high, thanks to the exceptional loyalty of our customer base and strength of our ecosystem. In fact, in the US, the last survey of consumers from 451 Research indicates iPhone customer satisfaction of 98% for iPhone 11, 11 Pro and 11 Pro Max combined.

Turning to services, as I said, we set an all-time revenue record of \$14.5 billion. We grew strong double-digits and set all-time records in App Store, cloud services, music, advertising and payment services. We also set an all-time record in AppleCare, as in-store traffic improved and we were able to support more customers.

Our new services, Apple TV+, Apple Arcade, Apple News+ and Apple Card are also contributing to overall services growth and continue to add users, content, and features. The key drivers for our services growth all continue to be moving in the right direction. First, our installed base continues to grow and is at all-time high across each major product category. Second, the number of both transacting and paid accounts on our digital content stores reached a new all-time high during the September quarter, with paid accounts increasing double-digits in each of our geographic segments. Third, paid subscriptions grew more than 35 million sequentially. And we now have over 585 million paid subscriptions across the services on our platform, up 135 million from just a year ago. With this momentum, we are very confident to reach and exceed our increased target of 600 million paid subscriptions before the end of calendar 2020.

Finally, as Tim mentioned, we continue to improve the breadth and the quality of our current services offerings and are adding new service offerings that we think our customers will love, like Apple One and Apple Fitness+.

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Wearables, Home and Accessories established a new September quarter record with revenue of \$7.9 billion, up 21% year-over-year. We set September quarter records in every geographic segment and for each of the three product categories, Wearables, Home and Accessories. As a result, our Wearables business is now the size of a Fortune 130 company. Importantly, Apple Watch continues to extend its reach with over 75% of the customers purchasing Apple Watch during the quarter being new to the product. We are very excited about the future of this category, including the recent launches of our new products. Apple Watch Series 6 and SE, HomePod mini and the MagSafe ecosystem of accessories.

Next, I'd like to talk about Mac. Revenue was by far an all-time record at \$9 billion, up 29% over last year and \$1.6 billion above our previous record, in spite of supply constraints during the quarter. We grew strong double-digits in each geographic segment and set all-time revenue records in the Americas and Rest of Asia Pacific, as well as September quarter records in Europe and Japan. We've seen amazing customer response to the new MacBook Air and MacBook Pro and very strong demand during the back-to-school season.

iPad performance was also very impressive with revenue of \$6.8 billion, up 46% and our highest September quarter revenue in eight years, despite supply constraints. Demand exceeded our expectations around the world as we grew very strong double-digits in every geographic segment including an all-time record in Japan and a September quarter record in the Americas.

Both Mac and iPad are incredibly relevant products for our customers in the current working and learning environments. And we are delighted that the most recent surveys of consumers from 451 Research measured customer satisfaction at 93% for Mac and 95% for iPad. With this level of customer satisfaction and with around half of the customers purchasing Mac and iPad during the quarter being new to that product, it is no surprise that the active installed base for both products reached a new all-time high.

In the enterprise market, our products are helping companies grow their business while achieving their sustainability goals. One example is Vestas, a leading producer of wind turbines. Vestas is using Apple products and native iOS apps extensively across their operations to deliver renewable energy efficiently to customers worldwide. For instance, they use iPads to optimize on-site construction operations, cutting crane usage on average by one day per project. Vestas field technicians are using iPhone for work orders, troubleshooting a remote collaboration, saving them 400,000 service hours annually. More recently, they've started piloting the augmented reality capability in iPads to help customers visualize wind turbine installations in the field. Another example of how organizations are using Apple products to reduce carbon impact is digitizing paper workflows. In Switzerland alone, Zurich Insurance has reduced paper consumption by over 10,000 sheets per day by equipping a 1,000 customer advisors with iPads. Air Canada is reducing its carbon footprint by over 2,200 metric tons annually by loading flight plans and manuals on to iPads rather than using paper. We are thrilled that our products are helping businesses run more efficiently and sustainably.

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Let me now turn to our cash position. We ended the quarter with almost \$192 billion in cash plus marketable securities. We issued \$5.5 billion of new term debt and decreased short-term borrowing facilities by \$6.2 billion during the quarter, leaving us with total debt of \$112 billion. As a result, net cash was \$79 billion at the end of the quarter as we continue on our path to reaching a net cash neutral position over time. We returned nearly \$22 billion to shareholders during the September quarter, including \$3.5 billion in dividends and equivalents and \$18 billion through open market repurchases of 168.7 million Apple shares. We also retired an additional 3.1 million shares in the final settlement of our 16th ASR.

Before looking ahead, I want to provide just a few highlights for the amazing fiscal year we just completed. In fiscal '20, we grew revenue by 6% to \$274.5 billion, a new all-time record. We showed remarkable resilience throughout the year, as we were able to grow both revenue and installed base of active devices in every quarter. In spite of the most challenging economic environment we can remember, we set new revenue records in the Americas, in Europe and in the Rest of Asia Pacific. We grew our business outside of iPhone by 16%. We grew earnings per share 10% to a new all-time record. And most importantly, we continue to deliver innovative products and services that our customers love.

As we move ahead into the December quarter, I'd like to provide some color on what we are seeing, which includes the types of forward-looking information that Tejas referred to at the beginning of the call. Given the continued uncertainty around the world in the near term, we will not be issuing revenue guidance for the coming quarter. However, we are providing some insights on our expectations for the December quarter for our product categories. These directional comments assume that COVID-related impacts to our business in November and December are similar to what we're seeing in October.

We just started shipping iPhone 12 and 12 Pro and we are off to a great start. We are also excited to start pre-orders on iPhone 12 Mini and 12 Pro Max next Friday. Given the tremendously positive response, we expect iPhone revenue to grow during the December quarter despite shipping iPhone 12 and 12 Pro four weeks into the quarter, and iPhone Mini and 12 Pro Max seven weeks into the quarter. We expect all other products in aggregate to grow double-digits and we also expect services to continue to grow double-digits.

For gross margin, we expect it to be similar to our most recent quarters despite the cost associated with the launch of several new products. For OpEx, we expect to be between \$10.7 billion and \$10.8 billion. We expect OI&E to be around \$50 million and the tax rate to be around 16%. Finally, today, our Board of Directors has declared a cash dividend of \$0.205 per share of common stock, payable on November 12, 2020 to shareholders of record as of November 9, 2020.

With that, let's open the call to questions.

**Tejas Gala** {BIO 20432011 <GO>}



Thank you, Luca. We ask you that you limit yourself to two questions. Operator, may we have the first question please?

## Questions And Answers

### Operator

Certainly, we'll hear first today from Shannon Cross, Cross Research.

### Q - Shannon Cross {BIO 1891806 <GO>}

Thank you very much. Tim, can you talk a bit more about China? And in terms of linearity, I think, Luca, you'd mentioned that services in all regions was up at an all-time high. I'm not sure exactly what your comment was, but maybe give us a little idea of whether you're seeing any blowback or benefit from the Huawei situation and just dig a bit more into the trends you're seeing in China? And then I have a follow-up. Thank you.

### A - Tim Cook {BIO 14014370 <GO>}

Thanks, Shannon. If you look at China and look at last quarters, I'll talk about both last quarter and this quarter a bit. Last quarter, what we saw was our non-iPhone business was up strong double-digit for the full quarter. And then if you look at iPhone and you look at it in two parts, one pre-mid-September, which is pre- the point at which the previous year we would have launched iPhones, that period of time which was the bulk of the quarter iPhone was growing from a customer demand point of view, and of course, the -- not shipping new iPhones for the last two-week of September makes that number in the aggregate a negative. But the net is the underlying business in China last quarter was very strong and perhaps very different than you might think from just a quick look at the stated number.

In terms of this quarter, given the explanation for last quarter and the momentum that we've got and as importantly, given the initial data points that we see on iPhone 12 and iPhone 12 Pro, although we don't guide to revenue, as Luca said, I would tell you that we are confident that we will grow this quarter in China. And so we are very bullish on what's going on there. A little more color on last quarter, we had a much more significant inventory drawdown on the channel side than other regions, and so that is one reason why the numbers are different than other regions. And additionally, the new products in the year-ago quarter were a higher percentage of our iPhone sales than they were in other regions. So hopefully, that explains what's going on in China.

In terms of the market there, 5G is fairly advanced there. They're forecasting 600,000 base stations by the end of the year. And so we're entering the market at a very good time and with the reception that we've gotten so far, we are very confident there.

### Q - Shannon Cross {BIO 1891806 <GO>}

Okay, great. And then can you talk a bit about just overall in the world, the cadence that you see sort of the 5G adoption launch, what you see will be sort of the key drivers? Obviously, there is a fair amount of subsidies going on in the US at this point. Thank you.

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**A - Tim Cook** {BIO 14014370 <GO>}

Yeah. We're working hard to provide the best experience for our iPhone users. To do so, we've been collaborating closely with carriers all around the world to ensure iPhone has great throughput and coverage and battery and call quality. We've completed 5G testing so far on over 100 carriers in over 30 regions. And so, it's pretty pervasive around the world. But grantedly, it will continue to roll out in more places as carriers continue to expand their coverage. And this will happen every week. And so it's just going to get better. There are obvious places in the world where it's more ahead than in others, but we feel like we are entering at a sort of -- at exactly the right time. Thanks, Shannon.

**Q - Shannon Cross** {BIO 1891806 <GO>}

Thank you.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thank you. Can we have the next question please?

**Operator**

That will be from Jeriel Ong with Deutsche Bank.

**Q - Jeriel Ong** {BIO 19758244 <GO>}

Yeah, thank you so much. I guess I appreciate the guidance for revenues to grow. But I guess my question perhaps if I could is relative to seasonality. You guys over the last five years, your seasonality is typically up about 50% quarter-on-quarter. Do you think that you can beat that even with the later release? I have a follow-up.

**A - Luca Maestri** {BIO 15738533 <GO>}

So as I said, Jeriel, we're not providing a range for the reasons that I explained during my prepared remarks. So you need to keep in mind a couple of things that are unique about this quarter versus the past. And then I mention again, the launch timing of the phones is different from the past. So we're launching the new iPhones four weeks into the quarter for two models, for the 12 and 12 Pro, and seven weeks into the quarter for the other two, the iPhone mini and 12 Pro Max. So that is something to keep in mind as you think about growth rates.

With regard to all the other product categories, as I said, we are expecting to grow double-digits essentially across the board for the rest of our products and for services. And so we are incredibly optimistic about what we're seeing so far. Obviously, we started taking pre-orders five days ago and so it's a bit early for the phone, but we think that there are a lot of tailwinds this year for iPhone for the entire cycle. Some of the comments that Tim has already made, right, we've got the best lineup of iPhones that we've ever had. We've got an installed base of iPhone that is very large, continues to grow, it's at an all-time high. Obviously, 5G is once-in-a-decade opportunity. And as you've seen in some markets, certainly here in the United States, carrier offers are very aggressive and so that is

very good for consumers and ultimately very good for us. So very, very optimistic given what we've seen so far.

**Q - Jeriel Ong** {BIO 19758244 <GO>}

Awesome. Thank you so much for that context and giving us some of the levers to think about. I'd like to ask a little bit more of a strategic line, little bit longer-term in nature. I think one thing that is interesting about the Apple One bundle is a desire-to-bundle in the first place. I guess, I'm wondering and some investors have asked me this as well is that why wouldn't you also take that rationale perhaps to hardware, perhaps maybe AirPods and iPhone, or AirPods, Watch and iPhone. Because if it makes sense to bundle services, would it also makes sense to bundle hardware? And if that's not the case and other benefits of services bundling that don't necessarily translate to hardware bundling. Thanks.

**A - Tim Cook** {BIO 14014370 <GO>}

Yeah, we don't have anything to announce today on hardware bundle. But backing up a bit and we do view that people like to pay for their hardware or at least some substantial portion of it monthly. And so that's the reason that we have implemented instalments in our stores and online. And that's the reason you see in some of the channels too selling the hardware on a per month kind of basis. It -- that begins to look like subscription, perhaps to some buyers, because they're used to holding the phone for X period of time and then turning it over and using the residual value of that phone in a way that gives them a de facto kind of subsidy on a new phone. And so it -- there is something today in the market that works somewhat similar.

On the services side, we had customers coming to us and asking for an easier way to buy all of our services and we wanted to provide that. And we are looking forward to tomorrow to getting Apple One out there. Thank you for the question.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thanks, Jeriel. Can we have the next question please?

**Operator**

That will come from Katy Huberty with Morgan Stanley.

**Q - Katy Huberty** {BIO 6993997 <GO>}

Thank you. Good afternoon. New technologies, including the chips that support 5G put upward pressure on costs this year, but you managed to leave ASPs for iPhones relatively unchanged this product cycle. How should we think about the margin profile of iPhone 12 relative to past iPhone cycles?

**A - Luca Maestri** {BIO 15738533 <GO>}

Hey, Katy. Obviously, we don't provide any outlook at gross margin level for product categories. What I said in my prepared remarks, we expect gross margins in total for the company to be pretty much in line where we've seen during the last quarter, which

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obviously as you said it's very good, right, because we are offering the new phones at price points that are essentially unchanged. And we're taking a lot of new technology into the phones. The -- I would say the commodity environment is good. For the first time in many, many quarters, I don't have to say that foreign exchange is a headwind and getting into the quarter it is not going to be a factor during the quarter.

As we've made clear in our comments, we are bullish about our sales performance expectations. So we should be getting some leverage. And so I think that the gross margin dynamics are good and it's very good to see that we are able to offer so much more technology and still able to deliver the level of gross margins that I think investors are expecting.

**Q - Katy Huberty** {BIO 6993997 <GO>}

Okay. And shifting to the Services business, this isn't dependent on certainly any one service, but licensing and other historically has been a driver of growth, that's where the ad-based revenue comes in. When you think about the Google antitrust pressure, what's the risk that you see some shrinkage in your licensing and other segment within Services and do you see opportunities for other services to make up for any potential weakness?

**A - Tim Cook** {BIO 14014370 <GO>}

We've got -- Katy, as you know, we've announced a number of services over the last couple of years. And we are ramping those between Apple TV+ and Apple News+ and Apple Arcade. We've got Apple Card. We've got Apple Fitness+ coming. We've got a number of services that have been launched a bit longer that are doing really well from the App Store to iCloud. And so there is a lot of room there and potential there. I have no idea how the DOJ suit will go, but I think it's a long way from a conclusion on it.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thanks, Katy. Can we have the next question please?

**Operator**

That will come from Evercore's Amit Daryanani.

**Q - Amit Daryanani** {BIO 7113568 <GO>}

Thanks for taking my question. I guess I have two as well. First off, Tim, on iPhones, you talked about the iPhone installed base I think being the highest and largest it's ever been, satisfaction rate is obviously pretty high. And our data would suggest replacement cycles are getting elongated. And if I take all of that together along with the fact that if iPhone users are like me with embarrassingly high weekly usage rate, does that in aggregate give you better confidence, better clarity that could enter an extensive period of iPhone revenue growth versus what we've seen in the last couple of years?

**A - Tim Cook** {BIO 14014370 <GO>}

We are very bullish on this cycle, very bullish on it. Because as I sort of step back from it and look at what we've now done, we have -- for the first time ever, we've launched four

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iPhones and there is an iPhone for everyone there. And it is the strongest lineup we've ever had by far. We have -- we do have a very large loyal and growing installed base. And we're also reaching out to switchers. And so I'm very optimistic there. We've got a once in a decade opportunity with 5G. There is a lot of excitement around 5G. And we've got some aggressive offers in the marketplace. And so, when I think about all of those, I'm really -- and I look at the initial data points that we've got on the iPhone 12 and the 12 Pro, we are off to a great start.

**Q - Amit Daryanani** {BIO 7113568 <GO>}

Got it. And I guess, Luca, I had a follow-up for you on the Services gross margin, which has kind of continued to move higher rather nicely. I mean, do you think these levels at 67% essentially are sustainable and what do you think are the two or three factors that are enabling these gross margins to remain here as we go forward?

**A - Luca Maestri** {BIO 15738533 <GO>}

I mean, obviously, we are very pleased with the level of gross margins in services. As you said, they've been expanding almost 300 basis points on a year-over-year basis. The reason for that is, of course, that we are growing the Services revenue and therefore we're getting leverage on a lot of the services, right. Some of it, as explained in the past, we have a portfolio of services, they've got different margin profiles. And so sometimes depending on the mix of products we have -- we can see margin expansion through mix as well. And so -- but we're also launching new services that where we need to invest heavily upfront. And -- but we think we've been able to show, for example, this year that we've launched a lot of new services, made all the necessary investments and still being able to expand gross margin. So we feel quite confident about the trajectory that we have for services. And we're very, very happy to see the customer response to really all of them, because as we've mentioned earlier, I mean, we've seen revenue records across essentially every category and across the entire world, right. We've seen September quarter records in every geography around the world. So all the dynamics, all the levers that we have in the Services business are working very well right now. And that translates also into margin, of course.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thanks, Amit. Can we have the next question please?

**Operator**

We'll hear from Samik Chatterjee with JP Morgan.

**Q - Samik Chatterjee** {BIO 15496543 <GO>}

Hi. Thanks for taking the question. I just wanted to start off with the iPhone lineup here, particularly as you mentioned, the carrier subsidies that you're seeing mixed optimistic about iPhone sales. I think just looking at some other factors here, earlier in the year, you had mentioned that iPhone sales was seeing an uptake with stimulus checks going out to consumers, helping in the consumer spending overall here in the US. So as we see some delays here on that front, are you seeing anything change on the consumer spending

side? Is the macro impacting how you think about iPhone sales, particularly even with the new product lineup? And I have a follow-up. Thank you.

**A - Tim Cook** {BIO 14014370 <GO>}

It's prior to mid-September we were seeing double-digit growth in customer demand on iPhone. So there is a lot of momentum there. And there is a lot of momentum even much more so now given the launch of the 12 Pro and the iPhone 12. If you're asking whether it could have been even more with a different macro-spending environment, I believe the answer to be yes. But you can't run the experiment. And so I don't know for sure. But I suspect that just the COVID, in general, takes something off from a worldwide economic point of view.

**Q - Samik Chatterjee** {BIO 15496543 <GO>}

Okay. Got it. And if I can just follow up, Tim, just following up on that COVID discussion. We are potentially here looking at a second wave, right, and I think all companies are trying to prepare for that, which you discussed as well in your prepared remarks. But if you can share any kind of thoughts about how you're preparing in relation to either inventory levels or sourcing from the supply chain to prepare for any potential disruption like we had earlier this year?

**A - Tim Cook** {BIO 14014370 <GO>}

Well, we're doing everything we can do. But we're prioritizing safety first obviously. And so with our stores as an example, we've come up with a new concept that puts and essentially turns the store into an Express storefront. And we've implemented that in a number of places, where we believe it helps from the safety of our employee and the safety of the customer's point of view, but still allows for an interaction to take place.

And so we've also put a lot more people on the phones, because a lot of more people are reaching out to us in that way. And, of course, the online store has stayed up and running through the whole of this. I think if you take some of those, the channel is doing some similar things and then some different things as well. And so I think everybody to the best of their ability is putting in contingency plans and finding a way to adapt to the environment. But it is difficult to call and there is a level of uncertainty in it obviously. And that's what Luca was referring to earlier.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thanks, Samik. Can we have the next question please?

**Operator**

That will come from Krish Sankar with Cowen and Company.

**Q - Krish Sankar** {BIO 16151788 <GO>}

Yeah, hi. Thanks for taking my question. I had two of them. First one for Luca. I understand you don't want to give color on gross margin by product or segments. But Luca, you mentioned gross margins should be similar in December versus September, and Services

should grow about double-digits. There is a general view that on the iPhone side, the BoM cost would be a headwind for gross margin, but carrier subsidies would be a tailwind. So I'm kind of curious how should we think about the different gross margin levels into December quarter? And then I have a follow-up for Tim.

**A - Luca Maestri** {BIO 15738533 <GO>}

Yeah. And so, typically during the December quarter, we have positive factors, because we have the typical seasonal leverage, right, sequentially as we go from September to the holiday season. And we also had an improved mix between products particularly this year, as you know, we've launched a new iPhone. At the same time, you shouldn't forget that we have launched a lot of new products during the last several weeks. We launched four new models of iPhone. We launched new models of Apple Watch, new models of iPads. And so clearly, every time we launch a new product, the cost structure is higher and so that is going to be the other side of the coin. But we think that those two things should balance out. And again as I was saying earlier, (technical difficulty)

**Q - Krish Sankar** {BIO 16151788 <GO>}

(technical difficulty) Luca, and then a follow-up for Tim. And Tim, kind of surprised you didn't say a lot about the payments ecosystem in this prepared comments. Kind of curious to find out from your vantage point how you think of your whole payment ecosystem including Apple Card, Apple Pay, Apple Cash and how you're disaggregating the whole FinTech environment?

**A - Tim Cook** {BIO 14014370 <GO>}

Thanks for the question. There is just a limited number of things I can talk about and that's the reason I didn't talk about it. We are -- we continue to be very enthusiastic about the whole payment services area. Apple Card is doing well and Apple Pay is doing exceptionally well. As you can imagine in this environment, people are less want-to-hand-over-a-card. So this contactless payment has taken on a different level of adoption and that I think will never go back. The US has been lagging a bit in contactless payment. And I think that the pandemic may well put the US on a different trajectory there. And so we are very bullish about this area and view that there are more things that Apple can do in this space, and so it's an area of great interest to us.

**Q - Krish Sankar** {BIO 16151788 <GO>}

Thanks, Tim.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thanks, Krish. Can we have the next question please?

**Operator**

That will come from Kyle McNealy with Jefferies.

**Q - Kyle McNealy** {BIO 21065231 <GO>}

FINAL

Hi. Thanks for taking the question. I wanted to ask a little bit about the supply chain, given your latest start for manufacturing for the flagship iPhone lineup this year. Do you think that supply will be able to meet demand through the end of the calendar year? And are there any component shortages that you're seeing? Or are there any actions that you can take to increase weekly output versus last year? Thanks.

**A - Tim Cook** {BIO 14014370 <GO>}

Yeah, Kyle, I don't know if you're talking about iPhone in particular. But if you look at iPhone, we are constrained today. And that's not a surprise we're at the front end of the ramp, if you will. And how long we will be supply-constrained, it's hard to predict. I mean, we haven't taken orders yet for the iPhone 12 mini or Pro Max either. And so those are coming and so we shall see. But right now we are supply-constrained. We are also supply-constrained for avoidance of any confusion. We're supply constrained on Mac. We're supply-constrained on iPad. And we're supply-constrained on some Apple Watches as well. And so we have a fair number of areas right now of focus and we're working really, really hard to remedy those as quickly as we can. But at this point, I can't estimate when we will be out of that.

**Q - Kyle McNealy** {BIO 21065231 <GO>}

Okay, great. Thanks a lot. And then switching to Mac and iPad. How do you think about the durability of the strength you're seeing there with Mac and iPad? Is there any potential for stronger than seasonal pullback after the strong back-to-school season and holiday season? And the supply constraints make it feel like there is a good chance for continuation of the stronger demand trends and flow through of that. What should we think about the seasonality into the December and March quarter being more positive and seasonal or less positive and seasonal? Thanks.

**A - Tim Cook** {BIO 14014370 <GO>}

Yeah, we placed our thoughts in the color that Luca provided when he said that all products, excluding iPhone, all products and services excluding iPhone -- or all products rather excluding iPhone would grow in the double-digits. And so we continue to be bullish on what Mac and iPad can do. I think the moves that have taken place to remote learning and remote work are not going to go back to normal. Normal will become something different. Because I think people are learning that there are aspects of this that work well. And so I don't believe that we're going to go back to where we were. And I think that means that iPads and Macs are even more important in those environments.

The growth in both of these last quarter were phenomenal. As you can tell from your data sheet with Mac at 29% and iPad at 46%, these are tremendous numbers. And as Luca said, the September quarter was the all-time high for Mac in the history of the company, and by -- not by a little bit, by \$1.6 billion. And so it was a substantial difference. Now, we did have a aggressive promotion for college students that were going back to school. And so that was invariably part of it. But I think the other part of it, the remote work thing is not something that's going to step back to the way it used to be any time soon.

**Q - Kyle McNealy** {BIO 21065231 <GO>}

Great. Thanks very much.



**A - Tim Cook** {BIO 14014370 <GO>}

Yeah.

**A - Tejas Gala** {BIO 20432011 <GO>}

Thank you. Can we have the next question please?

**Operator**

That will come from Chris Caso with Raymond James.

**Q - Chris Caso** {BIO 4815032 <GO>}

Yes, thank you. I guess, first question is on iPhone pricing and there were some changes in the iPhone price stack this year. The iPhone -- the pricepoint for iPhone 12 moved up a bit and I guess the difference, the gap between 12 and 12 Pro is smaller. And I guess that's after you made some adjustments years prior where the pricepoints came down a bit. Can you talk through the thought process behind that and the potential implications for either unit elasticity or blended ASP as a result of the price changes?

**A - Tim Cook** {BIO 14014370 <GO>}

Well, the iPhone 12 family starts at \$699 in many places. Because you can get -- and the deals that people are really paying are very different than that, because a lot of people, particularly in this country, but also in several of the other countries in the world connect to a carrier plan. And of course, those offers are much more aggressive. And so the price that our customer is paying is probably the most important one. The iPhone 12 is at \$799. And so I think what you're saying is there is a \$200 difference there. But I would guess that people are viewing it more as a \$300 difference between the 12 Mini and 12 Pro. And so we'll see what the mix turns out.

Right now, we have no data other than 12 and 12 Pro. We lack the data on the 12 mini and the Pro Max, because we're not taking orders yet. But what we try to always do in pricing is give the customer a great value. And I feel like we really did that this year, and that's despite, as mentioned earlier, all of the extra features that we placed into the phones including 5G. Thanks for the question.

**Q - Chris Caso** {BIO 4815032 <GO>}

Okay. As a follow-up, you mentioned some of the carrier incentives we've seen here in the US. If you could provide some more color about that, about what you're seeing now. And obviously as we went through years ago the incentives from carriers were a lot larger. Does this mark some shift in the approach of carriers as we're moving into 5G? What's the extent of the permanence of some of these incentives? And then as 5G rolls out around the world into other geographies, is this something we should expect that as either they try to protect from switchers or kind of promote the 5G networks, we'll see a higher prevalence of incentives from carriers as we go forward?

**A - Tim Cook** {BIO 14014370 <GO>}

FINAL

I don't want to speak for our carrier partners, that would be up to them to talk about their plans. Generally, I think it's too -- the vast, vast majority of carriers around the world to their -- in their interest to move customers to 5G. And I think it's in the customers' interest to move to 5G. And obviously, we like that as well. And so I think you have a situation where everyone is rowing in the same direction. And that's a very different kind of situation than normally we would have. And so it is one of the things as I alluded to earlier that makes me very bullish. Only point though, the other things are very important to the size of the installed base. The product lineup, I mean, these things are critically important as well.

## **A - Tejas Gala** {BIO 20432011 <GO>}

Thank you, Chris. A replay of today's call will be available for two weeks on Apple podcasts as a webcast on [apple.com/investor](https://apple.com/investor) and via telephone. The numbers for the telephone replay are 888-203-1112 or 719-457-0820. Please enter confirmation code 9501153. These replays will be available by approximately 5:00 PM Pacific Time today. Members of the press with additional questions can contact Kristin Huguet at 408-974-2414. Financial analysts can contact me with additional questions at 669-227-2402. Thank you again for joining us.

## **Operator**

And again, that does conclude today's conference. Thank you all for joining us today.

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