

An Insightful Analysis Report on APPLE,INC



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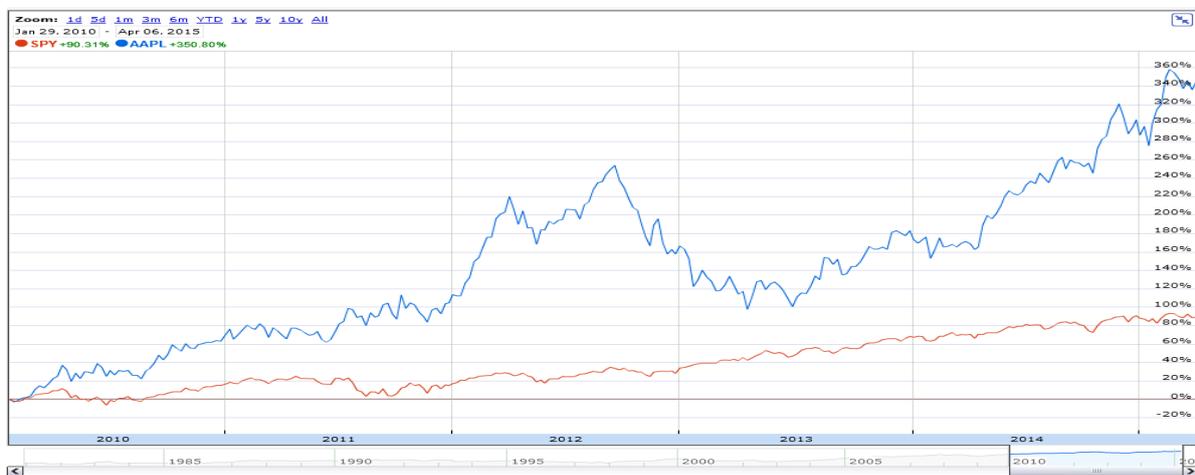
UConn SMF: 2014-2015

Prepared on: April 7th, 2015

Executive Summary

key Financial Metrics		
Stock Price: \$127.31	Market Cap: 741.78	Sector: Technology
52-Week High: \$133.60	P/E Ratio: 17.24	Industry: Computer/Peripherals
52-Week Low: \$73.05	EPS: \$7.39	ROE: 35.1%
Dividend Yield: 1.88%	Price to FCF: 10.1	ROA: 18.3%
Gross Margin: 39%	FCF/NI: 1.5	ROIC: 29.2%
Profit Margin: 30%	CFO/Sales: 32.7%	Curr Ratio: 1.1

Apple Stock Price VS SP500 in 5 Years



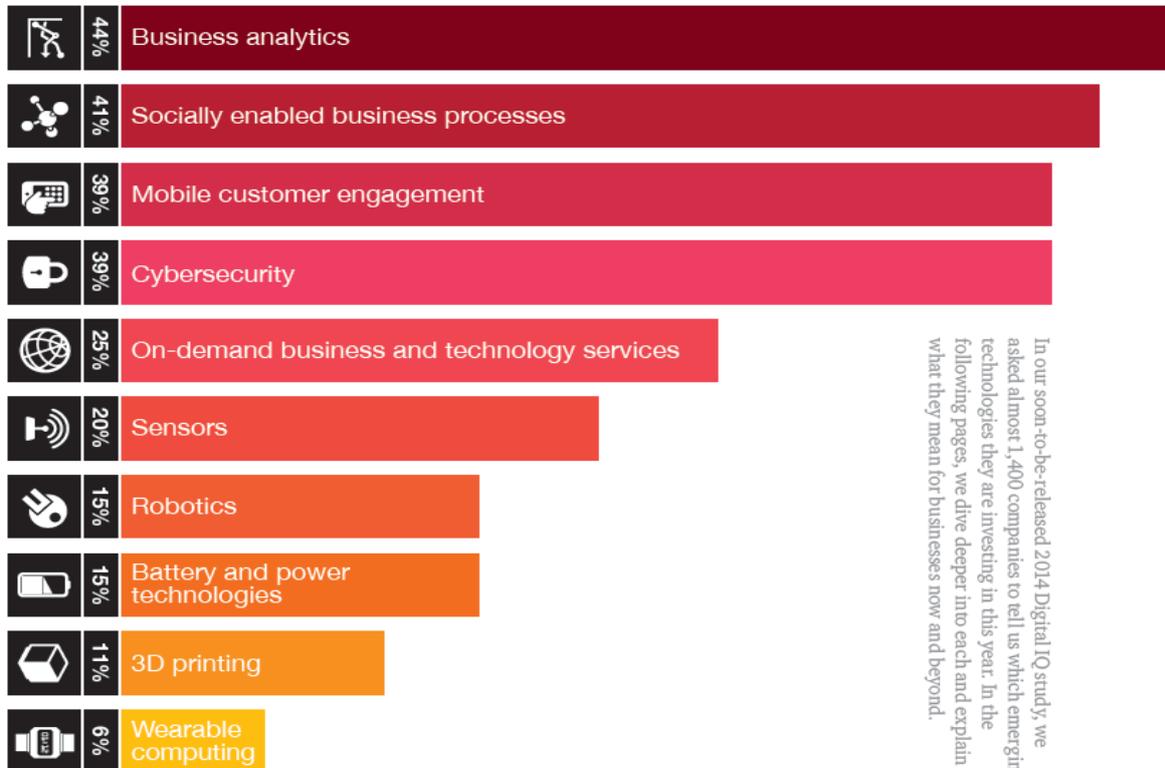
Business Summary

Apple Inc. designs, manufactures, and markets mobile communication and media devices, personal computers, and portable digital music players worldwide. The company also sells related software, services, accessories, networking solutions, and third-party digital content and applications. In addition, it offers various Apple-branded and third-party Mac-compatible and iOS-compatible accessories, including headphones, cases, displays, storage devices, and various other connectivity and computing products and supplies. The company sells and delivers digital content and applications through the iTunes Store, App Store, iBooks Store, and Mac App Store; and sells its products through its retail stores, online stores, and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers, and value-added resellers. It serves consumers, and small and mid-sized businesses, as well as education, enterprise, and government customers.

Investment Thesis

On September 30, 2013, Apple surpassed Coca-Cola to become the world's most valuable brand in the Omnicom Group's "Best Global Brands" report. Apple, as one of the largest electric products manufacturers and providers in the world, always has the capability and innovation to lead people's life. Also, as the economic expansion continues, people will be willing to spend money on the new Iphone product because of the brand recognition. These macro factors will benefit the Apple, Inc. Besides, the stock is undervalued around 45% based on free cash flow projected valuation respectively.

Top Trends for the Technology Sector



In our soon-to-be-released 2014 Digital IQ study, we asked almost 1,400 companies to tell us which emerging technologies they are investing in this year. In the following pages, we dive deeper into each and explain what they mean for businesses now and beyond.

Business analytics

Advances in sensors, display technologies, and devices are enabling companies to monitor people, entities, behaviors, events, and objects. Companies will use data originating from these and other technologies to apply new analytic, statistical and computational modeling techniques.

Socially enabled business processes

Social collaboration tools are making their debut in the HR and sourcing functions, far outside their original home in marketing, sales and service. Forward-thinking organizations are designing and managing business processes to create engaged and empowered organizations.

Mobile customer engagement

Mobile is the center of the consumer's universe. To meet consumers in their mobile worlds, companies are providing compelling, customer-centered products and services. They are elevating and expanding their mobile strategies with investments in disruptive technologies such as sensors, biometrics, Bluetooth, analytics and social media.

Wearable computing (device)

Embedded and wearable sensors are gaining the most ground in areas such as wellness, fitness and beauty that require little or no regulatory approvals and no clinical validation. Great examples are the many consumer-oriented devices that monitor physical activity.

Competitive Advantage

1. Business Strategy

Before returning to Apple, Steve Jobs said: “Apple was a company that was based on innovation. When I left Apple ten years ago, we were ten years ahead of everybody else.”

Apple’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 innovative design. Known for its innovation, Apple has established a unique reputation in the consumer electronics industry and has a loyal customer base for reasons as diverse as its philosophy of aesthetic design to its unusual advertising campaigns. The company believes a high-quality buying experience greatly enhances its ability to attract and retain customers.

2. Pricing Strategy

Apple attempts to increase market demand for its products through differentiation, which entails making its products unique and attractive to consumers. The company’s products have always been designed to be ahead of the curve compared to its peers. Apple has succeeded in creating demand for its products, giving the company power over prices through product differentiation, innovative advertising, ensured brand loyalty, and hype around the launch of new products. Apple uses a retail strategy called “minimum advertised price” (or MAP). Minimum advertised pricing policies prohibit resellers or dealers from advertising a manufacturer’s products below a certain minimum price. MAP is usually enforced through marketing subsidies offered by a manufacturer to its resellers. Apple’s cheapest products are usually priced in the mid-range, but they ensure a high-quality user experience with their features. The hardware and user interface are designed to provide a lot of value for the price, which keeps profits high. Meanwhile, a company can charge a premium price as long as it has a competitive advantage.

3. Vertical Integration

Vertical integration has given Apple a competitive advantage, as it owns chip manufacturers, controls manufacturing, follows extremely strict software standards, and operates in a nearly closed ecosystem of proprietary retail stores. With these advantages, the company has more control of its value chain and, more importantly, its component costs. Apple is known to have the most popular, addictive, and tightly integrated ecosystem of all technology companies. Applications work on multiple devices at the same time—even with a single purchase—and user interfaces are very similar across devices. Currently, Google, Microsoft, and Amazon have entered the fray by setting up their own ecosystems, including devices, books, games, music, media, and storage services. However, Apple had a



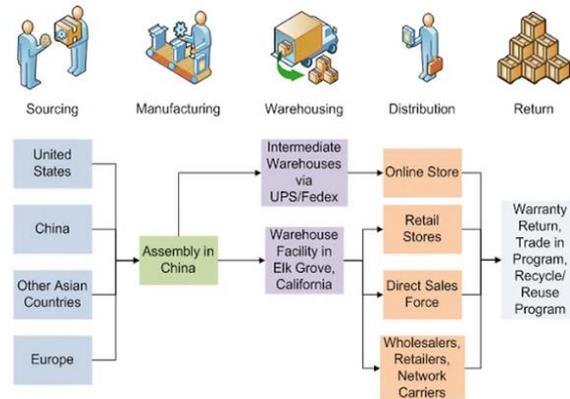
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head start with the success of its iPods, iTunes software, and iTunes Store, and Apple was also one of the pioneers of touchscreen technology in phones. Apple’s App Store recorded more than \$15 billion in sales in 2014, as the company announced. Its unique vertical system will be critical to drive future business opportunities for them.

4. Supply Chain Analysis

Apple’s products and components are manufactured by a number of suppliers around the world. Apple has built a closed ecosystem, with the company having control over nearly every activity in the supply chain—from design to retail. It has outsourced its assembly for economic reasons but has also partnered with manufacturing companies that understand that Apple’s products require different techniques and approaches, which often must be



accommodated by very little lead time. Apple uses some custom components that aren’t commonly used by its competitors, and Apple’s new products often use custom components available from only one source. A recent Bloomberg report said Apple is investing a record \$10.5 billion in new technology—from assembly robots to milling machines—in its supply chain to improve sales that have been slowing due to competition.

Risk Factors

1. Android and Windows competition in the smartphones and tablets
2. Carriers continue to lengthen replacement cycles and begin to lower subsidies as smartphone penetration matures in developed markets
3. Regulatory and legal risk as Apple gains profit share momentum in mobile devices
4. Weak global consumer demand

Valuation (Free Cash Flow Model)

ASSUMPTION

1) Growth period: 8 years

We carefully watched the growth period for a typical information technology device providers in the past and we found that 7-8 years should be an appropriate number for the growth period in this model.

2) Revenue Growth Rate:

We hold a very conservative opinion about the revenue growth in the following years. Although there is an estimation around 23.66% of growth from FY2014 to FY2015 because of the strong sales performance of iPhone 6 and 6 plus globally, we believe this high rate is not sustainable because of the nature of the mobile phone market. Besides, it takes time for the market to penetrate the new APPLE products such Apple Watch and Apple Mac. We designed a gradual decreasing rate model for better estimation of the revenue growth during the growth period.



3) Profitability

We also assume that because of the market competition and structural change for the product, the gross margin will be decreasing for the second half of the growth period (from previous 35% to 30%). Also, we think it is reasonable for the company to have more spending on the operating expense because of the sales and advertising as well as the R&D expense. Besides, the tax rate and the interest rate will remain the same.

4) Roe/Financial Leverage

From multiple reliable resource, we found the current level of ROE is higher than the normal average. Based on that, we decreased ROE gradually from 25% to 20% for the first 5 years and from 20% to 15% in the next three years. Meanwhile, we assume the financial leverage remains during all the growth period for we cannot find any indications which is reasonable enough for us to change.

Income Statement	year 2013	year 2014	year 2015	year 2016	year 2017	year 2018	year 2019	year 2020	year 2021	year 2022	year 2023
Return on equity	0.32	0.30	0.25	0.25	0.25	0.25	0.20	0.20	0.15	0.15	0.15
Financial Leverage	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70

5) Long Term Growth rate

3.0% is the best number for us to decide for the technology industry's long term growth rate.

6) Cost of Capital

The current weighted average cost of capital of APPLE is 8.3%. We believe it is changeable and average WACC for the industry is 9.7%. For the conservative estimation, we tend to use 10% as our discount rate. Also, we made a sensitivity analysis with the consideration for cost of capital and long term.

PRESENTATION

Based on the previous assumptions, we could reasonably made the projected income statement and cash flow statement to show future performance of the company.

Income Statement	year 2013	year 2014	year 2015	year 2016	year 2017	year 2018	year 2019	year 2020	year 2021	year 2022	year 2023
Revenue	170,910.00	182,795.00	226,038.00	259,943.70	293,736.38	331,922.11	365,114.32	401,625.75	433,755.81	455,443.60	469,106.91
Cost of Good Sold	106,606.00	112,258.00	146,924.70	168,963.41	190,928.65	215,749.37	255,580.03	281,138.03	303,629.07	318,810.52	328,374.84
Operating expenses	15,305.00	18,034.00	22,603.80	25,994.37	29,373.64	39,830.65	47,464.86	52,211.35	65,063.37	68,316.54	70,366.04
Other In/Ex	1,292.00	1,364.00									
EBIT	50,291.00	53,867.00	56,509.50	64,985.93	73,434.10	76,342.09	62,069.43	68,276.38	65,063.37	68,316.54	70,366.04
Interest expense	136.00	384.00	664.46	800.93	955.15	1,129.40	1,321.09	1,531.94	1,759.66	1,998.77	2,245.05
EBT	50,155.00	53,483.00	45,207.60	51,988.74	58,747.28	66,384.42	73,022.86	80,325.15	86,751.16	91,088.72	93,821.38
Tax expense	13,118.00	13,973.00	11,301.90	12,997.19	14,686.82	16,596.11	18,255.72	20,081.29	21,687.79	22,772.18	23,455.35
Net income	37,037.00	39,510.00	33,905.70	38,991.56	44,060.46	49,788.32	54,767.15	60,243.86	65,063.37	68,316.54	70,366.04

Statement of Cash Flows	year 2013	year 2014	year 2015	year 2016	year 2017	year 2018	year 2019	year 2020	year 2021	year 2022	year 2023
Cashflows from operation	53,666.00	64,055.00	11,864.14	34,922.87	40,005.34	45,206.03	50,784.08	63,895.01	61,850.37	66,147.76	68,999.71
+ After tax interest	102.00	288.00	498.35	600.70	716.36	847.05	990.82	1,148.96	1,319.75	1,499.08	1,683.79
-Fixed Capital Investment	-16,606.00	-7,305.00	1,307.20	-3,390.57	-3,379.27	-3,818.57	-3,319.22	-3,651.14	-3,213.01	-2,168.78	-1,366.33
Free cash flow to the firm	37,162.00	57,038.00	13,669.69	32,133.00	37,342.43	42,234.51	48,455.68	61,392.82	59,957.11	65,478.06	69,317.17
-After tax interest	-102.00	-288.00	-498.35	-600.70	-716.36	-847.05	-990.82	-1,148.96	-1,319.75	-1,499.08	-1,683.79
+Net borrowings/net debt	83,451.00	36,841.00	12,600.69	27,294.09	30,842.32	34,851.82	38,337.00	42,170.70	45,544.36	47,821.58	49,256.23
Free cash flow to equity (f)	120,511.00	93,591.00	25,772.03	58,826.39	67,468.39	76,239.28	85,801.87	102,414.57	104,181.72	111,800.56	116,889.60

After we got all the above, we can discount the projected future cash flow and use the current outstanding shares number to calculate the intrinsic value per share.

Free Cash flow from Growth Period	486,069.15
Free Cash flow from Terminal(Discounted)	729,425.42
Value of equity	1,215,494.57
Shares outstanding	6.35B
Intrinsic Value	191.42

SENSITIVITY ANALYSIS

		Sensitivity Analysis						
Long term Growth rate		1.50%	2.00%	2.50%	3.00%	3.50%	4.00%	4.50%
Cost of Equity		Intrinsic value per share(\$)						
	7%	208.23	216.45	225.76	236.41	248.69	263.02	279.96
	8%	194.16	201.72	210.29	220.08	231.38	244.56	260.14
	9%	181.27	188.23	196.12	205.13	215.53	227.66	241.99
	10%	169.45	175.85	183.12	191.42	200.99	212.17	225.37
	11%	158.58	164.49	171.18	178.83	187.66	197.96	210.13
	12%	148.59	154.04	160.21	167.27	175.42	184.92	196.14

APPENDIX 1- CONSOLIDATED STATEMENTS OF CASH FLOWS

CONSOLIDATED STATEMENTS OF CASH FLOWS (In millions)

	Years ended		
	September 27, 2014	September 28, 2013	September 29, 2012
Cash and cash equivalents, beginning of the year	\$ 14,259	\$ 10,746	\$ 9,815
Operating activities:			
Net income	39,510	37,037	41,733
Adjustments to reconcile net income to cash generated by operating activities:			
Depreciation and amortization	7,946	6,757	3,277
Share-based compensation expense	2,863	2,253	1,740
Deferred income tax expense	2,347	1,141	4,405
Changes in operating assets and liabilities:			
Accounts receivable, net	(4,232)	(2,172)	(5,551)
Inventories	(76)	(973)	(15)
Vendor non-trade receivables	(2,220)	223	(1,414)
Other current and non-current assets	167	1,080	(3,162)
Accounts payable	5,938	2,340	4,467
Deferred revenue	1,460	1,459	2,824
Other current and non-current liabilities	6,010	4,521	2,552
Cash generated by operating activities	59,713	53,666	50,856
Investing activities:			
Purchases of marketable securities	(217,128)	(148,489)	(151,232)
Proceeds from maturities of marketable securities	18,810	20,317	13,035
Proceeds from sales of marketable securities	189,301	104,130	99,770
Payments made in connection with business acquisitions, net	(3,765)	(496)	(350)
Payments for acquisition of property, plant and equipment	(9,571)	(8,165)	(8,295)
Payments for acquisition of intangible assets	(242)	(911)	(1,107)
Other	16	(160)	(48)
Cash used in investing activities	(22,579)	(33,774)	(48,227)
Financing activities:			
Proceeds from issuance of common stock	730	530	665
Excess tax benefits from equity awards	739	701	1,351
Taxes paid related to net share settlement of equity awards	(1,158)	(1,082)	(1,226)
Dividends and dividend equivalents paid	(11,126)	(10,564)	(2,488)
Repurchase of common stock	(45,000)	(22,860)	0
Proceeds from issuance of long-term debt, net	11,960	16,896	0
Proceeds from issuance of commercial paper, net	6,306	0	0
Cash used in financing activities	(37,549)	(16,379)	(1,698)
Increase/(decrease) in cash and cash equivalents	(415)	3,513	931
Cash and cash equivalents, end of the year	\$ 13,844	\$ 14,259	\$ 10,746
Supplemental cash flow disclosure:			
Cash paid for income taxes, net	\$ 10,026	\$ 9,128	\$ 7,682
Cash paid for interest	\$ 339	\$ 0	\$ 0

See accompanying Notes to Consolidated Financial Statements.

APPENDIX 2-CONSOLIDATED BALANCE SHEETS

CONSOLIDATED BALANCE SHEETS

(In millions, except number of shares which are reflected in thousands and par value)

	September 27, 2014	September 28, 2013
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 13,844	\$ 14,259
Short-term marketable securities	11,233	26,287
Accounts receivable, less allowances of \$86 and \$99, respectively	17,460	13,102
Inventories	2,111	1,764
Deferred tax assets	4,318	3,453
Vendor non-trade receivables	9,759	7,539
Other current assets	9,806	6,882
Total current assets	68,531	73,286
Long-term marketable securities	130,162	106,215
Property, plant and equipment, net	20,624	16,597
Goodwill	4,616	1,577
Acquired intangible assets, net	4,142	4,179
Other assets	3,764	5,146
Total assets	<u>\$ 231,839</u>	<u>\$ 207,000</u>
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	\$ 30,196	\$ 22,367
Accrued expenses	18,453	13,856
Deferred revenue	8,491	7,435
Commercial paper	6,308	0
Total current liabilities	63,448	43,658
Deferred revenue – non-current	3,031	2,625
Long-term debt	28,987	16,960
Other non-current liabilities	24,826	20,208
Total liabilities	120,292	83,451
Commitments and contingencies		
Shareholders' equity:		
Common stock and additional paid-in capital, \$0.00001 par value; 12,600,000 shares authorized; 5,866,161 and 6,294,494 shares issued and outstanding, respectively	23,313	19,764
Retained earnings	87,152	104,256
Accumulated other comprehensive income/(loss)	1,082	(471)
Total shareholders' equity	111,547	123,549
Total liabilities and shareholders' equity	<u>\$ 231,839</u>	<u>\$ 207,000</u>

See accompanying Notes to Consolidated Financial Statements.

APPENDIX 3-CONSOLIDATED STATEMENTS OF OPERATIONS

CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions, except number of shares which are reflected in thousands and per share amounts)

	Years ended		
	September 27, 2014	September 28, 2013	September 29, 2012
Net sales	\$ 182,795	\$ 170,910	\$ 156,508
Cost of sales	112,258	106,606	87,846
Gross margin	70,537	64,304	68,662
Operating expenses:			
Research and development	6,041	4,475	3,381
Selling, general and administrative	11,993	10,830	10,040
Total operating expenses	18,034	15,305	13,421
Operating income	52,503	48,999	55,241
Other income/(expense), net	980	1,156	522
Income before provision for income taxes	53,483	50,155	55,763
Provision for income taxes	13,973	13,118	14,030
Net income	\$ 39,510	\$ 37,037	\$ 41,733
Earnings per share:			
Basic	\$ 6.49	\$ 5.72	\$ 6.38
Diluted	\$ 6.45	\$ 5.68	\$ 6.31
Shares used in computing earnings per share:			
Basic	6,085,572	6,477,320	6,543,726
Diluted	6,122,663	6,521,634	6,617,483
Cash dividends declared per common share	\$ 1.82	\$ 1.64	\$ 0.38

APPENDIX 4-CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (In millions)

	Years ended		
	September 27, 2014	September 28, 2013	September 29, 2012
Net income	\$ 39,510	\$ 37,037	\$ 41,733
Other comprehensive income/(loss):			
Change in foreign currency translation, net of tax effects of \$50, \$35 and \$13, respectively	(137)	(112)	(15)
Change in unrecognized gains/losses on derivative instruments:			
Change in fair value of derivatives, net of tax benefit/(expense) of \$(297), \$(351) and \$73, respectively	1,390	522	(131)
Adjustment for net losses/(gains) realized and included in net income, net of tax expense/(benefit) of \$(36), \$255 and \$220, respectively	149	(458)	(399)
Total change in unrecognized gains/losses on derivative instruments, net of tax	1,539	64	(530)
Change in unrealized gains/losses on marketable securities:			
Change in fair value of marketable securities, net of tax benefit/(expense) of \$(153), \$458 and \$(421), respectively	285	(791)	715
Adjustment for net losses/(gains) realized and included in net income, net of tax expense/(benefit) of \$71, \$82 and \$68, respectively	(134)	(131)	(114)
Total change in unrealized gains/losses on marketable securities, net of tax	151	(922)	601
Total other comprehensive income/(loss)	1,553	(970)	56
Total comprehensive income	\$ 41,063	\$ 36,067	\$ 41,789