In education, business, and the home, people turn to one computer company for leadership and innovation.

Apple Computer, Inc.
1994 Annual Report

Key Achievements in 1994

- Set record net sales: $9.19 billion, up 15 percent over 1993. Macintosh computer unit shipments for the year surpassed 3.8 million.
- Introduced Power Macintosh computers: Apple shipped the Power Macintosh line of computers, based on the high-performance PowerPC processor. During fiscal 1994, sales of Power Macintosh computers topped 600,000 units.
- Reduced operating expenses: Operating expenses (excluding restructuring costs) dropped to 21.2 percent of net sales, down from 28.8 percent in 1993.
- Shipped Macintosh System 7.5: The newest release of the Macintosh operating system, Macintosh System 7.5, makes using a Macintosh computer even easier.
- Announced plans to license Macintosh technology: Apple moved forward with its plans to license Macintosh hardware and software technology to other vendors.
- Shipped high-performance servers: Apple introduced the PowerPC processor–based Workgroup Servers 6150, 8150, and 9150.

Financial Highlights

For the fiscal years ended September 30, 1994, and September 24, 1993
(In thousands, except employee, percentage, and per share data)

	1994	1993
Net sales	$9,188,748	$7,976,954
Net income	$310,178	$86,589
Earnings per share	$2.61	$0.73
Return on net sales	3.4%	1.1%
Shareholders' equity	$2,383,301	$2,026,378
Return on average shareholders' equity	14%	4%
Common and common equivalent shares	118,735	119,125
Total employees	14,592	14,938

Net Sales In millions

FY	
94	$9,188.7
93	$7,977.0
92	$7,086.5
91	$6,308.8
90	$5,558.4

Net Income In millions

FY	
94	$310.2
93	$86.6
92	$530.4
91	$309.8
90	$474.9

Earnings per Share

FY	
94	$2.61
93	$0.73
92	$4.33
91	$2.58
90	$3.77

Return on Average Shareholders' Equity

FY	
94	14%
93	4%
92	27%
91	19%
90	32%

Fellow shareholders:

In 1994, Apple delivered decisively on the objectives outlined in these pages one year ago. During the year, we successfully implemented a dramatic restructuring of our business, enabling Apple to compete profitably with much lower gross margins.

The numbers tell the story: In the fourth quarter of fiscal year 1992, Apple generated $97.6 million in income with gross margins of 42.7 percent of net sales. Two years later, in the same fiscal quarter, Apple generated $114.7 million in income—$17.1 million above the 1992 level—with gross margins of 27.2 percent, 15.5 points lower than 1992 gross margins. We raised revenues even as we reduced the number of regular employees, resulting in an increase in net sales per employee from $485,000 in fiscal year 1992 to $622,000 in 1994.

In addition to restructuring our financial model, we continued to bring to market the computer industry's most innovative solutions. For example, in 1994 we launched our first computers based on the PowerPC microprocessor. We shipped a new release of the Macintosh operating system, which incorporates new capabilities that streamline the way people work on computers. And we delivered sophisticated multimedia capabilities at an affordable price for home computer users.

As a result, we finished the 1994 fiscal year with improved earnings and revenue growth, disciplined financial management, and a revitalized competitive position. We revamped our entire portfolio of products, we expanded our new businesses, and we experienced rapid growth in emerging personal computer markets around the world.

For the year, Apple's revenues reached a new high of $9.19 billion, an increase of 15 percent over fiscal 1993. Net income was $310.2 million, or $2.61 a share, up from $86.6 million, or $0.73 a share, in fiscal 1993. Included in the Company's fiscal 1993 results was a charge of $320.9 million ($198.9 million, or $1.72 per share, after taxes) for restructuring expenses. Included in Apple's fiscal 1994 results was an adjustment that increased income by $126.9 million ($78.7 million, or $0.66 per share, after taxes) related to a reduction in the Company's estimates of the costs associated with its restructuring activities. Operating expenses (excluding restructuring costs) dropped to 21.2 percent of net sales in fiscal 1994, compared with 28.8 percent of net sales in fiscal 1993.

These achievements, however, are but a prologue. Because Apple is an established leader in some of the largest and fastest-growing areas of the computer industry, we believe we can expand our market presence in the coming years. Consider the facts:

• The computer industry is rapidly moving to the high-performance RISC (Reduced Instruction Set Computing) architecture—an architecture that until now has been used primarily in workstations. In just the few months since their introduction in March 1994, Apple's Power Macintosh computers have become the world's best-selling RISC-based computers.

• Industry research suggests that in 1995 the home market will—for the first time—prove to be a bigger market for personal computers in the United States than the corporate market. Apple is the world's number one vendor of personal computers for the home.

• Increasingly, customers are looking for solutions that are based on industry standards and that can be purchased from multiple vendors. In response, Apple announced an agreement in 1994 with IBM and Motorola to develop a common hardware reference platform for RISC-based computers. We also announced a strategy to broadly license the Macintosh operating system.

• Users want software that's easy to learn and customize, and software developers are looking for ways to streamline the development process. Apple is moving forward with OpenDoc, a component software architecture that meets the needs of both users and developers.

• Global markets represent tremendous opportunities for growth in the personal computer industry, and Apple has a strong presence in these markets. In Japan, the world's second-largest computer market, Apple holds the number two market position, with more than $1.2 billion in net sales in fiscal year 1994. The Company foresees new opportunities for growth in emerging markets such as China, India, Brazil, Korea, and Mexico, as well.

These industry developments—and Apple's ability to take advantage of them—augur well for the Company in the coming years. They also suggest that a full understanding of Apple's position in the computer industry requires a new perspective. We're not simply a hardware company or a software company. Apple is a company that delivers a full range of computing solutions.

This year's annual report is structured to offer a new way of looking at Apple: as a leader in key areas of the personal computer market; as an innovator in the industry; and as a company structured to leverage its research, development, and marketing investments profitably across many businesses.

Though challenges remain, we expect our strategy of creating comprehensive computing solutions will help us attract new customers in 1995. We plan to reinforce our leadership position with compelling new products in all of our businesses. And we aim to extend the overall market share of the Macintosh platform by introducing groundbreaking operating system technologies and by licensing the Macintosh operating system.

As the personal computer industry enters its third decade, its greatest priority must be a renewed commitment to meeting customer needs. For too long, the industry has provided technology to people without fully understanding how it affects the way they work.

At Apple, we aim to redouble our efforts in delivering products that direct the tremendous power of high technology toward one simple goal: meeting the needs of our customers.

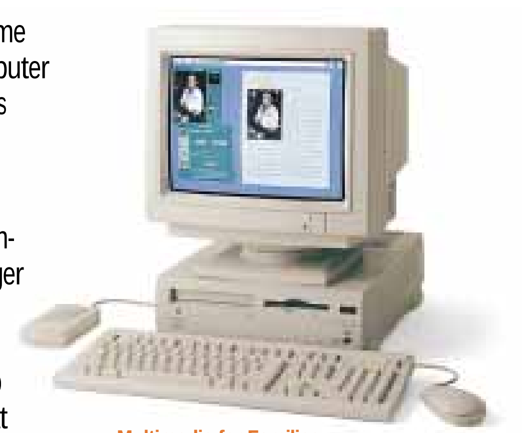
Looking back over the year, it's clear to me that 1994 was a test of character for Apple. To respond to the financial disappointment of 1993, we had to do more than just be willing to learn from the past. We had to show the persistence to overcome the inevitable cycles of global economics, and the spirit and discipline to deliver inspired solutions, even under tremendous organizational and competitive pressures.

These are the traits necessary to be a market leader and to realize a mission of changing the world. As 1994 demonstrated, they are also the traits that define this institution called Apple.

Michael Spindler
President
Chief Executive Officer

Apple in the Home

Industry research suggests that in 1995, for the first time, sales of computers to the home market will surpass sales to the corporate market in the United States. And home computer use is growing in other countries, as well. As the leader in home computing, Apple sees these developments as a tremendous opportunity.



Multimedia for Families

Apple's Macintosh Performa 630 series of computers enable families to produce their own multimedia projects. They make it easy for users to add video frames or sequences to documents, create presentations, and even watch television on the computer's display while they're working. *FamilyPC* magazine rated the Macintosh Performa 638CD the "best multimedia family Macintosh."

Anticipating customer needs

According to research published in 1994 by Dataquest, Apple® Macintosh® personal computers held 13.9 percent of the worldwide home computer market, and an even stronger 18.7 percent of the U.S. home computer market. This enviable position is the result of Apple's response to the unique requirements of home computer users. These users don't have a technical support staff at home, so they want a system that's easy to set up and learn. They buy home computers with their own money, so they want systems that are reliable and affordable. And they want their home furnishings to be attractive, so they want computers that look like they belong in a home instead of a stark cubicle.

Macintosh computers meet these requirements, with affordable systems that are simple to set up and maintain, with peripherals that actually work when they're plugged in, and with award-winning industrial design.

In addition, Apple's position in home computing has benefited from our leadership in education. As parents focus more on home learning, they look for the computer that their children use in school, and for the computer that runs educational software recommended by teachers. The result? They look to Macintosh.

Bringing new capabilities to home computers

We plan to extend this leadership position in the coming year through a number of key initiatives. First, we expect to extend our leadership in home multimedia computing. With the Macintosh Performa® 630 series of computers, we've already broken new ground by enabling people to do more than just passively watch multimedia programs on their home computer—now they can create their own multimedia materials at home.

Second, we aim to make it simpler for people to work from home and still have access to the libraries of information they need. Our Apple Remote Access software enables people to access files on their office computers and networks from their home computer. Our home computers offer the ability to work with DOS and Windows files, making it easier for people to bring work home from the office. With the growing acceptance of eWorld,™ our on-line service, and GeoPort,™ our telecommunications architecture, we expect to further reduce the barriers between home and business computing, giving people greater flexibility about how—and where—they spend their working hours.

Third, we intend to bring more powerful and comprehensive computing solutions to the home market at affordable prices. With the introduction of the Macintosh Performa 6100 series of computers in October 1994, we have already started to bring the power of RISC computing to the home user.

Simply put, we want to make home computers more useful to people. And we believe that our emphasis on providing affordable, innovative capabilities for the home user will extend our leadership in the fastest-growing segment of the computer industry.

Leadership in Home Computing

The home computer market is projected to be the largest computer market in the United States in 1995, and Apple is the leader in home computer unit sales. We've designed our Macintosh Performa computers to meet the growing needs of families. These computers are easy to set up, learn, and use. They come with a variety of software applications for every member of the family. And they're affordable, with a Performa model to suit almost any budget.

Apple Printers Complete the Picture

Our award-winning printers are natural companions to Apple computers. The Apple Color StyleWriter® 2400, for example, is designed for families who want an economical, compact color printer. Apple's peripherals business continues to play a key role in our strategy of providing customers with complete and integrated solutions.

Apple in Business

The Fastest Personal Computer Available

With the Power Macintosh line of computers, Apple became the first company to bring the high performance of PowerPC processors to personal computer users. The Power Macintosh 8100/110, with its 110-megahertz PowerPC processor, is the ideal choice for business and publishing professionals who need a computer that can handle calculation-intensive tasks.

Leadership in Publishing

Today's graphic design and publishing professionals require high-performance computing technology. The Lanman Companies, based in Washington, D.C., are publishing specialists—from design and production to prepress, printing, and multimedia. "Increasingly, we're converting our manufacturing from high-end dedicated computer systems to Macintosh solutions," says Lanman CEO Bruce Cunningham. "Our latest additions are 15 Power Macintosh 8100/80 computers. These machines give us substantial increases in productivity —more than 25 percent. In our design, prepress, database management, and multimedia areas, the Macintosh is an integral part of our process."

The strength of Apple's presence in business is much debated and often misunderstood. A few facts help clarify Apple's position:

- Apple is the third-largest personal computer vendor to business in the world, according to research by Dataquest. Apple generates more than $4 billion in annual sales to the business and government markets worldwide.
- Apple leads in one of the fastest-growing parts of the business market—business communication and publishing—which Apple estimates accounted for 25 percent of our net sales in 1994.
- Apple leads in one of the most promising segments of the business market—mobile computing. Apple's PowerBook Duo® computers are market leaders in the subnotebook category, and our PowerBook® computers continue to set the standard for innovation.
- Apple is extending our presence in business with a new line of PowerPC™ microprocessor–based Workgroup Servers.

Apple's commitment to business is significant—and we aim to increase our presence in this area in the coming year.

A growing market presence

It's clear even to the casual observer that businesses around the world are looking to decentralize management, streamline processes, and find ways to communicate faster and more effectively. We believe that Apple's strengths respond to these needs, and position us well for a greater share of the business market.

We anticipate that our solutions for mobile computing, collaboration among computer users, and graphics and multimedia will become increasingly relevant to global businesses. Apple's relationship with Bergen Brunswig, a leading supplier of pharmaceuticals and healthcare products, illustrates this point. Bergen Brunswig has developed a multimedia system based on Macintosh computers for its pharmacy network. With its AccuSource application and the Macintosh, Bergen Brunswig is enabling its thousands of pharmacy retailers to easily find information about products and prescription alternatives, and even view full-motion videos showing new products.

Publishing: A long-standing partnership

Apple's market-leading position in publishing is the result of our long-standing partnership with publishing customers and developers. We aim to be not just an equipment supplier, but a partner in discovering how technology can advance the publishing business.

In 1994, the introduction of our PowerPC microprocessor–based Power Macintosh™ computers galvanized the publishing industry. At a stroke, the high-performance computing capabilities once reserved for workstations came to the desktop. According to independent research by Market Presence, publishing applications designed to take advantage of the PowerPC microprocessor run up to eleven times faster on Power Macintosh computers than on comparable computers based on Intel Pentium processors—offering huge performance advantages to publishing professionals.

Publishers are expanding their business beyond producing paper-based publications to creating new media: videos, CD-ROM titles, interactive kiosks, on-line services, and other forms of publishing information. We believe this area offers considerable opportunity for Apple and our publishing partners.

Apple in Education

At Apple, we view the challenge of improving education as a global priority. Nowhere is our commitment to changing the world more evident than in the solutions we create to help children learn faster, to help people with disabilities participate more fully in society, and to help educational institutions move into the future.

Apple has a clear leadership position in education. Research by Dataquest indicates that we hold a 28 percent share of the worldwide education market—the number one position. Apple holds an even stronger lead in K–12 education, with a 61 percent market share of the U.S. installed base, according to research by Quality Education Data.

In 1994, education remained a tremendously important part of the Company's business. Apple estimates that sales to education contributed 20 percent of our net sales. Our strength in education also influences other parts of the computer market, most notably home computing, as parents look for computers their children use at school and that can run the learning software they want to use.

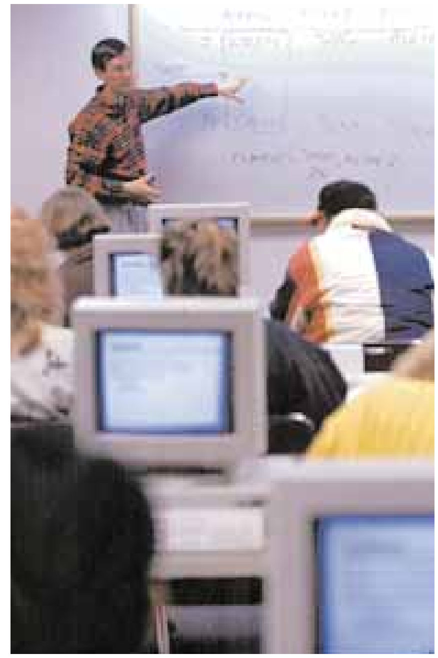
A rich history of collaboration

Apple continues to work closely with educators to develop new and comprehensive learning solutions. Many of the most appealing attributes of Apple's computer platform have been designed with the education customer in mind. For example, schools don't have the budget for on-site technical support, so Apple systems are designed to be easy to set up, connect to a network, and administer. Schools need computers that can be used by children as well as teachers and administrators, so Apple's computers are easy to learn. Schools' investments in hardware and software have to last a long time, so Apple has created a smooth transition path for customers—from our original Apple II to Macintosh, and now to Power Macintosh. And the huge library of education software that has been developed for Apple computers is unmatched.

Creating the future together

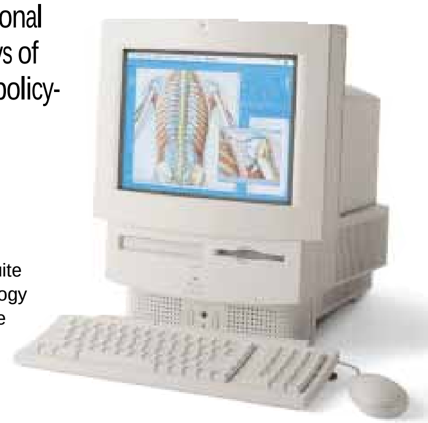
In 1994, products from all of Apple's businesses addressed the needs of people in education—whether they work in classrooms, in administration buildings, in dormitories, or in computer labs. For example, our Power Macintosh computers met with strong approval in higher education and secondary schools, with their exceptional performance and cross-platform capabilities. And our Workgroup Servers, combined with our AppleSearch® software, make it easier for people who have access to the Internet to explore the vast information resources of this network. AppleSearch allows students and educators to use commands in plain English to search through servers around the world for information, and it can perform these searches automatically at specified times.

As in publishing, Apple's commitment to education goes well beyond merely supplying equipment. We are deeply involved in the technological, social, and cultural issues that influence global education reform. As part of this involvement, we fund our own educational technology research group—the Apple Classrooms of Tomorrow—to explore new ways of teaching and learning. We are sharing the findings of this living laboratory with public policymakers to help them integrate technology into their plans for education reform.



Leadership in Education

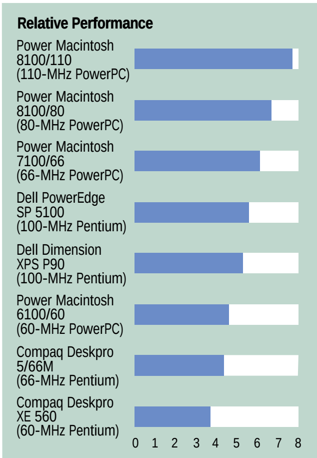
Power Macintosh computers are the systems of choice for students and faculty at Drake University in Des Moines, Iowa. In 1994, Drake added more than 1,100 Power Macintosh computers to its faculty offices, residence halls, and classrooms. With the Power Macintosh systems, students conduct research, search for information on the Internet, design publications, and create multimedia presentations. "Our experience with a computer-intensive curriculum affirms that the use of computers contributes to active learning, rather than passive learning," says Drake president Michael R. Ferrari. "It is critical that our graduates be well prepared to enter an increasingly global information-based economy, and they must have advanced learning tools to be successful in the coming years."



Complete Solutions for K-12 Education

In 1994, Apple introduced the Apple Education Series, a suite of products and programs that help educators use technology in a smooth, productive, and cost-efficient way. Each Apple Education Series product includes hardware, software, training, and technical support. Included with many of the Apple Education Series products is the Macintosh LC 575, Apple's powerful, all-in-one computer for education.

The Macintosh Computing Platform



Power Macintosh Leads in Performance

In a benchmark study conducted in November 1994 by Ingram Laboratories, a leading independent tester of personal computers, Apple's Power Macintosh computers outperformed comparable Intel Pentium processor–based computers running Microsoft Windows 3.1. The Power Macintosh 8100/110 was 39 percent faster overall than a computer based on a 100-megahertz Pentium processor. The Power Macintosh 7100/66 and 6100/60 computers were 15 percent and 24 percent faster, respectively, than comparable Pentium processor–based systems.

Apple has anticipated the major technology transitions that are realigning the computer industry. We have aggressive plans to extend our leadership in operating system software. And we have moved forward with our plans to make Apple technology more available in the marketplace through licensing.

Taken together, these developments enhance the competitive position of the Macintosh platform. The platform consists of the hardware and software technologies that give the Macintosh its acknowledged superiority in the marketplace.

The transition from CISC to RISC

Computer manufacturers are beginning to make the transition from CISC (Complex Instruction Set Computing) technology to RISC technology. RISC is fundamentally more powerful and efficient than CISC technology, which is used in nearly all Intel processor-based systems.

Apple has already successfully—and smoothly—made the transition to RISC. Our Power Macintosh computers run the same operating system as our Macintosh and PowerBook computers based on Motorola 680x0 processors, and they also run virtually all software created for other Macintosh systems. Less than a year after introducing the Power Macintosh line, Apple is the top-selling vendor of RISC-based computers worldwide—by a wide margin. The Power Macintosh line has also been important to the many developers who have delivered software products, known as native applications, that take advantage of the PowerPC processor's exceptional performance.

Our competition's transition to RISC looks rockier. It's unclear when manufacturers of systems that run Microsoft Windows software will offer RISC-based computers. And it's just as unclear which operating system these computers will run, because the personal computer versions of Microsoft Windows—Windows 3.1 and the yet-to-be-released Windows 95—can't run on RISC-based computers. The competing platform, as of today, has no high-volume operating system available to run on the microprocessor architecture of the future.

As a result, Apple—along with the third-party software and hardware developers that support the Macintosh platform—has a head start in delivering solutions for the next generation of computing.

Extending the Mac OS leadership

The Mac™ OS—the Macintosh operating system—has long been acknowledged as the industry leader in ease of use, plug-and-play compatibility, support for sophisticated graphics, and productivity for its users. This year, the introduction of Macintosh System 7.5—the latest release of the Mac OS—reinforced that leadership. System 7.5 offers many new features, including Apple Guide, an innovative help system that provides step-by-step guidance for new or complex tasks; QuickDraw™ GX, which offers advanced type and graphics technology; and Macintosh PC Exchange,™ which makes exchanging files with DOS and Windows software–based systems easier.

Mac™ OS

Expanding the Mac OS Market

In 1994, Apple announced plans to license the Mac OS to other personal computer vendors. Licensing is an important part of the Company's overall strategy to increase market share. The new Mac OS logo signifies Apple's more open approach to attracting new users to the platform, and manufacturers who license the Mac OS can display the logo on their products and packaging to indicate that the products are compatible with the Mac OS.

Hundreds of Native Applications for Power Macintosh

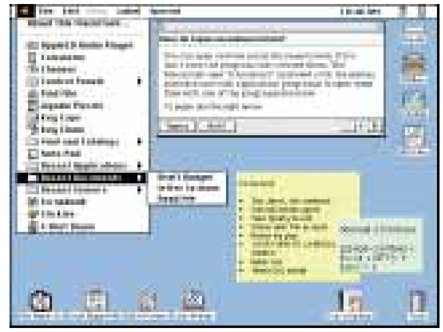
The list of native applications—software that has been accelerated to take full advantage of the high-performance PowerPC processor—continues to grow every day. More than 350 native applications have been introduced to date, by such major software developers as Microsoft, Adobe, Claris, Quark, and WordPerfect.

In the coming years, we will make even more improvements to the Macintosh operating system. First, we expect to deliver a user interface that conforms even more to the way people work and that can be modified to meet each user's needs. This interface will include technologies that allow "agents" to anticipate users' needs and learn from their work habits. We also plan to include improved speech-to-text and text-to-speech technologies, support for more languages, and improved scripting capabilities.

Second, future versions of the Mac OS will include OpenDoc,™ our cross-platform component software technology. OpenDoc is designed to allow users to customize their computer work environment, and we expect it to open new opportunities for developers. Industry leaders such as Xerox, Novell, IBM, Adobe, and Lotus have joined Apple in the creation of Component Integration Laboratories, an independent organization that will maintain standards and license OpenDoc.

Third, we aim to make it easier for people to work with multimedia. We intend to offer new products based on our QuickTime® multimedia software and QuickDraw GX graphics technology.

Finally, we plan to make the Macintosh computer an integrated tool for communications, consolidating the various communication devices people use today. For example, the "universal mailbox"—a feature of Macintosh System 7.5—provides a single place for users to receive voice messages, faxes, electronic mail from multiple applications, and paging messages. In the future, we expect to expand these communication capabilities to include navigation through on-line services and the Internet.



Apple Guide Brings New Ease of Use

This new feature is part of Macintosh System 7.5, the latest release of the Mac OS. Apple Guide helps to lower training costs by providing interactive on-screen help that guides users through tasks one step at a time. It also allows users to automate simple tasks, such as printing daily to-do lists.

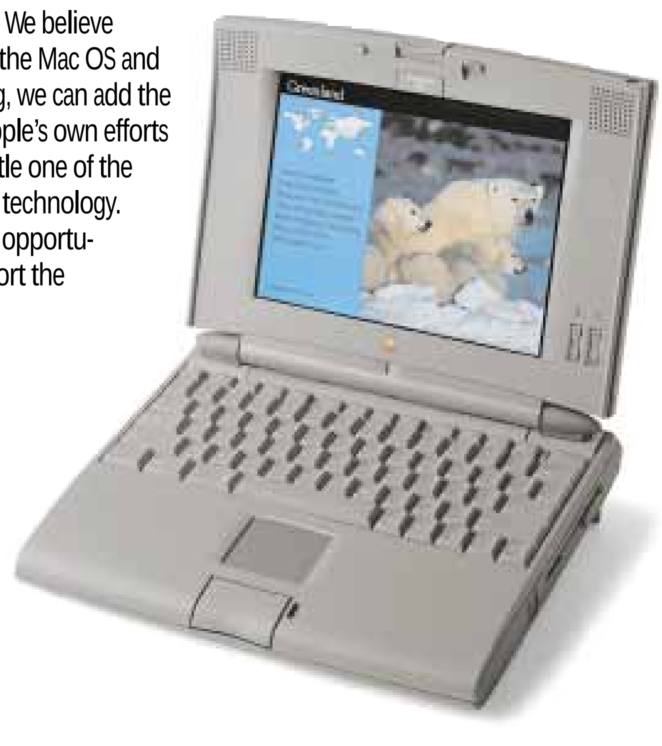
Expanding market share through licensing

During the year, Apple moved forward with plans to license Macintosh hardware and software in order to reach more customers with our technology. First, we announced our plans to license the Mac OS broadly around the world. Second, we agreed with IBM and Motorola to create a common hardware reference platform for computers based on the PowerPC microprocessor. This platform will offer customers the flexibility of running several different operating systems, including the Mac OS. It also makes it easier for new customers and potential licensees to adopt the Mac OS. In addition, we are exploring opportunities to license the Mac OS to vendors that create consumer electronics products. One of the primary goals of our licensing plans is to make our licensees successful in the global marketplace.

Licensing is a very important development for the Company. We believe licensing strengthens our ability to increase market share of both the Mac OS and Apple-branded Macintosh personal computers. Through licensing, we can add the sales, marketing, and distribution resources of our licensees to Apple's own efforts to expand the market share of Macintosh. In addition, we dismantle one of the final barriers to widespread acceptance of Macintosh: proprietary technology. This increased market share should, in turn, expand the business opportunities for third-party hardware and software companies that support the Macintosh platform.

The Leading Edge of Notebook Computing

Apple advanced its strong position in mobile computing in May 1994 with the introduction of the PowerBook 500 series of notebook computers, which combine innovative technologies and a sleek new design. The PowerBook 540c is Apple's top-of-the-line PowerBook—its high-performance features include an active-matrix color display, the Apple trackpad, Ethernet networking, and integrated productivity software.



Managing and Expanding the Business

High-Performance Servers

In 1994, Apple expanded its line of workgroup server solutions. The Workgroup Server 9150 is our most expandable, most powerful RISC-based server, capable of handling applications that require significant memory and storage capacity.

Two major initiatives underpin Apple's current business model: First, we plan to manage our assets and expenses efficiently to maximize our performance and financial returns. Second, we plan continued expansion in our new businesses.

Efficient financial management

Apple's financial rebound in the last twelve months is due in no small part to the Company's relentless restructuring for greater productivity. Our employees have cut costs, found more efficient ways of doing business, and, quite simply, figured out how to do more with less. Their tenacity and discipline proved instrumental in our recovery.

We are continuing to streamline operations by reengineering our component purchasing, inventory management, and customer distribution processes. We are improving our manufacturing cost competitiveness by using lower-cost, industry-standard parts in our products. And we are reducing our facilities costs by moving certain business functions to lower-cost areas in the United States and around the world.

Apple's new businesses

The installed base of more than 16 million Macintosh computers gives Apple a solid foundation on which we can build new businesses that capitalize on our strengths. The contribution to revenue from our new businesses—including our software subsidiary, our server business, our on-line services, and our personal electronics business—is currently small in comparison with our large personal computer revenue. But we believe these businesses can be important contributors to our revenue growth.

In fiscal 1994, unit shipments of software from Claris Corporation, our software subsidiary, increased 67 percent over 1993 levels—surpassing the 3 million mark. The best-selling ClarisWorks® application—which includes word processing, spreadsheet, drawing, painting, communications, and database programs, all in one package—was rated the "Best Buy" by *Home Office Computing* magazine. Also in 1994, Claris tripled its presence in the Windows software market. Its international presence expanded as well—Claris doubled its business in the fast-growing Japanese market in 1994.

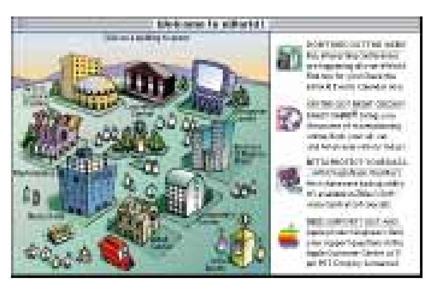
Also in 1994, Apple introduced competitively priced high-performance servers for workgroups consisting mostly of Macintosh users. We made great strides toward offering server systems that move beyond the Macintosh market into the much broader standards-based server market. Specifically, Novell announced plans to port its market-leading NetWare 4 network operating system to Apple's new PowerPC processor–based servers.

We continued to expand our on-line services business. We believe Apple's eWorld service is poised to become a key player in this dynamic growth market. eWorld software is included free with most Macintosh computers, giving this new service broad distribution.

And in our personal electronics business, Apple has already claimed a leadership position with its Newton® technology and MessagePad™ products. While the market for personal digital assistants is still in its early phases, industry research indicates that Newton technology holds a significant lead. We expect this lead to continue in the coming fiscal year.

Communicating in New Ways

The Newton MessagePad allows users to capture, organize, and communicate business and personal information. We expect the Newton MessagePad to continue to lead in specialized markets such as health care, financial services, and sales automation. In addition, we believe it will continue to compete strongly in the high-end personal organizer category.



A New World On-line

Apple's eWorld on-line service is designed around the metaphor of a community, giving users instant and easy access to information about hundreds of subjects. The intuitive eWorld interface, its growing library of information, and its global reach distinguish this service from its competitors.

1994 Financial Results

Apple's Worldwide Locations

- ■ Headquarters
- ▼ Operations Centers
- ● Manufacturing/Operations Centers
- ▲ Research and Development
- ● Sales Offices

Eleven-Year Financial History

	1994	1993	1992	1991
Results of Operations				
Net sales:				
Domestic	$ 4,987,539	$ 4,387,674	$ 3,885,042	$ 3,484,533
International	4,201,209	3,589,280	3,201,500	2,824,316
Total net sales	9,188,748	7,976,954	7,086,542	6,308,849
Costs and expenses:				
Cost of sales	6,844,915	5,248,834	3,991,337	3,314,118
Research and development (R&D)	564,303	664,564	602,135	583,046
Selling, general and administrative (SG&A)	1,384,111	1,632,362	1,687,262	1,740,293
Restructuring costs and other	(126,855)	320,856	—	224,043
	8,666,474	7,866,616	6,280,734	5,861,500
Operating income	522,274	110,338	805,808	447,349
Interest and other income (expense), net	(21,988)	29,321	49,634	52,395
Income before income taxes	500,286	139,659	855,442	499,744
Provision for income taxes	190,108	53,070	325,069	189,903
Net income	$ 310,178	$ 86,589	$ 530,373	$ 309,841
Earnings per common and common equivalent share	$ 2.61	$ 0.73	$ 4.33	$ 2.58
Common and common equivalent shares used in the calculations of earnings per share	118,735	119,125	122,490	120,283
Financial Position				
Cash, cash equivalents, and short-term investments	$ 1,257,856	$ 892,303	$ 1,435,500	$ 892,719
Accounts receivable, net	$ 1,581,347	$ 1,381,946	$ 1,087,185	$ 907,159
Inventories	$ 1,088,434	$ 1,506,638	$ 580,097	$ 671,655
Net property, plant, and equipment	$ 667,100	$ 659,546	$ 462,221	$ 447,978
Total assets	$ 5,302,746	$ 5,171,412	$ 4,223,693	$ 3,493,597
Current liabilities	$ 1,944,305	$ 2,508,085	$ 1,407,780	$ 1,198,920
Long-term debt	$ 304,472	$ 7,117	$ 17,740	$ 18,131
Deferred tax liabilities	$ 670,668	$ 629,832	$ 610,803	$ 509,870
Shareholders' equity	$ 2,383,301	$ 2,026,378	$ 2,187,370	$ 1,766,676
Cash dividends declared per common share	$ 0.48	$ 0.48	$ 0.48	$ 0.48
Other Data (Unaudited)				
Regular employees	11,287	11,963	12,166	12,386
Temporary employees and contractors	3,305	2,975	2,632	2,046
International net sales as a percentage of total net sales	46%	45%	45%	45%
Gross margin as a percentage of net sales	26%	34%	44%	47%
R&D as a percentage of net sales	6%	8%	8%	9%
SG&A as a percentage of net sales	15%	20%	24%	28%
Operating income as a percentage of net sales	6%	1%	11%	7%
Return on net sales	3%	1%	7%	5%
Return on average total assets	6%	2%	14%	10%
Return on average shareholders' equity	14%	4%	27%	19%
Price range per common share	$ 38⅛–$22½	$ 65–$24¼	$ 69⅞–$43¼	$ 72¾–$25

The number of shares and per share amounts for fiscal years 1984 through 1986 have been adjusted to reflect the two-for-one stock split effected on May 15, 1987.

Net income for fiscal year 1989 includes a pretax gain of approximately $79 million ($48 million, or $0.37 per share, after taxes) from the Company's sale of its common stock of Adobe Systems Incorporated.

Certain prior year amounts have been reclassified to conform to the current year presentation.

(In thousands, except employee, percentage, and per share data)

1990	1989	1988	1987	1986	1985	1984
$ 3,241,061	$ 3,401,462	$ 2,766,328	$ 1,940,369	$ 1,411,812	$ 1,490,396	$ 1,187,839
2,317,374	1,882,551	1,305,045	720,699	490,086	427,884	328,037
5,558,435	5,284,013	4,071,373	2,661,068	1,901,898	1,918,280	1,515,876
2,606,223	2,694,823	1,990,879	1,296,220	891,112	1,117,864	878,586
478,019	420,083	272,512	191,554	127,758	72,526	71,136
1,728,508	1,534,794	1,187,644	801,856	609,497	588,156	480,303
33,673	—	—	—	—	36,966	—
4,846,423	4,649,700	3,451,035	2,289,630	1,628,367	1,815,512	1,430,025
712,012	634,313	620,338	371,438	273,531	102,768	85,851
66,505	110,009	35,823	38,930	36,187	17,277	23,334
778,517	744,322	656,161	410,368	309,718	120,045	109,185
303,622	290,289	255,903	192,872	155,755	58,822	45,130
$ 474,895	$ 454,033	$ 400,258	$ 217,496	$ 153,963	$ 61,223	$ 64,055
$ 3.77	$ 3.53	$ 3.08	$ 1.65	$ 1.20	$ 0.49	$ 0.53
125,813	128,669	129,900	131,615	128,630	123,790	121,774
$ 997,091	$ 808,950	$ 545,717	$ 565,094	$ 576,215	$ 337,013	$ 114,888
$ 761,868	$ 792,824	$ 638,816	$ 405,637	$ 263,126	$ 220,157	$ 258,238
$ 355,473	$ 475,377	$ 461,470	$ 225,753	$ 108,680	$ 166,951	$ 264,619
$ 398,165	$ 334,227	$ 207,357	$ 130,434	$ 107,315	$ 90,446	$ 75,868
$ 2,975,707	$ 2,743,899	$ 2,082,086	$ 1,477,931	$ 1,160,128	$ 936,177	$ 788,786
$ 1,021,618	$ 893,764	$ 820,439	$ 476,266	$ 323,909	$ 287,978	$ 250,895
$ 5,437	$ 1,479	$ 6,654	$ 2,412	$ 4,626	$ 7,447	$ 4,289
$ 501,832	$ 362,910	$ 251,568	$ 162,765	$ 137,506	$ 90,265	$ 69,037
$ 1,446,820	$ 1,485,746	$ 1,003,425	$ 836,488	$ 694,087	$ 550,487	$ 464,565
$ 0.44	$ 0.40	$ 0.32	$ 0.12	—	—	—
12,307	12,068	9,536	6,236	4,950	4,326	5,382
2,221	2,449	1,300	992	636	325	—
42%	36%	32%	27%	26%	22%	22%
53%	49%	51%	51%	53%	42%	42%
9%	8%	7%	7%	7%	4%	5%
31%	29%	29%	30%	32%	31%	32%
13%	12%	15%	14%	14%	5%	6%
9%	9%	10%	8%	8%	3%	4%
17%	19%	22%	16%	15%	7%	10%
32%	36%	44%	28%	25%	12%	15%
$ 49½–$28¼	$ 49⅝–$33¾	$ 59¼–$28	$ 57½–$16¼	$ 19 7/16–$7½	$ 15 5/16–$7¼	$ 16 9/16–$8⅞

Selected Quarterly Financial Information (Unaudited)

(Tabular amounts in thousands, except per share amounts)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
1994				
Net sales	$ 2,493,286	$ 2,149,908	$ 2,076,700	$ 2,468,854
Gross margin	$ 678,873	$ 573,872	$ 499,064	$ 592,024
Net income	$ 114,655	$ 138,101	$ 17,404	$ 40,018
Earnings per common and common equivalent share	$ 0.95	$ 1.16	$ 0.15	$ 0.34
Cash dividends declared per common share	$ 0.12	$ 0.12	$ 0.12	$ 0.12
Price range per common share	$ 36⅜–$26⅛	$ 33½–$25⅛	$ 38⅛–$29¼	$ 34–$22½
1993				
Net sales	$ 2,140,789	$ 1,861,979	$ 1,973,894	$ 2,000,292
Gross margin	$ 550,428	$ 606,004	$ 760,763	$ 810,925
Net income (loss)	$ 2,664	$ (188,316)	$ 110,900	$ 161,341
Earnings (loss) per common and common equivalent share	$ 0.02	$ (1.63)	$ 0.92	$ 1.33
Cash dividends declared per common share	$ 0.12	$ 0.12	$ 0.12	$ 0.12
Price range per common share	$ 40⅛–$24¼	$ 58¾–$39⅝	$ 65–$52¾	$ 60⅝–$43⅜

At September 30, 1994, there were 32,219 shareholders of record.

The Company began declaring quarterly cash dividends on its common stock in April 1987. The dividend policy is determined quarterly by the Board of Directors and is dependent on the Company's earnings, capital requirements, financial condition, and other factors.

The price range per common share represents the highest and lowest closing prices for the Company's common stock on the Nasdaq National Market during each quarter.

Net income for the third quarter of 1994 includes a restructuring adjustment that increased income by $127 million ($79 million, or $0.66 per share, after taxes). Net loss for the third quarter of 1993 includes a restructuring charge of $321 million ($199 million, or $ 1.72 per share, after taxes).

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto. All information is based on the Company's fiscal calendar.

(Tabular information: Dollars in millions, except per share amounts)

Results of Operations	1994	Change	1993	Change	1992
Net sales	$ 9,189	15%	$ 7,977	13%	$ 7,087
Gross margin	$ 2,344	–14%	$ 2,728	–12%	$ 3,095
Percentage of net sales	25.5%		34.2%		43.7%
Operating expenses (excluding restructuring costs)	$ 1,948	–15%	$ 2,297	—	$ 2,289
Percentage of net sales	21.2%		28.8%		32.3%
Restructuring costs	$ (127)	–140%	$ 321	—	—
Percentage of net sales	(1.4%)		4.0%		—
Net income	$ 310	258%	$ 87	–84%	$ 530
Earnings per share	$ 2.61	258%	$ 0.73	–83%	$ 4.33

Net Sales

Net sales increased $1,212 million, or 15%, in fiscal 1994, compared with an increase of $890 million, or 13%, in fiscal 1993. The net sales growth in 1994 over 1993 was primarily due to two factors: unit sales growth and, to a lesser extent, an increase in the average aggregate revenue per Macintosh computer unit. Total Macintosh computer unit sales increased 16% over the prior year. This growth resulted principally from strong sales of the Company's new Power Macintosh products, first introduced on March 14, 1994, and from sales of newer product offerings within the Macintosh Performa line of desktop personal computers and, to a lesser extent, within the PowerBook family of notebook personal computers. This growth was partially offset by declining unit sales in certain of the Company's more established products and older product versions. The average aggregate revenue per Macintosh unit increased slightly, primarily due to fluctuations in product mix throughout the year, despite pricing actions undertaken by the Company in response to continuing industrywide pricing pressures.

Total Macintosh computer unit sales increased 32% from 1992 to 1993, reflecting strong unit sales of the Company's newer product offerings within the Macintosh Quadra®, LC, and Performa lines of desktop personal computers and within the PowerBook family of notebook personal computers. This growth was partially offset by declining unit sales of certain of the Company's more established products and older product versions. The average aggregate revenue per unit declined 15% in 1993 compared with 1992, primarily as a result of pricing actions undertaken by the Company in response to continuing industrywide pricing pressures.

In 1994, domestic net sales increased 14% over the prior year, compared with an increase of 13% in 1993 over 1992. International net sales grew 17% from 1993 to 1994, compared with 12% growth from 1992 to 1993, primarily as a result of strong sales growth in the Pacific region, particularly in Japan. International net sales represented 46% of net sales in 1994 compared with 45% of net sales in both 1993 and 1992.

Gross Margin

Gross margin in 1994 continued to decline as a percentage of net sales from 1993 and 1992 levels. The gross margin percentage declined to 25.5% in 1994 from 34.2% in 1993. The downward trend in gross margin as a percentage of net sales was primarily a result of pricing and promotional actions undertaken by the Company in response to industrywide competitive pricing pressures.

Gross margin was also affected somewhat adversely by changes in foreign currency exchange rates as a result of a stronger U.S. dollar relative to certain foreign currencies in 1994 compared with 1993. Results from the Company's ongoing foreign currency hedging activities offset a portion of this adverse foreign currency impact on gross margin. Although the Company's results of operations can be significantly affected in the short term by fluctuations in foreign currency exchange rates, the Company's operating strategy and pricing take into account changes in exchange rates over time.

The decline in gross margin as a percentage of net sales from 43.7% in 1992 to 34.2% in 1993 was primarily the result of industrywide competitive pressures and associated pricing and promotional actions. Inventory valuation reserves recorded against certain products also contributed to the decline in gross margin as a percentage of net sales. The Company's results of operations were minimally affected by changes in foreign currency exchange rates in 1993 compared with 1992.

Although the Company's gross margin percentage was 27.2% for the fourth quarter of 1994, resulting primarily from strong sales of Power Macintosh computers and the PowerBook 500 series of notebook personal computers, it is anticipated that gross margins will remain under pressure and could fall below prior years' levels worldwide due to a variety of factors, including continued industrywide pricing pressures, increased competition, and compressed product life cycles.

Operating Expenses	1994	Change	1993	Change	1992
Research and development	$ 564	–15%	$ 665	10%	$ 602
Percentage of net sales	6.1%		8.3%		8.5%

Research and development expenditures decreased in amount during 1994 compared with 1993 and 1992. This decrease reflected the results of the Company's restructuring actions aimed at reducing costs, including product development expenditures. The increase in research and development expenditures from 1992 to 1993 reflected net additions to the Company's engineering staff and related costs. Research and development expenditures, as a percentage of net sales, decreased since 1992 as a result of revenue growth during 1993 and 1994, coupled with the Company's continuing efforts to focus its research and development project spending.

The Company believes that continued investment in research and development is critical to its future growth and competitive position in the marketplace, and is directly related to continued, timely development of new and enhanced products. Although the Company continues to manage operating expense growth relative to gross margin levels, it anticipates that research and development expenditures in 1995 will increase slightly in amount.

	1994	Change	1993	Change	1992
Selling, general and administrative	$ 1,384	–15%	$ 1,632	–3%	$ 1,687
Percentage of net sales	15.1%		20.5%		23.8%

Selling, general and administrative expenses decreased in amount and as a percentage of net sales in 1994 and 1993 compared with 1993 and 1992, respectively. These decreases reflect the Company's ongoing efforts to manage operating expense growth relative to gross margin levels.

In 1994, selling, general and administrative expenses decreased in amount and as a percentage of net sales compared with 1993, primarily because of lower employee-related and facilities costs resulting from the restructuring actions taken in the third quarter of 1993. In addition, revenue growth in 1994 contributed to the decrease in selling, general and administrative expenses as a percentage of net sales.

General and administrative expenses decreased in 1993 compared with 1992, primarily because of reduced employee-related expenses resulting from the restructuring actions taken in the third quarter of 1993. This decrease in general and administrative expenses was offset slightly by an increase in sales and marketing expenses as a result of increases in costs for product marketing and advertising programs related to new product introductions and efforts to increase product demand.

The Company will continue to face the challenge of managing growth in selling, general and administrative expenses relative to gross margin levels, particularly in light of the Company's expectation of continued pressure on gross margins and continued competitive pressures worldwide. The Company anticipates an increase in selling, general and administrative expenses in 1995 from current levels, primarily resulting from marketing and advertising expenditures.

	1994	Change	1993	Change	1992
Restructuring costs	$ (127)	–140%	$ 321	—	—
Percentage of net sales	(1.4%)		4.0%		—

For information regarding the Company's restructuring actions, refer to pages 27–28 of the Notes to Consolidated Financial Statements.

Interest and Other Income (Expense), Net	1994	Change	1993	Change	1992
Interest and other income (expense), net	$ (22)	–175%	$ 29	–41%	$ 50

Interest and other income (expense), net, decreased by $51 million, to $22 million in expense in 1994 compared with $29 million of income in 1993. Higher interest rates and larger average borrowing balances used to fund working capital needs served to significantly increase interest expense, and accounted for $28 million of the $51 million increase in expenses during 1994. Other factors contributing to this variance include interest income, which was higher in 1993 than in 1994 primarily due to a $15 million interest payment received on a nonrecurring income tax refund from the Internal Revenue Service in 1993, and interest income from the Company's interest rate risk management program, which contributed $6 million in 1993, and reduced interest income by $7 million in 1994.

Interest and other income (expense), net, decreased in amount in 1993 compared with 1992 because of lower interest rates, lower cash balances, expenses associated with certain financing transactions, lower gains on the sale of certain of the Company's venture capital investments, an increase in the cost of hedging certain foreign currency exposures, and an increase in interest expense due to higher commercial paper borrowing levels. This decrease was partially offset by interest earned on an income tax refund from the Internal Revenue Service and gains realized on the Company's ongoing foreign exchange risk management programs.

For more information regarding the Company's strategy and accounting for financial and other derivative instruments, refer to pages 24–26 of the Notes to Consolidated Financial Statements.

Provision for Income Taxes	1994	Change	1993	Change	1992
Provision for income taxes	$ 190	258%	$ 53	–84%	$ 325
Effective tax rate	38%		38%		38%

The Company's effective tax rate remained unchanged in 1994, 1993, and 1992. For additional information regarding income taxes, refer to pages 29–30 of the Notes to Consolidated Financial Statements.

Factors That May Affect Future Results and Financial Condition

The Company's future operating results and financial condition are dependent on the Company's ability to successfully develop, manufacture, and market technologically innovative products in order to meet dynamic customer demand patterns. Inherent in this process are a number of factors that the Company must successfully manage in order to achieve favorable future operating results and financial condition.

Product Introductions and Transitions

Due to the highly volatile nature of the personal computer industry, which is characterized by dynamic customer demand patterns and rapid technological advances, the Company frequently introduces new products and product enhancements. The success of new product introductions is dependent on a number of factors, including market acceptance, the Company's ability to manage the risks associated with product transitions, the effective management of inventory levels in line with anticipated product demand, and the manufacturing of products in appropriate quantities to meet anticipated demand. Accordingly, the Company cannot determine the ultimate effect that new products will have on its sales or results of operations.

On March 14, 1994, the Company introduced Power Macintosh, a new line of Macintosh computers based on a new PowerPC family of RISC microprocessors. The Company's results of operations and financial condition may be adversely affected if it is unable to successfully complete the transition of its lines of personal computers and servers from the Motorola 68000 series of microprocessors to the PowerPC microprocessor. The success of this ongoing transition will depend on the Company's ability to continue to sell products based on the Motorola 68000 series of microprocessors while gaining market acceptance of the new PowerPC processor–based products, to successfully manage inventory levels of both product lines simultaneously, and to continue to coordinate the timely development and distribution by independent software vendors of new "native" software applications specifically designed for the PowerPC processor–based products.

The rate of product shipments immediately following introduction of a new product is not necessarily an indication of the anticipated future rate of shipments for that product, which depends on many factors, some of which are not under the control of the Company. These factors may include initial large purchases by a small segment of the user population that tends to purchase new technology prior to its acceptance by the majority of users ("early adopters"); purchases in satisfaction of pent-up demand by users who anticipated new technology and as a result deferred purchases of other products; and overordering by dealers who anticipate shortages due to the aforementioned factors. The preceding may also be offset by other factors, such as the deferral of purchases by many users until new technology is accepted as "proven" and for which commonly used software products are available; and the reduction of orders by dealers once they believe they can obtain sufficient supply of product previously in backlog.

Backlog is often volatile after new product introductions due to the aforementioned demand factors, often increasing sharply coincident with introduction, and then reducing sharply once dealers and customers believe they can obtain sufficient supply of product.

The measurement of demand for newly introduced products is further complicated by the availability of different product configurations, which may include various types of built-in peripherals and software. Configurations may also require certain localization (such as language) for various markets and, as a result, demand in different geographic areas may be a function of the availability of third-party software in those localized versions. For example, the availability of European-language versions of software products manufactured by U.S. producers may lag behind the availability of U.S. versions by a quarter or more. This may result in lower initial demand for the Company's new products outside the United States, although localized versions of the products may be available.

Competition

The personal computer industry is highly competitive and continues to be characterized by consolidations in the hardware and software industries, aggressive pricing practices, and downward pressure on gross margins. The Company's results of operations and financial condition could be adversely affected should the Company be unable to effectively manage the impact of industry-wide pricing pressures and continue to realize the anticipated cost-reduction benefits associated with the restructuring plan initiated in the third quarter of 1993.

The Company's future operating results and financial condition may also be affected by the Company's ability to offer customers competitive technologies while effectively managing the impact on inventory levels and the potential for customer confusion created by product proliferation.

On November 7, 1994, the Company reached an agreement with International Business Machines Corporation (IBM) and Motorola, Inc. on a new hardware reference platform for the PowerPC microprocessor that is intended to deliver a much wider range of operating system and application choices for computer customers. As a result of this agreement, the Company intends to port the Macintosh operating system to the common platform. Accordingly, the Company's future operating results and financial condition may be affected by its ability to implement this and certain other collaboration agreements entered into, and to manage the associated competitive risk.

The Company's future operating results and financial condition may also be affected by the Company's ability to increase market share in its personal computer business. Currently, the Company is the only maker of hardware that uses the Macintosh operating system, and it has a minority market share in the personal computer market, which is dominated by makers of computers that run the MS-DOS and Microsoft Windows operating systems. Certain of the Company's personal computer products are capable of running software designed for the MS-DOS or Windows operating system, through software emulation of Intel microprocessor chips (except for one product, which does so by means of a coprocessor card). Optimal performance of the Company's products is obtained by use of software specifically designed for the Company's products, either those based on the Motorola 68000 series of microprocessors or those based on the PowerPC microprocessor. However, as a result of the collaboration agreement noted in the preceding paragraph, the Company will have the opportunity to increase its market share in the personal computer business as the Macintosh operating system becomes available on computers based on the new hardware reference platform.

Decisions by customers to purchase the Company's personal computers, as opposed to MS-DOS or Windows-based systems, are often based on the availability of third-party software for particular applications. The Company believes that the availability of third-party application software for the Company's hardware products depends in part on third-party developers' perception and analysis of the relative benefits of developing such software for the Company's products versus software for the larger MS-DOS and Windows market. This analysis is based on factors such as the relative market share of the Company's products, the anticipated potential revenue that may be earned, and the costs of developing such software products.

In an effort to increase overall market share, the Company plans to license the Macintosh operating system to other personal computer vendors beginning in 1995. The Company anticipates that the licensing activities will result in a variety of these vendors bringing to market personal computers that will run application software based on the Macintosh operating system. The Company also believes that licensing will offer software vendors a broader installed base on which they can develop and provide technical innovations for the Macintosh platform. At this time, the Company cannot determine the ultimate effect that licensing of the Macintosh operating system will have on its sales or results of operations.

Microsoft Corporation is the developer of the MS-DOS and Windows operating systems, which are the principal competing operating systems to the Company's Macintosh operating system. Microsoft is also an important developer of application software for the Company's products. Accordingly, Microsoft's interest in producing application software for the Company's products may be influenced by Microsoft's perception of its interests as an operating system vendor.

The Company's ability to produce and market competitive products is also dependent on the ability of IBM and Motorola, Inc., the suppliers of the new PowerPC RISC microprocessor for certain of the Company's products, to continue to supply to the Company microprocessors that produce superior price/performance results compared with those supplied to the Company's competitors by Intel Corporation, the developer and producer of the microprocessors used by most personal computers using the MS-DOS and Windows operating systems. IBM produces personal computers based on the Intel microprocessors as well as on the PowerPC microprocessor, and is also the developer of OS/2, a competing operating system to the Company's Macintosh operating system. Accordingly, IBM's interest in supplying the Company with improved versions of microprocessors for the Company's products may be influenced by IBM's perception of its interests as a competing manufacturer of personal computers and as a competing operating system vendor.

The Company's future operating results and financial condition may also be affected by the Company's ability to successfully expand its new businesses and product offerings into other markets, such as the markets for on-line services and personal digital assistant (PDA) products.

Global Market Risks

A large portion of the Company's revenue is derived from its international operations. As a result, the Company's operations and financial results could be significantly affected by international factors, such as changes in foreign currency exchange rates or weak economic conditions in the foreign markets in which the Company distributes its products. When the U.S. dollar strengthens against other currencies, the U.S. dollar value of non-U.S. dollar–based sales decreases. When the U.S. dollar weakens, the U.S. dollar value of non-U.S. dollar–based sales increases. Correspondingly, the U.S. dollar value of non-U.S. dollar–based costs increases when the U.S. dollar weakens and decreases when the U.S. dollar strengthens. 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 may negatively affect the Company's consolidated sales and gross margins (as expressed in U.S. dollars).

To mitigate the short-term impact of fluctuating currency exchange rates on the Company's non-U.S. dollar–based sales, product procurement, and operating expenses, the Company regularly hedges its non-U.S. dollar–based exposures. Specifically, the Company enters into foreign exchange forward and option contracts to hedge firmly committed transactions. Currently, hedges of firmly committed transactions do not extend beyond one year. The Company also purchases foreign exchange option contracts to hedge certain other probable, but not firmly committed transactions. Hedges of probable, but not firmly committed transactions do not extend beyond one year. To reduce the costs associated with these ongoing foreign exchange hedging programs, the Company also regularly sells foreign exchange option contracts and enters into certain other foreign exchange transactions. All foreign exchange forward and option contracts not accounted for as hedges, including all transactions intended to reduce the costs associated with the Company's foreign exchange hedging programs, are carried at fair value and are adjusted each balance sheet date for changes in exchange rates.

While the Company is exposed with respect to the interest rates of 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 interest paid on its short-term borrowings and long-term debt. To mitigate the impact of fluctuations in U.S. interest rates, the Company has entered into interest rate swap and option transactions. Certain of these swaps are intended to better match the Company's floating-rate interest income on its cash, cash equivalents, and short-term investments with the fixed-rate interest expense on its long-term debt. The Company also enters into interest rate swap, swaption, and option transactions in order to extend the effective duration of a portion of its cash, cash equivalent, and short-term investment portfolios. These swaps may extend the Company's cash investment horizon up to a maximum effective duration of three years.

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 nonhedge portfolios, the Company continually monitors its foreign exchange forward and option positions, and its interest rate swap, swaption, and option positions 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, there can be no assurance that 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. As such, the Company's operating results and financial position may be adversely affected.

Inventory

The Company's products include certain components, such as specific microprocessors manufactured by Motorola, Inc., that are currently available only from single sources. Any availability limitations, interruptions in supplies, or price increases of these and other components could adversely affect the Company's business and financial results. The Company's future operating results and financial condition may also be adversely affected by the Company's ability to manage inventory levels and lead times required to obtain components in order to be more responsive to short-term shifts in customer demand patterns. In addition, if anticipated unit sales growth for new and current product offerings is not realized, inventory valuation reserves may be necessary that would adversely affect the Company's results of operations and financial condition.

Marketing and Distribution

A number of uncertainties exist regarding the marketing and distribution of the Company's products. Currently, the Company's primary means of distribution is through third-party computer resellers. However, in response to changing industry practices and customer preferences, the Company is continuing its expansion into various consumer channels, such as mass-merchandise stores (for example, Sears and Wal-Mart), consumer electronics outlets, and computer superstores. The Company's business and financial results could be adversely affected if the financial condition of these sellers weakens or if sellers within consumer channels decide not to continue to distribute the Company's products.

Other Factors

The majority of the Company's research and development activities, its corporate headquarters, and other critical business operations are located near major seismic faults. The Company's operating results and financial condition could be materially adversely affected in the event of a major earthquake.

The Company plans to replace its current transaction systems (which include order management, distribution, manufacturing, and finance) with a single integrated system as part of its ongoing effort to increase operational efficiency. The Company's future operating results and financial condition could be adversely affected by its ability to implement and effectively manage the transition to this new integrated system.

Because of the foregoing factors, as well as other factors affecting the Company's operating results and financial condition, 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. In addition, the Company's participation in a highly dynamic industry often results in significant volatility of the Company's common stock price.

Liquidity and Capital Resources

	1994	1993	1992
Cash, cash equivalents, and short-term investments, net of short-term borrowings	$ 966	$ 69	$ 1,251
Working capital	$ 2,532	$ 1,830	$ 2,151
Cash generated by (used for) operations	$ 737	$ (651)	$ 921
Cash used for investment activities, excluding short-term investments	$ 163	$ 228	$ 264
Cash generated by (used for) financing activities	$ (208)	$ 336	$ (114)

The Company's financial position with respect to cash, cash equivalents, and short-term investments, net of short-term borrowings, increased to $966 million at September 30, 1994, from $69 million at September 24, 1993. This increase reflects a $300 million issuance of ten-year unsecured notes, the proceeds of which replaced a portion of the Company's short-term financing. The improvement in the Company's financial condition was also attributable to the Company's continued efforts to increase profit levels and to manage working capital, particularly in the area of inventory management.

More cash was generated by operations in 1994 compared with 1993, primarily because of a significant decrease in inventory levels, as well as increased sales levels. The significant decrease in inventory levels during 1994 resulted from improved inventory management, higher 1994 sales levels attributable to various pricing and promotional actions, and strong sales of new product inventory that had been built up in preparation for the introduction of Power Macintosh. Profit levels improved as operating expenses decreased due to the Company's implementation of restructuring actions initiated in the third quarter of 1993.

Cash generated by operations in 1994 was partially offset by cash used for restructuring and an increase in accounts receivable. The increase in accounts receivable reflected an increase in sales levels achieved during 1994. The balance of accrued restructuring costs decreased as the restructuring actions initiated in the third quarter of 1993 continued to be implemented. In addition, in the third quarter of 1994, the Company lowered its estimate of the costs associated with the restructuring and recorded an adjustment that increased income by $127 million ($79 million, or $0.66 per share, after taxes). This adjustment primarily reflected the modification or cancelation of certain elements of the Company's original restructuring plan because of changing business and economic conditions that made certain elements of the restructuring plan financially less attractive than originally anticipated.

More cash was used for operations in 1993 compared with 1992, primarily because of a significant increase in inventory levels; decreases in net income, income taxes payable, and other current liabilities; and an increase in accounts receivable levels. Cash used for operations was offset slightly by increases in accrued restructuring costs and accounts payable.

Inventory increased substantially during 1993 as a result of higher levels of purchased parts, work in process, and finished goods inventory in support of an expanded product line and distribution channels and anticipated higher sales volumes. The decrease in net income resulted primarily from a reduction in gross margins and the restructuring charge included in operating expenses for the third quarter. The reduction in earnings also contributed to the decrease in income taxes payable. Other current liabilities decreased as the Company continued to manage operating expense levels. The increase in accounts receivable corresponded to the higher sales levels achieved in 1993 compared with 1992, coupled with slower collections resulting from economic pressures in the reseller industry, and the Company's expansion into consumer channels, where payment terms are generally longer. These uses of cash were offset slightly by increases in accrued restructuring costs as a result of the Company's plan to restructure its operations worldwide and increases in accounts payable, reflecting the higher level of inventory purchases.

Excluding short-term investments, net cash used for investments declined in 1994 compared with 1993 and 1992 levels. Net cash used for the purchase of property, plant, and equipment totaled $160 million in 1994, and was primarily made up of increases in land, buildings, machinery, and equipment. The Company anticipates that capital expenditures in 1995 will be slightly above 1994 expenditures.

The Company leases the majority of its facilities and certain of its equipment under noncancelable operating leases. In 1994, rent expense under all operating leases was approximately $122 million. The Company's future lease commitments are discussed on page 32 of the Notes to Consolidated Financial Statements.

The Company's balance of long-term debt increased during 1994, due to the issuance of $300 million aggregate principal amount of 6.5% unsecured notes under an omnibus shelf registration statement filed with the Securities and Exchange Commission. This shelf registration was for the registration of debt and other securities for an aggregate offering amount of $500 million. The notes were sold at 99.925% of par, for an effective yield to maturity of 6.51%. The notes pay interest semiannually and mature on February 15, 2004. The 6.51% fixed rate was subsequently effectively converted to a floating rate through ten-year interest rate swaps based on the six-month U.S. dollar London Interbank Offered Rate (LIBOR). The impact of the swaps during 1994 was to reduce the 6.51% fixed-rate yield to a 5.62% yield. To mitigate the credit risk associated with these ten-year swap transactions, the Company entered into margining agreements with its third-party bank counterparties. Margining under these agreements generally does not start until 1997. Furthermore, these agreements would require the Company to post margin only if certain credit risk thresholds were exceeded. It is anticipated that any margin the Company may be required to post in the future would not have a material adverse effect on the Company's liquidity position.

Short-term borrowings at September 30, 1994, were approximately $531 million lower than at September 24, 1993, as the proceeds from the issuance of $300 million in long-term debt were used to pay down the balance of short-term borrowings. The Company's short-term borrowings reflect borrowings made under its commercial paper program and short-term uncommitted bid-line arrangements with certain commercial banks. In particular, Apple Japan, Inc., a wholly owned subsidiary of the Company, incurred short-term yen-denominated borrowings from several Japanese banks during 1994, the balance of which aggregated the U.S. dollar equivalent of approximately $202 million at September 30, 1994. During the first quarter of 1994, the Company also entered into a 364-day $500 million committed revolving-credit facility, which terminated on December 8, 1994, with a syndicate of banks primarily in support of its commercial paper program. No borrowings were made under this facility.

The Company expects that it will continue to incur short- and long-term borrowings from time to time to finance U.S. working capital needs and capital expenditures, because a substantial portion of the Company's cash, cash equivalents, and short-term investments is held by foreign subsidiaries, generally in U.S. dollar–denominated holdings. Amounts held by foreign subsidiaries would be subject to U.S. income taxation upon repatriation to the United States; the Company's financial statements provide fully for any related tax liability on amounts that may be repatriated. Refer to the Income Taxes footnote on pages 29–30 of the Notes to Consolidated Financial Statements for further discussion.

The Company believes that its balances of cash, cash equivalents, and short-term investments, together with funds generated from operations and short- and long-term borrowing capabilities, will be sufficient to meet its operating cash requirements on a short- and long-term basis.

Consolidated Balance Sheets

(Dollars in thousands)

September 30, 1994, and September 24, 1993	1994	1993
Assets:		
Current assets:		
Cash and cash equivalents	$ 1,203,488	$ 676,413
Short-term investments	54,368	215,890
Accounts receivable, net of allowance for doubtful accounts of $90,992 ($83,776 in 1993)	1,581,347	1,381,946
Inventories	1,088,434	1,506,638
Deferred tax assets	293,048	268,085
Other current assets	255,767	289,383
Total current assets	4,476,452	4,338,355
Property, plant, and equipment:		
Land and buildings	484,592	404,688
Machinery and equipment	572,728	578,272
Office furniture and equipment	158,160	167,905
Leasehold improvements	236,708	261,792
	1,452,188	1,412,657
Accumulated depreciation and amortization	(785,088)	(753,111)
Net property, plant, and equipment	667,100	659,546
Other assets	159,194	173,511
	$ 5,302,746	$ 5,171,412
Liabilities and Shareholders' Equity:		
Current liabilities:		
Short-term borrowings	$ 292,200	$ 823,182
Accounts payable	881,717	742,622
Accrued compensation and employee benefits	136,895	144,779
Accrued marketing and distribution	178,294	174,547
Accrued restructuring costs	58,238	307,932
Other current liabilities	396,961	315,023
Total current liabilities	1,944,305	2,508,085
Long-term debt	304,472	7,117
Deferred tax liabilities	670,668	629,832
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par value; 320,000,000 shares authorized; 119,542,527 shares issued and outstanding in 1994 (116,147,035 shares in 1993)	297,929	203,613
Retained earnings	2,096,206	1,842,600
Accumulated translation adjustment	(10,834)	(19,835)
Total shareholders' equity	2,383,301	2,026,378
	$ 5,302,746	$ 5,171,412

See accompanying notes.

Consolidated Statements of Income

(In thousands, except per share amounts)

Three fiscal years ended September 30, 1994	1994	1993	1992
Net sales	$ 9,188,748	$ 7,976,954	$ 7,086,542
Costs and expenses:			
Cost of sales	6,844,915	5,248,834	3,991,337
Research and development	564,303	664,564	602,135
Selling, general and administrative	1,384,111	1,632,362	1,687,262
Restructuring costs	(126,855)	320,856	—
	8,666,474	7,866,616	6,280,734
Operating income	522,274	110,338	805,808
Interest and other income (expense), net	(21,988)	29,321	49,634
Income before income taxes	500,286	139,659	855,442
Provision for income taxes	190,108	53,070	325,069
Net income	$ 310,178	$ 86,589	$ 530,373
Earnings per common and common equivalent share	$ 2.61	$ 0.73	$ 4.33
Common and common equivalent shares used in the calculations of earnings per share	118,735	119,125	122,490

See accompanying notes.

Consolidated Statements of Shareholders' Equity

(In thousands, except per share amounts)

	Common Stock		Retained	Accumulated Translation	Notes Receivable from	Total Shareholders'
	Shares	Amount	Earnings	Adjustment	Shareholders	Equity
Balance at September 27, 1991	118,386	$ 278,865	$ 1,492,024	$ (2,377)	$ (1,836)	$ 1,766,676
Common stock issued under stock option and purchase plans, including related tax benefits	4,093	155,388	—	—	—	155,388
Repurchase of common stock	(4,000)	(151,943)	(60,682)	—	—	(212,625)
Repayment of notes receivable from shareholders	—	—	—	—	1,836	1,836
Cash dividends of $0.48 per common share	—	—	(57,196)	—	—	(57,196)
Accumulated translation adjustment	—	—	—	2,918	—	2,918
Net income	—	—	530,373	—	—	530,373
Balance at September 25, 1992	118,479	282,310	1,904,519	541	—	2,187,370
Common stock issued under stock option and purchase plans, including related tax benefits	2,693	101,842	—	—	—	101,842
Repurchase of common stock	(5,025)	(180,539)	(92,915)	—	—	(273,454)
Cash dividends of $0.48 per common share	—	—	(55,593)	—	—	(55,593)
Accumulated translation adjustment	—	—	—	(20,376)	—	(20,376)
Net income	—	—	86,589	—	—	86,589
Balance at September 24, 1993	116,147	203,613	1,842,600	(19,835)	—	2,026,378
Common stock issued under stock option and purchase plans, including related tax benefits	3,396	94,316	—	—	—	94,316
Cash dividends of $0.48 per common share	—	—	(56,572)	—	—	(56,572)
Accumulated translation adjustment	—	—	—	9,001	—	9,001
Net income	—	—	310,178	—	—	310,178
Balance at September 30, 1994	119,543	$ 297,929	$ 2,096,206	$ (10,834)	$ —	$ 2,383,301

See accompanying notes.

Consolidated Statements of Cash Flows

(In thousands)

Three fiscal years ended September 30, 1994	1994	1993	1992
Cash and cash equivalents, beginning of the period	$ 676,413	$ 498,557	$ 604,147
Operations:			
Net income	310,178	86,589	530,373
Adjustments to reconcile net income to cash generated by (used for) operations:			
Depreciation and amortization	167,958	166,113	217,182
Net book value of property, plant, and equipment retirements	11,130	13,145	14,687
Changes in assets and liabilities:			
Accounts receivable	(199,401)	(294,761)	(180,026)
Inventories	418,204	(926,541)	91,558
Deferred tax assets	(24,963)	(68,946)	23,841
Other current assets	33,616	(96,314)	(87,376)
Accounts payable	139,095	315,686	69,852
Income taxes payable	50,045	(54,724)	100,361
Accrued restructuring costs	(249,694)	202,894	(57,327)
Other current liabilities	39,991	(13,383)	96,915
Deferred tax liabilities	40,836	19,029	100,933
Cash generated by (used for) operations	736,995	(651,213)	920,973
Investments:			
Purchase of short-term investments	(312,073)	(1,431,998)	(2,121,341)
Proceeds from sale of short-term investments	473,595	2,153,051	1,472,970
Purchase of property, plant, and equipment	(159,587)	(213,118)	(194,853)
Other	(3,737)	(15,169)	(69,410)
Cash generated by (used for) investment activities	(1,802)	492,766	(912,634)
Financing:			
Increase (decrease) in short-term borrowings	(530,982)	638,721	35,895
Increase (decrease) in long-term borrowings	297,355	(10,624)	(391)
Increases in common stock, net of related tax benefits and changes in notes receivable from shareholders	82,081	85,289	120,388
Repurchase of common stock	—	(273,454)	(212,625)
Cash dividends	(56,572)	(55,593)	(57,196)
Other	—	(48,036)	—
Cash generated by (used for) financing activities	(208,118)	336,303	(113,929)
Total cash generated (used)	527,075	177,856	(105,590)
Cash and cash equivalents, end of the period	$ 1,203,488	$ 676,413	$ 498,557
Supplemental cash flow disclosures:			
Cash paid during the year for:			
Interest	$ 34,387	$ 11,748	$ 8,778
Income taxes, net	$ 45,692	$ 226,080	$ 97,667
Schedule of noncash transactions:			
Tax benefit from stock options	$ 12,235	$ 16,553	$ 36,836

See accompanying notes.

Notes to Consolidated Financial Statements

Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of Apple Computer, Inc. and its wholly owned subsidiaries (the Company). Intercompany accounts and transactions have been eliminated. The Company's fiscal year-end is the last Friday in September.

Revenue Recognition

The Company recognizes revenue at the time products are shipped. Provisions are made currently for estimated product returns and price protection that may occur under Company programs. Historically, actual amounts recorded for product returns and price protection have not varied significantly from estimated amounts.

Warranty Expense

The Company provides currently for the estimated cost that may be incurred under product warranties when products are shipped.

Foreign Currency

Gains and losses resulting from foreign currency translation are accumulated as a separate component of shareholders' equity until the foreign entity is sold or liquidated. Gains and losses resulting from foreign currency transactions are included in the consolidated statements of income.

Financial Instruments

All highly liquid investments with a maturity of three months or less at the date of purchase are considered to be cash equivalents; investments with maturities between three and twelve months are considered to be short-term investments. A substantial portion of the Company's cash, cash equivalents, and short-term investments is held by foreign subsidiaries and is generally based in U.S. dollar–denominated holdings. Amounts held by foreign subsidiaries would be subject to U.S. income taxation upon repatriation to the United States; the Company's financial statements provide fully for any related tax liability on amounts that may be repatriated, aside from undistributed earnings that are intended to be indefinitely invested.

The Company has not elected early adoption of Financial Accounting Standard No. 115 (FAS 115), "Accounting for Certain Investments in Debt and Equity Securities." FAS 115 becomes effective beginning with the Company's first quarter of fiscal year 1995. The principal impact of the new statement is to replace the historical cost accounting approach for certain investments in debt and equity securities with one based on fair value. The Company does not expect adoption of FAS 115 to have a material effect on its financial position or results of operations.

For further information regarding the Company's accounting treatment of other financial and derivative instruments, refer to pages 24–26 of the Notes to Consolidated Financial Statements.

Income Taxes

Effective September 25, 1993, the Company adopted Financial Accounting Standard No. 109 (FAS 109), "Accounting for Income Taxes," which changes the method of accounting for income taxes from the deferred method to the liability method. This change in accounting principle has been adopted on a prospective basis, and the financial statements of years ended prior to September 25, 1993, have not been restated. The cumulative effect of the change was not material. Under FAS 109, deferred tax assets and liabilities reflect the future income tax effects of temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates that apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under FAS 109, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Prior to 1994, the Company accounted for income taxes under the provisions of APB Opinion No. 11, which recognized deferred taxes for the effect of timing differences between pretax accounting income and taxable income. Under the deferred method of APB Opinion No. 11, deferred taxes were not adjusted for subsequent changes in tax rates.

U.S. income taxes have not been provided on a cumulative total of $335 million of undistributed earnings of certain of the Company's foreign subsidiaries. It is intended that these earnings will be indefinitely invested in operations outside the United States. It is not practicable to determine the income tax liability that might be incurred if these earnings were to be distributed. Except for such indefinitely invested earnings, the Company provides federal and state income taxes currently on undistributed earnings of foreign subsidiaries.

Earnings per Share

Earnings per share are computed using the weighted average number of common and dilutive common equivalent shares attributable to stock options outstanding during the period. Loss per share is computed using the weighted average number of common shares outstanding during the period.

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market. If the cost of the inventories exceeds their market value, provisions are made currently for the difference between the cost and the market value.

Property, Plant, and Equipment

Property, plant, and equipment is stated at cost. Depreciation and amortization is computed by use of the declining balance and straight-line methods over the estimated useful lives of the assets.

Reclassifications

Certain prior year amounts on the Consolidated Balance Sheets, Consolidated Statements of Cash Flows, Industry Segment and Geographic Information, and Income Taxes footnotes have been reclassified to conform to the current year presentation.

Financial Instruments

Financial Instruments with Off-Balance-Sheet Risk

In the ordinary course of business and as part of the Company's asset and liability management, the Company enters into various types of transactions that involve contracts and financial instruments with off-balance-sheet risk. These instruments are entered into in order to manage financial market risk, including interest rate and foreign exchange risk. The Company enters into these financial instruments with major international financial institutions utilizing over-the-counter as opposed to exchange traded instruments.

Interest Rate Derivatives

The Company enters into interest rate derivatives, including interest rate swaps, swaptions, and options, with financial institutions in order to better match the Company's floating-rate interest income on its cash equivalents and short-term investments with the fixed-rate interest expense of its long-term debt. These instruments are also used to extend the effective duration of a portion of the Company's short-term investment portfolio up to a maximum duration of three years, and to diversify a portion of its exposure away from changes in U.S. interest rates.

Foreign Currency Instruments

The Company enters into foreign exchange forward and option contracts with financial institutions primarily to protect against currency exchange risks associated with certain firmly committed and certain other probable, but not firmly committed transactions. The Company's foreign exchange risk management policy requires it to hedge substantially all of its material foreign exchange transaction exposures. However, the Company does not hedge certain foreign exchange transaction exposures that are immaterial either in terms of their minimal U.S. dollar value or in terms of their high correlation with the U.S. dollar.

Anticipated transactions comprise sales of the Company's products in currencies other than the U.S. dollar. A majority of these non-U.S. dollar–based sales are made through the Company's subsidiaries in Europe, Asia (particularly Japan), Canada, and Australia. The duration of these anticipated hedging transactions does not exceed one year. The Company also sells foreign exchange option contracts, in order to partially finance the purchase of foreign exchange option contracts used to hedge both firmly committed and certain other probable, but not firmly committed transactions. The Company enters into other foreign exchange transactions, which are intended to reduce the costs associated with its foreign exchange risk management programs.

Fair Value, Notional Principal, and Credit Risk Amounts

The table on page 25 shows the notional principal, fair value, and credit risk amounts of the Company's interest rate derivative and foreign currency instruments as of September 30, 1994. The notional principal amounts for off-balance-sheet instruments provide one measure of the transaction volume outstanding as of year end, and do not represent the amount of the Company's exposure to credit or market loss. The credit risk amount shown in the table on page 25 represents the Company's gross exposure to potential accounting loss on these transactions if all counterparties failed to perform according to the terms of the contract, based on then-current currency exchange and interest rates at each respective date. The Company's exposure to credit loss and market risk will vary over time as a function of interest rates and currency exchange rates.

The estimates of fair value are based on applicable and commonly used pricing models using prevailing financial market information as of September 30, 1994. In certain instances where judgment is required in estimating fair value, price quotes were obtained from several of the Company's counterparty financial institutions. Although the table on page 25 reflects the notional principal, fair value, and credit risk amounts of the Company's interest rate and foreign exchange instruments, it does not reflect the gains or losses associated with the exposures and transactions that the interest rate and foreign exchange instruments are intended to hedge. The amounts ultimately realized upon settlement of these financial instruments, together with the gains and losses on the underlying exposures, will depend on actual market conditions during the remaining life of the instruments.

(In millions)

	1994			1993[A]		
	Notional Principal	Fair Value	Credit Risk Amount	Notional Principal	Fair Value	Credit Risk Amount
Transactions Qualifying as Accounting Hedges						
Interest rate instruments						
Swaps	$ 669	$ (40)	—	—	—	—
Foreign exchange instruments						
Spot/Forward contracts	$ 2,385	$ (23)	$ 15	$ 2,114	$ 6	$ 19
Purchased options	$ 1,510	$ 17	$ 21	$ 1,637	$ 28	$ 33
Sold options	$ 302	$ (1)	—	$ 765	—[B]	—
Transactions Other Than Accounting Hedges						
Interest rate instruments						
Swaps	—	—	—	$ 112	—[B]	—
Sold options	$ 148	—[B]	—	$ 67	—[B]	—
Foreign exchange instruments						
Spot/Forward contracts	$ 300	—[B]	—[B]	$ 574	$ 2	$ 10
Purchased options	$ 1,600	$ 32	$ 32	$ 1,608	$ 24	$ 24
Sold options	$ 5,511	$ (45)	—	$ 5,282	$ (39)	—

(A) Adjusted to conform with current year presentation.
(B) Fair value is less than $0.5 million.

The interest rate swaps shown above generally require the Company to pay a floating interest rate based on three- or six-month U.S. dollar LIBOR and receive a fixed rate of interest based on two-, three-, and ten-year swap rates without exchanges of the underlying notional amounts. Maturity dates for interest rate swaps currently range from one to ten years. Interest rate option contracts require the Company to make payments should certain interest rates either fall below or rise above predetermined levels. All interest rate option contracts outstanding at September 30, 1994, expire within 18 months.

Interest rate contracts not accounted for as hedges are carried at fair value with gains and losses recorded currently in income. Unrealized gains and losses on interest rate contracts that are designated and effective as hedges are deferred and recognized in income in the same period as the hedged transaction. Unrealized losses on such agreements totaled approximately $40 million at September 30, 1994, primarily reflecting the net present value of unrealized losses on the ten-year swap contracts, which effectively convert the Company's fixed-rate ten-year debt to floating-rate debt. There were no deferred gains and losses on interest rate contracts as of September 24, 1993.

The foreign exchange forward contracts not accounted for as hedges are carried at fair value and are adjusted each balance sheet date for changes in exchange rates. Unrealized gains and losses on foreign exchange forward contracts that are designated and effective as hedges are deferred and recognized in income in the same period as the hedged transactions. Deferred gains and losses on such agreements at September 30, 1994, and at September 24, 1993, were immaterial. All foreign exchange forward contracts expire within one year.

Purchased and sold foreign exchange option contracts that qualify for hedge accounting treatment are reported on the balance sheet at the premium cost, which is amortized over the life of the option. Unrealized gains and losses on these option contracts are deferred until the occurrence of the hedged transaction and recognized as a component of the hedged transaction. Deferred gains and losses on such agreements were immaterial at September 30, 1994, and at September 24, 1993. Maturity dates for purchased foreign exchange option contracts range from one to twelve months.

Purchased and sold foreign exchange option contracts that do not qualify for hedge accounting treatment are carried at fair value and, as such, are adjusted each balance sheet date for changes in exchange rates. Gains and losses associated with these financial instruments are recorded currently in income. As of September 30, 1994, maturity dates for these sold option contracts ranged from one to six months.

The Company monitors its interest rate and foreign exchange positions daily based on applicable and commonly used pricing models. The correlation between the changes in the fair value of hedging instruments and the changes in the underlying hedged items is assessed periodically over the life of the hedged instrument. In the event that it is determined that a hedge is ineffective, the Company recognizes in income the change in market value of the instrument beginning on the date it was no longer an effective hedge.

Other Financial Instruments

The carrying amounts and estimated fair values of the Company's other financial instruments are as follows:

(In millions)

	1994		1993	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	$ 1,203	$ 1,203	$ 676	$ 676
Short-term investments	$ 54	$ 54	$ 216	$ 216
Short-term borrowings	$ 292	$ 292	$ 823	$ 823
Long-term debt:				
Ten-year unsecured notes	$ 300	$ 259	—	—
Other	$ 4	$ 4	$ 7	$ 7

Short-term investments are carried at cost plus accrued interest, which approximates fair value. The carrying amount of short-term borrowings approximates their fair value due to their short-term maturities. The fair value of the ten-year unsecured notes is based on their listed market value as of September 30, 1994.

Concentrations of Credit Risk

The Company distributes its products principally through third-party computer resellers and various education and consumer channels. Concentrations of credit risk with respect to trade receivables are limited because of flooring arrangements for selected customers with third-party financing companies and because the Company's customer base consists of large numbers of geographically diverse customers dispersed across several industries. As such, the Company generally does not require collateral from its customers.

The counterparties to the agreements relating to the Company's investments and foreign exchange and interest rate instruments consist of a number of major international financial institutions. To date, no such counterparty has failed to meet its financial obligations to the Company. The Company does not believe that there is significant risk of nonperformance by these counterparties because the Company continually monitors its positions and the credit ratings of such counterparties, and limits the financial exposure and the amount of agreements and contracts it enters into with any one party. The Company generally does not require collateral from counterparties, except for margin agreements associated with the ten-year interest rate swaps on the Company's long-term debt. To mitigate the credit risk associated with these ten-year swap transactions, the Company entered into margining agreements with its third-party bank counterparties. Margining under these agreements generally does not start until 1997. Furthermore, these agreements would require the Company or the counterparty to post margin only if certain credit risk thresholds were exceeded.

Inventories

Inventories consist of the following:

(In thousands)

	1994	1993
Purchased parts	$ 469,420	$ 504,201
Work in process	206,654	284,440
Finished goods	412,360	717,997
	$ 1,088,434	$ 1,506,638

Borrowings

Short-Term Borrowings	1994	1993
		(In thousands)
Commercial paper	$ 89,817	$ 823,182
Notes payable to banks	202,383	—
	$ 292,200	$ 823,182

The weighted average interest rates for commercial paper borrowings at September 30, 1994, and September 24, 1993, were approximately 5.0% and 3.3%, respectively. The weighted average interest rate for the Japanese yen-denominated notes payable to banks at September 30, 1994, was approximately 2.6%. Interest expense on short-term borrowings was $24.9 million, $8.9 million, and $6.5 million for 1994, 1993, and 1992, respectively.

On December 9, 1993, the Company entered into a 364-day $500 million committed revolving-credit facility with a syndicate of banks primarily in support of its commercial paper program. This facility terminated on December 8, 1994. No borrowings were made under this facility. The cost of this facility was immaterial.

Long-Term Debt

On February 10, 1994, the Company issued $300 million aggregate principal amount of 6.5% unsecured notes under the Company's $500 million omnibus shelf registration statement filed with the Securities and Exchange Commission. The notes were sold at 99.925% of par, for an effective yield to maturity of 6.51%. The notes pay interest semi-annually and mature on February 15, 2004. Interest expense on the ten-year unsecured notes for the year ended September 30, 1994, was approximately $12 million. Other long-term debt of approximately $4 million and $7 million at September 30, 1994, and September 24, 1993, respectively, and the related interest expense in each of the three years ended September 30, 1994, was immaterial.

For information regarding the Company's estimated fair value of short- and long-term debt, refer to page 26 of the Notes to Consolidated Financial Statements.

Restructuring of Operations

In the third quarter of 1993, the Company initiated a plan to restructure its operations worldwide in order to address the competitive conditions in the personal computer industry, including the increased market demand for lower-priced products. In connection with this plan, the Company recorded a $321 million charge to operating expenses ($199 million, or $1.72 per share, after taxes). The restructuring costs included $162 million of estimated employee-related expenses and $159 million of estimated facilities, equipment, and other expenses associated with the consolidation of operations and the relocation and termination of certain operations and employees. The restructuring plan originally contemplated the termination or relocation of approximately 4,150 employees worldwide and the reduction in worldwide office space, which primarily consisted of approximately 1.6 million square feet of office space in the San Francisco Bay Area, within one year from the date the restructuring was initiated.

In the third quarter of 1994, the Company lowered its estimate of the total costs associated with the restructuring and recorded an adjustment that increased income by $127 million ($79 million, or $0.66 per share, after taxes). This adjustment primarily reflected the modification or cancelation of certain elements of the Company's original restructuring plan because of changing business and economic conditions that made certain elements of the restructuring plan financially less attractive than originally anticipated. In addition, some actions were completed at a lower cost than originally estimated.

The most significant element of the adjustment was associated with $61 million in costs accrued to terminate or move a number of employees from the San Francisco Bay Area to a lower-cost location. This element of the Company's restructuring plan was expected to result in the termination or relocation of approximately 2,000 employees and the closure of certain leased facilities, at a cost of $39 million and $22 million, respectively. However, the expected benefits of this move were reduced since the plan's inception because of changes to the cost differential between the Company's current and alternative locations. For example, the Company favorably renegotiated the lease terms of certain facilities in its current locations, the salary growth rate differentials between the Bay Area and alternative locations were reduced, and recent changes to the California income tax laws made it more attractive for companies to do business in California. The Company canceled this action in the third quarter of 1994, when management decided that the extended estimated pay-back period no longer justified the initial cash investment and the unquantifiable cost of business disruption that such a move would precipitate.

At the end of fiscal year 1994, approximately 1,760 employees had been terminated and approximately 80 had been relocated, and the Company had reduced its use of office space in the Bay Area by approximately 867,000 square feet.

At the time the restructuring was announced, management had publicly set a goal of reducing operating costs below $500 million per quarter and increasing sales significantly to achieve acceptable profitability. These goals were met by the end of the third quarter of fiscal 1994. The Company continues to search for ways to permanently reduce its cost structure. Although the Company has achieved a lower level of operating expenses without fully implementing all of the restructuring actions as originally planned, there can be no assurance that this level of operating expenses will be maintained in the future. For example, operating expenses (excluding restructure) in 1994 were reduced by $349 million, or 15%, compared with 1993, despite an increase in net sales of 15%.

As of September 30, 1994, the Company had $58 million of accrued restructuring costs for actions that are currently under way and expected to be completed during 1995. Approximately $52 million of this accrual represents cash charges primarily for estimated facilities, equipment, and other expenses, the majority of which are expected to be incurred during 1995. Cash spending beyond one year primarily relates to approximately $6 million of recurring payments under certain noncancelable operating leases.

The following table depicts a roll-forward reconciliation of the activity in the restructuring accrual balance from September 24, 1993, to September 30, 1994:

(In thousands)

Category	Balance at September 24, 1993	Spending	Adjustments	Balance at September 30, 1994
Employee termination payments (C)	$ 84,062	$ 42,376	$ 30,933	$ 10,753
Other costs relating to terminated employees (B)	4,282	3,227	1,055	—
Provisions relating to employees who will not be terminated (C)	41,818	8,536	28,603	4,679
Termination payments for leases and other contracts (C)	92,736	32,907	39,728	20,101
Write-down of operating assets to be sold (N)	16,864	9,748	5,925	1,191
Provisions for litigation (C)	3,600	—	1,856	1,744
R&D project cancelations (C)	14,858	7,043	1,624	6,191
Other provisions and write-downs (B)	31,863	10,254	8,875	12,734
1991 accrued restructuring costs (B)	17,849	8,748	8,256	845
	$ 307,932	$ 122,839	$ 126,855	$ 58,238

(C) Cash; (N) Noncash; (B) Both cash and noncash.

Interest and Other Income (Expense), Net

Interest and other income (expense), net, consists of the following:

(In thousands)

	1994	1993	1992
Interest income	$ 43,284	$ 70,225	$ 71,686
Interest expense	(39,653)	(11,800)	(8,708)
Discount on foreign exchange instruments	(34,304)	(31,803)	(27,062)
Other income (expense), net	8,685	2,699	13,718
	$ (21,988)	$ 29,321	$ 49,634

Income Taxes

The provision for income taxes consists of the following:

(In thousands)

	FAS 109 Method	APB 11 Method	
	1994	1993	1992
Federal:			
Current	$ 60,757	$ 13,637	$ 108,512
Deferred	19,673	(23,757)	100,355
	80,430	(10,120)	208,867
State:			
Current	5,769	3,144	26,935
Deferred	20,352	633	13,891
	26,121	3,777	40,826
Foreign:			
Current	71,095	39,512	65,144
Deferred	12,462	19,901	10,232
	83,557	59,413	75,376
Provision for income taxes	$ 190,108	$ 53,070	$ 325,069

The foreign provision for income taxes is based on foreign pretax earnings of approximately $474 million, $416 million, and $611 million in 1994, 1993, and 1992, respectively. The tax benefit credited directly to common stock as a result of compensation expense attributable to employee stock option and purchase plans recognized differently for financial reporting and tax purposes was $11 million in 1994.

As discussed in the Summary of Significant Accounting Policies, the Company adopted FAS 109 effective as of the beginning of the fiscal year ended September 30, 1994. Prior to 1994, the Company accounted for income taxes under the provisions of APB Opinion No. 11. Under FAS 109, deferred tax assets and liabilities reflect the future income tax effects of temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases.

At September 30, 1994, the significant components of the Company's deferred tax assets and liabilities were as follows:

(In thousands)

	September 30, 1994
Deferred tax assets:	
Accounts receivable and inventory reserves	$ 140,842
Accrued liabilities and other reserves	125,402
Basis of capital assets and investments	66,256
Total deferred tax assets	332,500
Less: Valuation allowance	10,948
Net deferred tax assets	321,552
Deferred tax liabilities:	
Unremitted earnings of subsidiaries	656,806
Other	28,791
Total deferred tax liabilities	685,597
Net deferred tax liability	$ 364,045

The net change in the total valuation allowance for the year ended September 30, 1994, was an increase of $11 million.

Under APB Opinion No. 11, deferred income taxes result from timing differences between years in the recognition of certain revenue and expense items for financial and tax reporting purposes. The sources of timing differences and the related tax effects for 1993 and 1992 are as follows:

(In thousands)

	1993	1992
Income of foreign subsidiaries not taxable in current year	$ 53,150	$ 71,429
Warranty, bad debt, and other expenses	(80,126)	35,494
Depreciation	(3,796)	(3,398)
Inventory valuation	(16,835)	(1,940)
State income taxes	2,607	(10,959)
Other individually immaterial items	41,777	33,852
Total deferred taxes	$ (3,223)	$ 124,478

A reconciliation of the provision for income taxes, with the amount computed by applying the statutory federal income tax rate (35.00% in 1994, 34.75% in 1993, and 34.00% in 1992) to income before income taxes, is as follows:

(In thousands)

	FAS 109 Method	APB 11 Method	
	1994	1993	1992
Computed expected tax	$ 175,100	$ 48,532	$ 290,850
State taxes, net of federal benefit	16,978	2,465	26,945
Research and development tax credit	(1,000)	(8,000)	(7,000)
Indefinitely invested earnings of foreign subsidiaries	(49,350)	(21,083)	(31,280)
Valuation allowance	9,016	—	—
Other individually immaterial items	39,364	31,156	45,554
Provision for income taxes	$ 190,108	$ 53,070	$ 325,069
Effective tax rate	38%	38%	38%

The Internal Revenue Service has proposed federal income tax deficiencies for the years 1984 through 1988, and the Company has made prepayments thereon. The Company has contested these alleged deficiencies and is pursuing administrative and judicial remedies. Management believes that adequate provision has been made for any adjustments that may result from these tax examinations.

Common Stock

Shareholder Rights Plan

In May 1989, the Company adopted a shareholder rights plan and distributed a dividend of one right to purchase one share of common stock (a Right) for each outstanding share of common stock of the Company. The Rights become exercisable in certain limited circumstances involving a potential business combination transaction of the Company and are initially exercisable at a price of $200 per share. Following certain other events after the Rights have become exercisable, each Right entitles its holder to purchase for $200 an amount of common stock of the Company, or, in certain circumstances, securities of the acquiror, having a then-current market value of two times the exercise price of the Right. The Rights are redeemable and may be amended at the Company's option before they become exercisable. Until a Right is exercised, the holder of a Right, as such, has no rights as a shareholder of the Company. The Rights expire on April 19, 1999.

Stock Option Plans

The Company has in effect a 1990 Stock Option Plan (the 1990 Plan) and a 1987 Executive Long Term Stock Option Plan (the 1987 Plan). The 1981 Stock Option Plan terminated in October 1990. Options granted before that date remain outstanding in accordance with their terms. Options may be granted under the 1990 Plan to employees, including officers and directors who are employees, at not less than the fair market value on the date of grant. These options generally become exercisable over varying periods, based on continued employment, and generally expire ten years after the grant date. The 1990 Plan permits the granting of incentive stock options, nonstatutory stock options, and stock appreciation rights.

The 1987 Plan permits the granting of nonstatutory options to certain officers of the Company to purchase Apple common stock at prices not less than 75% of the fair market value on the date of grant. Options under the 1987 Plan are generally not exercisable for 18 months after the date of grant, and then become exercisable at varying rates over the subsequent seven years, based on continued service to the Company.

Summarized information regarding the Company's stock option plans as of September 30, 1994, is as follows:

(In thousands, except per share amounts)

	Number of Shares	Price per Share
Outstanding at September 24, 1993	13,096	$7.50–$68.00
Granted	4,705	
Exercised	(2,223)	$23.50–$38.25
Expired or canceled	(2,167)	
Outstanding at September 30, 1994	13,411	$7.50–$68.00
Exercisable	5,475	
Reserved for issuance	19,286	
Available for future grant	5,879	

Restricted Stock Plan

On April 1, 1993, the Company's Board of Directors approved a Restricted Stock Plan for officers of the Company (the RSP), which became effective July 1, 1993. The RSP was subsequently ratified by the shareholders on January 26, 1994. The RSP is designed to provide an incentive for officers to continue to own shares of the Company's common stock acquired upon exercise of options under any of the Company's Stock Option Plans, thus more closely aligning officers' financial interests with those of the shareholders. The RSP provides that officers who exercise stock options and continue to hold the exercised shares for at least three years will receive up to three Awards of shares of restricted stock. Each such Award is for one-third the number of shares held for the requisite retention period. Each restricted stock Award granted pursuant to the plan becomes fully vested three years after the grant date, provided that the officer maintains continuous employment with the Company and that other vesting requirements are met.

Employee Stock Purchase Plan

The Company has an employee stock purchase plan (the Purchase Plan) under which substantially all employees may purchase common stock through payroll deductions at a price equal to 85% of the lower of the fair market values as of the beginning or end of the offering period. Stock purchases under the Purchase Plan are limited to 10% of an employee's compensation, up to a maximum of $25,000 in any calendar year. As of September 30, 1994, approximately 1 million shares were reserved for future issuance under the Purchase Plan.

Stock Repurchase Programs

In November 1992, the Board of Directors authorized the purchase of up to 10 million shares of the Company's common stock in the open market. No shares were repurchased under this authorization in 1994, while approximately 3.4 million shares were repurchased under this authorization in 1993. In September 1990, the Board of Directors authorized the purchase of up to 10 million shares of the Company's common stock in the open market. During 1993 and 1992, the Company repurchased the remaining shares under this authorization, which approximated to 1.6 million and 4.0 million shares, respectively.

Savings Plan

The Company has an employee savings plan (the Savings Plan) that qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. Under the Savings Plan, participating U.S. employees may defer a portion of their pretax earnings, up to the Internal Revenue Service annual contribution limit ($9,240 for calendar year 1994). Effective July 1, 1994, the Company matches 30% to 70% of each employee's contributions, depending on length of service, up to a maximum 6% of the employee's earnings. Prior to July 1, 1994, the Company matched 30% to 50% of each employee's contributions, depending on length of service, up to a maximum 6% of the employee's earnings. The Company's matching contributions to the Savings Plan were approximately $10.7 million in 1994 and $11.1 million in each of 1993 and 1992.

Preferred Stock

Five million shares of preferred stock have been authorized for issuance in one or more series. The Board of Directors is authorized to fix the number and designation of any such series and to determine the rights, preferences, privileges, and restrictions granted to or imposed on any such series.

Commitments and Contingencies

Lease Commitments

The Company leases various facilities and equipment under noncancelable operating lease arrangements. The major facilities leases are for terms of five to ten years and generally provide renewal options for terms of up to five additional years. Rent expense under all operating leases was approximately $122 million, $170 million, and $160 million in 1994, 1993, and 1992, respectively. Future minimum lease payments under these noncancelable operating leases having remaining terms in excess of one year as of September 30, 1994, are as follows:

	(In thousands)
1995	$ 85,090
1996	60,127
1997	38,025
1998	16,928
1999	6,908
Later years	24,256
Total minimum lease payments	$ 231,334

Leases for facilities that were subject to the Company's restructuring actions initiated in the third quarter of 1991 and in the third quarter of 1993 are included in the preceding table. Future lease payments associated with these facilities were provided for in the Company's restructuring reserves recorded in 1993 and 1991, and therefore do not represent future operating expenses. Minimum lease payments may decline in the future, as the leases for facilities subject to restructuring actions are terminated or otherwise completed. For additional information regarding restructuring of operations, refer to pages 27–28 of the Notes to Consolidated Financial Statements.

In January 1994, a wholly owned subsidiary of the Company exercised its option to purchase, for $51.9 million, the remaining partnership interest in the Cupertino Gateway Partners partnership, a general partnership, which owns the Company's campus-type office facilities located in Cupertino, California (the "Campus"). As a result of this purchase, the Company's wholly owned subsidiary now owns 100% of the right, title, and interest in the Campus, as opposed to a 50.001% investment in the partnership held in the prior year. Because of this purchase, future minimum lease payments to the partnership of approximately $162 million have been excluded from the preceding table.

Litigation

Apple v. Microsoft Corporation and Hewlett-Packard Company

In March 1988, the Company filed suit in the U.S. District Court for the Northern District of California (the Court) against Microsoft Corporation (Microsoft) and Hewlett-Packard Company (HP), alleging that their Microsoft Windows and HP NewWave computer programs infringe the Company's audiovisual copyrights protecting the Macintosh user interface. On August 24, 1993, the district court entered final judgment for Microsoft and HP, dismissing the Company's action.

On September 21, 1993, the Court denied defendants' motions for an award of full defense costs and attorneys' fees under 17 U.S.C. Section 505, but allowed defendants to renew their motions should the Supreme Court alter the standard for the award of attorneys' fees in copyright cases in the case of *Fogerty v Fantasy, Inc.,* 114 S. Ct. 1023 (1994).

On September 20, 1993, the Company appealed the case to the U.S. Court of Appeals for the Ninth Circuit. On September 24, 1994, the Court of Appeals issued its decision affirming the district court judgment on the merits but remanding the case on the issue of attorneys' fees in light of the *Fogerty* decision. The Company plans to file a petition for a *writ of certiorari* in the Supreme Court of the United States.

In re Apple Securities Litigation (1993)

In 1993, a number of civil class action complaints relating to the June 1993 drop in price of Apple stock were filed in U.S. District Court against the Company and certain of its officers and directors, alleging violations of federal securities laws for alleged material misrepresentations and omissions of fact concerning the Company's business. The cases were subsequently consolidated into *In re Apple Securities Litigation,* Civ. No. C-93-20521-RPA (EAI). These suits were filed on behalf of the named plaintiffs and all others who purchased the Company's common stock between October 15, 1992, and July 15, 1993. Plaintiffs seek an award of damages according to proof, with interest.

1993 State Court Shareholders Action

In 1993, certain derivative class action complaints relating to the June 1993 drop in price of Apple stock were filed against the Company, as nominal defendant, and certain of its officers and directors. The suits allege violations of California law. On September 28, 1993, all parties entered into a stipulation that consolidated the derivative actions and stayed them in their entirety until the conclusion of the 1993 class action litigation.

Lemelson v. Apple

On September 25, 1992, Jerome Lemelson filed a complaint against the Company in the U.S. District Court, District of Nevada, which complaint was amended on April 8, 1993, alleging infringement of two patents relating to information storage and retrieval systems. Mr. Lemelson seeks injunctive relief, damages in an unspecified amount, and an award of attorneys' fees and costs. The case is set for trial in January 1995.

Grant v. Apple

On February 11, 1993, Richard B. Grant filed a complaint against the Company in the U.S. District Court for the Central District of California alleging infringement of a natural-language patent. This matter has been resolved.

The Company believes the suits cited above to be without merit and intends to vigorously defend against these actions. The Company believes the resolution of all of these matters will not have a material adverse effect on its financial condition and results of operations as reported in the accompanying financial statements. However, depending on the amount and timing of an unfavorable resolution of these lawsuits, it is possible that the Company's future results of operations or cash flow could be materially affected in a particular period.

Industry Segment and Geographic Information

The Company operates in one principal industry segment: the design, manufacture, and sale of personal computing products. The Company's products are sold primarily to the business, education, home, and government markets.

Geographic financial information is as follows:

(In thousands)

	1994	1993	1992
Net sales to unaffiliated customers:			
United States	$ 4,982,298	$ 4,387,674	$ 3,885,042
Europe	2,096,257	2,001,593	2,017,840
Pacific	1,581,571	1,075,711	716,517
Other countries	528,622	511,976	467,143
Total net sales	$ 9,188,748	$ 7,976,954	$ 7,086,542
Transfers between geographic areas (eliminated in consolidation):			
United States	$ 408,635	$ 420,323	$ 458,167
Europe	234,011	262,554	246,745
Pacific	1,633,413	1,772,440	1,156,433
Other countries	—	2,160	1,237
Total transfers	$ 2,276,059	$ 2,457,477	$ 1,862,582
Operating income (loss):			
United States	$ 45,292	$ (253,499)	$ 245,810
Europe	263,190	79,440	301,865
Pacific	197,318	262,426	227,183
Other countries	22,876	24,146	18,998
Eliminations	(6,402)	(2,175)	11,952
Corporate income (expense), net	(21,988)	29,321	49,634
Income before income taxes	$ 500,286	$ 139,659	$ 855,442
Identifiable assets:			
United States	$ 2,317,192	$ 2,534,545	$ 1,536,705
Europe	814,670	973,741	767,765
Pacific	796,803	637,857	341,200
Other countries	165,193	161,332	115,272
Eliminations	(58,372)	(49,838)	(43,716)
Corporate assets	1,267,260	913,775	1,506,467
Total assets	$ 5,302,746	$ 5,171,412	$ 4,223,693

"Other countries" consists of Canada and Australia. Prior year amounts have been restated to conform to the current year presentation. Net sales to unaffiliated customers is based on the location of the customers. Transfers between geographic areas are recorded at amounts generally above cost and in accordance with the rules and regulations of the respective governing tax authorities. Operating income (loss) by geographic area consists of total net sales less operating expenses, and does not include an allocation of general corporate expenses. The restructuring charge and adjustment recorded in 1993 and 1994, respectively, are included in the calculation of operating income (loss) for each geographic area. Identifiable assets of geographic areas are those assets used in the Company's operations in each area. Corporate assets include cash and cash equivalents, joint venture investments, and short-term investments.

Report of Ernst & Young LLP, Independent Auditors

The Shareholders and Board of Directors of Apple Computer, Inc.

We have audited the accompanying consolidated balance sheets of Apple Computer, Inc. as of September 30, 1994 and September 24, 1993, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended September 30, 1994. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Apple Computer, Inc. at September 30, 1994 and September 24, 1993, and the consolidated results of its operations and its cash flows for each of the three years in the period ended September 30, 1994, in conformity with generally accepted accounting principles.

Ernst & Young LLP
San Jose, California
October 17, 1994

Elected Executive Officers of Apple Computer, Inc.

Michael H. Spindler	President and Chief Executive Officer
Joseph A. Graziano	Executive Vice President and Chief Financial Officer
Ian W. Diery	Executive Vice President and General Manager, Personal Computer Division
James J. Buckley	Senior Vice President and President, Apple USA
Daniel L. Eilers	Senior Vice President, Apple Computer, Inc., and President and Chief Executive Officer, Claris Corporation
John Floisand	Senior Vice President and President, Apple Pacific
G. Frederick Forsyth	Senior Vice President, Worldwide Operations
David C. Nagel	Senior Vice President and General Manager, AppleSoft Division
Kevin J. Sullivan	Senior Vice President, Human Resources
Robert A. Lauridsen	Vice President, Corporate Development
Jeanne Seeley	Vice President, Finance, and Corporate Controller
Edward B. Stead	Vice President, General Counsel, and Secretary

Appointed Officers of Apple Computer, Inc.

Apple Business Systems Division

James R. Groff	Vice President and General Manager, Apple Business Systems

Apple USA Division

Terry Crane, Ed. D.	Vice President and General Manager, Education Division
George W. Everhart	Vice President, U.S. Sales Division
Keith R. Fox	Vice President, Apple USA Marketing and Channel Strategy
Jackie Whiting	Vice President, Customer Services Division

Apple Pacific Division

Robin Abrams	Vice President and General Manager, Apple Far East
Peter V. Jones	Vice President and General Manager, Canada
Kwok Wah Lau	Vice President, Pacific Operations
Frank (Seiji) Sanda	President, Apple Japan, and Vice President and General Manager, Apple Computer, Inc.

Apple Europe Division

James McCluney	Vice President, European Operations
Ernest O'Leary	Vice President, Finance
Michael Newton	Vice President and General Manager, United Kingdom and Ireland
Gian Carlo Zanni	Vice President and General Manager, Apple France

AppleSoft Division

Guerrino De Luca	Vice President, AppleSoft Sales and Marketing
Ike Nassi	Vice President, AppleSoft Operating Systems Products
Rick K. Spitz	Vice President, Apple Learning Strategy
Donald W. Strickland	Vice President, Macintosh OS Licensing, and Publishing
Lawrence G. Tesler	Vice President and Chief Scientist

Advanced Technology Group

Richard A. LeFaivre	Vice President, Advanced Technology Group

Personal Computer Division

Howard F. Lee	Senior Vice President, Macintosh Desktop, PowerBook, and Imaging
Michael J. Campi	Vice President, Worldwide Materials and Service Operations
Satjiv S. Chahil	Vice President, New Media
H. L. Cheung	Vice President, Entry Macintosh Products
Brodie C. Keast	Vice President, PowerBook Products
Steve Manser	Vice President, Macintosh Desktop Systems
Rick Shriner	Vice President, Apple Core Technologies
Michael Willcocks	Vice President, Global Accounts

Personal Interactive Electronics Division

Shane V Robison	Vice President and General Manager, Personal Interactive Electronics Division

Apple Online Services

Peter H. Friedman	Vice President and General Manager, Apple Online Services

Apple Corporate Administration

Glenn N. Barber	Vice President, Real Estate, Construction, and Facilities
Mary Ann Cusenza	Vice President and Treasurer
Michael L. Dionne	Vice President, Worldwide Communications and Marketing Services
Barbara J. Krause	Vice President, Worldwide Corporate Communications
Joseph D. Riera	Vice President, Information Systems and Technology

Board of Directors of Apple Computer, Inc.

A. C. Markkula, Jr., Chairman	Chairman, ACM Aviation, Inc.—Fixed-base operation at San Jose International Airport; Vice Chairman, Echelon Corporation—Control and communications technology company; Director, San Jose Jet Center; Chairman, Volant Ski Corporation
Dr. Gilbert F. Amelio	President and Chief Executive Officer, National Semiconductor, Inc.
Peter O. Crisp	General Partner, Venrock Associates—Venture capital investments
Bernard Goldstein	Partner, Broadview Associates—Venture capital investments
Joseph A. Graziano	Executive Vice President and Chief Financial Officer, Apple Computer, Inc.
B. Jürgen Hintz	President du Directoire and Chief Executive Officer, Carnaud MetalBox S.A.
Katherine M. Hudson	President and Chief Executive Officer, W. H. Brady Company
Delano E. Lewis	President and Chief Executive Officer, National Public Radio
Michael H. Spindler	President and Chief Executive Officer, Apple Computer, Inc.

Stockholder and Investor Information

Company Profile

Apple Computer, Inc., an information industry innovator, creates powerful solutions based on easy-to-use personal computers, servers, peripherals, software, on-line services, and personal digital assistants. Apple develops, manufactures, licenses, and markets products, technologies, and services for the business, education, consumer, scientific, engineering, and government markets in more than 140 countries.

Stock Trading

Apple Computer's common stock is traded on the over-the-counter market and is quoted on the Nasdaq National Market under the symbol AAPL, on the Tokyo Stock Exchange under the symbol APPLE, and on the Frankfurt Stock Exchange under the symbol APCD. Options are traded on the Chicago Board Options Exchange and the American Stock Exchange.

Independent Auditors

Ernst & Young LLP
San Jose, California

SEC Form 10-K

Copies of our Annual Report on Form 10-K for the fiscal year ended September 30, 1994, are available, on request, without charge. If you would like to receive a copy of this report, you may contact or send your written request to:

Investor Relations
Apple Computer, Inc.
1 Infinite Loop, M/S 38E
Cupertino, California 95014-2084
Telephone: (408) 974-2421
Fax: (408) 974-3108 or (408) 974-2113

If you represent a business or library, you can ask to be placed on a permanent mailing list for future reports.

Corporate and Investor Information

Please direct inquiries to:

Investor Relations
Apple Computer, Inc.
1 Infinite Loop, M/S 38E
Cupertino, California 95014-2084
Telephone: (408) 974-2421

Transfer Agent and Registrar

The First National Bank of Boston
Boston, Massachusetts

Shareholder Information

Shareholders with inquiries about stock ownership, changes of address, lost certificates, or dividend payments may contact:

The First National Bank of Boston
Shareholder Services Division
P.O. Box 644, Mailstop 45-02-09
Boston, Massachusetts 02102
Telephone: (617) 575-3400 or 1-800-733-5001

Dividend Reinvestment Plan

Apple Computer, Inc. does not have a dividend reinvestment plan. A cash dividend of $0.12 per common share was declared in each quarter of 1994 for a total annual dividend of $0.48.

Annual Meeting

The annual meeting of shareholders will be on Tuesday, January 24, 1995, at 10 A.M. at:

Apple Computer, Inc.
Town Hall Auditorium
4 Infinite Loop
Cupertino, California

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