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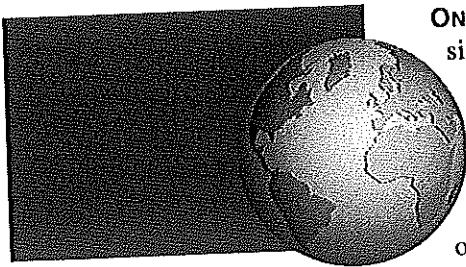
General Issues in Strategic Management

Industry One – Information Technology

CASE 7

Apple Inc.: Performance in a Zero-Sum World Economy

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ON NOVEMBER 1, 2010, JOHN TARPEY, SENIOR FINANCIAL ANALYST at a securities firm, was sitting at his conference table to begin the task of fully analyzing the 2010 financial performance and strategic strategies of Apple Inc. On his table were hundreds of articles, reports, SEC documents, and company documents. The basic question he sought answers to with this in-depth analysis was how Apple's performance continued to be outstanding, while the world and U.S. economy was flat to negative.

A second, and more important question, was if Apple could sustain this high level of performance and major innovation. Exhibit 1 shows unit sales by key products, net sales by the same products, net sales by the company's operating segments, and Mac unit sales by operating segments. John noted that there were nine positive increases versus three negative ones. He saw that the positive increases outnumbered the negative changes by three to one. In 2010, there were only three negative changes compared with nine changes for 2009. Net sales of desktop computers were up 43% in 2010, compared with a 23% drop in sales in 2009.

John considered Apple's Consolidated Statement of Operations (see Exhibit 2) and Balance Sheet (see Exhibit 3).

This case was prepared by Professors Thomas L. Wheelen, Moustafa H. Abdelsamad, Hitesh (John) Adhia, Professor David B. Croll, Professor Bernard A. Morin, Professor Lawrence C. Pettit Jr., Kathryn E. Wheelen, Richard D. Wheelen, and Thomas L. Wheelen II. Copyright ©2010 by Richard D. Wheelen. The copyright holder is solely responsible for the case content. This case was edited for *Strategic Management and Business Policy*, 13th edition. Reprinted by permission only for the 13th edition of *Strategic Management and Business Policy* (including international and electronic versions of the book). Any other publication of this case (translation, any form of electronic or media) or sale (any form of partnership) to another publisher will be in violation of copyright law unless Richard D. Wheelen has granted additional written reprint permission.

EXHIBIT 1 Selected Sales Information: Apple Inc. (Sales in millions, except unit sales in thousands)

	2010	Change	2009	Change	2008
NET SALES BY OPERATING SEGMENT					
Americas net sales	\$24,498	29%	\$18,981	15%	\$16,552
Europe net sales	18,692	58%	11,810	28%	9,233
Japan net sales	3,981	75%	2,279	32%	1,728
Asia-Pacific net sales	8,256	160%	3,179	18%	2,686
Retail net sales	9,798	47%	6,656	-9%	7,292
Total net sales	<u>\$65,225</u>	52%	<u>\$42,905</u>	14%	<u>\$37,491</u>
MAC UNIT SALES BY OPERATING SEGMENT					
Americas Mac unit sales	4,976	21%	4,120	4%	3,980
Europe Mac unit sales	3,859	36%	2,840	13%	2,519
Japan Mac unit sales	481	22%	395	2%	389
Asia-Pacific Mac unit sales	1,500	62%	926	17%	793
Retail Mac unit sales	2,846	35%	2,115	4%	2,034
Total Mac unit sales	<u>13,662</u>	31%	<u>10,396</u>	7%	<u>9,715</u>
NET SALES BY PRODUCT					
Desktops	\$6,201	43%	\$4,324	-23%	\$5,622
Portables	11,278	18%	9,535	9%	8,732
Total Mac net sales	17,479	26%	13,859	9%	14,354
iPod	8,274	2%	8,091	-12%	9,153
Other music-related products/services	4,948	23%	4,036	21%	3,340
iPhone and related products/services	25,179	93%	13,033	93%	6,742
iPad and related products/services	4,958	-	0	-	0
Peripherals and other hardware	1,814	23%	1,475	-13%	1,694
Software, service, and other sales	2,573	7%	2,411	9%	2,208
Total net sales	<u>\$65,225</u>	52%	<u>\$42,905</u>	14%	<u>\$37,491</u>
UNIT SALES BY PRODUCT					
Desktops	4,627	45%	3,182	-14%	3,712
Portables	9,035	23%	7,214	20%	6,003
Total Mac unit sales	13,662	31%	10,396	7%	9,715
Net sales per Mac unit sold	<u>\$1,279</u>	-4%	<u>\$1,333</u>	-10%	<u>\$1,478</u>
iPod unit sales	50,312	-7%	54,132	-1%	54,828
Net sales per iPod unit sold	<u>\$164</u>	10%	<u>\$149</u>	-11%	<u>\$167</u>
iPhone units sold	39,989	93%	20,731	78%	11,627
iPad units sold	<u>7,458</u>	-	<u>0</u>	-	<u>0</u>

Note: The notes were deleted.

SOURCE: Apple Inc., SEC 10-K Report, (September 25, 2010), p. 33.

EXHIBIT 2
Consolidated
Statements of
Operations: Apple
Inc. (Amounts in
millions, except
share amounts
which are reflected
in thousands and
per share amounts)

Year Ending September 25	2010	2009	2008
NET SALES	\$65,225	\$42,905	\$37,491
Cost of sales	<u>39,541</u>	<u>25,683</u>	<u>24,294</u>
Gross margin	<u>25,684</u>	<u>17,222</u>	<u>13,197</u>
Operating expenses:			
Research and development	1,782	1,333	1,109
Selling, general and administrative	<u>5,517</u>	<u>4,149</u>	<u>3,761</u>
Total operating expenses	<u>7,299</u>	<u>5,482</u>	<u>4,870</u>
Operating income	18,385	11,740	8,327
Other income and expenses	<u>155</u>	<u>326</u>	<u>620</u>
Income before provision for income taxes	18,540	12,066	8,947
Provision for income taxes	4,527	3,831	2,828
NET INCOME	<u>\$14,013</u>	<u>\$8,235</u>	<u>\$6,119</u>
Earnings per common share:			
Basic	\$15.41	\$9.22	\$6.94
Diluted	\$15.15	\$9.08	\$6.78
Shares used in computing earnings per share:			
Basic	909,461	893,016	881,592
Diluted	924,712	907,005	902,139

SOURCE: Apple Inc., SEC 10-K Form (September 25, 2010), p.46.

Management's View of the Company¹

John searched and found in the 10-K report management's views on the company's performance in 2010 as stated below.

First, the company designed, manufactured, and marketed a range of personal computers, mobile communication and media devices, and portable digital music players, and sold a variety of related software, services, peripherals, networking solutions, and third-party digital content and applications. The company's products and services included Mac computers, iPhone, iPad, iPod, Apple TV, Xserve, a portfolio of consumer and professional software applications, the Mac OS X and iOS operating systems, third-party digital content and applications through the iTunes Store, and a variety of accessory, service, and support offerings. The company sold its products worldwide through its retail stores, online stores, and direct sales force, as well as third-party cellular network carriers, wholesalers, retailers, and value-added resellers. In addition, the company sold a variety of third-party Mac, iPhone, iPad, and iPod compatible products, including application software, printers, storage devices, speakers, headphones, and various other accessories and peripherals through its online and retail stores. The company sold to SMB, education, enterprise, government, and creative markets.

Second, the company was committed to bringing the best user experience to its customers through its innovative hardware, software, peripherals, services, and Internet offerings. The company's business strategy leverages its unique ability to design and develop its own operating systems, hardware, application software, and services to provide its customers new products and solutions with superior ease-of-use, seamless integration, and

EXHIBIT 3
Consolidated
Balance Sheets:
Apple Inc. (Dollar
amounts in millions,
except share
amounts)

Years Ending September 30	2010	2009
ASSETS		
Current assets		
Cash and cash equivalents	\$ 11,261	\$ 5,263
Short-term marketable securities	14,359	18,201
Accounts receivable, less allowances of \$55 and \$52, respectively	5,510	3,361
Inventories	1,051	455
Deferred tax assets	1,636	1,135
Vendor non-trade receivables	4,414	1,696
Other current assets	3,447	1,444
Total current assets	41,678	31,555
Long-term marketable securities	\$ 25,391	\$ 10,528
Property, plant, and equipment, net	4,768	2,954
Goodwill	741	206
Acquired intangible assets, net	342	247
Other assets	2,263	2,011
Total assets	\$ 75,183	\$ 47,501
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 12,015	\$ 5,601
Accrued expenses	5,723	3,852
Deferred revenue	2,984	2,053
Total current liabilities	20,722	11,506
Deferred revenue—non-current	1,139	853
Other non-current liabilities	5,531	3,502
Total liabilities	27,392	15,861
Commitments and contingencies		
Shareholders' equity		
Common stock, no par value; 1,800,000,000 shares authorized; 915,970,050, and 899,805,500 shares issued and outstanding, respectively	10,668	8,210
Retained earnings	37,169	23,353
Accumulated other comprehensive (loss)/income	-46	77
Total shareholders' equity	47,791	31,640
Total Liabilities and Stockholders' Equity	\$ 75,183	\$ 47,501

SOURCE: Apple Inc., SEC 10-K Form (September 25, 2010).

innovative industrial design. The company believed continual investment in research and development was critical to the development and enhancement of innovative products and technologies. In conjunction with its strategy, the company continued to build and host a robust platform for the discovery and delivery of third-party digital content and applications through the iTunes Store. Within the iTunes Store, the company expanded its offerings through the App Store and iBookstore, which allowed customers to browse, search for, and purchase third-party applications and books through either a Mac or Windows-based computer or by wirelessly downloading directly to an iPhone, iPad, or iPod touch. The company

also worked to support a community for the development of third-party software and hardware products and digital content that complement the company's offerings. Additionally, the company's strategy included expanding its distribution network to effectively reach more customers and provide them with a high-quality sales and post-sales support experience. The company was therefore uniquely positioned to offer superior and well-integrated digital lifestyle and productivity solutions.

Third, the company participated in several highly competitive markets, including personal computers with its Mac computers; mobile communications and media devices with its iPhone, iPad, and iPod product families; and distribution of third-party digital content and applications with its online iTunes Store. While the company was widely recognized as a leading innovator in the markets where it competes, these markets were highly competitive and subject to aggressive pricing. To remain competitive, the company believed that increased investment in research and development, marketing, and advertising was necessary to maintain or expand its position in these markets. The company's research and development spending was focused on further developing its existing Mac line of personal computers; the Mac OS X and iOS operating systems; application software for the Mac; iPhone, iPad, and iPod and related software; development of new digital lifestyle consumer and professional software applications; and investments in new product areas and technologies. The company also believed increased investment in marketing and advertising programs was critical to increasing product and brand awareness.

The company utilized a variety of direct and indirect distribution channels, including its retail stores, online stores, and direct sales force, as well as third-party cellular network carriers, wholesalers, retailers, and value-added resellers. The company believed that sales of its innovative and differentiated products were enhanced by knowledgeable salespersons who could convey the value of the hardware, software, and peripheral integration; demonstrate the unique digital lifestyle solutions that were available on its products; and demonstrate the compatibility of the Mac with the Windows platform and networks. The company further believed providing direct contact with its targeted customers was an effective way to demonstrate the advantages of its products over those of its competitors, and that providing a high-quality sales and after-sales support experience is critical to attracting new—and retaining existing—customers. To ensure a high-quality buying experience for its products in which service and education were emphasized, the company continued to expand and improve its distribution capabilities by expanding the number of its own retail stores worldwide. Additionally, the company invested in programs to enhance reseller sales by placing high-quality Apple fixtures, merchandising materials, and other resources within selected third-party reseller locations. Through the Apple Premium Reseller Program, certain third-party resellers focused on the Apple platform by providing a high level of integration and support services, as well as product expertise.

History of Apple Inc.²

The history of Apple can be broken into five separate time periods, each with its own strategic issues and concerns.

1976–1984: The Founders Build a Company

Founded in a California garage on April 1, 1976, Apple created the personal computer revolution with powerful yet easy-to-use machines for the desktop. Steve Jobs sold his Volkswagen bus and Steve Wozniak hocked his HP programmable calculator to raise \$1,300 in seed money to start their new company. Not long afterward, a mutual friend helped recruit A. C. "Mike" Markkula to help market the company and give it a million-dollar image. Even

though all three founders had left the company's management team during the 1980s, Markkula continued serving on Apple's Board of Directors until August 1997.

The early success of Apple was attributed largely to marketing and technological innovation. In the high-growth industry of personal computers in the early 1980s, Apple grew quickly, staying ahead of competitors by contributing key products that stimulated the development of software for the computer. Landmark programs such as Visicalc (forerunner to Lotus 1-2-3 and other spreadsheet programs) were developed first for the Apple II. Apple also secured early dominance in the education and consumer markets by awarding hundreds of thousands of dollars in grants to schools and individuals for the development of education software.

Even with enormous competition, Apple revenues continued to grow at an unprecedented rate, reaching \$583.3 million by fiscal 1982. The introduction of the Macintosh graphical user interface in 1984, which included icons, pull-down menus, and windows, became the catalyst for desktop publishing and instigated the second technological revolution attributable to Apple. Apple kept the architecture of the Macintosh proprietary; that is, it could not be cloned like the "open system" IBM PC. This allowed the company to charge a premium for its distinctive "user-friendly" features.

A shakeout in the personal computer industry began in 1983 when IBM entered the PC market, initially affecting companies selling low-priced machines to consumers. Companies that made strategic blunders or that lacked sufficient distribution or brand awareness of their products disappeared.

1985–1997: Professional Managers Fail to Extend the Company

In 1985, amid a slumping market, Apple saw the departure of its founders, Jobs and Wozniak. As Chairman of the Board, Jobs had recruited John Sculley, an experienced executive from PepsiCo, to replace him as Apple's CEO in 1983. Jobs had challenged Sculley when recruiting him by saying, "Do you want to spend the rest of your life selling sugared water, or do you want to change the world?" Jobs willingly gave up his title as CEO so that he could have Sculley as his mentor. In 1985, a power struggle took place between Sculley and Jobs. With his entrepreneurial orientation, Jobs wanted to continue taking the company in risky new directions. Sculley, in contrast, felt that Apple had grown to the point where it needed not only to be more careful in its strategic moves, but also better organized and rationally managed. The board of directors supported Sculley's request to strip Jobs of his duties, since it felt that the company needed an experienced executive to lead Apple into its next stage of development.

Jobs then resigned from the company he had founded and sold all but one share of his Apple stock. Under the leadership of John Sculley, CEO and Chairman, the company engineered a remarkable turnaround. He instituted a massive reorganization to streamline operations and expenses. During this time Wozniak left the company. Macintosh sales gained momentum throughout 1986 and 1987. Sales increased 40% from \$1.9 billion to \$2.7 billion in fiscal 1987, and earnings jumped 41% to \$217 million.

In the early 1990s, Apple sold more personal computers than any other computer company. Net sales grew to over \$7 billion, net income to over \$540 million, and earnings per share to \$4.33. The period from 1993 to 1995 was, however, a time of considerable change in the management of Apple. The industry was rapidly changing. Personal computers using Microsoft's Windows operating system and Office software plus Intel microprocessors began to dominate the personal computer marketplace. (The alliance between Microsoft and Intel was known in the trade as Wintel.) Dell, Hewlett-Packard, Compaq, and Gateway replaced both IBM and Apple as

the primary makers of PCs. The new Windows system had successfully imitated the user-friendly "look and feel" of Apple's Macintosh operating system. As a result, Apple lost its competitive edge. In June 1993, Sculley was forced to resign and Michael H. Spindler was appointed CEO of the company. At this time, Apple was receiving a number of offers to acquire the company. Many of the company's executives advocated Apple's merging with another company. However, when no merger took place, many executives chose to resign.

Unable to reverse the company's falling sales, Spindler was soon forced out and Gilbert Amelio was hired from outside Apple to serve as CEO. Amelio's regime presided over an accelerated loss of market share, deteriorating earnings, and stock that had lost half of its value. Apple's refusal to license the Mac operating system to other manufacturers had given Microsoft the opening it needed to take the market with its Windows operating system. Wintel PCs now dominated the market—pushing Apple into a steadily declining market niche composed primarily of artisans and teachers. By 1996, Apple's management seemed to be in utter disarray.

Looking for a new product with which Apple could retake the initiative in personal computers, the company bought NeXT for \$402 million on December 20, 1996. Steve Jobs, who formed the NeXT computer company when he left Apple, had envisioned his new company as the developer of the "next generation" in personal computers. Part of the purchase agreement was that Jobs would return to Apple as a consultant. In July of 1997, Amelio resigned and was replaced by Steve Jobs as Apple's interim CEO (iCEO). This ended Steve Jobs' 14-year exile from the company that he and Wozniak had founded. In addition to being iCEO of Apple, Jobs also served as CEO of Pixar, a company he had personally purchased from Lucasfilm for \$5 million. Receiving only \$1.00 a year as CEO of both Pixar and Apple, Jobs held the Guinness World Record as the "Lowest Paid Chief Executive Officer."

1998–2001: Jobs Leads Apple "Back to the Future"

Once in position as Apple's CEO, Steve Jobs terminated many of the company's existing projects. Dropped were the iBook and the AirPort products series, which had helped popularize the use of wireless LAN technology to connect a computer to a network.

In May 2001, the company announced the reopening of Apple Retail Stores. Like IBM and Xerox, Apple had opened its own retail stores to market its computers during the 1980s. All such stores had been closed however, when Wintel-type computers began being sold by mass merchandisers, such as Sears and Circuit City, as well as through corporate websites.

Apple introduced the iPod portable digital audio player, and the company opened its own iTunes music store to provide downloaded music to iPod users. Given the thorny copyright issues inherent in the music business, analysts doubted if the new product would be successful.

2002–2006: A Corporate Renaissance?

In 2002, Apple introduced a redesigned iMac using a 64-bit processor. The iMac had a hemispherical base and a flat-panel all-digital display. Although it received a lot of press, the iMac failed to live up to the company's sales expectations.

In 2004 and 2005, Apple opened its first retail stores in Europe and Canada. By November 2006, the company had 149 stores in the United States, 4 stores in Canada, 7 stores in the United Kingdom, and 7 stores in Japan.

In 2006, Jobs announced that Apple would sell an Intel-based Macintosh. Previously, Microsoft had purchased all of its microprocessors from Motorola. By this time, Microsoft's

operating system with Intel microprocessors was running on 97.5% of the personal computers sold, with Apple having only a 2.5% share of the market. The company also introduced its first Intel-based machines, the iMac and MacBook Pro.

By this time, Apple's iPod had emerged as the market leader of a completely new industry category, which it had created. In 2006, Apple controlled 75.6% of the market, followed by SunDisk with 9.7%, and Creative Technology in third place with 4.3%. Although one analyst predicted that more than 30 million iPods would be sold in fiscal 2006, Apple actually sold 41,385,000. Taking advantage of its lead in music downloading, the company's next strategic move was to extend its iTunes music stores by offering movies for \$9.99 each. An analyst reviewing this strategic move said that Apple was able to create a \$1 billion-a-year market for the legal sale of music. Apple may be able to provide the movie industry with a similar formula.

2007–Present: Mobile Consumer Electronics Era

While delivering his keynote speech at the Macworld Expo on January 9, 2007, Jobs announced that Apple Computer, Inc. would from that point on be known as Apple Inc., due to the fact that computers were no longer the singular focus for the company. This change reflected the company's shift of emphasis to mobile electronic devices from personal computers. The event also saw the announcement of the iPhone and the Apple TV. The following day, Apple shares hit \$97.80, an all-time high at that point. In May, Apple's share price passed the \$100 mark. In an article posted on Apple's website on February 6, 2007, Steve Jobs wrote that Apple would be willing to sell music on the iTunes Store with DRM (which would allow tracks to be played on third-party players) if record labels would agree to drop the technology. On April 2, 2007, Apple and EMI jointly announced the removal of DMR technology from EMI's catalog in the iTunes Store, effective in May. Other record labels followed later that year.

In July of the following year, Apple launched the App Store to sell third-party applications for the iPhone and iPod Touch. Within a month, the store sold 60 million applications and brought in \$1 million daily on average, with Jobs speculating that the App Store could become a billion-dollar business for Apple. Three months later, it was announced that Apple had become the third-largest mobile handset supplier in the world due to the popularity of the iPhone.

On December 16, 2008, Apple announced that, after over 20 years, 2009 would be the last year Steve Jobs would be attending the Macworld Expo, and that Phil Schiller would deliver the 2009 keynote speech in lieu of the expected Jobs. Almost exactly one month later, on January 14, 2009, an internal Apple memo from Jobs announced that he would be taking a six-month leave of absence, until the end of June 2009, to allow him to better focus on his health and to allow the company to better focus on its products without having the rampant media speculating about his health. Despite Jobs' absence, Apple recorded its best non-holiday quarter (q1 FY 2009) during the recession with revenue of \$8.16 billion and a profit of \$1.21 billion.

After years of speculation and multiple rumored "leaks," Apple announced a large screen, tablet-like media device known as the iPad on January 27, 2010. The iPad ran the same touch-based operating system that the iPhone used and many of the same iPhone apps were compatible with the iPad. This gave the iPad a large app catalog on launch even with very little development time before the release. Later that year on April 3, 2010, the iPad was launched in the United States and sold more than 300,000 units on that day, reaching 500,000 by the end of the first week. In May 2010, Apple's market cap exceeded that of competitor Microsoft for the first time since 1989.

In June 2010, Apple released the fourth generation iPhone, which introduced video calling, multitasking, and a new insulated stainless steel design which served as the phone's antenna. Because of this antenna implementation, some iPhone 4 users reported a reduction in signal strength when the phone was held in specific ways. Apple offered buyers a free rubber "bumper" case until September 30, 2010, as cases had been developed to solve/improve the signal strength issue.

In September 2010, Apple refreshed its iPod line of MP3 players, introducing a multi-touch iPod Nano, iPod Touch with FaceTime, and iPod Shuffle with buttons. In October 2010, Apple shares hit an all-time high, eclipsing \$300. Additionally, on October 20, Apple updated its MacBook Air laptop, iLife suite of applications, and unveiled Mac OS X Lion, the latest installment in its Mac OS X operating system. On November 16, 2010, Apple Inc., after years of negotiations, finalized a deal to allow iTunes to sell The Beatles' music at \$1.29 per song. The five major Web-TV boxes were (1) Apple TV, (2) Boxee, (3) Google TV, (4) WD TV Hub, and (5) Roku.

Steven P. Jobs: Entrepreneur and Corporate Executive³

In 2010, Steve Jobs was chosen as "Executive of the Decade" by *Fortune* magazine. He has also been referred to as the "Henry Ford" of the current world business market. Steven P. Jobs was born on February 24, 1955, in San Francisco. He was adopted by Paul and Clara Jobs in February 1955. In 1972, Jobs graduated from Homestead High School in Los Altos, California. His high school electronics teacher said, "He was somewhat of a loner and always had a different way of looking at things." After graduation, Jobs was hired by Hewlett-Packard as a summer employee. This is where he met Steve Wozniak, a recent dropout from The University of California at Berkeley. Wozniak had a genius IQ and was an engineering whiz with a passion for inventing electronic gadgets. At this time, Wozniak was perfecting his "blue box," an illegal pocket-size telephone attachment that allowed the user to make free long-distance calls. Jobs helped Wozniak sell this device to customers.⁴

In 1972, Jobs enrolled at Reed College in Portland, Oregon, but dropped out after one semester. He remained around Reed for a year and became involved in the counterculture. During that year, he enrolled in various classes in philosophy and other topics. In a later speech at Stanford University, Jobs explained, "If I had never dropped in on that single course (calligraphy), that Mac would have never had multiple typefaces or proportionally spaced fonts."⁵

In early 1974, Jobs took a job as a video-game designer for Atari, a pioneer in electronic arcade games. After earning enough money, Jobs went to India in search of personal spiritual enlightenment. Later that year, Jobs returned to California and began attending meetings of Steve Wozniak's "Homebrew Computer Club." Wozniak converted his TV monitor into what would become a computer. Wozniak was a very good engineer and extremely interested in creating new electronic devices. Although Jobs was not interested in developing new devices, he realized the marketability of Wozniak's converted TV. Together they designed the Apple I computer in Jobs' bedroom and built the first prototype in Jobs' garage. Jobs showed the Apple I to a local electronics retailer, the Byte Shop, and received a \$25,000 order for 50 computers. Jobs took this purchase order to Cramer Electronics to order the components needed to assemble the 50 computers.

The local credit manager asked Jobs how he was going to pay for the parts and he replied, "I have this purchase order from the Byte Shop chain of computer stores for 50 of my computers and the payment terms are COD. If you give me the parts on net 30 day terms, I can build and deliver the computers in that time frame, collect my money from Turrell at the Byte Shop

and pay you." With that, the credit manager called Paul Turrell, who was attending an IEEE computer conference, and verified the validity of the purchase order. Amazed at the tenacity of Jobs, Turrell assured the credit manager that if the computers showed up in his stores Jobs would be paid and would have more than enough money to pay for the parts order. The two Steves and their small crew spent day and night building and testing the computers and delivered them to Turrell on time to pay his suppliers and have a tidy profit left over for their celebration and next order. Steve Jobs had found a way to finance his soon-to-be multimillion dollar company without giving away one share of stock or ownership.⁶

Jobs and Wozniak decided to start a computer company to manufacture and sell personal computers. They contributed \$1,300 of their own money to start the business. Jobs selected the name Apple for the company based on his memories of a summer job as an orchard worker. On April 1, 1976, Apple Computer company was formed as a partnership.

During Jobs' early tenure at Apple, he was a persuasive and charismatic evangelist for the company. Some of his employees have described him at that time as an erratic and tempestuous manager. An analyst said that many persons who look at Jobs' management style forget that he was 30 years old in 1985 and he received his management and leadership education on the job. Jobs guided the company's revenues to \$1,515,616,000 and profits of \$64,055,000 in 1984. Jobs was cited in several articles as having a demanding and aggressive personality. One analyst said that these two attributes described most of the successful entrepreneurs. Jobs strategically managed the company through a period of new product introduction, rapidly changing technology, and intense competition—a time during which many companies have failed.

In 1985, after leaving Apple, Jobs formed a new computer company, NeXT Computer Inc. Jobs served as Chairman and CEO.⁷ NeXT was a computer company that built machines with futuristic designs and ran the UNIX-derived NeXT step operating system. It was marketed to academic and scientific organizations. NeXT was not a commercial success, however, in part because of its high price.

In 1986, Jobs purchased Pixar Animation from Lucasfilm for \$5 million. He provided another \$5 million in capital, owned 50.6% of the stock, and served as Chairman and CEO. Pixar created three of the six highest grossing domestic (gross revenues) animated films of all time—*Toy Story* (1995), *A Bug's Life* (1998), and *Toy Story 2* (1999). Each of these films, released under a partnership with the Walt Disney Company, was the highest grossing animated film for the year in which it was released. During this period, Jobs delegated more to his executives. Many analysts felt that the excellent executive staff and animators were prime reasons that Disney management subsequently wanted to acquire Pixar. Jobs served as CEO of NeXT and Pixar from 1985 to 1997. Jobs ultimately sold NeXT in 1996 to Apple for \$402 million and became iCEO of Apple in July 1997.⁸

At Pixar, Jobs focused on business duties, which was different than his earlier management style at Apple. The creative staff was given a great deal of autonomy. Sources say he spent less than one day a week at the Pixar campus in Emeryville, just across the San Francisco Bay from Apple's headquarters. A Pixar employee said, "Steve did not tell us what to do." He further stated, "Steve's our benevolent benefactor."⁹

Michael D. Eisner, CEO of the Walt Disney Company, did not have a smooth relationship with Jobs during the years of the Pixar/Disney partnership. Critics explained that Eisner was unable to work with Jobs because both men were supremely confident (some said arrogant) that their own judgment was correct—regardless of what others said. In 2005, in response to Eisner's unwillingness to modify Disney's movie distribution agreement with Pixar, Jobs refused to renew the contract. At the time, Disney's own animation unit was faltering and unable to match Pixar's new computer technology and creativity. Concerned with Eisner's leadership style and his inability to support the company's distinctive competence in animation, Roy Disney led a shareholders' revolt. On October 1, 2005, Eisner was replaced by Robert A. Iger as CEO of Disney.¹⁰

On January 24, 2006, CEO Iger announced that Disney had agreed to pay \$7.4 billion in stock to acquire Pixar Animation Studios. Since this deal made Jobs the largest stockholder (6.67%) in Disney, he was appointed to Disney's board of directors.¹¹

Edward S. Woodward Jr., former chairman of Apple Computer, told Apple's board of directors, "He (Jobs) has a good relationship with you; there is nobody better with you; there is nobody better in the world to work with. Iger made a very wise move, and two years from now everyone will be saying that."¹²

Peter Burrows and Ronald Grover stated in an article: "The alliance between Jobs and Disney is full of promise. If he can bring to Disney the same kind of industry-sharing, boundary-busting energy that has lifted Apple and Pixar sky-high, he could help the staid company become the leading laboratory for media convergences. It's not hard to imagine a day when you could fire up your Apple TV and watch net-only spin-offs of popular TV shows from Disney's ABC Inc. (DIS). Or use your Apple iPhone to watch Los Angeles Lakers superstar Kobe Bryant's video blog delivered via Disney's ESPN Inc. 'We've been talking about a lot of things,' said Jobs. 'It's going to be a pretty exciting world looking ahead over the next five years'."¹³

An expert on Jobs asked, "So what is Jobs' secret?" His answer: "There are many, but it starts with focus and a non-religious faith in his strategy." In his return to Apple, he took a proprietary approach as he cut dozens of projects and products. Many on Wall Street were not initially happy with Jobs' new directions for the company, but soon were impressed by Apple's successful turnaround.¹⁴

Jim Cramer, host of *Mad Money*, has said several times on his television program that Steve Jobs is the "Henry Ford" of this period of America's industry. Others claim Steve is the present Thomas Edison. Steve Jobs over the years has received many honors, such as the National Medal of Technology (with Steve Wozniak) from President Reagan in 1985. Jobs was among the first people to ever receive the honor, and a Jefferson Award for Public Service in the category "Greatest Public Service by an Individual 35 Years or Under" (a.k.a. the *Samuel S. Beard Award*) in 1987. On November 27, 2007, California Governor Arnold Schwarzenegger and First Lady Maria Shriver inducted Jobs into the California Hall of Fame, located at the California Museum for History, Women and the Arts. In August 2009, Jobs was selected the most admired entrepreneur among teenagers on a survey by Junior Achievement. On November 5, 2009, Jobs was named the CEO of the decade by *Fortune* Magazine. On November 22, 2010, *Forbes* Magazine named Steve Jobs the "17th Most Powerful Person on Earth." The list had only 68 individuals out of the world population of 6.8 billion people.¹⁵

Health Concerns

In mid-2004, Jobs announced to his employees that he had been diagnosed with a cancerous tumor in his pancreas. The prognosis for pancreatic cancer was usually very grim; Jobs, however, stated that he had a rare, far less aggressive type known as islet cell neuro-endocrine tumor. After initially resisting the idea of conventional medical intervention and embarking on a special diet to thwart the disease, Jobs underwent a pancreaticoduodenectomy (or "Whipple procedure") in July 2004 that appeared to successfully remove the tumor. Jobs apparently did not require nor receive chemotherapy or radiation therapy. During Jobs' absence, Timothy D. Cook, head of worldwide sales and operations at Apple, ran the company.

In early August 2006, Jobs delivered the keynote speech for Apple's annual Worldwide Developers Conference. His "thin, almost gaunt" appearance and unusually "listless" delivery, together with his choice to delegate significant portions of his keynote speech to other presenters, inspired a flurry of media and Internet speculation about his health. In contrast, according to an *Ars Technica* journal report, WWDC attendees who saw Jobs in person said he "looked fine"; following the keynote, an Apple spokesperson said that "Steve's health is robust."

Two years later, similar concerns followed Jobs' 2008 WWDC keynote address; Apple officials stated Jobs was victim to a "common bug" and that he was taking antibiotics, while others surmised his cachectic appearance was due to the Whipple procedure. During a July conference call discussing Apple earnings, participants responded to repeated questions about Steve Jobs' health by insisting that it was a "private matter." Others, however, opined that shareholders had a right to know more, given Jobs' hands-on approach to running his company. The *New York Times* published an article based on an off-the-record phone conversation with Jobs, noting that "while his health issues have amounted to a good deal more than 'a common bug,' they weren't life-threatening and he doesn't have a recurrence of cancer."

On August 28, 2008, Bloomberg mistakenly published a 2,500-word obituary of Jobs in its corporate news service, containing blank spaces for his age and cause of death. (News carriers customarily stockpile up-to-date obituaries to facilitate news delivery in the event of a well-known figure's untimely death.) Although the error was promptly rectified, many news carriers and blogs reported on it, intensifying rumors concerning Jobs' health. Jobs responded at Apple's September 2008 Let's Rock keynote by quoting Mark Twain: "Reports of my death are greatly exaggerated"; at a subsequent media event, Jobs concluded his presentation with a slide reading "110 / 70," referring to his blood pressure, stating he would not address further questions about his health.

On December 16, 2008, Apple announced that Marketing Vice-President Phil Schiller would deliver the company's final keynote address at the Macworld Conference and Expo 2009, again reviving questions about Jobs' health. In a statement given on January 5, 2009, on Apple.com, Jobs said that he had been suffering from a "hormone imbalance" for several months. On January 14, 2009, in an internal Apple memo, Jobs wrote that in the previous week he had "learned that my health-related issues are more complex than I originally thought" and announced a six-month leave of absence until the end of June 2009 to allow him to better focus on his health. Tim Cook, who had previously acted as CEO in Jobs' 2004 absence, became acting CEO of Apple, with Jobs still involved with "major strategic decisions."

In April 2009, Jobs underwent a liver transplant at Methodist University Hospital Transplant Institute in Memphis, Tennessee. Jobs' prognosis was "excellent."¹⁶

On June 29, 2010, Steve Jobs returned to his position as leader at Apple. Jobs had about 10 serious discussions with associates about the possibility of him not returning to active management at Apple, and what impact his decision would have on Apple's future success. Most felt that if Steve departed Apple, "Apple's future success was in question."¹⁷

Surprised Leave of Absence Announced—2011

On January 17, 2011, Steve Jobs sent the following e-mail to all Apple employees:

Team,

At my request, the board of directors has granted me a medical leave of absence so I can focus on my health. I will continue as CEO and be involved in major strategic decisions for the company.

I have asked Tim Cook to be responsible for all of Apple's day to day operations. I have great confidence that Tim and the rest of the executive management team will do a terrific job executing plans we have in place for 2011.

I love Apple so much and hope to be back as soon as I can. In the meantime, my family and I would deeply appreciate respect for our privacy.

Steve

This was Job's second leave of absence. The first one was from January 2009 until June 2009.

Tim Cook, chief operating officer, again took over the day-to-day activities of the CEO position, but Jobs kept the title as he did on his first leave of absence. After Jobs' first medical leave of absence was granted in January 2009, a 10% drop occurred in the stock. On January 19, 2011, the stock's close price was \$348.48; as of the last trade January 20, it was \$340.65 (a change down \$7.83 or 2.25%).¹⁸ This was not in line with the trading in the past month.

The following is Timothy (Tim) Cook's biography sketch as it appeared in the Apple Inc. 2011 Proxy Statement:

Timothy D. Cook, (50) Chief Operating Officer, joined the company in March 1998. Mr. Cook also served as Executive Vice President, Worldwide Sales Operations from 2002 to 2005. In 2004, his responsibilities were expanded to include the company's Macintosh hardware engineering. From 2000 to 2002, Mr. Cook served as Senior Vice President, Worldwide Operations. Prior to joining the company, Mr. Cook was Vice President, corporate materials for Compaq Computer Corporation ("Compaq"). Prior to his work at Compaq, Mr. Cook was Chief Operating Officer of the Reseller Division at Intelligent Electronics. Mr. Cook also spent 12 years with International Business Machines Corporation ("IBM"), most recently as Director of North American Fulfillment. Mr. Cook also served as a director for NIKE, Inc. since November 2005.¹⁹

The Apple Board of Directors rewarded Cook's performance in covering for Jobs in his day-to-day operations as CEO with a \$5 million bonus and \$52.5 million in stock options. The company's financial performance excelled during these six months.

A side effect of Jobs' latest announcement was the indefinite delay in the announcement of the launch of Rupert Murdoch's iPad-only newspaper *The Daily*—which had been scheduled to take place later in January 2011 in San Francisco.²⁰

A shareholder proposal for the 2011 Apple's Annual Meeting focused on asking the board for an executive succession plan and publishing the plan. The board opposed this proposal.²¹ The meeting was scheduled for February 23, 2011.

On January 18, 2011, Apple announced its first quarter results, which surpassed the analysts' expected results. Key financial results are shown in the following table.²²

First Quarter December 31	(Dollars in Thousands except per Share)	
	2011	2010
Revenue	\$26,741	\$15,683
Gross profit	10,298	6,471
Total operating expenses	2,471	1,686
Net income	6,004	3,378
EPS—Basic	\$6.53	\$3.74
EPS—Diluted	\$6.43	\$3.67

"We had a phenomenal holiday quarter with record Mac, iPhone, and iPad sales" said Steve Jobs, Apple CEO. "We are firing on all cylinders and we've got some exciting things in the pipeline for this year including iPhone on Verizon and consumers can't wait to get their hands on it."²³

Corporate Governance²⁴

Exhibit 4 lists the eight members of the board of directors and the executive officers as of January 26, 2010. Steve Jobs, as CEO, was the only internal board member and the only member who had served on the original board. On September 30, 2006, Fred Anderson, who had joined the board in 2004, resigned from the board over a stock options investigation. On August 28, 2006, Dr. Eric Schmidt, CEO of Google, was appointed to the board. Shaw Nu, analyst, said, "He (Schmidt) gives Jobs and Apple more perspective on dealing with Microsoft. . . . And like Jobs, Schmidt has lost at times against (Microsoft)." As soon as Schmidt's board appointment was announced, speculation began about the potential for future partnerships between Google and Apple.

On August 3, 2009, Dr. Eric Schmidt resigned from the board because Google was developing new products which would directly compete with Apple's products. In 2008, Andrea Jung became the newest member of the eight member board (see Exhibit 4).

Directors were eligible to receive up to two free computer systems, as well as discounts on the purchase of additional products. On the fourth anniversary of joining the board, each member was entitled to receive an option to acquire 30,000 shares of stock.

EXHIBIT 4 Apple's
Board of Directors
and Top
Management

A. Directors			
Name	Position	Age	Since
Fred A. Anderson	Director	61	2004
William V. Campbell	Co-lead Director	65	1997
Millard S. Drexler	Director	61	1999
Albert A. Gore Jr.	Director	57	2000
Steven P. Jobs	Director and CEO	50	1997
Andrea Jung	Co-lead Director	51	2008
Arthur D. Levinson, PhD	Co-lead Director	55	2000
Jerome B. York	Director	67	1997
B. Executives			
Steven P. Jobs	Dr. Avdias "Avie" Tevanian Jr.		
CEO, Apple	Chief Software Technology Officer		
CEO, Pixar			
Director, Apple	Jon Rubinstein		
Director, Walt Disney	Senior Vice President iPod Division		
Timothy D. Cook			
Chief Operating Officer	Philip W. Schiller		
	Senior Vice President		
Nancy R. Heinen	Worldwide Product Marketing		
Senior Vice President and General Counsel	Bertrand Seriet		
	Senior Vice President		
Ron Johnson	Software Engineering		
Senior Vice President Retail	Sina Tamaddon		
	Senior Vice President, Applications		
Peter Oppenheimer			
Senior Vice President			
Chief Financial Officer			

SOURCE: Apple Inc. *SEC DEFR 14a* (January 26, 2010), pp. 8 & 13.

Although Steve Jobs' annual salary was only \$1.00 as CEO of Apple, the board gave Jobs a bonus of \$84 million in 2001, consisting of \$43.5 million for a private jet, a Gulfstream V; as well as \$40.5 million to pay Jobs' income taxes on this bonus. Jobs owned 10,200,004 shares (1.25%) of Apple's stock. The closing price on November 8, 2010, was \$318.62 per share.

Business Strategy²⁵

The company was committed to bringing the best user experience to its customers through its innovative hardware, software, peripherals, services, and Internet offerings. The company's business strategy leveraged its unique ability to design and develop its own operating systems, hardware, application software, and services to provide its customers new products and solutions with superior ease-of-use, seamless integration, and innovative industrial design. The company believed continual investment in research and development was critical to the development and enhancement of innovative products and technologies. In conjunction with its strategy, the company continued to build and host a robust platform for the discovery and delivery of third-party digital content and applications through the iTunes Store. The iTunes Store included the App Store and iBookstore, which allowed customers to discover and download third-party applications and books through either a Mac or Windows-based computer or wirelessly through an iPhone, iPad, or iPod touch. The company also worked to support a community for the development of third-party software and hardware products and digital content that complemented the company's offerings. Additionally, the company's strategy included expanding its distribution to effectively reach more customers and provided them with a high-quality sales and post-sales support experience. The company was therefore uniquely positioned to offer superior and well-integrated digital lifestyle and productivity solutions.

Consumer and Small and Mid-Sized Business

The company believed a high-quality buying experience with knowledgeable salespersons who could convey the value of the company's products and services greatly enhanced its ability to attract and retain customers. The company sold many of its products and resells certain third-party products in most of its major markets directly to consumers and businesses through its retail and online stores. The company has also invested in programs to enhance reseller sales by placing high-quality Apple fixtures, merchandising materials, and other resources within selected third-party reseller locations. Through the Apple Premium Reseller Program, certain third-party resellers focused on the Apple platform by providing a high level of integration and support services, as well as product expertise.

As of September 25, 2010, the company had opened a total of 317 retail stores—233 stores in the United States and 84 stores internationally. The company typically located its stores at high-traffic locations in quality shopping malls and urban shopping districts. By operating its own stores and locating them in desirable high traffic locations, the company was better positioned to control the customer buying experience and attract new customers. The stores were designed to simplify and enhance the presentation and marketing of the company's products and related solutions. To that end, retail store configurations had evolved into various sizes to accommodate market-specific demands. The company believed providing direct contact with its targeted customers was an effective way to demonstrate the advantages of its products over those of its competitors. The stores employed experienced and knowledgeable personnel who provided product advice, service, and training. The stores offered a wide selection of third-party hardware, software, and various other accessories and peripherals that complemented the company's products.

Education

Throughout its history, the company focused on the use of technology in education and was committed to delivering tools to help educators teach and students learn. The company believed effective integration of technology into classroom instruction can result in higher levels of student achievement, especially when used to support collaboration, information access, and the expression and representation of student thoughts and ideas. The company designed a range of products, services, and programs to address the needs of education customers, including individual laptop programs and education road shows. In addition, the company supported mobile learning and real-time distribution and accessibility of education-related materials through iTunes U, which allowed students and teachers to share and distribute educational media directly through their computers and mobile communication and media devices. The company sold its products to the education market through its direct sales force, select third-party resellers, and its online and retail stores.

Enterprise, Government, and Creative

The company also sold its hardware and software products to customers in enterprise, government, and creative markets in each of its geographic segments. These markets were also important to many third-party developers who provided Mac-compatible hardware and software solutions. Customers in these markets utilized the company's products because of their high-powered computing performance and expansion capabilities, networking functionality, and seamless integration with complementary products. The company designed its high-end hardware solutions to incorporate the power, expandability, compatibility, and other features desired by these markets.

Other

In addition to consumer, SMB, education, enterprise, government, and creative markets, the company provided hardware and software products and solutions for customers in the information technology and scientific markets.

Business Organization²⁶

The company managed its business primarily on a geographic basis. The company's reportable operating segments consisted of the Americas, Europe, Japan, Asia-Pacific, and Retail. The Americas, Europe, Japan, and Asia-Pacific reportable segments did not include activities related to the Retail segment. The Americas segment included both North and South America. The Europe segment included European countries, as well as the Middle East and Africa. The Asia-Pacific segment included Australia and Asia, but did not include Japan. The Retail segment operated Apple-owned retail stores in the United States and in international markets. Each reportable operating segment provided similar hardware and software products and similar services.

Each of the five operating centers is discussed below.

1. Americas

During 2010, net sales in the Americas segment increased \$5.5 billion or 29% compared to 2009. This increase in net sales was driven by increased iPhone revenue, strong demand for

the iPad, continued demand for Mac desktop and portable systems, and higher sales of third-party digital content and applications from the iTunes Store. Americas Mac net sales and unit sales increased 18% and 21%, respectively, during 2010 compared to 2009, largely due to strong demand for MacBook Pro. The Americas segment represented 37% and 44% of the company's total net sales in 2010 and 2009, respectively.

During 2009, net sales in the Americas segment increased \$2.4 billion or 15% compared to 2008. The increase in net sales during 2009 was attributable to the significant year-over-year increase in iPhone revenue, higher sales of third-party digital content and applications from the iTunes Store, and increased sales of Mac portable systems, partially offset by a decrease in sales of Mac desktop systems and iPods. Americas Mac net sales decreased 6% due primarily to lower average selling prices, while Mac unit sales increased by 4% on a year-over-year basis. The increase in Mac unit sales was due primarily to strong demand for the MacBook Pro. The Americas segment represented approximately 44% of the company's total net sales in both 2009 and 2008.

2. Europe

During 2010, net sales in Europe increased \$6.9 billion or 58% compared to 2009. The growth in net sales was due mainly to a significant increase in iPhone revenue attributable to continued growth from existing carriers and country and carrier expansion, increased sales of Mac desktop and portable systems, and strong demand for the iPad, partially offset by a stronger U.S. dollar. Europe Mac net sales and unit sales increased 32% and 36%, respectively, during the year due to strong demand for MacBook Pro and iMac. The Europe segment represented 29% and 28% of the company's total net sales in 2010 and 2009, respectively.

During 2009, net sales in Europe increased \$2.6 billion or 28% compared to 2008. The increase in net sales was due mainly to increased iPhone revenue and strong sales of Mac portable systems, offset partially by lower net sales of Mac desktop systems, iPods, and a stronger U.S. dollar. Mac unit sales increased 13% in 2009 compared to 2008, which was driven primarily by increased sales of Mac portable systems, particularly MacBook Pro, while total Mac net sales declined as a result of lower average selling prices across all Mac products. iPod net sales decreased year-over-year as a result of lower average selling prices, partially offset by increased unit sales of the higher priced iPod touch. The Europe segment represented 28% and 25% of total net sales in 2009 and 2008, respectively.

3. Japan

During 2010, Japan's net sales increased \$1.7 billion or 75% compared to 2009. The primary contributors to this growth were significant year-over-year increases in iPhone revenue, strong demand for iPad, and to a lesser extent strength in the Japanese Yen. Mac net sales increased by 8% driven by a 22% increase in unit sales due primarily to strong demand for MacBook Pro and iMac, partially offset by lower average selling prices in Japan on a year-over-year basis. The Japan segment represented 6% and 5% of the company's total net sales for 2010 and 2009, respectively.

Japan's net sales increased \$551 million or 32% in 2009 compared to 2008. The primary contributors to this growth were increased iPhone revenue, stronger demand for certain Mac portable systems and iPods, and strength in the Japanese Yen, partially offset by decreased sales of Mac desktop systems. Net sales and unit sales of Mac portable systems increased during 2009 compared to 2008, driven primarily by stronger demand for MacBook Pro. Net sales and unit sales of iPods increased during 2009 compared to 2008, driven by strong demand for iPod touch and iPod nano. The Japan segment represented approximately 5% of the company's total net sales in both 2009 and 2008.

4. Asia-Pacific

Net sales in Asia-Pacific increased \$5.1 billion or 160% during 2010 compared to 2009. The significant growth in Asia-Pacific net sales was due mainly to increased iPhone revenue, which was primarily attributable to country and carrier expansion and continued growth from existing carriers. Asia-Pacific net sales were also favorably affected by strong demand for Mac portable and desktop systems and for the iPad. Particularly strong year-over-year growth was experienced in China, Korea, and Australia. The Asia-Pacific segment represented 13% and 7% of the company's total net sales for 2010 and 2009, respectively. Net sales in Asia-Pacific increased \$493 million or 18% during 2009 compared to 2008, reflecting strong growth in sales of iPhone and Mac portable systems, offset partially by a decline in sales of iPods and Mac desktop systems, as well as a strengthening of the U.S. dollar against the Australian dollar and other Asian currencies. Mac net sales and unit sales grew in the Asia-Pacific region by 4% and 17%, respectively, due to increased sales of the MacBook Pro. The Asia-Pacific segment represented approximately 7% of the company's total net sales in both 2009 and 2008.

5. Retail

Retail net sales increased \$3.1 billion or 47% during 2010 compared to 2009. The increase in net sales was driven primarily by strong demand for iPad, increased sales of Mac desktop and portable systems, and a significant year-over-year increase in iPhone revenue. Mac net sales and unit sales grew in the retail segment by 25% and 35%, respectively, during 2010. The company opened 44 new retail stores during the year, 28 of which were international stores, ending the year with 317 stores open compared to 273 stores at the end of 2009. With an average of 288 stores and 254 stores opened during 2010 and 2009, respectively, average revenue per store increased to \$34.1 million in 2010, compared to \$26.2 million in 2009. The Retail segment represented 15% and 16% of the company's total net sales in 2010 and 2009, respectively.

Retail net sales decreased \$636 million or 9% during 2009 compared to 2008. The decline in net sales was driven largely by a decrease in net sales of iPhones, iPods, and Mac desktop systems, offset partially by strong demand for Mac portable systems. The year-over-year decline in Retail net sales was attributable to continued third-party channel expansion, particularly in the United States where most of the company's stores were located, and also reflects the challenging consumer-spending environment in 2009. The company opened 26 new retail stores during 2009, including 14 international stores, ending the year with 273 stores open. This compared to 247 stores open as of September 27, 2008. With an average of 254 stores and 211 stores opened during 2009 and 2008, respectively, average revenue per store decreased to \$26.2 million for 2009 from \$34.6 million in 2008.

The Retail segment reported operating income of \$2.4 billion during 2010 and \$1.7 billion during both 2009 and 2008. The increase in Retail operating income during 2010 compared to 2009 was attributable to higher overall net sales. Despite the decline in Retail net sales during 2009 compared to 2008, the Retail segment's operating income was flat at \$1.7 billion in 2009 compared to 2008, due primarily to a higher gross margin percentage in 2009 consistent with that experienced by the overall company.

Expansion of the Retail segment has required, and will continue to require, a substantial investment in fixed assets and related infrastructure, operating lease commitments, personnel, and other operating expenses. Capital asset purchases associated with the Retail segment since its inception totaled \$2.2 billion through the end of 2010. As of September 25, 2010, the Retail segment had approximately 26,500 full-time equivalent employees and had outstanding lease commitments associated with retail space and related facilities of \$1.7 billion. The company would incur substantial costs if it were to close multiple retail stores, and such costs could adversely affect the company's financial condition and operating results.

Product Support and Services²⁷

AppleCare® offered a range of support options for the company's customers. These options included assistance that was built into software products, printed and electronic product manuals, online support including comprehensive product information as well as technical assistance, and the AppleCare Protection Plan ("APP"). APP was a fee-based service that typically included two to three years of phone support and hardware repairs, dedicated web-based support resources, and user diagnostic tools.

Markets and Distribution²⁸

The company's customers were primarily in the consumer, SMB, education, enterprise, government, and creative markets. The company utilized a variety of direct and indirect distribution channels, such as its retail stores, online stores, and direct sales force, as well as third-party cellular network carriers, wholesalers, retailers, and value-added resellers. The company believed that sales of its innovative and differentiated products were enhanced by knowledgeable salespersons who could convey the value of the hardware, software, and peripheral integration; demonstrate the unique digital lifestyle solutions that were available on its products; and demonstrate the compatibility of the Mac with the Windows platform and networks. The company further believed providing direct contact with its targeted customers was an effective way to demonstrate the advantages of its products over those of its competitors and providing a high-quality sales and after-sales support experience was critical to attracting new—and retaining existing—customers. To ensure a high-quality buying experience for its products in which service and education were emphasized, the company continued to expand and improve its distribution capabilities by expanding the number of its own retail stores worldwide. Additionally, the company invested in programs to enhance reseller sales by placing high-quality Apple fixtures, merchandising materials, and other resources within selected third-party reseller locations. Through the Apple Premium Reseller Program, certain third-party resellers focused on the Apple platform by providing a high level of integration and support services, as well as product expertise. One of the company's customers accounted for 11% of net sales in 2009; there was no single customer that accounted for more than 10% of net sales in 2010 or 2008.

Competition²⁹

The company was confronted by aggressive competition in all areas of its business. The markets for the company's products and services were highly competitive. These markets were characterized by frequent product introductions and rapid technological advances that had substantially increased the capabilities and use of personal computers, mobile communication and media devices, and other digital electronic devices. The company's competitors who sold personal computers based on other operating systems had aggressively cut prices and lowered their product margins to gain or maintain market share. The company's financial condition and operating results could be adversely affected by these and other industry-wide downward pressures on gross margins. The principal competitive factors included price, product features, relative price/performance, product quality and reliability, design innovation, availability of software and peripherals, marketing and distribution capability, service and support, and corporate reputation.

The company was focused on expanding its market opportunities related to mobile communication and media devices, including iPhone and iPad. The mobile communications and

media device industries were highly competitive and included several large, well-funded, and experienced participants. The company expected competition in these industries to intensify significantly as competitors attempted to imitate some of the iPhone and iPad features and applications within their own products or, alternatively, collaborate with each other to offer solutions that were more competitive than those they currently offered. These industries were characterized by aggressive pricing practices, frequent product introductions, evolving design approaches and technologies, rapid adoption of technological and product advancements by competitors, and price sensitivity on the part of consumers and businesses.

The company's iPod and digital content services faced significant competition from other companies promoting their own digital music and content products and services, including those offering free peer-to-peer music and video services. The company believed it offered superior innovation and integration of the entire solution including the hardware (personal computer, iPhone, iPad, and iPod), software (iTunes), and distribution of digital content and applications (iTunes Store, App Store, and iBookstore). Some of the company's current and potential competitors had substantial resources and may have been able to provide such products and services at little or no profit or even at a loss to compete with the company's offerings. Alternatively, these competitors may have collaborated with each other to offer solutions that were more integrated than those they currently offered.

The company's future financial condition and operating results were substantially dependent on the company's ability to continue to develop and offer new innovative products and services in each of the markets it competed in. In 2010, only AT&T was the carrier for the iPhone. Verizon began selling a version of the iPhone in early 2011. AT&T activated 11 million iPhone accounts in the first nine months of 2010. Before Verizon, the iPhone had been exclusive to AT&T since its launch in 2007.

Supply of Components³⁰

Although most components essential to the company's business were generally available from multiple sources, certain key components including but not limited to microprocessors, enclosures, certain liquid crystal displays ("LCDs"), certain optical drives, and application-specific integrated circuits ("ASICs") were currently obtained by the company from single or limited sources, which subjected the company to significant supply and pricing risks. Many of these and other key components that were available from multiple sources, including but not limited to NAND flash memory, dynamic random access memory ("DRAM"), and certain LCDs, were subject at times to industry-wide shortages and significant commodity pricing fluctuations. In addition, the company entered into certain agreements for the supply of key components including but not limited to microprocessors, NAND flash memory, DRAM, and LCDs at favorable pricing. However, there was no guarantee the company would be able to extend or renew these agreements on similar favorable terms, or at all, upon expiration or otherwise obtain favorable pricing in the future. Therefore, the company remained subject to significant risks of supply shortages and/or price increases that could materially adversely affect its financial condition and operating results.

The company and other participants in the personal computer and mobile communication and media device industries also competed for various components with other industries that experienced increased demand for their products. In addition, the company used some custom components that were not common to the rest of these industries, and introduced new products that often utilized custom components available from only one source. When a component or product used new technologies, initial capacity constraints existed until the suppliers' yields had matured or manufacturing capacity had increased. If the company's supply of a key single-sourced component for a new or existing product was delayed or constrained, if such components were available only at significantly higher prices, or if a key manufacturing

vendor delayed shipments of completed products to the company, the company's financial condition and operating results could be materially adversely affected. The company's business and financial performance could also be adversely affected depending on the time required to obtain sufficient quantities from the original source, or to identify and obtain sufficient quantities from an alternative source. Continued availability of these components at acceptable prices, or at all, may be affected if those suppliers decided to concentrate on the production of common components instead of components customized to meet the company's requirements.

Substantially all of the company's Macs, iPhones, iPads, iPods, logic boards, and other assembled products were manufactured by outsourcing partners, primarily in various parts of Asia. A significant concentration of this outsourced manufacturing was performed by only a few outsourcing partners of the company, including Hon Hai Precision Industry Co. Ltd. and Quanta Computer Inc. The company's outsourced manufacturing was often performed in single locations. Among these outsourcing partners were the sole-sourced supplier of components and manufacturing outsourcing for many of the company's key products, including but not limited to final assembly of substantially all of the company's Macs, iPhones, iPads, and iPods. Although the company worked closely with its outsourcing partners on manufacturing schedules, the company's operating results would be adversely affected if its outsourcing partners were unable to meet their production commitments. The company's purchase commitments typically covered the company's requirements for periods ranging from 30 to 150 days.

The company sources components from a number of suppliers and manufacturing vendors. The loss of supply from any of these suppliers or vendors, whether temporary or permanent, would materially adversely affect the company's business and financial condition.

Research and Development³¹

Because the industries in which the company competed were characterized by rapid technological advances, the company's ability to compete successfully was heavily dependent upon its ability to ensure a continual and timely flow of competitive products, services, and technologies to the marketplace. The company continued to develop new products and technologies and to enhance existing products that expanded the range of its product offerings and intellectual property through licensing and acquisition of third-party business and technology. Total research and development expense were \$1.8 billion, \$1.3 billion, and \$1.1 billion in 2010, 2009, and 2008, respectively.

Patents, Trademarks, Copyrights, and Licenses³²

The company currently held rights to patents and copyrights relating to certain aspects of its Macs; iPhone, iPad, and iPod devices; peripherals; software; and services. In addition, the company registered and/or applied to register trademarks and service marks in the United States and a number of foreign countries for "Apple," the Apple logo, "Macintosh," "Mac," "iPhone," "iPad," "iPod," "iTunes," "iTunes Store," "Apple TV," "MobileMe," and numerous other trademarks, and service marks. Although the company believed the ownership of such patents, copyrights, trademarks, and service marks was an important factor in its business and that its success depended in part on the ownership thereof, the company relied primarily on the innovative skills, technical competence, and marketing abilities of its personnel.

The company regularly filed patent applications to protect inventions arising from its research and development, and was currently pursuing thousands of patent applications around the world. Over time, the company had accumulated a portfolio of several thousand

issued patents in the United States and worldwide. In addition, the company held copyrights relating to certain aspects of its products and services. No single patent or copyright was solely responsible for protecting the company's products. The company believed the duration of the applicable patents it had been granted was adequate relative to the expected lives of its products. Due to the fast pace of innovation and product development, the company's products were often obsolete before the patents related to them expired—and sometimes were obsolete before the patents related to them were even granted.

Many of the company's products were designed to include intellectual property obtained from third parties. While it may be necessary in the future to seek or renew licenses relating to various aspects of its products and business methods, the company believed, based upon past experience and industry practice, that such licenses generally could be obtained on commercially reasonable terms; however, there was no guarantee such licenses could be obtained at all. Because of technological changes in the industries in which the company competed, current extensive patent coverage, and the rapid rate of issuance of new patents, it was possible certain components of the company's products and business methods may unknowingly infringe upon existing patents or the intellectual property rights of others. From time to time, the company had been notified that it may be infringing upon certain patents or other intellectual property rights of third parties.

Foreign and Domestic Operations and Geographic Data³³

The United States represented the company's largest geographic marketplace. Approximately 44% of the company's net sales in 2010 came from sales to customers inside the United States. Final assembly of the company's products was performed in the company's manufacturing facility in Ireland, and by external vendors in California, Texas, the People's Republic of China ("China"), the Czech Republic, and the Republic of Korea ("Korea"). The supply and manufacture of many critical components was performed by sole-sourced third-party vendors in the United States, China, Germany, Ireland, Israel, Japan, Korea, Malaysia, the Netherlands, the Philippines, Taiwan, Thailand, and Singapore. Sole-sourced third-party vendors in China performed final assembly of substantially all of the company's Macs, iPhones, iPads, and iPods. Margins on sales of the company's products in foreign countries, and on sales of products that include components obtained from foreign suppliers, can be adversely affected by foreign currency exchange rate fluctuations and by international trade regulations, including tariffs and antidumping penalties.

Seasonal Business³⁴

The company historically experienced increased net sales in its first and fourth fiscal quarters compared to other quarters in its fiscal year due to the seasonal demand of consumer markets related to the holiday season and the beginning of the school year; however, this pattern was less pronounced following the introductions of the iPhone and iPad. This historical pattern should not be considered a reliable indicator of the company's future net sales or financial performance.

Warranty³⁵

The company offered a basic limited parts and labor warranty on most of its hardware products, including Macs, iPhones, iPads, and iPods. The basic warranty period was typically one year

from the date of purchase by the original end-user. The company also offered a 90-day basic warranty for its service parts used to repair the company's hardware products. In addition, consumers may purchase the APP, which extended service coverage on many of the company's hardware products in most of its major markets.

Backlog³⁶

In the company's experience, the actual amount of product backlog at any particular time was not a meaningful indication of its future business prospects. In particular, backlog often increased in anticipation of or immediately following new product introductions as dealers anticipated shortages. Backlog was often reduced once dealers and customers believed they were able to obtain sufficient supply. Because of the foregoing, backlog should not be considered a reliable indicator of the company's ability to achieve any particular level of revenue or financial performance.

Environmental Laws

Compliance with federal, state, local, and foreign laws enacted for the protection of the environment has to date had no significant effect on the company's capital expenditures, earnings, or competitive position. In the future, however, compliance with environmental laws could materially adversely affect the company.

Production and marketing of products in certain states and countries may subject the company to environmental and other regulations including, in some instances, the requirement to provide customers with the ability to return a product at the end of its useful life, as well as place responsibility for environmentally safe disposal or recycling with the company. Such laws and regulations had been passed in several jurisdictions in which the company operates including various countries within Europe and Asia and certain states and provinces within North America. Although the company did not anticipate any material adverse effects in the future based on the nature of its operations and the thrust of such laws, there was no assurance that such existing laws or future laws will not materially adversely affect the company's financial condition or operating results.

Employees

As of September 25, 2010, the company had approximately 46,600 full-time equivalent employees and an additional 2,800 full-time equivalent temporary employees and contractors.

Legal Proceedings

As of September 25, 2010, the company was subject to the various legal proceedings and claims as well as certain other legal proceedings and claims that had not been fully resolved and that had arisen in the ordinary course of business. In the opinion of management, the company did not have a potential liability related to any current legal proceeding or claim that would individually or in the aggregate materially adversely affect its financial condition or operating results. However, the results of legal proceedings could not be predicted with certainty. Should the company fail to prevail in any of these legal matters or should several of these legal matters be resolved against the company in the same reporting period, the operating results

of a particular reporting period could be materially adversely affected. The company settled certain matters during the fourth quarter of 2010 that did not individually or in the aggregate have a material impact on the company's financial condition and results of operations.

Software Development Costs

Research and development costs were expensed as incurred. Development costs of computer software to be sold, leased, or otherwise marketed were subject to capitalization beginning when a product's technological feasibility has been established and ending when a product was available for general release to customers. In most instances, the company's products were released soon after technological feasibility had been established. Therefore, costs incurred subsequent to achievement of technological feasibility were usually not significant, and generally most software development costs have been expensed as incurred.

The company did not capitalize any software development costs during 2010. In 2009 and 2008, the company capitalized \$71 million and \$11 million, respectively, of costs associated with the development of Mac OS X.

Properties

The company's headquarters were located in Cupertino, California. As of September 25, 2010, the company owned or leased approximately 10.6 million square feet of building space, primarily in the United States and, to a lesser extent, in Europe, Japan, Canada, and the Asia-Pacific regions. Of that amount, approximately 5.6 million square feet was leased, of which approximately 2.5 million square feet was retail building space. Additionally, the company owned a total of 480 acres of land in various locations.

As of September 25, 2010, the company owned a manufacturing facility in Cork, Ireland, that also housed a customer support call center and facilities in Elk Grove, California, that included warehousing and distribution operations and a customer support call center. In addition, the company owned facilities for research and development and corporate functions in Cupertino, California, including land for the future development of the company's second corporate campus. The company also owned a data center in Newark, California, and land in North Carolina for a new data center facility currently under construction. Outside the United States, the company owned additional facilities for various purposes.

John Tarpey's Decision

After analyzing Apple's most recent balance sheets and income statements and integrating that information with his knowledge of the company, John Tarpey was unsure of his next move. As a senior financial analyst of a securities firm, he was obligated to make a recommendation. Should he tell his clients to buy, hold, or sell Apple's common stock?

He had a number of concerns about the company's future. For example, how dependent was Apple on Steve Jobs? The shareholder proposal at the most recent shareholder meeting asking the board to develop an executive succession plan indicated that current shareholders were certainly worried about Jobs' health and ability to lead the company. In addition, how long would it take for Apple's competitors to catch up with the company's lead in product development and perhaps even surpass Apple? There was no doubt in John's mind that Apple's stock price had done very well over the past few years. Even *Mad Money's* Jim Cramer was still touting Apple as the industry's leader and "best of breed." Was this a good time to be

buying more Apple stock or was the smarter move to sell the stock and take some profit while it was still a solid performer?

Given Apple's history of boom-and-bust performance over its lifetime, what should the company be doing to cement its market leadership in this constantly evolving industry?

NOTES

1. This section was directly quoted from *Apple Inc.*, "SEC 10-K," p. 22, September 25, 2010, p. 32.
 2. This section, History of Apple, is a combination of information from previous revisions of the Apple Case in this book, *Strategic Management and Business Policy*, over the past 20 years, Wikipedia, the free encyclopedia, "History of Apple, Inc.," pp. 1–20.
 3. This section was directly quoted from "Steve Jobs," Wikipedia, the free encyclopedia, pp. 1–8.
 4. *Ibid.*, pp. 1–2.
 5. *Ibid.*
 6. "History of Apple, Inc.," pp. 2–3.
 7. Previous Apple Case.
 8. Pixar, "Corporate Overview," p. 1.
 9. "Steve Jobs Magic Kingdom," *Business Week*, p. 3.
 10. *Ibid.*, pp. 1–5, and Vandana Sinna, "Disney, Pixar Give Marriage Second Chance," pp. 1–3.
 11. "Steve Jobs Magic Kingdom," p. 1.
 12. *Ibid.*, p. 2.
 13. *Ibid.*
 14. *Ibid.*
 15. "The Most Powerful People on Earth," *Forbes*, November 22, 2010, p. 88, and Peter Newcomb, "Business-Person of the Year," pp. 136–137.
 16. This section was directly quoted from "Steve Jobs—Health Concerns," Wikipedia, the free encyclopedia, p. 11.
 17. This section was directly quoted from *Apple Inc.*, "SEC 10-K," September 23, 2010.
 18. These five sections below were directly quoted from *Apple Inc.*, "SEC 10-K," September 25, 2010, p. 1.
 19. This section and its five subsections below are directly quoted from *Apple Inc.*, "SEC 10-K," September 25, 2010, pp. 36–37.
 20. *Ibid.*, p. 5.
 21. *Ibid.*, p. 6.
 22. *Ibid.*, pp. 6–7.
 23. *Ibid.*, p. 7.
 24. *Ibid.*, pp. 7–8.
 25. *Ibid.*, p. 8.
 26. *Ibid.*, pp. 8–9.
 27. *Ibid.*, p. 9.
 28. *Ibid.*
 29. *Ibid.*
 30. *Ibid.*
 31. *Ibid.*, p. 10.
 32. *Ibid.*, p. 10.
 33. *Ibid.*, p. 22.
 34. *Ibid.*, p. 8.
 35. *Ibid.*, p. 21.
- Note: Footnotes 20–35 were directly quoted from Apple, Inc., "SEC 10-K," September 25, 2010.
36. Peter Oppenheimer (Chief Financial Officer of Apple Inc.), "Live Update: Apple 4Q Financial Report." Presented at Macworld live conference. www.macworld.com