

Q2 2020 Earnings Call

Company Participants

- Luca Maestri, Chief Financial Officer and Senior Vice President
- Tejas Gala, Corporate Finance and Investor Relations
- Timothy D. Cook, Chief Executive Officer and Director

Other Participants

- Amit Daryanani, Analyst
- Chris Caso, Analyst
- Jeriel Ong, Analyst
- Katy Huberty, Analyst
- Samik Chatterjee, Analyst
- Shannon Cross, Analyst
- Wamsi Mohan, Analyst

Presentation

Operator

Good day, everyone. Welcome to the Apple Incorporated Second 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 the call over to Mr. Tejas Gala Senior Manager, Corporate Finance and Investor Relations. Please go ahead.

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'll be followed by CFO, Luca Maestri. After that, we'll open the call to questions from analyst.

Please note that some of the information you'll hear during our 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. Actual results or trends could differ materially from our forecast.

For more information, please refer to the risk factors discussed in Apple's most recently filed periodic reports on Form 10-K, and Form 10-Q 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.

Timothy D. Cook {BIO 14014370 <GO>}

Thanks, Tejas. Good afternoon, everyone. Thanks for joining us today. I hope you are staying safe and well. Today Apple reports \$58.3 billion in revenue, an all-time record for services and a quarterly record for Wearables, Home and Accessories. It was also a quarterly revenue record for Apple Retail, powered by phenomenal growth in our online store, amid the most challenging global environment in which we've ever operated our business, we are proud to say that Apple grew during the quarter.

But before we dive more deeply into the numbers, I want to speak just for a bit on COVID-19. This is something Apple has been contending with since January, and I think that how we have responded, what we have been inspired to do tells an important story about Apple's great durability as a business and the enduring importance of our products in our customers' lives.

It also speaks to Apple's unmatched capacity to be creative to think always in terms of the long-term and to forge ahead when others may feel an instinct to pull back. Before COVID-19 was on the horizon, we anticipated that Q2 was going to be a prolific and energetic period for Apple. And when the pandemic did strike our teams not only succeeded in growing the business, in introducing powerful new products and in meeting our customers' needs but they also rose to the occasion in terms of meeting our broader obligations to the communities in which we live and work.

Let's look quickly across the business. At the same time that they were leaving no stone unturned to get our latest generation of devices manufactured and into our customers' hands, our worldwide network of supply chain partners, logistics and operations folks in every part of the company were also sourcing more than 30 million masks for front-line medical workers ensuring they are donated to places of greatest need in every region around the world.

While our product teams were preparing to launch of new iPad Pro, Magic Keyboard, MacBook Air and the new iPhone SE, all of which have been very well received by reviewers and consumers alike, they were also working with our suppliers to design, test, manufacture and distribute more than 7.5 million face shields and we continue to ship more than \$1 million of these every week to the doctors, nurses and medical personnel on the front lines.

In a quarter, where our Services teams achieved strong growth which Luca will dig into in a minute and which speaks to the real durability of our services strategy these teams were also putting COVID-19 front and center. As Apple News reached 125 million monthly active users, we elevated trusted information from reliable sources through a special

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COVID-19 vertical. We let customers skip payments without incurring interest on Apple Card from March and April in light of financial hardship for many families.

We worked with everyone from Oprah to Lady Gaga to inform, entertain and get back through Apple TV and services like Face Time and messages set new all-time records for daily volume during this quarter as users rely on their devices to stay connected in a new reality. In software, at the same time did our teams work with great creativity and excitement as we prepared to deliver our first ever all online Worldwide Developers Conference later this quarter, they also worked with the same creativity and speed to put together our COVID-19 symptom checking website and app in partnership with the CDC.

As of today, the app has been installed nearly 2 million times and the web tool has received over 3 million unique visits. And just this month to accelerate contact tracing we are launching a joint effort with Google to enable to use Bluetooth technology to help governments and health agencies spread the -- reduce the spread of the virus with user privacy and security central to the design.

We paired these programmatic efforts with our broader strategy to get back to who need it most. We've made major corporate donations to response efforts around the world to support global citizens, as well as a new fund for Americans experiencing food insecurity as a result of the crisis. When you tally these things up and consider our ongoing two-to-one match for employee donations, Apple's contributions to the global response are significant, diverse and a great source of pride for the whole team.

We're also doing what we can to help our employees, their families and by extension their communities stay safe and well by modifying our operations where appropriate. This extends, of course, to our retail employees. They are Apple's face to our customers and an instrumental part of our business and we're compensating them normally despite store closures.

During the quarter, where circumstances evolved by the hour, we have been gratified by the resilience and adaptability of our global supply chain. While we felt some temporary supply constraints in February, our operations team, suppliers and manufacturing partners have been safely returning to work and production was back at typical levels towards the end of March.

At this time of social distance, of shuttered schools and gathering places, of delayed plans and new ways of socializing, we have seen significant evidence that our products have taken a renewed importance for our customers. Teachers and students around the world are relying on our technology to teach, learn and stay connected with each other. We are in the process of deploying major orders of iPads to school systems working to keep learning going strong at a distance including tens of thousands in Ontario, Canada, Glasgow, Scotland and Puerto Rico 100,000 to the City of Los Angeles and 350,000 to New York City, our largest educational iPad deployment ever.

Since early March, we've seen unprecedented demand for pro apps from students, enthusiasts and creative professionals. These folks are keeping us all entertained and

inspired as we stay at home and to help them do it we made Final Cut Pro X and Logic Pro X available for free for 90 days for everyone and the reaction has been overwhelming driving software downloads and usage to record levels.

And doctors and medical professionals are making even greater use of Apple Watch and other health features to communicate with patients and to treat them safely from a distance when necessary. With new FDA guidance on non-invasive remote patient monitoring for example, the ECG app on Apple Watch is increasingly being used to facilitate remote ECG measurements and recordings for telemedicine usage reducing patient and healthcare provider contact and exposure.

Many hospitals such as Geisinger Health System, NYU Langone Health and Stanford Healthcare are using apps on iPad and iPhone to support communication and video conferences between hospitalized patients and their care teams. This enables the care teams to keep a close watch on patients without entering isolation rooms, which helps to minimize exposure and reduces some of the need for personal protective equipment.

Now, when you step back and tally all this up, when you consider all the ways COVID-19 has touched Apple, our customers and the way we work this may not have been the quarter it could have been absent this pandemic. But I don't think I can recall a quarter where I've been prouder of what we do or how we do it.

As I said at the outset, we achieved revenue of \$58.3 billion and underneath that was product revenue of \$45 billion. The performance of our product business had three very different phases during the March quarter. Based on Apple's performance during the first five weeks of the quarter, we were confident we were headed toward a record second quarter at the very high end of our expectations.

In the next five weeks of the quarter, as COVID-19 started impacting China iPhone supply was temporarily affected, as well as demand for our products within China. This caused us to withdraw our revenue guidance in February. At that point, demand for our products outside of China was still strong and in line with our expectations.

During the last three weeks of the quarter as the virus spread globally and social distancing measures were put in place worldwide, including the closure of all our retail stores outside of Greater China on March 13, and many channel partner points of sales around the world, we saw a downward pressure on demand particularly for iPhone and wearables.

Given the lack of visibility and certainty in the near term, we will not be issuing guidance for the coming quarter. Over the long term though, we have a high degree of confidence in the enduring strength of our business. Our global supply chain is profoundly durable and resilient. We have shown the consistent ability to meet and manage temporary supply challenges like those caused by COVID-19.

We have continued to deliver innovative new products across multiple categories that appeal to a broad cross-section of customers, including the all-new iPhone SE which

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achieved unmatched technological capacity at an incredible value. Our teams worldwide have tackled the complexities of this moment with unmatched creativity, good humor and dedication to our customers. For a company whose business is innovation, there are real upsides and periodically having to figure out how to do just about everything in a brand new way.

Our long-running investment in our services strategy is succeeding. This business is growing and is a reflection of our enduring large and growing installed base. We expect to meet our long-standing goal of doubling our fiscal 2016 Services revenue in 2020. We have always run Apple for the long term. We entered this period with unmatched financial strength, a robust cash position and our best product pipeline ever.

Major investments, including our five-year commitment to contribute \$350 billion to the economy here in the United States are moving forward full speed ahead. It's in these moments that we set ourselves apart. We've always managed through difficult moments by doubling down and investing in the next generation of innovation and that's our strategy today.

And so while we can't say for sure how many chapters are in this book, we can have confidence that the ending will be a good one. Apple will continue to do everything we can do to help the global response and to keep our customers learning, creating, sharing and connecting so that life can remain as normal as it can during this challenging time.

With that I'll hand things off to Luca.

Luca Maestri {BIO 15738533 <GO>}

Thank you, Tim. Good afternoon, everyone. It has been a very different quarter than we were expecting when we last talked to you at the end of January. But we could not be more proud of our Apple teams around the world, our role in supporting local communities and our partners throughout the value chain and how resilient our business and financial performance has been during these challenging times.

So, the revenue for the quarter was \$58.3 billion, up 1% from a year ago despite the extreme circumstances from the impact of COVID-19 and a headwind of 100 basis points from foreign exchange. Products revenue was \$45 billion, down 3%. After a very strong January, our performance was impacted particularly during the last three weeks of the quarter where lock downs and point of sale closures increased due to COVID-19 spreading around the world and affected our product sales. However, on a demand basis our performance was stronger than our reported results as we reduced iPhone channel inventory more than we did a year ago.

Importantly, our installed base of active devices reached an all-time high in all of our geographic segments and all major product categories. Services revenue followed a different trend with very strong year-over-year growth of 17%. We set a new all-time revenue record of \$13.3 billion with all-time records in many of our services categories and in most countries we track. I'll provide more details on this later.

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Company gross margin was 38.4% flat sequentially with cost savings and mix shift toward services, offset by the seasonal loss of leverage. Products gross margin was 30.3% decrease in 380 basis points sequentially due to loss of leverage and unfavorable mix. This drop was more pronounced than under normal circumstances, due to the COVID-19 impact I mentioned earlier.

Services gross margin was 65.4%, up 100 basis points sequentially driven by favorable mix. Our reported tax rate for the quarter was 14.4%. This was lower than our 16.5% guidance due to one-time discrete items. Net income was \$11.2 billion and earnings per share were \$2.55, up 4%. Operating cash flow was very strong at \$13.3 billion, an improvement of \$2.2 billion over a year ago.

Let me get into more detail for each of our revenue categories. iPhone revenue of \$29 billion declined 7% year-over-year as both iPhone supply and demand were affected by the impact of COVID-19 at some point during the quarter. On the supply side, we suffered from some temporary supply shortages during February. But we've been extremely pleased with the resilience and adaptability of our global supply chain as well as its ability to get people back to work safely when circumstances allow.

Our operations team and manufacturing partners put forth an extraordinary effort to restore production quickly and we exited the quarter in a good supply position for most of our product lines. On the demand side, after a very strong first five weeks, we saw the impact of COVID-19 affect demand in China for the next five weeks, and then more broadly around the world for the last three weeks of the quarter, when lock downs and point of closures became more widespread in many countries.

While we did see a slight elongation in our replacement cycle towards the end of the quarter, which we attribute to the widespread point of sale closures, our active installed base of iPhones has reached an all-time high. This speaks to the quality of our products and the strength of our ecosystem. In fact in the US, the latest survey of consumers from 451 Research indicates iPhone customer satisfaction of 99% for iPhone 11, 11 Pro and 11 Pro Max combined.

Turning to Services, we set an all-time revenue record of \$13.3 billion. We had strong performance across the board with all-time revenue records in the App Store, Apple Music, Video, cloud services and our App Store search ad business and we also set a March quarter record for Apple care. Our new services Apple TV plus, Apple Arcade, Apple News Plus and Apple Card continued to add users, content and features while contributing to overall Services growth.

As Tim mentioned, we are well on our way to accomplishing our goal of doubling our fiscal '16 services revenue during 2020. App Store revenue grew by strong double-digits, thanks to robust customer demand for both in-app purchases and subscriptions. Our third-party subscription business grew across multiple categories and increased over 30% year-over-year, reaching a new all-time high.

Our first-party subscription services also continue to perform very well. Apple Music and cloud services both set all-time revenue records and Apple care set the March quarter record. Paid subscriptions for all three of these services were up strong double-digits. Customer engagement in our ecosystem continues to grow strongly and the number of both transacting and paid accounts on our digital content stores reached a new all-time high during the March quarter.

In particular, the number of paid accounts increased double-digits in all of our geographic segments. We now have over 515 million paid subscriptions across the services on our platform, up 125 million from a year ago. On a sequential basis paid subscriptions grew by over 35 million, this is the highest sequential growth we have ever experienced. With this momentum, we are confident we will reach our increased target of 600 million paid subscriptions before the end of calendar 2020.

Wearables, Home and Accessories established a new March quarter record with revenue of \$6.3 billion, up 23% year-over-year with strong double-digit performance across all five geographic segments. Our Wearables business now the size of a Fortune 140 company and we're very excited by the many opportunities in front of us for this product category. For example, Apple Watch continues to extend its reach that's over 75% of the customers purchasing Apple Watch around the world during the quarter were new to the product.

Next I'd like to talk about Mac and iPad. Mac revenue was \$5.4 billion, iPad revenue was \$4.4 billion. Towards the end of the quarter, we launched a brand new iPad Pro that includes a first-in-class LIDAR scanner with some really exciting augmented reality applications. And MacBook Air with significantly improved performance at a lower price. We're very pleased with the strong customer interest for both products.

Importantly, around half of the customers purchasing Macs and iPads around the world during the quarter were new to that product and the active installed base for both Mac and iPad reached a new all-time high. And the most recent surveys of consumers from 451 Research measured customer satisfaction at 95% for iPad and 96% for Mac.

In the enterprise market business is everywhere have been making the transition to working remotely. We've created content to assist our customers in this transition, including and on-demand video learning series focused on topics like remote deployments of iPads and Macs and security. We have also realigned our own retail business and enterprise teams to provide timely and relevant support to customers as they navigate new work environments.

Some of our largest customers offering Mac to employees, such as IBM and SAP have been able to pivot quickly to allow employees to easily set up and secure their devices for home, benefiting from Apple Business Manager and Zero Touch deployment. And we've seen countless examples of new projects and remote deployments implemented in just a few hours.

Peloton, for instance, worked with our New York teams to deploy an entire fleet of Macs overnight, so their team could work remotely. In essential sectors such as grocery and

financial services we've seen organizations adopt our technology to better serve their customers safely. Leading grocers around the world like Trader Joe's, Woolworths, Larson's, Sainsbury's, Lidl and Carrefour offer Apple Pay so customers can use contactless payments. And a store shift to become fulfillment centers for online orders organizations are leveraging apps for remote shoppers and food delivery to reduce foot traffic.

In banking where safety and security is a top your priority, one way to protect company and client information is by providing corporate iOS devices to employees who use mobile phones daily as part of their jobs. As an example Bank of America is purchasing tens of thousands of additional iOS devices for their workforce.

Let me now turn to our cash position. First I want to note that liquidity has not been an issue for us during this highly unusual financial market conditions. We have an extraordinarily strong balance sheet, very deep access to capital markets and unmatched free cash flow generation. We ended the quarter with \$193 billion in cash plus marketable securities, total debt of one \$110 billion. And as a result, net cash was \$83 billion at the end of the quarter.

We returned \$22 billion to shareholders during the March quarter, including \$18.5 billion through open market repurchases of 64.7 million Apple shares and \$3.4 billion in dividends and equivalents. Finally, as we move ahead into the June 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.

As Tim mentioned, given the lack of visibility and certainty in the near term, we will not be issuing guidance for the coming quarter. However, based on what we have seen in April and how we think things might play out, I would like to provide some additional insight on headwinds and tailwinds we are facing.

From a foreign exchange standpoint, the US dollar has appreciated recently against most currencies around the world. And as a result, we expect our revenue to be negatively impacted by more than \$1.5 billion on a year-over-year basis. Our global supply chain is back up and running, we are in a typical supply position including our usual ramp associated with new products recently launched. These newly launched products iPad Pro, MacBook Air and iPhone SE have all received outstanding customer response even during these extreme circumstances.

On iPhone and Wearables, we expect the year-over-year revenue performance to worsen in the June quarter relative to the March quarter. On iPad and Mac we expect the year-over-year revenue performance to improve in the June quarter. On Services, we are seeing two distinct trends. First, customers are actively engaging with our ecosystem and digital services and we believe the very strong recent performance in the App Store, video, music and cloud services will continue throughout the June quarter.

Second, due to the overall reduced level of economic activity due to the lock-downs around the world services like Apple care and advertising have been impacted. Apple care is comprised of our product repair business and the warranty agreements with our

customers, both of which have been obviously affected by store closures, and reduced level of customer traffic.

Advertising, which is comprised of third-party agreements, our App Store search ads and Apple News ads has been impacted by overall economic weakness and uncertainty on when businesses will reopen. For gross margin sequential headwinds include foreign exchange, the mix within products and the seasonal loss of leverage on our product business. Foreign exchange will have a 70 basis points impact sequentially and 130 basis points impact year-over-year.

Regarding product mix. Keep in mind the commentary we provided at the revenue level. Sequential tailwinds include cost savings and the mix shift towards services. With regard to capital allocation, our approach remains unchanged. We continue to invest confidently in our future, while also returning value to our shareholders. We are in the midst of developing our most exciting pipeline of products and services ever, while contributing over \$350 billion to the US economy and expanding our footprint in many cities around the country over a five-year period.

We also continue to believe that there is great value in our stock and we are maintaining our target of reaching a net cash neutral position over time. As a testament to the confidence we have in our business today and into the future, our Board has authorized \$50 billion for share repurchases in addition to the over \$40 billion authorization remaining under the current share repurchase plan.

Our Board has also authorized a 6% increase in our quarterly dividend and today declared a cash dividend of \$0.82 per share of common stock, payable on May 14, 2020, to shareholders of record as of May 11, 2020. Finally and most importantly, we are managing Apple for the long term, as we've always done. During uncertain times historically, we have continued to invest in the business and this remains our philosophy. We will continue to stay focused on what we do best, investing in our product and service pipeline, managing the business wisely and taking care of our teams and believe we will come out from this stronger.

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

Tejas Gala {BIO 20432011 <GO>}

Thank you, Luca. We asked that you limit...

Operator

Thank you.

Tejas Gala {BIO 20432011 <GO>}

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

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Questions And Answers

Operator

Yes, that will come from Shannon Cross, Cross Research.

Q - Shannon Cross {BIO 1891806 <GO>}

Thank you very much for taking my question. And I hope everyone is well. Tim, you talked about seeing some improvement in the second half of April. So I was wondering if you could just talk maybe a bit more on the segment geographic basis what you're seeing in the various regions that you're selling in and what you're hearing from your customers? And then I have a follow-up. Thank you.

A - Timothy D. Cook {BIO 14014370 <GO>}

Sure. Shannon. If you look at -- I'll start with China, if you look at what happened in China, we were having a really good January, the lock downs started there towards the end of January as you know, February we saw a steep decline in demand, we closed our stores in February as the lockdown completed in mid-February towards the second half of February, we began to open stores. We reopened it on a staggered basis that took about 30 days until mid-March.

And from a demand point of view, we saw then an improvement in March over February. And if you look at kind of where we are today, we've seen further improvement in April as compared to March. And so that's China. If you look at the rest of the world, we were doing great in January, the first five weeks of the quarter and we do believe that we were headed towards the sort of the top end of our expectations that we had talked to you about on the last call. That the next five weeks were spent sort of reacting and getting the supply chain back up in full force and working through the sharp decline in China that I already talked about.

The real thing for the rest of the world happened in March when the shelter-in-place orders went in and the work from home began. For those two, three weeks period at the end of the quarter, we saw a sharp decline in demand. If you now step out into April and look at that early April started like the end of March. But in the second half of April, we've seen an uptick across -- really across the board. It's not, just related to a certain geo or a certain product.

We think by looking at it, a part of it is due to just our new products, a part of it is due to the stimulus programs taking effect in April and then a part of it is probably the consumer behavior of knowing, this is going to go on for a little while longer and getting some devices and so forth lined up to work at home more. In particular for, as I think Lucas shared, we believe that iPad and Mac are going to improve on a year-over-year basis during this quarter and that's customers that are either taking online education or working remotely.

And so complex answer to your question, but that's what we're seeing.

Q - Shannon Cross {BIO 1891806 <GO>}

Thank you. That was helpful. Luca, if I missed that, you talked about various puts and takes in the quarter but didn't really discuss operating expenses. I know you mentioned some cost savings on the COGS line. I'm curious how you're thinking about your spending in OpEx, given some of the macro challenges that you may be facing? Thank you.

A - Luca Maestri {BIO 15738533 <GO>}

Yes, well, Shannon, as we said, we manage the company for the long term, right? So we know that the core of the business, the core of the company is innovation and product and services developments. So we will continue to invest in our pipeline. We're very excited about what we have in store. And so we will continue to invest there.

Obviously, we are aware of the environment and so we will manage the SG&A portion of the company tightly. We are making new investments in the new services that we launched recently, we -- as you know we purchase the baseband activities from Intel and obviously we want to develop that technology because we consider it's a core technology for us. And so we would try to balance the need to continue to invest during difficult circumstances and the fact that we like to manage the business wisely.

A - Tejas Gala {BIO 20432011 <GO>}

Thank you, Shannon.

Q - Shannon Cross {BIO 1891806 <GO>}

Thank you.

A - Tejas Gala {BIO 20432011 <GO>}

Can we have the next question, please?

Operator

That will be from Wamsi Mohan with Bank of America.

Q - Wamsi Mohan {BIO 15994435 <GO>}

Yes. Thank you. Tim, I think I speak for everyone on the call that we're all very appreciative of Apple's contribution during this pandemic we all appreciate it.

A - Timothy D. Cook {BIO 14014370 <GO>}

Thank you very much for that.

Q - Wamsi Mohan {BIO 15994435 <GO>}

Tim in past downturns, we have not really seen Apple pull back from investing and you as a company have largely maintained the product introduction cadence, but given these are unprecedented times and there are a lot of challenges associated with product

development during a time when you have a global footprint for such activities and unable to really do a lot of things in person. How should we think about the product development and introduction cadence as we go over the next several quarters? And I will follow-up.

A - Timothy D. Cook {BIO 14014370 <GO>}

We're continuing to operate. And so as you can tell, along with everything else going on, we were able to launch and ship the iPhone SE, the iPad Pro with the Magic Keyboard and the MacBook Air. And so the business continues and the new products are our lifeblood and so we are continuing to work, everybody is getting used to the work at home in some areas of the company people maybe even more productive in some other areas they're not as productive and so it's a mix depending upon what the roles are.

But as you can tell from what we did this quarter, despite the environment, we have our head down and are working because we know that our customers want the products that we've got. They are even more important in these times.

Q - Wamsi Mohan {BIO 15994435 <GO>}

Thank you, Tim. As a follow-up, I know you're doing a lot with both the Apple Card and financing plan for iPhones to get your products in the hands of customers, but I was wondering, would you consider using the strength of your balance sheet, maybe a little differently, structure may be deferred payments or things like that and? Or do you think that there could be other steps like bundling that you will consider versus what you already currently do? Thank you.

A - Timothy D. Cook {BIO 14014370 <GO>}

Well, as you know, we launched the payment plan earlier on Apple Card for iPhone. We are working on doing that for other products as well and you will see something on that shortly. So we're very focused on the affordability point. The trade-in programs also are fairly wide across the board and act as both something great for the environment also something great from a way to get that entry price down.

In terms of deferred payments nothing to announce today. But as you know, having access to the card at least in the United States gives us more degrees of freedom. And that is not using our balance sheet, it's -- but we play a key role in deciding what kind of programs go with the card.

A - Tejas Gala {BIO 20432011 <GO>}

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

Operator

That will come from Morgan Stanley's Katy Huberty.

Q - Katy Huberty {BIO 6993997 <GO>}

Thank you for the question. I hope the whole team is staying healthy and safe. Tim, I want to start on a longer-term question, where do you see structural changes on the back of this health crisis that might present opportunities for new revenue streams at Apple and I'm particularly thinking about your past comments on health and augmented reality, but I'm sure there's even more areas of inspiration and creativity coming out of the company? And then I have a follow-up.

A - Timothy D. Cook {BIO 14014370 <GO>}

I think there are things from -- just a great reminder of how important our products are in the -- for remote work and it's pretty clear to me that where things will get a lot closer to normal than they are today. Obviously, I think many people are finding that they can learn remotely and so I suspect that trend will accelerate some. I think that's probably also true about working remotely on in some areas in some jobs.

And so I think we have significant solutions and products for those -- for all of those groups. On the health area, I gave some examples in my opening comments about the ECG being used on the Watch. You can bet that we're looking at other areas in this, we were already doing that because we view that area was a huge opportunity for the company and a way for us to help a lot of people. And so you will see us continue on that. I wouldn't say that the health door opened wider. I would say it was already opened fairly wide.

Q - Katy Huberty {BIO 6993997 <GO>}

Okay. And then as a follow-up. The \$50 billion share repurchase authorization is impressive enough absolute terms, but it is a bit lower than the last couple of years. So just any context around the thought process of landing on \$50 billion? And then related to that, you have one of the strongest balance sheets in the world. Does the current environment change your thinking at all around M&A opportunities?

A - Luca Maestri {BIO 15738533 <GO>}

Well, let me answer that, Katy. First of all on the buyback, as I said, in general our approach to capital allocation has remained the same for the last several years and it's not changing now. Keep in mind here we're talking about just the authorization, right? And when you look at our actual results at the end of every quarter, you see how much we actually do in terms of share repurchases.

The \$50 billion is in addition to over \$40 billion that is still remaining from the past authorization that we received from our Board, right? So, it's the total available or outstanding in terms of authorization is over \$90 billion. And as you look at our run rate during the last several years you know that is very adequate amount. And as you know, we will provide an additional update a year from now. So nothing really has changed there and nothing has changed on our approach for M&A. We've been quite active over the last several years. We purchased companies on a very regular basis. We're always looking for ways to accelerate our product roadmaps or fill gaps in our portfolio both on the hardware side, on the software side, on the services side. So we will continue to do that. And so -- also on the M&A front, nothing has changed.

Q - Katy Huberty {BIO 6993997 <GO>}

Thank you. Be well.

A - Luca Maestri {BIO 15738533 <GO>}

Thank you.

A - Tejas Gala {BIO 20432011 <GO>}

Thanks, Katy, can we have the next question, please?

Operator

That will come from Amit Daryanani with Evercore.

Q - Amit Daryanani {BIO 7113568 <GO>}

Thanks for taking my question. I have two as well. I guess first up on the channel inventory, I was hoping if you could talk about how the channel inventory looked like in the March quarter because it sounds like it may be below the historical ranges. And then the discussion you had for June quarter performance of iPhones, what are you embedding from a channel building back inventory levels or not in that expectation?

A - Timothy D. Cook {BIO 14014370 <GO>}

Amit, it's Tim. If you look at the iPhone channel inventory during Q2, the reduction of it was more than the reduction from the previous year, it's not unusual that we reduce in Q2 and in fact if you look back on generally speaking in the first half of the calendar year, we reduce channel inventories during the second half of the calendar year, we generally raise channel inventories. That's a seasonal thing and I believe --sitting here today, I believe that will happen this year as well. So hopefully that answers your question.

And by the way we ended in a comfortable position, so you conclude from that that we were within a target range.

Q - Amit Daryanani {BIO 7113568 <GO>}

Great. That's really helpful. Just a follow up, Tim, I was hoping you could maybe talk a little bit about how do you think about Apple's manufacturing strategy and perhaps need for some diversity, especially given everything the company that we've gone through over the last 12 months, how do you think about that and do you feel comfortable that the supply chain or the manufacturing base is well situated to-date to launch that traditional fall products that we used to get from Apple.

A - Timothy D. Cook {BIO 14014370 <GO>}

Yeah. As you know our supply chain is global. And so our products are truly made everywhere and I would focus on that versus focus on one element of the manufacturing process, which tends to get more visibility which is the final assembly. We have some final assembly in the United States. We have final assembly in China as well. I think you'd have

to conclude, or at least I conclude that if you look at the shock to the supply chain that took place this quarter for it to come back up so quickly really demonstrates that it's durable and resilient. And so, I feel good about where we are. That said, we're always looking at tweaks and it's just not something we talk about, because we view it as confidential and competitive information. And so we will look at the -- as we get out of this totally, we will look to see what we learned and what we should change.

A - Tejas Gala {BIO 20432011 <GO>}

Thank you, Amit. Can we have the next question, please?

Operator

We'll hear from Jeriel Ong with Deutsche Bank.

Q - Jeriel Ong {BIO 19758244 <GO>}

Hi, guys, thanks. Let me ask couple of questions. So I want to focus the question on services, the segment was solid in the quarter on overall macro weakness I just kind of see logic behind it being strong despite product weakness overall. You have look into the rest of the year, do you think that sustained or at some point do macro impacts worldwide impact the services line?

A - Luca Maestri {BIO 15738533 <GO>}

Yeah, let me take that one. We typically don't give a lot of specifics about our categories. But I've said as we look into the June quarter, we see two distinct trends in our Services business overall. Our ecosystem is very strong. Our customers are very engaged. We are continuing to grow double-digits. The number of transacting accounts and paid accounts. And so we expect our digital services to continue at the same level of performance that we have seen during the March quarter and that includes the App Store, of course, our video business, our music business, cloud services. So we expect all these businesses to continue to grow very strongly.

Given the overall economic environment and level of demand right now there are the two businesses that we believe are going to be impacted during the June quarter. One of them is Apple care, Apple care is essentially comprised of our product repair business and the warranty agreements that we sign with our customers when they purchase our devices. Both these businesses have been affected, obviously, by the store closures. Not only our retail stores, but also our partners points of sale and obviously the reduced level of customer traffic because of the social distancing measures, right? And we do expect Apple care to be affected during the June quarter.

The other business, which we think is going to be impacted by the overall economic weakness and the uncertainty on when businesses will reopen is advertising, which is the sum of our advertising business on the App Store, on Apple News and the third-party agreements that we have on the advertising front. So these are two things that during the June quarter, will create a headwind for the Services business.

Q - Jeriel Ong {BIO 19758244 <GO>}

Got it. Appreciate that. My second question comes about the overall purchasing decisions the consumers are making. So far through April, have you seen increase perhaps downticks across your product lines? So, for example, somebody might have a shift may be towards the lower end of the storage mix of certain products. And do you expect that going forward as unemployment uptick and macro impacts kind of layer on through the rest of '20? Thanks.

A - Timothy D. Cook {BIO 14014370 <GO>}

I haven't seen what you're asking. No, I have seen a strong customer response to iPhone SE, which is our most affordable iPhone, but it appears that those customers are primarily coming from wanting a smaller form factor with the latest technology or coming over from Android. And so those are the two principal kind of segments versus somebody buying down as you are talking about it.

We've also seen -- we launched the iPad Pro in the midst of all of this and the reception there has also been incredibly good. And that's, obviously, our top of the line iPad. And so I'm not seeing what you're alluding to at least at this point.

A - Tejas Gala {BIO 20432011 <GO>}

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

Q - Jeriel Ong {BIO 19758244 <GO>}

Thanks, guys.

Operator

That will be from JP Morgan's Samik Chatterjee.

Q - Samik Chatterjee {BIO 15496543 <GO>}

Hi, thanks for taking the question. So if I can just start with a question on kind of what you're seeing in China. You mentioned kind of the pickup in activity, but is that driven by more kind of footfall in the stores or what you seeing relative to online activity and how much of this recovery has been driven online, any thoughts on that, please?

A - Timothy D. Cook {BIO 14014370 <GO>}

Yeah, what we saw in China for the full quarter and I'll speak about Mainland China because I think that's the source of your question. We saw strong results in iPad and in wearables and in services. And if you look up underneath the full quarter, we saw strong January and then a significantly reduced demand in February as the shelter-in-place orders and the lock downs went into effect in China and the stores closed. And then in March as stores reopened we've -- the recovery began and then we've seen further recovery in April. Where that goes, we will see, but that's kind of what we've seen so far there.

To your question about store traffic. Store traffic is obviously up from where it was in February, but it is not back to where it was pre the lockdown. There has been, however, more move to online. And as I've mentioned earlier in my remarks, the -- and it's pretty phenomenal actually, retail had a quarterly record for us during the quarter, and that's despite stores being closed for the three-week period around the world and our ex-China and then China was closed prior to that three weeks and that's partly because of the online store had such a phenomenal quarter and that included in China, but it was also other regions as well.

So there is definitely a move and whether that's a permanent shift I would hesitate to go that far because I think people like to be out and about. They just know that now is not the time to do that.

Q - Samik Chatterjee {BIO 15496543 <GO>}

Got it. And if I can just follow-up on your previous comment about the strong demand you're seeing for iPhone SE. Just given the price point I'm wondering if you're expecting any change in terms of the geographic mix of where the demand comes from relative to typically, what do you see for other iPhones from the line-up, just given the lower price point?

A - Timothy D. Cook {BIO 14014370 <GO>}

I think it plays in every geo but I would expect to see it, doing even better in areas where the median incomes are less. And so we'll see how that plays out and I expect some fair number of people switching over to iOS and so it's an unbelievable offer, it's -- if you will, the engine of our top phones in a very affordable package and I think -- and it is faster than the fastest Android phones and so it's an exceptional value.

A - Tejas Gala {BIO 20432011 <GO>}

Thank you. Can we have the next question, please?

Operator

Certainly. Our last question today will be from Chris Caso with Raymond James.

Q - Chris Caso {BIO 4815032 <GO>}

Yes, thank you. I wanted to follow up with another question on iPhone SE and the decision to bring it back and where it sits within the total iPhone strategy. And I guess, coupled with the fact that iPhone 11 you made the decision to bring that at the lower price point. What does that tell us with respect to your approach to iPhone pricing and flexibility, is this helping to add users and kind of bring people into the ecosystem? And if so, what does that imply for gross margins?

A - Timothy D. Cook {BIO 14014370 <GO>}

First, we've always been about delivering the best product at a good price and that fundamental strategy has not changed at all. As you know, we did have SE for a while. It's

great to bring it back. It was a beloved product. And so I wouldn't read anything into that other than we want to give people the best deal that we can while making the best product.

Q - Chris Caso {BIO 4815032 <GO>}

Okay. As a follow-up, the follow-up question is on commodity pricing and I think you had expected to see some commodity price declines through the March quarter. If you could talk about what you expect as you go through the year perhaps in this new environment? And again whether that turns into a tailwind or a headwind for the gross margins as you go into the second half?

A - Timothy D. Cook {BIO 14014370 <GO>}

Yeah, for March, Chris, we saw NAND pricing increase slightly while DRAM and displays and the other commodities declined. For the June quarter, we would expect NAND and DRAM pricing to remain at this historically low level, while displays and most other commodity prices we expect to decline.

Q - Chris Caso {BIO 4815032 <GO>}

Thank you.

A - Tejas Gala {BIO 20432011 <GO>}

Yeah. Thank you, Chris. A replay of today's call will be available for two weeks on Apple podcast as a webcast on Apple.com/investor and via telephone. The numbers for the telephone replay are 888-203-1112 or 719-457-0820 Please enter confirmation code 3229513. 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 that does conclude today's conference. Thank you all for joining us today.

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