10-Q 1 a2038036z10-q.txt 10-Q UNITED STATES SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 ----------------- FORM 10-Q ----------------- (MARK ONE) X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE - SECURITIES EXCHANGE ACT OF 1934 - For the quarterly period ended December 30, 2000 OR TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from _______ to ________. Commission file number 0-10030 ----------- APPLE COMPUTER, INC. (EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER) ----------- CALIFORNIA 942404110 (STATE OR OTHER JURISDICTION (I.R.S. EMPLOYER IDENTIFICATION NO.) OF INCORPORATION OR ORGANIZATION) 1 Infinite Loop Cupertino, California 95014 (ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE) REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (408) 996-1010 Securities registered pursuant to Section 12(b) of the Act: None Securities registered pursuant to Section 12(g) of the Act: Common Stock, no par value Common Share Purchase Rights (Titles of classes) ----------- Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No --- --- 346,028,976 shares of Common Stock Issued and Outstanding as of January 30, 2001 PART I. FINANCIAL INFORMATION ITEM 1. FINANCIAL STATEMENTS APPLE COMPUTER, INC. CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited) (in millions, except share and per share amounts)

Three Months Ended ------------------ December 30, 2000 January 1, 2000 ----------------- ---------------

~~Net sales $1,007 $2,343 Cost of sales 1,028 1,736 --------- --------- Gross margin (21) 607 ------------------ Operating expenses: Research and development 102 90 Selling, general, and administrative 297 319 Special charges: Executive bonus --- 90 Restructuring costs --- 8 --------- --------- Total operating expenses 399 507 --------- --------- Operating income (loss) (420) 100 Gains from sales of investments~~

~~71 134 Unrealized loss on convertible securities (13) -- Interest and other income, net 67 40 --------- --------- Total interest and other income, net 125 174 --------- --------- Income (loss) before provision (benefit) for income taxes (295) 274 Provision (benefit) for income taxes (88) 91 --------- --------- Income (loss) before accounting change (207) 183 Cumulative effect of accounting change, net of income taxes of $5 12 -- --------- --------- Net income (loss) $ (195) $ 183~~

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~~Earnings (loss) per common share before accounting change: Basic $(0.61) $ 0.57 Diluted $(0.61) $ 0.51 Earnings (loss) per common share after accounting change: Basic $(0.58) $~~

~~0.57 Diluted $(0.58) $ 0.51 Shares used in computing earnings (loss) per share (in thousands): Basic 337,170 322,077 Diluted 337,170 356,834~~

See accompanying notes to condensed consolidated financial statements. 2 APPLE COMPUTER, INC. CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited) (in millions, except share amounts) ASSETS:

December 30, 2000 September 30, 2000 ----------------- ------------------ ~~Current assets: Cash and cash equivalents $1,737 $1,191 Short-term investments 2,328 2,836 Accounts receivable, less allowances of $61 and $64, respectively 441 953 Inventories 21 33 Deferred tax assets 231 162 Other current assets 168 252 ------ ------ Total current assets 4,926 5,427 Property, plant and equipment, net 325 313 Non-current debt and equity investments 447 786 Other assets 288 277 ------ ------ Total assets $5,986 $6,803 ====== ====== LIABILITIES AND SHAREHOLDERS' EQUITY: Current liabilities: Accounts payable $ 637 $1,157 Accrued expenses 1,000 776 ------ ------ Total current liabilities 1,637 1,933 Long-term debt 311 300 Deferred tax liabilities 326 463 --~~

~~---- ------ Total liabilities 2,274 2,696 ------ ------ Commitments and contingencies Shareholders' equity: Series A non-voting convertible preferred stock, no par value; 150,000 shares authorized, 3,300 and 75,750 issued and outstanding, respectively 3 76 Common stock, no par value; 900,000,000 shares authorized; 345,307,408 and 335,676,889 shares issued and outstanding, respectively 1,578 1,502 Retained earnings 2,090 2,285 Accumulated other comprehensive income 41 244 ------ ------ Total shareholders' equity 3,712 4,107 ------ ------ Total liabilities and shareholders' equity $5,986 $6,803~~

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See accompanying notes to condensed consolidated financial statements. 3 APPLE COMPUTER, INC. CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (in millions)

Three Months Ended ------ ------------ December 30, 2000 January 1, 2000 ------- ---------- -- ------------

~~Cash and cash equivalents, beginning of the period $ 1,191 $ 1,326 ------ - ------- Operating: Net income~~

~~(loss) (195) 183 Cumulative effect of accounting change, net of taxes (12) -- Adjustments to reconcile net income to cash generated (used) by operating activities: Depreciation and amortization 24 20 Provision for deferred income taxes (92) 64 Loss on sale of property, plant, and equipment -- 3 Gains from sales of investments (71) (134) Unrealized loss on convertible securities 13 -- Changes in operating assets and liabilities: Accounts receivable 512 (211) Inventories 12 5 Other current assets 116 4 Other assets (16) 3 Accounts payable (520) 362 Other current liabilities 216 74 -------- -------- Cash generated by (used for) operating activities (13) 373 --------~~

~~------ Investing: Purchase of short-term investments (634) (693) Proceeds from maturities of short-term investments 1,142 519 Purchase of long-term investments (1) -- Purchase of property, plant, and equipment (22) (38) Proceeds from sales of equity investments 74 136 Other (3) (13) ------- ------- Cash generated by (used for) investing activities 556 (89) ------- ------- Financing: Proceeds from issuance of common stock 3 17 Cash used for repurchase of common stock -- (41) ------- ------- Cash generated by (used for) financing activities 3 (24) ------- ------- Increase in cash and cash equivalents 546 260 ------- ------- Cash and~~

~~cash equivalents, end of the period $ 1,737 $ 1,586~~

~~Supplemental cash flow disclosures: Cash paid for interest $ -- $ -- Cash paid for income taxes, net $ 9 $ 8 Noncash transactions: Issuance of common stock for conversion of Series A Preferred Stock $ 73 $ --~~

See accompanying notes to condensed consolidated financial statements. 4 APPLE COMPUTER, INC. Notes to Condensed Consolidated Financial Statements (Unaudited) NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES BASIS OF PRESENTATION AND PREPARATION Interim information is unaudited; however, in the opinion of the Company's management, all adjustments of a normal recurring nature necessary for a fair statement of interim periods presented have been included. The results for interim periods are not necessarily indicative of results to be expected for the entire year. These condensed consolidated financial statements and accompanying notes should be read in conjunction with the Company's annual consolidated financial statements and the notes thereto for the fiscal year ended September 30, 2000, included in its Annual Report on Form 10-K for the year ended September 30, 2000 (the 2000 Form 10-K). Approximately every six years, the Company reports a 53-week fiscal year to align its fiscal quarters with calendar quarters by adding a week to its first fiscal quarter. Consequently, an additional week was added to the first quarter of fiscal 2000. DERIVATIVE FINANCIAL INSTRUMENTS On October 1, 2000, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards for derivative instruments, hedging activities, and exposure definition. SFAS No. 133 requires that all derivatives be recognized as either assets or liabilities at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in fair value will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings, or recognized in other comprehensive income until the hedged item is recognized in earnings. Net of the related income tax effect of approximately $5 million, adoption of SFAS No. 133 resulted in a favorable cumulative-effect-type adjustment to net income of approximately $12 million. Net of the related income tax effect of approximately $5 million, adoption of SFAS No. 133 resulted in a favorable cumulative-effect-type adjustment to other comprehensive income of approximately $12 million, all of which is expected to be reclassified to earnings by the end of the third quarter of fiscal 2001. Management does not believe that ongoing application of SFAS No. 133 will significantly alter the Company's hedging strategies. However, its application may increase the volatility of other income and expense and other comprehensive income. For derivative instruments that hedge the exposure of variability in expected future cash flows that is attributable to a particular risk and that are designated as cash flow hedges, the effective portion of the net gain or loss on the derivative instrument is reported as a component of other comprehensive income in stockholders' equity and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The remaining net gain or loss on the derivative instrument in excess of the cumulative change in the present value of the future cash flows on the hedged item, if any, is recognized in current earnings. For derivative instruments that hedge the exposure to changes in the fair value of an asset or a liability or an identified portion thereof that is attributable to a particular risk and that are designated as fair value hedges, the net gain or loss on the derivative instrument as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in earnings in the current period. The net gain or loss on a derivative instrument that is designated as, and is effective as, an economic hedge of the foreign currency translation exposure of the net investment in a foreign operation is reported in the same manner as a foreign currency translation adjustment to the extent it is effective as a hedge. For derivative instruments not designated as hedging instruments, changes in fair value are recognized in earnings in the current period. For foreign currency forward contracts designated as cash flow hedges, hedge effectiveness is measured based on changes in the fair value of the contract attributable to changes in the forward exchange rate. Changes in the expected future cash flows on the forecasted hedged transaction and changes in the fair value of the forward hedge are both measured from the contract rate to the forward exchange rate associated with the forward contract's maturity date. 5 For currency option contracts, hedge effectiveness is assessed based on changes in the option's intrinsic value. Apple defines intrinsic value as the present value of the gain or loss on the option contract calculated from the option's strike price to the forward rate associated with the option's cash settlement date. Hedge effectiveness is assessed by comparing the present value of the cumulative change in expected future cash flows on the forecasted hedged transaction attributable to the hedged risk with the cumulative change in the intrinsic value of the option. Changes in the expected future cash flows on the forecasted transaction and changes in the intrinsic value of the option hedge are both measured from the option strike price to the forward exchange rate. Changes in fair value of the option contract attributable to time value are excluded from the measurement of hedge effectiveness and are recognized in current earnings. For interest rate swap agreements qualifying as fair value hedges, the Company assumes no ineffectiveness as each interest rate swap meets the criteria for accounting under the short-cut method defined in SFAS No. 133. RECENT ACCOUNTING PRONOUNCEMENTS In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin (SAB) No. 101, "Revenue Recognition in Financial Statements." SAB No. 101, as amended, summarizes certain of the SEC's views in applying generally accepted accounting principles to revenue recognition in financial statements and provides guidance on revenue recognition issues in the absence of authoritative literature addressing a specific arrangement or a specific industry. The Company adopted SAB No. 101 in the first quarter of fiscal year 2001. Adoption of this guidance did not have a material impact on the Company's financial position or results of operations. NOTE 2 - EARNINGS PER SHARE Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during the period increased to include the number of additional common shares that would have been outstanding if dilutive potential common shares had been issued. The dilutive effect of outstanding options is reflected in diluted earnings per share by application of the treasury stock method. The dilutive effect of convertible securities is reflected using the if-converted method. Common stock options and convertible preferred stock were not included in the computation of diluted loss per share in the first quarter of 2001 as their effect was antidilutive. On June 21, 2000, the Company effected a two-for-one stock split in the form of a Common Stock dividend to shareholders of record as of May 19, 2000. All per share data and numbers of Common shares have been retroactively adjusted to reflect the stock split. 6 The following table sets forth the computation of basic and diluted earnings (loss) per share (in thousands, except net income (loss) and per share amounts):

FOR THE THREE MONTHS ENDED ------------------------------ - 12/30/00 1/1/00 -------- ------

~~Numerator (in millions): Net income (loss) $ (195) $ 183 -------- -------- Denominator: Denominator for basic earnings (loss) per share -- weighted-average shares outstanding 337,170 322,077 Effect of dilutive securities: Convertible preferred stock -- 18,182 Dilutive options -- 16,575 -------- -------- Dilutive potential~~

~~common shares -- 34,757 -------- --------~~

~~Denominator for diluted earnings (loss) per share 337,170 356,834~~

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~~Basic earnings (loss) per share before accounting change \$ (0.61) \$ 0.57~~

~~Cumulative effect of accounting change, net of tax \$ 0.03 \$ -- -------- --------~~

~~Basic earnings (loss) per share after accounting change \$ (0.58) \$ 0.57~~

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~~Diluted earnings (loss) per share before accounting change \$ (0.61) \$ 0.51~~

~~Cumulative effect of accounting change, net of tax \$ 0.03 \$ -- -------- --------~~

~~Diluted earnings (loss) per share after accounting change \$ (0.58) \$ 0.51~~

Options to purchase approximately 14.8 million shares of common stock that were outstanding at January 1, 2000, were not included in the computation of diluted earnings per share for the first quarter of 2000 because the options' exercise price was greater than the average market price of the Company's common stock during this period and, therefore, the effect would be antidilutive. At December 30, 2000, the Company had options to purchase approximately 90.6 million shares of its common stock outstanding, all of which were excluded from the computation of diluted loss per share for the first quarter of 2001 because the effect would have been antidilutive. 7 NOTE 3 - CONSOLIDATED FINANCIAL STATEMENT DETAILS (IN MILLIONS)

INVENTORIES 12/30/00 9/30/00 --------------- ~~Purchased parts $ 2 $ 1 Work in process 3 2 Finished goods 16 30 ---------------- Total inventories $21 $33~~

~~PROPERTY, PLANT, AND EQUIPMENT 12/30/00 9/30/00 --------------- Land and buildings $ 332 $ 324 Machinery and equipment 190 185 Office furniture and equipment 63 60 Leasehold improvements 129 131 Accumulated depreciation and amortization (389) (387) ---------------- Net property, plant, and equipment $ 325 $ 313~~

~~ACCRUED EXPENSES 12/30/00 9/30/00 --------------- Accrued compensation and employee benefits $ 182 $ 176 Accrued marketing and distribution 229 149 Accrued warranty and related costs~~

~~101 108 Other current liabilities 488 343 --------- -------- Total accrued expenses $1,000 $ 776~~

~~INTEREST AND OTHER INCOME, NET THREE MONTHS ENDED --------------------------------- 12/30/00 1/1/00 -------- ------- Interest income $ 64 $ 47 Interest expense (5) (5) Other income (expense), net 8 (2) -------- ------- Interest and other income (expense), net $ 67 $ 40~~

NOTE 4 - NON-CURRENT DEBT AND EQUITY INVESTMENTS AND OTHER STRATEGIC INVESTMENTS The Company holds significant investments in ARM Holdings plc (ARM), Akamai Technologies, Inc. (Akamai) and EarthLink Network, Inc. (EarthLink). These investments are reflected in the consolidated balance sheets as non-current debt and equity investments and have been categorized as available-for-sale requiring that they be carried at fair value with unrealized gains and losses, net of taxes, reported in equity as a component of accumulated other comprehensive income. If it is determined that a decline in value of any of these investments is other than temporary, then the investment's basis would be written down to fair value, and the write down would be included in earnings as a loss. All realized gains on the sale of these investments have been included in other income. The Company believes it is likely there will be significant fluctuations in the fair value of these investments in the future. The Company has additional minority debt and equity investments of approximately $34 million in several privately held technology companies. These investments, which are reflected in the consolidated balance sheets in other assets, are inherently risky because the products of these companies may be under development and/or because the markets for the technologies or products these companies have under development are typically in the early stages of development. 8 ARM HOLDINGS ARM is a publicly held company in the United Kingdom involved in the design and licensing of high performance microprocessors and related technology. As of September 30, 2000, the Company held 34.8 million shares of ARM stock with a fair value of $383 million. During the first quarter of 2001, the Company sold approximately 3.8 million shares of ARM stock for net proceeds of approximately $35 million and a gain before taxes of $35 million. As of December 30, 2000, the Company holds 31 million shares of ARM stock with a fair value of $234 million. AKAMAI In June 1999, the Company invested $12.5 million in Akamai, a global Internet content delivery service. The investment was in the form of convertible preferred stock that converted into 4.1 million shares of Akamai common stock (adjusted for subsequent stock splits) at the time of Akamai's initial public offering in October 1999. Beginning in the first quarter of 2000, the Company categorized its shares in Akamai as available-for-sale. The fair value of the Company's investment in Akamai was approximately $216 million as of September 30, 2000. During the first quarter of 2001, the Company sold 1 million shares of Akamai stock for net proceeds of approximately $39 million and a gain before taxes of approximately $36 million. As of December 30, 2000, the Company holds approximately 3.1 million shares of Akamai stock with a fair value of approximately $66 million. EARTHLINK In January 2000, the Company invested $200 million in EarthLink, an Internet service provider (ISP). The investment is in EarthLink's Series C Convertible Preferred Stock, which is convertible by the Company after January 4, 2001, into approximately 7.1 million shares of EarthLink common stock. Concurrent with this investment, EarthLink and the Company entered into a multi-year agreement to deliver ISP service to Macintosh users in the United States. Under the terms of the agreement, the Company profits from each new Mac customer that subscribes to EarthLink's ISP service for a specified period of time, and EarthLink is the default ISP in Apple's Internet Setup Software included with all Macintosh computers sold in the United States. The fair value of the Company's investment in EarthLink was approximately $36 million as of December 30, 2000. SAMSUNG During the fourth quarter of 1999, the Company invested $100 million in Samsung Electronics Co., Ltd. (Samsung), to assist in the further expansion of Samsung's TFT-LCD flat-panel display production capacity. The investment, in the form of three year unsecured bonds, is convertible into approximately 550,000 shares of Samsung common stock beginning in July 2000. The bonds carry an annual coupon rate of

2% and pay a total yield to maturity of 5% if redeemed at their maturity. This investment is reflected in the consolidated balance sheets as a non-current debt and equity investment. The Company categorizes its investment in Samsung as available-for-sale requiring that it be carried at fair value with unrealized gains and losses, net of taxes, reported in equity as a component of accumulated other comprehensive income. With the adoption of SFAS No. 133 on October 1, 2000, the Company is required to account for the conversion option embedded in the Samsung bonds separately from the related debt. The conversion feature is carried at fair value with any changes in fair value recognized in earnings in the period in which they occur. Included in the $17 million gross SFAS No. 133 transition adjustment recorded in earnings was a $23 million favorable adjustment for the restatement to fair value as of October 1, 2000, of the derivative component of the Company's investment in Samsung. To adjust the carrying value of the derivative component of its investment in Samsung to fair value as of December 30, 2000, the Company recognized an unrealized loss of approximately $13 million during the first quarter of 2001. The Company believes it is likely there will be significant fluctuations in the fair value of the embedded conversion option of this investment in the future. 9 NOTE 5 - SHAREHOLDER'S EQUITY STOCK REPURCHASE PLAN In July 1999, the Company's Board of Directors authorized a plan for the Company to repurchase up to $500 million of its common stock. This repurchase plan does not obligate the Company to acquire any specific number of shares or acquire shares over any specified period of time. During 2000, the Company repurchased a total of 2.55 million shares of its common stock at a cost of $116 million. No shares were repurchased in the first quarter of 2001. Since inception of the plan, the Company has repurchased a total of 5.05 million shares of its common stock at a cost of $191 million. PREFERRED STOCK In August 1997, the Company and Microsoft Corporation (Microsoft) entered into patent cross licensing and technology agreements. In addition, Microsoft purchased 150,000 shares of Apple Series A nonvoting convertible preferred stock ("preferred stock") for $150 million. Upon any sale of the preferred stock by Microsoft, the shares will automatically be converted into shares of Apple common stock at a conversion price of $8.25 per share, and the shares can be converted at Microsoft's option at such price after August 5, 2000. On September 15, 2000, 74,250 shares of preferred stock were converted to 9 million shares of the Company's common stock. In the first quarter of 2001, an additional 72,400 shares of preferred stock were converted to 8.8 million shares of the Company's common stock. NOTE 6 - DERIVATIVE FINANCIAL INSTRUMENTS The Company uses derivatives to partially offset its business exposure to currency and interest rate risk. Forward and option contracts are used to offset the foreign exchange risk on certain existing assets and liabilities and to hedge the foreign exchange risk of future cash flows on certain forecasted revenues and cost of sales. From time to time, the Company enters into interest rate swap agreements to modify the interest rate profile of certain investments and debt. The Company's accounting policies for these instruments are based on whether the instruments are designated as hedge or non-hedge instruments. The Company records all derivatives on the balance sheet at fair value. FOREIGN EXCHANGE RISK MANAGEMENT The Company enters into foreign exchange forward and option contracts with financial institutions primarily to protect against currency exchange risk associated with expected future cash flows, existing assets and liabilities, and certain firmly committed transactions. Generally, the Company's practice is to hedge a majority of its existing material foreign exchange transaction exposures. However, the Company may not hedge certain foreign exchange transaction exposures due to immateriality, prohibitive economic cost of hedging particular exposures, and availability of appropriate hedging instruments. 10 In accordance with SFAS No. 133, hedges related to anticipated transactions are designated and documented at hedge inception as cash flow hedges and evaluated for hedge effectiveness quarterly. For currency forward contracts, hedge effectiveness is measured based on changes in the fair value of the contract attributable to changes in the forward exchange rate. Changes in the expected future cash flows on the forecasted hedged transaction and changes in the fair value of the forward hedge are both measured from the contract rate to the forward exchange rate associated with the forward contract's maturity date. For currency option contracts, hedge effectiveness is measured based on changes in the option's intrinsic value. Apple defines intrinsic value as the present value of the gain or loss on the option contract calculated from the option's strike price to the forward rate associated with the option's cash settlement date. Hedge effectiveness is assessed by comparing the present value of the cumulative change in expected future cash flows on the forecasted transaction attributable to the hedged risk with the cumulative change in the intrinsic value of the option. Changes in the expected future cash flows on the forecasted transaction and changes in the intrinsic value of the option hedge are both measured from the option strike price to the forward exchange rate. Changes in fair value of the option contract attributable to time value are excluded from the measurement of hedge effectiveness and are recognized in current earnings. The effective portions of the net gains or losses on derivative instruments are reported as components of other comprehensive income in stockholders' equity and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Any residual changes in fair value of the instruments, including option time value or ineffectiveness are recognized in current earnings in interest and other income and expense. To protect gross margins from fluctuations in foreign currency exchange rates, the Company's U.S. dollar functional subsidiaries hedge a portion of forecasted foreign currency revenues, and the Company's non-U.S. dollar functional subsidiaries selling in foreign currencies hedge a portion of forecasted inventory purchases not denominated in the subsidiaries' functional currency. Other comprehensive income associated with hedges of foreign currency sales is recognized as a component of net sales in the same period as the related sales are recognized, and other comprehensive income related to inventory purchases is recognized as a component of cost of sales in the same period as the related costs are recognized. Typically, the Company hedges portions of its forecasted foreign currency exposure associated with revenues and inventory purchases over a time horizon of 3 to 9 months. The Company also enters into foreign currency forward and option contracts to offset the foreign exchange gains and losses generated by the remeasurement of certain recorded assets and liabilities in non-functional currencies. Changes in the fair value of these derivatives are recognized in current earnings in interest and other income as offsets to the changes in the fair value of the related assets or liabilities. The Company may enter into foreign currency forward contracts to offset the translation and economic exposure of a net investment position in a foreign subsidiary. Hedge effectiveness on forwards designated as net investment hedges is measured based on changes in the fair value of the contract attributable to changes in the spot exchange rate. The effective portion of the net gain or loss on a derivative instrument designated as a hedge of the net investment position in a foreign subsidiary is reported in the same manner as a foreign currency translation adjustment. Any residual changes in fair value of the forward contract, including changes in fair value based on the differential between the spot and forward exchange rates are recognized in current earnings in interest and other income and expense. For the quarter ended December 30, 2000, the Company recorded a net favorable adjustment of $4.0 million in the accumulated translation adjustment for derivatives designated as net investment hedges. 11 As discussed above, the Company enters into foreign currency option contracts as designated cash flow hedges and, sometimes, as items which provide an offset to the remeasurement of certain recorded assets and liabilities denominated in non-functional currencies. All changes in the fair value of these derivative contracts based on changes in option time value are recorded in current earnings in interest and other income and expense. Due to market movements, changes in option time value can lead to increased volatility in other income and expense. For the quarter ended December 30, 2000, the Company recorded a net loss of $7.5 million in interest and other income related to adjusting to fair value the change in time value of outstanding option contracts. Derivative instruments designated as cash flow hedges must be de-designated as hedges when it is probable that the forecasted hedged transaction will not occur in the initially identified time period. Deferred gains and losses in other comprehensive income associated with such derivative instruments are immediately reclassified into earnings in interest and other income. Any subsequent changes in fair value of such derivative instruments are also reflected in current earnings unless they are re-designated as hedges of other transactions. During the first quarter of 2001, the Company recorded a net gain of $5.1 million in interest and other income related to the loss of hedge designation on discontinued cash flow hedges due to changes in the Company's forecast of future net sales and cost of sales. INTEREST RATE RISK MANAGEMENT The Company sometimes enters into interest rate derivative transactions, including interest rate swaps, collars, and floors, with financial institutions in order to better match the Company's floating-rate interest income on its cash equivalents and short-term investments with its fixed-rate interest expense on its long-term debt, and/or to diversify a portion of the Company's exposure away from fluctuations in short-term U.S. interest rates. The Company may also enter into interest rate contracts that are intended to reduce the cost of the interest rate risk management program. The Company assumes no ineffectiveness with regard to the debt swaps as each interest rate swap meets the criteria for accounting under the short-cut method defined in SFAS No. 133 for fair value hedges of debt instruments. Accordingly, no net gains or losses were recorded in income relative to the Company's underlying debt and interest rate swaps. The Company's asset swaps do not qualify for hedge accounting treatment and are recorded at fair value on the balance sheet with associated gains and losses recorded in interest and other income. Included in the transition adjustment for SFAS No. 133 was an unfavorable adjustment before tax of approximately $5.7 million that adjusted the asset swaps to fair value as of October 1, 2000. For the quarter ended December 30, 2000, the Company recorded a before tax gain on the asset swaps of approximately $3.8 million. DERIVATIVE ACTIVITY IN ACCUMULATED OTHER COMPREHENSIVE INCOME As of December 30, 2000, the Company had a net deferred gain associated with cash flow hedges of approximately $13 million net of taxes, all of which is expected to be reclassified to earnings by the end of the third quarter of fiscal 2001. The following table summarizes activity in other comprehensive income related to derivatives, net of taxes, held by the Company during the period from October 1, 2000 through December 30, 2000 (in millions):

~~Cumulative effect of adopting SFAS No. 133 $ 12 Changes in fair value of derivatives 11 Gains reclassified from OCI (10) ---- Accumulated derivative gain $ 13~~
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12 NOTE 7 - COMPREHENSIVE INCOME Comprehensive income is comprised of two components, net income and other comprehensive income. Other comprehensive income refers to revenue, expenses, gains and losses that under generally accepted accounting principles are recorded as an element of shareholders' equity but are excluded from net income. The Company's other comprehensive income is comprised of foreign currency translation adjustments from those subsidiaries not using the U.S. dollar as their functional currency, changes in fair value of derivatives designated as and effective as cash flow hedges, and unrealized gains and losses, net of taxes, on marketable securities categorized as available-for-sale. Refer to "Note 4 - Non-Current Debt and Equity Investments and Other Strategic Investments" for additional information regarding unrealized gains and losses on available-for-sale securities and "Note 6 - Derivative Financial Instruments" regarding accounting for derivative financial instruments. The components of comprehensive income, net of tax, are as follows (in millions):

	FOR THE THREE MONTHS ENDED	
	12/30/00	1/1/00
~~Net income (loss)~~	~~$ (195)~~	~~$ 183~~
~~Other comprehensive income:~~		
~~Change in unrealized gain on derivative instruments~~	~~13~~	~~--~~
~~Change in accumulated translation adjustment~~	~~3~~	~~(1)~~
~~Unrealized gains (losses) on investments~~	~~(153)~~	~~1,233~~
~~Reclassification adjustment for investment gains included in net income~~	~~(66)~~	~~(101)~~
~~Total comprehensive income~~	~~$ (398)~~	~~$ 1,314~~

NOTE 8 - SPECIAL CHARGES RESTRUCTURING ACTIONS During the first quarter of 2000, the Company initiated restructuring actions resulting in recognition of an $8 million restructuring charge. This charge was comprised of $3 million for the write-off of various operating assets and $5 million for severance payments to approximately 95 employees associated with consolidation of various domestic and international sales and marketing functions. Of the $5 million accrued for severance, $2.5 million had been spent by September 30, 2000, and an additional $1 million was spent in the first quarter of 2001. Of the $3 million accrued for the write-off of various assets, substantially all was utilized by the end of the second quarter of 2000. EXECUTIVE BONUS During the first quarter of 2000, the Company's Board of Directors approved a special executive bonus for the Company's Chief Executive Officer for past services in the form of an aircraft with a total cost to the company of approximately $90 million, the majority of which is not tax deductible. Approximately half of the total charge is the cost of the aircraft. The other half represents all other costs and taxes associated with the bonus. This executive bonus has been presented outside selling, general, and administrative expenses as a special charge. NOTE 9 - SEGMENT INFORMATION AND GEOGRAPHIC DATA The Company manages its business primarily on a geographic basis. The Company's reportable segments are comprised of the Americas, Europe, and Japan. The Americas segment includes both North and South America. The European segment includes European countries as well as the Middle East and Africa. Other operating segments include Asia-Pacific, which includes Australia and Asia except for Japan, and the Company's subsidiary, Filemaker, Inc. Each reportable operating segment provides similar products and services, and the accounting policies of the various segments are the same as those described in the 2000 Form 10-K. 13 The Company evaluates the performance of its operating segments based on net sales and operating income. Operating income for each segment includes revenue, cost of sales, and operating expenses directly attributable to the segment. Net sales are based on the location of the customers. Operating income for each segment excludes other income and expense and certain expenses that are managed outside the reportable segment. Costs excluded from segment operating income include various corporate expenses, income taxes, and nonrecurring charges for purchased in-process research and development, restructuring, and acquisition related costs. Corporate expenses include research and development, manufacturing expenses not included in segment cost of sales, corporate marketing expenses, and other separately managed general and administrative expenses. The Company does not include intercompany transfers between segments for management reporting purposes. Summary information by segment follows (in millions):

	Three Months Ended	
	12/30/00	1/1/00
~~Americas:~~		
~~Net sales~~	~~$ 513~~	~~$1,189~~
~~Operating income (loss)~~	~~$ (93)~~	~~$ 166~~
~~Europe:~~		
~~Net sales~~	~~$ 326~~	~~$ 626~~
~~Operating income (loss)~~	~~$ (10)~~	~~$ 114~~
~~Japan:~~		
~~Net sales~~	~~$ 84~~	~~$ 412~~
~~Operating income (loss)~~	~~$ (29)~~	~~$ 114~~
~~Other Segments:~~		
~~Net sales~~	~~$ 84~~	~~$ 116~~
~~Operating income~~	~~$ 11~~	~~$ 25~~

A reconciliation of the Company's segment operating income to the condensed consolidated financial statements follows (in millions):

12/30/00
1/1/00 -----
--- ------
~~Segment operating income (loss) (121) 419 Corporate expenses, net (299) (221) Restructuring costs -- (8) Executive bonus -- (90) -------- ------ Total operating income (loss) $(420) $ 100~~

Information regarding net sales by product is as follows (in millions):
12/30/00
1/1/00 -----
--- ------
~~Power Macintosh $ 267 $ 707 PowerBook 84 212 G4 Cube 14 -- iMac 265 795 iBook 146 351 Software, service, and other net sales 231 278 -------- ------ Total net sales $1,007 $2,343~~

14 NOTE 10 - CONTINGENCIES The Company is subject to various legal proceedings and claims that are discussed in detail in the 2000 Form 10-K. The Company is also subject to certain other legal proceedings and claims which have arisen in the ordinary course of business and which have not been fully adjudicated. The results of legal proceedings cannot be predicted with certainty; however, in the opinion of management, the Company does not have a potential liability related to any legal proceedings and claims that would have a material adverse effect on its financial condition or results of operations. The Internal Revenue Service (IRS) has proposed federal income tax deficiencies for the years 1984 through 1991, and the Company has made certain prepayments thereon. The Company contested the proposed deficiencies by filing petitions with the United States Tax Court, and most of the issues in dispute have now been resolved. On June 30, 1997, the IRS proposed income tax adjustments for the years 1992 through 1994. Although most of the issues for these years have been resolved, certain issues still remain in dispute and are being contested by the Company. Management believes adequate provision has been made for any adjustments that may result from tax examinations. 15 ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS THIS SECTION AND OTHER PARTS OF THIS FORM 10-Q CONTAIN FORWARD-LOOKING STATEMENTS THAT INVOLVE RISKS AND UNCERTAINTIES. THE

COMPANY'S ACTUAL RESULTS MAY DIFFER SIGNIFICANTLY FROM THE RESULTS DISCUSSED IN THE FORWARD-LOOKING STATEMENTS. FACTORS THAT MIGHT CAUSE SUCH DIFFERENCES INCLUDE, BUT ARE NOT LIMITED TO, THOSE DISCUSSED IN THE SUBSECTION ENTITLED "FACTORS THAT MAY AFFECT FUTURE RESULTS AND FINANCIAL CONDITION" BELOW. THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH THE 2000 FORM 10-K AND THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES THERETO INCLUDED ELSEWHERE IN THIS FORM 10-Q. ALL INFORMATION IS BASED ON THE COMPANY'S FISCAL CALENDAR. RESULTS OF OPERATIONS Tabular information (dollars in millions, except per share amounts):

------------ -

FIRST
FIRST
FIRST
FOURTH
QUARTER
QUARTER
CHANGE
QUARTER
QUARTER
CHANGE
2001 2000
2001 2000 -

----------- --

~~Net sales $~~
~~1,007 $~~
~~2,343 (57)%~~
~~$ 1,007 $~~
~~1,870 (46)%~~
~~Macintosh~~
~~CPU unit~~
~~sales (in~~
~~thousands)~~
~~659 1,377~~
~~(52)% 659~~
~~1,122 (41)%~~
~~Gross margin~~
~~$ (21) $ 607~~
~~(103)% $~~
~~(21) $ 467~~
~~(104)%~~
~~Percentage~~
~~of net sales~~
~~(2.1)%~~
~~25.9%~~
~~(2.1)%~~
~~25.0%~~
~~Research and~~
~~development~~
~~$ 102 $ 90~~
~~13% $ 102 $~~
~~101 1%~~
~~Percentage~~
~~of net sales~~

~~10% 4%~~
~~10% 5%~~
~~Selling,~~
~~general and~~
~~administrative~~
~~$ 297 $ 319~~
~~(7)% $ 297~~
~~$ 282 5%~~
~~Percentage~~
~~of net sales~~
~~29% 14%~~
~~29% 15%~~
~~Special~~
~~Charges $ --~~
~~$ 98 NM $ -~~
~~- $ -- NM~~
~~Gains from~~
~~sales of~~
~~investments $~~
~~71 $ 134~~
~~(47)% $ 71~~
~~$ 83 (14)%~~
~~Unrealized~~
~~loss on~~
~~convertible~~
~~securities $~~
~~(13) $ --~~
~~NM $ (13) $~~
~~-- NM~~
~~Interest and~~
~~other income,~~
~~net $ 67 $ 40~~
~~68% $ 67 $~~
~~62 8%~~
~~Provision~~
~~(benefit) for~~
~~income taxes~~
~~$ (88) $ 91~~
~~(197)% $~~
~~(88) $ 59~~
~~(249)%~~
~~Effective tax~~
~~rate 30%~~
~~33% 30%~~
~~26% Net~~
~~income (loss)~~
~~before~~
~~accounting~~
~~change $~~
~~(207) $ 183~~
~~(213)% $~~
~~(207) $ 170~~
~~(222)%~~
~~Effect of~~
~~accounting~~
~~change, net $~~
~~12 $ -- NM~~
~~$ 12 $ --~~
~~NM Net~~
~~income (loss)~~
~~$ (195) $~~

~~183 (207)%~~
~~$ (195) $~~
~~170 (215)%~~
~~Basic earnings (loss) per share before accounting change $ (0.61) $ -- NM $ (0.61) $ -- NM~~
~~Diluted earnings (loss) per share before accounting change $ (0.61) $ -- NM $ (0.61) $ -- NM~~
~~Basic earnings (loss) per share $ (0.58) $ 0.57 (202)% $ (0.58) $ 0.52 (212)%~~
~~Diluted earnings (loss) per share $ (0.58) $ 0.51 (214)% $ (0.58) $ 0.47 (223)%~~

NM: Not Meaningful 16 NET SALES Net sales for geographic operating segments and Macintosh unit sales by geographic segment and by product follow (net sales in millions and Macintosh unit sales in thousands):

Three Months Ended Yr-to-Yr Three Months Ended Sequential -
------------------ ----- -------------
-- 12/30/00 1/1/00 Change 12/30/00 9/30/00 Change ----
---- ------ -
----- ------
-- ------- --

~~Americas net sales $~~

~~513 $1,189 (57)% $ 513 $1,099 (53)% Europe net sales $ 326 $ 626 (48)% $ 326 $ 369 (12)% Japan net sales $ 84 $ 412 (80)% $ 84 $ 281 (70)% Asia Pacific net sales $ 50 $ 77 (35)% $ 50 $ 86 (42)% Americas Macintosh unit sales 329 708 (54)% 329 688 (52)% Europe Macintosh unit sales 230 389 (41)% 230 224 3% Japan Macintosh unit sales 61 235 (74)% 61 156 (61)% Asia Pacific Macintosh unit sales 39 45 (13)% 39 54 (28)% -------- ------ -------- ------- Total Macintosh unit sales 659 1,377 (52)% 659 1,122 (41)%~~

~~======== ====== ======== =======~~

~~Power Macintosh unit sales 173 355~~

~~(51)% 173 269 (36)% PowerBook unit sales 49 84 (42)% 49 86 (43)% G4 Cube unit sales 29 -- NM 29 107 (73)% iMac unit sales 308 702 (56)% 308 571 (46)% iBook unit sales 100 236 (58)% 100 89 12% -------- ------ ------ ----- ------- -- Total Macintosh unit sales 659 1,377 (52)% 659 1,122 (41)%~~

FIRST QUARTER FISCAL 2001 Net sales decreased 57% to $1.007 billion in the first quarter of 2001 compared to the same quarter in 2000 and decreased 46% from the fourth quarter of 2000. Both the year-over-year and sequential declines in net sales are attributable to several factors including continued deterioration in worldwide demand for personal computers and rebate programs and price cuts instituted by the Company during the quarter that negatively affected the Company's net sales for the quarter by approximately $138 million. In addition, the Company implemented a plan to reduce substantially the level of inventory in its distribution channels from the amounts at the end of fiscal 2000 to more normal levels by the end of the first quarter of 2001. The Company ended fiscal 2000 with substantially more inventory in its distribution channels than planned due to the lower than expected sell-through of the Company's products during the fourth quarter of that year. The Company reduced channel inventory during the first quarter by approximately 300,000 units. These factors contributed to the 52% year-over-year decline in total Macintosh unit sales that were experienced across the Company's entire product line. These factors also reduced the average revenue per Macintosh unit shipped (a function of total net sales generated by hardware shipments and total Macintosh CPU unit sales) during the first quarter of 2001 to $1,476, a decline of approximately 12% from the same period in 2000. OUTLOOK For all of 2001, the Company anticipates net sales will decline as compared to 2000 to approximately $6 billion. The Company currently expects that it will be profitable, before the effect of any investment gains, during each of the last three quarters of 2001. The foregoing statements concerning the Company's anticipated net sales for all of 2001 and profitability for the remainder of fiscal 2001 are forward-looking. The Company's actual results could differ. The Company's future operating results and financial condition are dependent upon general economic conditions, market conditions within the PC industry, and the Company's ability to successfully develop, manufacture, and market technologically innovative products in order to meet the dynamic conditions within the highly competitive market for personal computers. Some of the potential risks and uncertainties that could affect the Company's future operating results and financial condition are discussed throughout this Item 2, including the discussion under the heading "Factors That May Affect Future Results and Financial Condition." 17 SEGMENT OPERATING PERFORMANCE The Company manages its business primarily on a geographic basis. The Company's reportable geographic segments include the Americas, Europe, and Japan. The Americas segment includes both North and South America. The European segment includes European countries as well as the Middle East and Africa. The Japan segment includes only Japan. Each geographic operating segment provides similar hardware and software products and similar services. Further information regarding the Company's operating segments may be found in this Form 10-Q in the Notes to Condensed Consolidated Financial Statements at Note 9, "Segment Information and Geographic Data." AMERICAS AND EUROPE The operating results of these two segments reflect the Company's overall results. Net sales in the Americas segment during the first quarter of fiscal 2001 decreased $676 million or 57% compared to the same period in 2000. Macintosh unit sales in the Americas decreased 54% on a year-over-year basis. Net sales in the Europe segment decreased $300 million or 48% during the first quarter of 2001 as compared to the same quarter in 2000, while the segment's Macintosh unit sales decreased 41%. These two segments combined represent approximately 83% of the Company's total net sales during the first quarter of 2001 and account for approximately $103 million of the Company's total operating loss for the first quarter of 2001. JAPAN Net sales in Japan declined 80% or $328 million and Macintosh unit sales declined 74% during the first quarter of 2001 as compared to the same quarter in 2000. The Company's Japan segment was most impacted by the Company's plan to reduce channel inventory during the first quarter of 2001 which is reflected in the 91% decrease in unit sales of iMac in Japan during the first quarter of 2001 compared to the same quarter in 2000. GROSS MARGIN Gross margin for the first quarter of 2001 was (2.1)% compared to 25.9% for the same quarter in 2000 and 25.0% for the fourth quarter of 2000. In addition to lower than normal net sales, margins were negatively impacted by the rebate programs and price cuts discussed above instituted by the Company during the first quarter that decreased revenue by approximately $138 million. Additionally, actual and forecasted declines in net sales caused the Company to recognize during the first quarter approximately $122 million of charges associated with purchase order cancellations and loss commitments for component purchases. Without these charges, gross margin for the first quarter of 2001 would have been approximately 21%. There can be no assurance that historical or current gross margin will be maintained, targeted gross margin levels will be achieved, or current margins on existing individual products will be maintained. In general, gross margin and margins on individual products will remain under significant downward pressure due to a variety of factors, including continued industry wide global pricing pressures, increased competition, compressed product life cycles, potential increases in the cost and availability of raw material and outside manufacturing services, and potential changes to the Company's product mix, including higher unit sales of consumer products with lower average selling prices and lower gross margins. In response to these downward pressures, the Company expects it will continue to take pricing actions with respect to its products. Gross margin could also be affected by the Company's ability to effectively manage quality problems and warranty costs and to stimulate demand for certain of its products. The Company's operating strategy and pricing take into account anticipated changes in foreign currency exchange rates over time; however, the Company's results of operations can be significantly affected in the short term by fluctuations in exchange rates. OPERATING EXPENSES Selling, general and administrative expenses, excluding special charges, decreased $22 million or 7% during the first quarter of 2001 as compared to the same period in 2000. The decrease in selling, general and administrative expenses during the first quarter of 2001 is the result of lower variable selling and marketing expenses resulting from the year-over-year 57% decrease in net sales and due to lower discretionary spending on marketing and advertising. Expenditures for research and development increased 13% between the first quarter of fiscal 2001 and the same quarter in 2000 primarily as a result of increased spending in 2001 to support multiple new product manufacturing ramps and increased research and development headcount of approximately 8%. 18 During the first quarter of fiscal 2000, the Company initiated restructuring actions resulting in recognition of an $8 million restructuring charge. This charge was comprised of $3 million for the write-off of various operating assets and $5 million for employee termination benefits associated with consolidation of various domestic and international sales and marketing functions. Of the $5 million accrued for severance, $2.5 million had been spent by September 30, 2000, and an additional $1 million was spent in the first quarter of 2001. Of the $3 million accrued for the write-off of various assets, substantially all was utilized by the end of the second quarter of 2000. In December 1999, the Company's Board of Directors approved a special executive bonus for the Company's Chief Executive Officer for past services in the form of an aircraft with a total cost to the company of approximately $90 million, the majority of which is not tax deductible. Approximately half of the total charge is the cost of the aircraft. The other half represents all other costs and taxes associated with the purchase. INTEREST AND OTHER INCOME (EXPENSE), NET Interest and other income and expense (net) increased $27 million or 68% to $67 million during the first quarter of fiscal 2001 compared to the same quarter in 2000. This increase is attributable primarily to two factors. First, interest income increased approximately $17 million or 36% between the first quarter of 2001 and the same quarter in 2000 as a result of higher cash, cash equivalents, and short-term investment balances and due to an increase in the overall yield earned on the Company's investment portfolio. Second, net gains from foreign exchange and net gains classified in other income and expense associated with derivative instruments were approximately $10 million higher in the first quarter of 2001 compared to the same period in 2000. For the second half of fiscal 2001, the Company expects a moderate decline in net interest income as a result of declining market interest rates. During the first quarter of 2001, the Company sold 3.8 million shares of ARM stock for net proceeds of approximately $35 million and a gain before taxes of $35 million. During the first quarter of 2001, the Company also sold 1 million shares of Akamai stock for net proceeds of approximately $39 million and a gain before taxes of $36 million. On October 1, 2000, the Company adopted SFAS No. 133. SFAS No. 133 establishes accounting and reporting standards for derivative instruments, hedging activities, and exposure definition. Net of the related income tax effect of approximately $5 million, adoption of SFAS No. 133 resulted in favorable cumulative-effect-type adjustment to net income of approximately $12 million. The $17 million gross transition adjustment was comprised of a $23 million favorable adjustment for the restatement to fair value of the derivative component of the Company's investment in Samsung, partially offset by the unfavorable adjustments to certain foreign currency and interest rate derivatives. Management does not believe that adoption of SFAS No. 133 will significantly alter the Company's hedging strategies. However, its application may increase the volatility of other income and expense and other comprehensive income. SFAS No. 133 also requires the Company to adjust the carrying value of the derivative component of its investment in Samsung to earnings on a go-forward basis, the before tax effect of which during the first quarter of 2001 was an unrealized loss of approximately $13 million. PROVISION FOR INCOME TAXES As of December 30, 2000, the Company had deferred tax assets arising from deductible temporary differences, tax losses, and tax credits of $612 million before being offset against certain deferred tax liabilities for presentation on the Company's balance sheet. This asset is generally realizable based on the ability to offset existing deferred tax liabilities. As of December 30, 2000, a valuation allowance of $30 million was recorded against the deferred tax asset for the benefits of tax losses that may not be realized. The valuation allowance relates principally to the operating loss carryforwards acquired from NeXT, the utilization of which is subject to certain limitations imposed by the Internal Revenue Code. The Company will continue to evaluate the realizability of the deferred tax assets quarterly by assessing the need for and amount of the valuation allowance. 19 The Company's effective tax rate for the three months ended December 30, 2000, was approximately 30%. This effective rate is less than the statutory federal income tax rate of 35% due primarily to the reversal of a portion of the previously established valuation allowance for tax loss and credit carryforwards and certain undistributed foreign earnings for which no U.S. taxes will be provided. The Company's effective tax rate for the first quarter of 2000 was approximately 33% and includes the effect of the special executive bonus of $90 million accrued during that quarter. The effective tax rate during the first quarter of 2000 without this charge was approximately 25%. THE COMPANY CURRENTLY BELIEVES THAT ITS EFFECTIVE TAX RATE FOR THE REMAINDER OF FISCAL 2001 WILL BE APPROXIMATELY 30%. THE FOREGOING-STATEMENTS ARE FORWARD- LOOKING. THE COMPANY'S ACTUAL RESULTS COULD DIFFER BECAUSE OF SEVERAL FACTORS, INCLUDING THOSE SET FORTH BELOW IN THE SUBSECTION ENTITLED "FACTORS THAT MAY AFFECT FUTURE RESULTS AND FINANCIAL CONDITION." ADDITIONALLY, THE ACTUAL FUTURE TAX RATE WILL BE

SIGNIFICANTLY IMPACTED BY THE AMOUNT OF AND JURISDICTION IN WHICH THE COMPANY'S FOREIGN PROFITS ARE EARNED. 20 LIQUIDITY AND CAPITAL RESOURCES The following table presents selected financial information and statistics for each of the fiscal quarters ending on the dates indicated (dollars in millions):

	12/30/00	9/30/00	1/1/00
Cash, cash equivalents, and short-term investments	$ 4,065	$ 4,027	$ 3,660
Accounts receivable, net	$ 441	$ 953	$ 892
Inventory	$ 21	$ 33	$ 15
Working capital	$ 3,289	$ 3,494	$ 2,944
Non-current debt and equity investments	$ 447	$ 786	$ 2,140
Long-term debt	$ 311	$ 300	$ 300
Days sales in accounts receivable (a)	40	46	37
Days of supply in inventory (b)	2	2	1
Days payables outstanding (c)	57	74	66
Operating cash flow (quarterly)	$ (13)	$ 158	$ 373

(a) Based on ending net trade receivables and most recent quarterly net sales for each period (b) Based on ending inventory and most recent quarterly cost of sales for each period (c) Based on ending accounts payable and most recent quarterly cost of sales adjusted for the change in inventory As of December 30, 2000, the Company had $4.065 billion in cash, cash equivalents, and short-term investments, an increase of $38 million or 1% over the same balances at the end of fiscal 2000. For the first quarter of fiscal 2001, the Company's primary source of cash was $556 million in cash flows from investing activities. Cash generated by investing activities consisted primarily of $1 billion in proceeds from the maturities of short-term investments and $74 million in proceeds from the sale of ARM and Akamai shares. These sources of cash were partially offset by purchases of short-term investments for $634 million. Cash used for operating activities was primarily from a net loss of $195 million and decreases in accounts payable partially offset by a decrease in accounts receivable and an increase in other current liabilities. In July 1999, the Company's Board of Directors authorized a plan for the Company to repurchase up to $500 million of its common stock. This repurchase plan does not obligate the Company to acquire any specific number of shares or acquire shares over any specified period of time. During 2000, the Company repurchased a total of 2.55 million shares of its common stock at a cost of $116 million. No shares were repurchased in the first quarter of 2001. Since inception of the plan, the Company has repurchased a total of 5.05 million shares of its common stock at a cost of $191 million. The Company believes its balances of cash, cash equivalents, and short-term investments will be sufficient to meet its cash requirements over the next twelve months, including any cash utilized by its stock repurchase plan. However, given the Company's current non-investment grade debt ratings (Standard and Poor's Rating Agency of BB and Moody's Investor Services of Ba2), if the Company should need to obtain short-term borrowings, there can be no assurance such borrowings could be obtained at favorable rates. The inability to obtain such borrowings at favorable rates could materially adversely affect the Company's results of operations, financial condition, and liquidity. NON-CURRENT DEBT AND EQUITY INVESTMENTS The Company holds significant investments in ARM Holdings plc (ARM), Samsung Electronics Co., Ltd. (Samsung), Akamai Technologies, Inc. (Akamai) and EarthLink Network, Inc. (EarthLink). These investments are carried at fair value in the consolidated balance sheets and are classified as non-current debt and equity investments. Any realized gains on the sale of these investments have been included in other income. The Company believes it is likely there will be significant fluctuations in the fair value of these investments in the future. Additional information related to the Company's non-current debt and equity investments may be found in this Form 10-Q in the Notes to Consolidated Financial Statements at Note 4, " Non-Current Debt and Equity Investments and Other Strategic Investments." 21 FACTORS THAT MAY AFFECT FUTURE RESULTS AND FINANCIAL CONDITION The Company operates in a rapidly changing environment that involves a number of uncertainties, some of which are beyond the Company's control, that will affect the Company's future results and business and may cause the Company's actual results to differ from those currently expected. Therefore, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods. The personal computer industry is highly competitive and is characterized by aggressive pricing practices, downward pressure on gross margins, frequent introduction of new products, short product life cycles, continual improvement in product price/performance characteristics, price sensitivity on the part of consumers, and a large number of competitors. The Company's results of operations and financial condition have been, and in the future may continue to be, adversely affected by industry wide pricing pressures and downward pressures on gross margins. The personal computer industry has also been characterized by rapid technological advances in software functionality, hardware performance, and features based on existing or emerging industry standards. Further, as the personal computer industry and its customers place more reliance on the Internet, an increasing number of Internet devices that are smaller and simpler than traditional personal computers may compete for market share with the Company's existing products. Several competitors of the Company have either targeted or announced their intention to target certain of the Company's key market segments, including consumer, education, and design and publishing. Additionally, several of the Company's competitors have introduced or announced plans to introduce products that mimic many of the unique design, technical features, and solutions of the Company's products. Many of the Company's competitors have greater financial, marketing, manufacturing, and technological resources, as well as broader product lines and larger installed customer bases than those of the Company. Additionally, the Company's future operating results and financial condition may be affected by overall demand for personal computers and general customer preferences for one platform over another or one set of product features over another. The Company is currently the only maker of hardware using the Mac OS. The Mac OS has a minority market share in the personal computer market, which is dominated by makers of computers utilizing Microsoft Windows operating systems. The Company's future operating results and financial condition are substantially dependent on its ability to continue to develop improvements to the Macintosh platform in order to maintain perceived design and functional advantages over competing platforms. Additional risks and uncertainties that could have an adverse impact on the Company's future operating results and financial condition include, among other things, continued or worsening worldwide and regional economic conditions, risks associated with product introductions and transitions, including the planned introduction of Mac OS X in 2001; risk that the Company will forecast incorrectly and produce or order from third parties excess or insufficient inventories of particular products; the Company's ability to supply products free of latent defects or other faults; increasing dependence on third-parties for manufacturing and other outsourced functions such as logistics; the availability of key components on terms acceptable to the Company; the availability of certain components and services essential to the Company's business currently obtained by the Company from sole or limited sources, including PowerPC RISC microprocessors developed by and obtained from IBM and Motorola and the final assembly of certain of the Company's products; the ability of the Company's suppliers to provide a sufficient supply of microprocessors with price/performance features that compare favorably with those supplied to the Company's competitors; the Company's ability to increase its share of the education market or maintain its existing share of the market; the continued viability of the Company's existing distribution channels; risks associated with international operations, including economic and labor conditions, regional economic problems, political instability, tax laws, and currency fluctuations; the continued support of third-party software developers and the continued availability of third-party software for particular applications; the future availability of any necessary patent or other rights to technology on commercially reasonable terms; fluctuations in the product, geographic, and channel mix of the Company's net sales; the Company's ability to attract, motivate and retain key employees; volatility in and/or impairment of the fair value of certain of the Company's minority debt and equity investments; managing the continuing impact of the European Union's transition to the Euro as its common legal currency; and continued volatility of the Company's stock price. For a discussion of these and other factors affecting the Company's future results and financial condition, see "Item 7 -- Management's Discussion and Analysis -- Factors That May Affect Future Results and Financial Condition" and "Item 1 - Business" in the Company's 2000 Form 10-K. 22 ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK THE INFORMATION PRESENTED BELOW REGARDING MARKET RISK CONTAINS FORWARD-LOOKING STATEMENTS THAT ARE SUBJECT TO RISKS AND UNCERTAINTIES. THE COMPANY'S ACTUAL RESULTS MAY DIFFER SIGNIFICANTLY FROM THOSE DISCUSSED BELOW AND ELSEWHERE IN THIS FORM 10-Q REGARDING MARKET RISK. THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH THE 2000 FORM 10-K AND THE CONDENSED

CONSOLIDATED FINANCIAL STATEMENTS AND NOTES THERETO INCLUDED ELSEWHERE IN THIS FORM 10-Q. FOREIGN CURRENCY RISK Overall, the Company is a net receiver of currencies other than the U.S. dollar and, as such, benefits from a weaker dollar and is adversely affected by a stronger dollar relative to major currencies worldwide. Accordingly, changes in exchange rates, and in particular a strengthening of the U.S. dollar, may negatively affect the Company's net sales and gross margins as expressed in U.S. dollars. The Company enters into foreign exchange forward and option contracts with financial institutions primarily to protect against currency exchange risk associated with expected future cash flows, existing assets and liabilities, certain firmly committed transactions, and probable but not firmly committed transactions. Generally, the Company's practice is to hedge a majority of its existing material foreign exchange transaction exposures. However, the Company may not hedge certain foreign exchange transaction exposures due to immateriality, prohibitive economic cost of hedging particular exposures, and availability of appropriate hedging instruments. Foreign exchange forward contracts are carried at fair value in other current assets and liabilities. INTEREST RATE RISK The Company's exposure to market risk for changes in interest rates relates primarily to the Company's investments and long-term debt obligations and related derivative financial instruments. The Company places its investments with high credit quality issuers and, by policy, limits the amount of credit exposure to any one issuer. The Company's general policy is to limit the risk of principal loss and ensure the safety of invested funds by limiting market and credit risk. While the Company is exposed to interest rate fluctuations in many of the world's leading industrialized countries, the Company's interest income and expense is most sensitive to fluctuations in the general level of U.S. interest rates. In this regard, changes in U.S. interest rates affect the interest earned on the Company's cash, cash equivalents, and short-term investments as well as costs associated with foreign currency hedges. During the last two years, the Company has entered into interest rate swaps with financial institutions in order to better match the Company's floating-rate interest income on its cash equivalents and short-term investments with its fixed-rate interest expense on its long-term debt, and/or to diversify a portion of the Company's exposure away from fluctuations in short-term U.S. interest rates. The Company may also enter into interest rate contracts that are intended to reduce the cost of the interest rate risk management program. The Company does not hold or transact in such financial instruments for purposes other than risk management. RISK MANAGEMENT ACTIVITIES To ensure the adequacy and effectiveness of the Company's foreign exchange and interest rate hedge positions, as well as to monitor the risks and opportunities of the non-hedge portfolios, the Company continually monitors its foreign exchange forward and option positions, and its interest rate swap, option and floor positions both on a stand-alone basis and in conjunction with its underlying foreign currency and interest rate related exposures, respectively, from both an accounting and an economic perspective. However, given the effective horizons of the Company's risk management activities and the anticipatory nature of the exposures intended to hedge, there can be no assurance the aforementioned programs will offset more than a portion of the adverse financial impact resulting from unfavorable movements in either foreign exchange or interest rates. In addition, the timing of the accounting for recognition of gains and losses related to derivative instruments for any given period may not coincide with the timing of gains and losses related to the underlying economic exposures and, therefore, may adversely affect the Company's operating results and financial position. On October 1, 2000, the Company adopted SFAS No. 133. SFAS No. 133 establishes accounting and reporting standards for derivative instruments, hedging activities, and exposure definition. Management does not believe that adoption of or ongoing application of SFAS No. 133 will significantly alter the Company's hedging strategies. However, its application may increase the volatility of other income and expense and other comprehensive income. The Company's market risks at December 30, 2000, are not significantly different from those discussed "Item 7A. -Disclosures About Market Risk" in the Company's 2000 Form 10-K. Also, refer to "Note 6 - Derivative Financial Instruments," of this Form 10-Q for additional discussion regarding the Company's market risks, its accounting for derivatives, and the impact of adoption of SFAS No. 133. 23 PART II. OTHER INFORMATION ITEM 1. LEGAL PROCEEDINGS The Company is subject to various legal proceedings and claims which are discussed in the 2000 Form 10-K. The Company is also subject to certain other legal proceedings and claims that have arisen in the ordinary course of business and which have not been fully adjudicated. The results of legal proceedings cannot be predicted with certainty; however, in the opinion of management, the Company does not have a potential liability related to any legal proceedings and claims that would have a material adverse effect on its financial condition or results of operations. ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K (a) EXHIBITS None (b) REPORTS ON FORM 8-K None 24 SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized. APPLE COMPUTER, INC. (Registrant) By: /s/ Fred D. Anderson --------------------- Fred D. Anderson Executive Vice President and Chief Financial Officer February 12, 2001 25