

Apple Inc.

F1Q17 Results: Entering Into Another Mega-Upgrade Cycle? Maintain Buy; Raise PT

Summary

Apple reported upside to estimates with iPhone units/ASPs showing outperformance. Management sounded positive about incremental strength across the product portfolio with ongoing services attach to installed base. The company's F2Q outlook showed modest downside to revenue estimates but seemed better than feared. We like what we see and remain positive about the upcoming upgrade cycle opportunity given strong installed base growth. Maintain Buy rating on attractive risk-reward and raise PT to \$135 from \$130.

Key Points

Broad-based strength in fourth quarter results. Apple reported revenues of \$78bn (+3% Y/Y) which showed modest upside to consensus. iPhone, Mac and Services all showed strength and all regions did well. While greater China posted Y/Y decline, mainland China posted growth as the company gained many new users. Gross margin of 38.5% ended up toward the upper-end of outlook range on better product mix. EPS of \$3.36 showed modest upside as well on cost management.

We find double-digit growth in installed base encouraging. iPhone units of 78mm were slightly better than consensus while ASP of \$695 showed upside on better mix toward 7/7+. Management called out a constrained supply environment through DecQ with balance achieved in the month of January. Management also indicated strong double-digit growth in the installed base as it capitalized on the issues at Samsung and attracted meaningful new users. Additionally, results gained from better attach of services.

F2Q17 outlook better than feared. Management guided second quarter revenues of \$51.5-53.5bn (+2-6% Y/Y) implying growth for a second consecutive qtr, vs. consensus of \$54bn. Outlook includes Y/Y FX headwind of ~\$1.2bn. For gross margin, outlook of 38-39% (including Q/Q currency impact of 80bps) was in-line with estimates. Given recent commentary from supply chain, we think investors were expecting weaker guidance. Since Apple will likely have to build inventory in multiple categories, outlook seems reasonable.

Maintain Buy rating; raise PT to \$135 from \$130. We remain in favor of the stock on our view of a robust upcoming upgrade cycle, expanding installed base and easier compare over the next few qtrs. At ~10x EV to our FY17 FCF estimates, we believe risk-reward remains compelling based on potential upside to n-t estimates as well as l-t lifetime value per customer analysis.

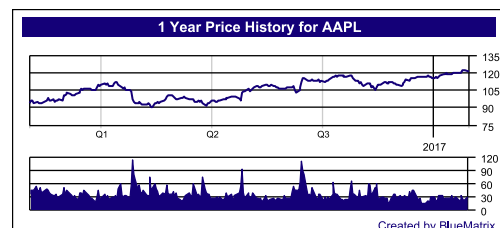
Rating	Buy
Previous Rating	No Change
Price (1/31)	\$121.35
Price Target	\$135.00
Previous Price Target	\$130.00

Key Data	
Symbol	AAPL (NASDAQ)
52-Week Range	\$122.44 - \$89.47
Market Cap (\$mm)	\$638,036
Shares Outstanding (mm)	5,257.8
Float	4,916.7
Average Daily Volume	30,175,422
Dividend/Yield	\$2.18/1.8%

Fiscal Year-End: Sep 30

	2016A	2017E		2018E	
		Prior	Curr	Prior	Curr
Revenue (\$bn)					
1Q	75.8A	76.6A	78.4A	79.3E	78.6E
2Q	50.5A	-	52.7E	54.4E	53.7E
3Q	42.4A	44.9E	44.2E	46.8E	46.0E
4Q	46.9A	49.3E	48.8E	51.3E	50.5E
Yr	215.6A	223.5E	224.0E	231.8E	228.9E
P/	3.0x	-	2.8x	-	2.8x

Earnings per Share (\$)					
1Q	3.28A	3.14A	3.36A	3.42E	3.40E
2Q	1.90A	2.00E	1.98E	2.11E	2.00E
3Q	1.42A	1.58E	1.48E	1.64E	1.50E
4Q	1.67A	1.81E	1.72E	1.86E	1.73E
Yr	8.28A	-	8.53E	9.03E	8.63E
P/E	14.7x	-	14.2x	-	14.1x



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Exhibit 1: F1Q17 Results Versus Our Expectations

	Estimate Dec-16	Actual Dec-16	Variance	QoQ Growth	YoY Growth
Mac Units (K)	4,862	5,374	11%	10%	1%
ASP	\$1,234	\$1,348	9%	15%	6%
Mac Revenue	\$6,002	\$7,244	21%	26%	7%
iPhone Units (K)	75,839	78,290	3%	72%	5%
Implied ASP	\$687	\$695	1%	12%	1%
iPhone Revenue	\$52,136	\$54,378	4%	93%	5%
iPad Units (K)	15,663	13,081	-16%	41%	-19%
Implied ASP	\$450	\$423	-6%	-8%	-4%
iPad Revenue	\$7,048	\$5,533	-21%	30%	-22%
Other	\$11,462	\$11,196	-2%	29%	8%
Net Sales	\$76,647	\$78,351	2%	67%	3%
Gross Margin	38.3%	38.5%	25bps	49bps	-158bps
Operating Expenses	\$6,967	\$6,817	-2%	13%	9%
Operating Margin	29.2%	29.8%	64bps	471bps	-204bps
EPS	\$3.14	\$3.36	7%	101%	2%

Source: FactSet, company data and Mizuho Securities USA estimates

Exhibit 2: Changes to our Estimates

	Old Mar-17	New Mar-17	Old Jun-17	New Jun-17	Old Sep-17	New Sep-17	Old FY17	New FY17
Mac Units (K)	4,002	4,208	4,292	4,430	5,104	5,179	18,261	19,191
ASP	\$1,219	\$1,318	\$1,216	\$1,288	\$1,182	\$1,252	\$1,212	\$1,302
Mac Revenue	\$4,878	\$5,545	\$5,219	\$5,705	\$6,033	\$6,484	\$22,132	\$24,977
iPhone Units (K)	51,798	51,907	40,564	40,649	45,253	45,348	213,454	216,194
Implied ASP	\$647	\$650	\$619	\$609	\$628	\$623	\$652	\$653
iPhone Revenue	\$33,516	\$33,754	\$25,116	\$24,765	\$28,436	\$28,246	\$139,204	\$141,143
iPad Units (K)	10,222	8,929	9,795	8,735	9,525	8,494	45,205	39,240
Implied ASP	\$463	\$436	\$445	\$418	\$437	\$411	\$449	\$422
iPad Revenue	\$4,737	\$3,890	\$4,358	\$3,653	\$4,161	\$3,488	\$20,304	\$16,564
Other	\$10,539	\$10,228	\$22,071	\$20,153	\$7,255	\$7,441	\$34,527	\$33,968
Net Sales	\$52,669	\$52,674	\$44,877	\$44,202	\$49,317	\$48,774	\$223,510	\$224,000
Gross Margin	38%	39%	38%	38%	38%	38%	38%	38%
Operating Expenses	\$6,129	\$6,551	\$5,932	\$6,616	\$6,124	\$6,739	\$25,152	\$26,723
Operating Margin	27%	26%	24%	23%	25%	24%	27%	26%
EPS	\$2.00	\$1.98	\$1.58	\$1.48	\$1.81	\$1.72	\$8.53	\$8.53

Source: FactSet, company data and Mizuho Securities USA estimates

Exhibit 3: Revenue Detail (\$ in millions except ASP, units in thousands)

Apple Revenue Detail	FY16A					Total	FY17E					Total	FY18E					Total
	1QA Dec 15	2QA Mar 16	3QA Jun 16	4QA Sep 16	FY16A		1QA Dec 16	2QE Mar 17	3QE Jun 17	4QE Sep 17	FY17E		1QE Dec 17	2QE Mar 18	3QE Jun 18	4QE Sep 18	FY18E	
Mac	5,312	4,034	4,252	4,886	18,484	5,374	4,208	4,430	5,179	19,191	5,205	4,119	4,400	5,219	18,944			
q/q growth	-7.0%	-24.1%	5.4%	14.9%		10.0%	-21.7%	5.3%	16.9%		0.5%	-20.9%	6.8%	18.6%				
y/y growth	-3.8%	-11.6%	-11.3%	-14.4%	-10.2%	1.2%	4.3%	4.2%	6.0%	3.8%	-3.1%	-2.1%	-0.7%	0.8%	-1.3%			
ASP	\$1,270	\$1,266	\$1,232	\$1,175	\$1,235	\$1,348	\$1,318	\$1,288	\$1,252	\$1,302	\$1,378	\$1,360	\$1,327	\$1,293	\$1,339			
q/q growth	5.3%	-0.3%	-2.7%	-4.7%		14.8%	-2.3%	-2.3%	-2.8%		10.1%	-1.3%	-2.5%	-2.5%				
y/y growth	0.9%	2.9%	-2.0%	-2.6%	-0.2%	6.1%	4.1%	4.5%	6.6%	5.4%	2.2%	3.2%	3.0%	3.3%	2.9%			
Mac Revenue	\$6,746	\$5,107	\$5,239	\$5,739	\$22,831	\$7,244	\$5,545	\$5,705	\$6,484	\$24,977	\$7,172	\$5,602	\$5,838	\$6,751	\$25,363			
% of revenue	8.9%	10.1%	12.4%	12.2%	10.6%	9.2%	10.5%	12.9%	13.3%	11.2%	9.1%	10.4%	12.7%	13.4%	11.1%			
q/q growth	-2.0%	-24.3%	2.6%	9.5%		26.2%	-23.5%	2.9%	13.6%		10.6%	-21.9%	4.2%	15.6%				
y/y growth	-2.9%	-9.0%	-13.1%	-16.6%	-10.4%	7.4%	8.6%	8.9%	13.0%	9.4%	-1.0%	1.0%	2.3%	4.1%	1.5%			
iTunes/Software/Services	\$6,056	\$5,991	\$5,976	\$6,325	\$24,348	\$7,172	\$7,209	\$7,259	\$7,441	\$29,081	\$8,463	\$8,228	\$8,205	\$8,294	\$33,191			
% of revenue	8.0%	11.8%	14.1%	13.5%	11.3%	9.2%	13.7%	16.4%	15.3%	13.0%	10.8%	15.3%	17.8%	16.4%	14.5%			
q/q growth	19.1%	-1.1%	-0.3%	5.8%		13.4%	0.5%	0.7%	2.5%		13.7%	-2.8%	-0.3%	1.1%				
y/y growth	26.2%	19.9%	18.9%	24.4%	22.3%	18.4%	20.3%	21.5%	17.7%	19.4%	18.0%	14.1%	13.0%	11.5%	14.1%			
iPhone Units (K)	74,779	51,193	40,399	45,513	211,884	78,290	51,907	40,649	45,348	216,194	77,467	52,972	42,173	46,641	219,253			
q/q growth	55.6%	-31.5%	-21.1%	12.7%		72.0%	-33.7%	-21.7%	11.6%		70.8%	-31.6%	-20.4%	10.6%				
y/y growth	0.4%	-16.3%	-15.0%	-5.3%	-8.4%	4.7%	1.4%	0.6%	-0.4%	2.0%	-1.1%	2.1%	3.7%	2.9%	1.4%			
Implied ASP	\$691	\$642	\$595	\$619	\$645	\$695	\$650	\$609	\$623	\$653	\$682	\$639	\$610	\$624	\$646			
q/q growth	3.0%	-7.0%	-7.3%	3.9%		12.3%	-6.4%	-6.3%	2.2%		9.6%	-6.4%	-4.5%	2.3%				
y/y growth	0.5%	-2.5%	-9.8%	-7.7%	-3.8%	0.6%	1.3%	2.3%	0.7%	1.2%	-1.8%	-1.8%	0.2%	0.2%	-1.1%			
iPhone Revenue	\$51,635	\$32,857	\$24,048	\$28,160	\$136,700	\$54,378	\$33,754	\$24,765	\$28,246	\$141,143	\$52,861	\$33,843	\$25,744	\$29,113	\$141,561			
% of revenue	68.1%	65.0%	56.8%	60.1%	63.4%	69.4%	64.1%	56.0%	57.9%	63.0%	67.2%	63.0%	56.0%	57.6%	61.8%			
q/q growth	60.3%	-36.4%	-26.8%	17.1%		93.1%	-37.9%	-26.6%	14.1%		87.1%	-36.0%	-23.9%	13.1%				
y/y growth	0.9%	-18.4%	-23.3%	-12.6%	-11.8%	5.3%	2.7%	3.0%	0.3%	3.2%	-2.8%	0.3%	4.0%	3.1%	0.3%			
Accessories	\$4,351	\$2,189	\$2,219	\$2,373	\$11,132	\$4,024	\$2,276	\$2,819	\$3,115	\$12,235	\$4,865	\$2,356	\$2,654	\$3,019	\$12,894			
% of revenue	5.7%	4.3%	5.2%	5.1%	5.2%	5.1%	4.3%	6.4%	6.4%	5.5%	6.2%	4.4%	5.8%	6.0%	5.6%			
q/q growth	42.7%	-49.7%	1.4%	6.9%		69.6%	-43.4%	23.9%	10.5%		56.2%	-51.6%	12.6%	13.8%				
y/y growth	61.8%	29.6%	-16.0%	-22.1%	10.6%	-7.5%	4.0%	27.0%	31.3%	9.9%	20.9%	3.5%	-5.9%	-3.1%	5.4%			
iPad Units (K)	16,122	10,251	9,950	9,267	45,590	13,081	8,929	8,735	8,494	39,240	12,669	8,352	8,138	7,734	36,893			
q/q growth	63.1%	-36.4%	-2.9%	-6.9%		41.2%	-31.7%	-2.2%	-2.8%		49.1%	-34.1%	-2.6%	-5.0%				
y/y growth	-24.7%	-18.8%	-9.0%	-6.2%	-16.9%	-18.9%	-12.9%	-12.2%	-8.3%	-13.9%	-3.2%	-6.5%	-6.8%	-8.9%	-6.0%			
Implied ASP	\$439	\$430	\$490	\$459	\$452	\$423	\$436	\$418	\$411	\$422	\$417	\$442	\$439	\$431	\$430			
q/q growth	1.6%	-2.0%	13.8%	-6.3%		-7.9%	3.0%	-4.0%	-1.8%		1.5%	6.1%	-0.8%	-1.8%				
y/y growth	4.7%	0.1%	18.0%	6.1%	6.9%	-3.7%	1.2%	-14.7%	-10.6%	-6.7%	-1.5%	1.5%	4.9%	4.9%	1.9%			
Total iPad Revenue	\$7,084	\$4,413	\$4,876	\$4,255	\$20,628	\$5,533	\$3,890	\$3,653	\$3,488	\$16,564	\$5,280	\$3,692	\$3,570	\$3,331	\$15,872			
% of revenue	9.3%	8.7%	11.5%	9.1%	9.6%	7.1%	7.4%	8.3%	7.2%	7.4%	6.7%	6.9%	7.8%	6.6%	6.9%			
q/q growth	65.7%	-37.7%	10.5%	-12.7%		30.0%	-29.7%	-6.1%	-4.5%		51.4%	-30.1%	-3.3%	-6.7%				
y/y growth	-21.2%	-18.7%	7.4%	-0.5%	-11.2%	-21.9%	-11.8%	-25.1%	-18.0%	-19.7%	-4.6%	-5.1%	-2.3%	-4.5%	-4.2%			
Net Sales	\$75,872	\$50,557	\$42,358	\$46,852	\$215,639	\$78,351	\$52,674	\$44,202	\$48,774	\$224,000	\$78,641	\$53,722	\$46,010	\$50,508	\$228,881			
q/q growth	47.3%	-33.4%	-16.2%	10.6%		67.2%	-32.8%	-16.1%	10.3%		61.2%	-31.7%	-14.4%	9.8%				
y/y growth	1.7%	-12.8%	-14.6%	-9.0%	-7.7%	3.3%	4.2%	4.4%	4.1%	3.9%	0.4%	2.0%	4.1%	3.6%	2.2%			

Source: Company data and Mizuho Securities USA estimates

Exhibit 4: Income Statement (\$ in millions, except per share data)

	FY16A					Total FY16A	FY17E					Total FY17E	FY18E					Total FY18E
	1QA Dec 15	2QA Mar 16	3QA Jun 16	4QA Sep 16			1QA Dec 16	2QE Mar 17	3QE Jun 17	4QE Sep 17			1QE Dec 17	2QE Mar 18	3QE Jun 18	4QE Sep 18		
Net Sales	\$75,872	\$50,557	\$42,358	\$46,852	\$215,639	\$78,351	\$52,674	\$44,202	\$48,774	\$224,000	\$78,641	\$53,722	\$46,010	\$50,508	\$228,881			
% growth q/q	47.3%	-33.4%	-16.2%	10.6%		67.2%	-32.8%	-16.1%	10.3%		61.2%	-31.7%	-14.4%	9.8%				
% growth y/y	1.7%	-12.8%	-14.6%	-9.0%	-7.7%	3.3%	4.2%	4.4%	4.1%	3.9%	0.4%	2.0%	4.1%	3.6%	2.2%			
Cost of Sales	\$45,449	\$30,636	\$26,252	\$29,039	\$131,376	\$48,175	\$32,359	\$27,475	\$30,268	\$138,276	\$48,064	\$33,114	\$28,848	\$31,642	\$141,668			
% of revenue	59.9%	60.6%	62.0%	62.0%	60.9%	61.5%	61.4%	62.2%	62.1%	61.7%	61.1%	61.6%	62.7%	62.6%	61.9%			
% growth q/q	46.8%	-32.6%	-14.3%	10.6%		65.9%	-32.8%	-15.1%	10.2%		58.8%	-31.1%	-12.9%	9.7%				
% growth y/y	1.3%	-10.8%	-12.3%	-6.2%	-6.2%	6.0%	5.6%	4.7%	4.2%	5.3%	-0.2%	2.3%	5.0%	4.5%	2.5%			
Gross Margin	\$30,423	\$19,921	\$16,106	\$17,813	\$84,263	\$30,176	\$20,315	\$16,727	\$18,506	\$85,724	\$30,577	\$20,608	\$17,163	\$18,865	\$87,213			
Gross Margin %	40.1%	39.4%	38.0%	38.0%	39.1%	38.5%	38.6%	37.8%	37.9%	38.3%	38.9%	38.4%	37.3%	37.4%	38.1%			
Research and development	\$2,404	\$2,511	\$2,560	\$2,570	\$10,045	\$2,871	\$2,880	\$2,848	\$2,871	\$11,469	\$3,078	\$3,259	\$3,356	\$3,452	\$13,146			
% of revenue	3.2%	5.0%	6.0%	5.5%	4.7%	3.7%	5.5%	6.4%	5.9%	5.1%	3.9%	6.1%	7.3%	6.8%	5.7%			
% growth q/q	8.3%	4.5%	2.0%	0.4%		11.7%	0.3%	-1.1%	0.8%		7.2%	5.9%	3.0%	2.9%				
% growth y/y	26.9%	30.9%	25.9%	15.8%	24.5%	19.4%	14.7%	11.3%	11.7%	14.2%	7.2%	13.2%	17.8%	20.3%	14.6%			
SG&A	\$3,848	\$3,423	\$3,441	\$3,482	\$14,194	\$3,946	\$3,672	\$3,768	\$3,869	\$15,254	\$3,961	\$3,745	\$3,784	\$3,855	\$15,344			
% of revenue	5.1%	6.8%	8.1%	7.4%	6.6%	5.0%	7.0%	8.5%	7.9%	6.8%	5.0%	7.0%	8.2%	7.6%	6.7%			
% growth q/q	3.9%	-11.0%	0.5%	1.2%		13.3%	-7.0%	2.6%	2.7%		2.4%	-5.4%	1.0%	1.9%				
% growth y/y	6.9%	-1.1%	-3.5%	-6.0%	-0.9%	2.5%	7.3%	9.5%	11.1%	7.5%	0.4%	2.0%	0.4%	-0.4%	0.6%			
Total operating expenses	\$6,252	\$5,934	\$6,001	\$6,052	\$24,239	\$6,817	\$6,551	\$6,616	\$6,739	\$26,723	\$7,039	\$7,004	\$7,140	\$7,307	\$28,489			
% of revenue	8.2%	11.7%	14.2%	12.9%	11.2%	8.7%	12.4%	15.0%	13.8%	11.9%	9.0%	13.0%	15.5%	14.5%	12.4%			
% growth q/q	5.5%	-5.1%	1.1%	0.8%		12.6%	-3.9%	1.0%	1.9%		4.4%	-0.5%	1.9%	2.3%				
% growth y/y	13.8%	10.3%	7.2%	2.1%	8.2%	9.0%	10.4%	10.2%	11.4%	10.2%	3.3%	6.9%	7.9%	8.4%	6.6%			
Operating Income	\$24,171	\$13,987	\$10,105	\$11,761	\$60,024	\$23,359	\$13,764	\$10,111	\$11,767	\$59,001	\$23,538	\$13,604	\$10,023	\$11,558	\$58,724			
Operating Margin %	31.9%	27.7%	23.9%	25.1%	27.8%	29.8%	26.1%	22.9%	24.1%	26.3%	29.9%	25.3%	21.8%	22.9%	25.7%			
% growth q/q	12.2%	-13.2%	-13.8%	5.2%		18.8%	-12.4%	-12.5%	5.5%		24.1%	-15.4%	-14.0%	5.1%				
% growth y/y	-0.3%	-23.5%	-28.2%	-19.6%	-15.7%	-3.4%	-1.6%	0.1%	0.0%	-1.7%	0.8%	-1.2%	-0.9%	-1.8%	-0.5%			
Interest and other income	\$402	\$155	\$364	\$427	\$1,348	\$821	\$401	\$403	\$402	\$2,027	\$410	\$439	\$439	\$437	\$1,725			
Income before taxes	\$24,573	\$14,142	\$10,469	\$12,188	\$61,372	\$24,180	\$14,165	\$10,514	\$12,169	\$61,027	\$23,949	\$14,043	\$10,462	\$11,996	\$60,449			
Provision for income taxes (Benefit)	\$6,212	\$3,626	\$2,673	\$3,174	\$15,685	\$6,289	\$3,684	\$2,735	\$3,165	\$15,873	\$6,229	\$3,652	\$2,721	\$3,120	\$15,722			
Effective tax rate	25.3%	25.6%	25.5%	26.0%	25.6%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%			
Net Earnings	\$18,361	\$10,516	\$7,796	\$9,014	\$45,687	\$17,891	\$10,481	\$7,779	\$9,004	\$45,155	\$17,720	\$10,391	\$7,741	\$8,876	\$44,727			
Net income (w ESO exp)	\$18,361	\$10,516	\$7,796	\$9,014	\$45,687	\$17,891	\$10,481	\$7,779	\$9,004	\$45,155	\$17,720	\$10,391	\$7,741	\$8,876	\$44,727			
Net Margin %	24.2%	20.8%	18.4%	19.2%	21.2%	22.8%	19.9%	17.6%	18.5%	20.2%	22.5%	19.3%	16.8%	17.6%	19.5%			
Basic shares outstanding	5,558.9	5,514.4	5,443.1	5,366.9	5,470.8	5,298.7	5,295	5,266	5,238	5,274.3	5,211	5,184	5,157	5,130	5,170.3			
Basic EPS (w ESO exp)	\$3.45	\$2.05	\$1.58	\$1.82	\$8.92	\$3.55	\$2.13	\$1.63	\$1.87	\$9.20	\$3.59	\$2.17	\$1.67	\$1.89	\$9.33			
% growth y/y	0.2%	-11.1%	-14.5%	-10.9%	-8.1%	-5.6%	-4.3%	-4.4%	-4.0%	3.1%	-1.3%	-2.8%	-4.4%	-4.8%	1.5%			
Diluted shares outstanding	5,594.1	5,540.9	5,472.8	5,393.3	5,500.3	5,328.0	5,299.6	5,271.2	5,242.7	5,285.4	5,215.8	5,188.9	5,161.9	5,134.8	5,175.3			
Diluted EPS (w ESO exp)	\$3.28	\$1.90	\$1.42	\$1.67	\$8.28	\$3.36	\$1.98	\$1.48	\$1.72	\$8.53	\$3.40	\$2.00	\$1.50	\$1.73	\$8.63			
% growth y/y	7.1%	-18.4%	-23.0%	-14.6%	-10.0%	2.3%	4.2%	3.6%	2.8%	3.1%	1.2%	1.3%	1.6%	0.6%	1.2%			

Source: Company data and Mizuho Securities USA estimates

Exhibit 5: Cash Flow Statement (\$ in millions)

	FY16					Total FY16	FY17					Total FY17	FY18					Total FY18
	1QA Dec 15	2QA Mar 16	3QA Jun 16	4QA Sep 16			1QA Dec 16	2QE Mar 17	3QE Jun 17	4QE Sep 17			1QE Dec 17	2QE Mar 18	3QE Jun 18	4QE Sep 18		
Operating Activities																		
Net Income	\$18,361	\$10,516	\$7,796	\$9,014	\$45,687	\$17,891	\$10,481	\$7,779	\$9,004	\$45,155	\$17,720	\$10,391	\$7,741	\$8,876	\$44,727			
Adjustments to reconcile net income to net cash																		
Depreciation and Amortization	2,954	2,477	2,526	2,548	10,505	2,987	2,008	1,685	1,859	8,540	2,998	2,048	1,754	1,926	8,726			
Stock compensation expense	1,078	1,048	1,054	1,030	4,210	1,256	1,100	1,107	1,082	4,545	1,319	1,155	1,162	1,136	4,772			
Deferred income taxes	1,592	1,500	2,099	(253)	4,938	1,452				1,452					0			
Loss on Sale of PP&E	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Tax benefit from employee stock option plans	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Non-Cash Restructuring	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Cumulative effects fo accounting changes, net of tax	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Other non-cash items	0	0	0	0	0	(274)				(274)					0			
Changes in operating assets and liabilities:																		
Accounts receivable	3,896	724	515	(4,040)	1,095	1,697	1,181	2,562	(5,402)	38	(2,634)	7,605	(502)	(5,028)	(559)			
Inventories	(102)	170	450	(301)	217	(580)	195	685	(859)	(558)	(514)	1,365	(404)	(569)	(122)			
Other current assets	1,826	4,073	(4,756)	(1,194)	(51)	(375)	12,348	(3,837)	(2,872)	5,264	5,413	2,344	(1,410)	(664)	5,683			
Other assets	(893)	1,193	5,866	(5,076)	1,090	(1,446)	(12)	2,366	(1,641)	(733)	1,196	(259)	2,070	(1,729)	1,278			
Accounts payable	(852)	(8,623)	(147)	11,413	1,791	2,460	(12,138)	(994)	13,952	3,280	(4,700)	(7,439)	(400)	9,562	(2,977)			
Other liabilities	(368)	(1,725)	(3,402)	3,391	(2,104)	1,946	(3,392)	641	1,455	650	5,857	(5,594)	2,285	5,825	8,374			
Deferred revenue	(29)	248	(1,367)	(406)	(1,554)	42	209	(494)	240	(3)	(348)	63	(806)	301	(790)			
Net Cash from Operations	\$27,463	\$11,601	\$10,634	\$16,126	\$65,824	\$27,056	\$11,979	\$11,501	\$16,818	\$67,354	\$26,307	\$11,679	\$11,490	\$19,635	\$69,110			
Year over Year Growth	-19%	-39%	-29%	20%	-19%	-1%	3%	8%	4%	2%	-3%	-3%	0%	17%	3%			
Net Income Growth	3%	-20%	-24%	-17%	-13%	-2%	0%	0%	0%	-1%	-1%	0%	0%	-1%	-1%			
Investing Activities																		
Purchase of marketable securities	(47,836)	(38,406)	(25,826)	(30,360)	(142,428)	(54,272)				(54,272)					0			
Proceeds from maturity of marketable securities	3,514	5,634	5,767	6,343	21,258	6,525				6,525					0			
Proceeds from sales of marketable securities	28,262	21,789	19,875	20,610	90,536	32,166				32,166					0			
Purchases of other long-term investments					0					0					0			
Payments for business acquisitions, net of cash	(86)	(54)	(6)	(151)	(297)	(17)				(17)					0			
Acquisitions of property and equipment	(3,612)	(2,336)	(2,809)	(3,977)	(12,734)	(3,334)	(3,037)	(3,652)	(5,170)	(15,193)	(3,834)	(3,492)	(4,199)	(5,946)	(17,471)			
Acquisition of intangible assets	(394)	(263)	(96)	(61)	(814)	(86)				(86)					0			
Other	(298)	(24)	(1,375)	199	(1,498)	(104)				(104)					0			
Net Cash from Investing	(\$20,450)	(\$13,660)	(\$4,470)	(\$7,397)	(\$45,977)	(\$19,122)	(\$3,037)	(\$3,652)	(\$5,170)	(\$30,895)	(\$3,834)	(\$3,492)	(\$4,199)	(\$5,946)	(\$17,471)			
Financing Activities																		
Proceeds from issuance of common stock	1	246	0	248	495	0				0					0			
Excess tax benefits from stock-based comp	224	40	127	16	407	178				178					0			
Cash used to net share settle equity awards	(597)	(154)	(610)	(209)	(1,570)	(629)				(629)					0			
Proceeds from Issuance of Long-Term and Other	0	0	0	0	0	0				0					0			
Repurchase of common stock	(6,863)	(6,667)	(10,166)	(6,026)	(29,722)	(10,851)	(5,000)	(5,000)	(5,000)	(25,851)	(5,000)	(5,000)	(5,000)	(5,000)	(20,000)			
Proceeds from issuance of long term debt ,net	0	15,584	2,400	6,970	24,954	0				0					0			
Repayments of commercial paper ,net	(1,240)	737	1,995	(4,389)	(2,897)	2,385				2,385					0			
Dividend	(2,969)	(2,902)	(3,187)	(3,092)	(12,150)	(3,130)	(3,113)	(3,097)	(3,080)	(12,420)	(3,064)	(3,048)	(3,032)	(3,016)	(12,161)			
Net Cash from Financing	(\$11,444)	\$6,884	(\$9,441)	(\$6,482)	(\$20,483)	(\$12,047)	(\$8,113)	(\$8,097)	(\$8,080)	(\$38,722)	(\$8,064)	(\$8,048)	(\$8,032)	(\$8,016)	(\$32,161)			
Net Change in Cash	(\$4,431)	\$4,825	(\$3,277)	\$2,247	(\$636)	(\$4,113)	\$829	(\$248)	\$3,568	(\$2,263)	\$14,408	\$139	(\$742)	\$5,673	\$19,478			
Beginning Cash Balance	21,120	16,689	21,514	18,237	21,120	20,484	16,371	17,200	16,953	20,484	18,221	32,630	32,769	32,026	18,221			
Ending Cash Balance	\$16,689	\$21,514	\$18,237	\$20,484	\$20,484	\$16,371	\$17,200	\$16,953	\$20,520	\$18,221	\$32,630	\$32,769	\$32,026	\$37,699	\$37,699			

Source: Company data and Mizuho Securities USA estimates

Exhibit 6: Balance Sheet (\$ in millions)

Balance Sheet (in millions, except share amounts)	FY16					FY17					FY18				
	1QA	2QA	3QA	4QA	Total	1QA	2QE	3QE	4QE	Total	1QE	2QE	3QE	4QE	Total
	Dec 15	Mar 16	Jun 16	Sep 16	FY16	Dec 16	Mar 17	Jun 17	Sep 17	FY17	Dec 17	Mar 18	Jun 18	Sep 18	FY18
Assets															
Cash and cash equivalents	16,689	21,514	18,237	20,484	20,484	16,371	17,200	16,953	20,520	18,221	32,630	32,769	32,026	37,699	37,699
Short-term Investments	21,385	33,769	43,519	46,671	46,671	44,081	44,081	44,081	44,081	44,081	44,081	44,081	44,081	44,081	44,081
Cash and short-term investments	\$38,074	\$55,283	\$61,756	\$67,155	\$67,155	\$60,452	\$61,281	\$61,034	\$64,601	\$62,302	\$76,711	\$76,850	\$76,107	\$81,780	\$81,780
Receivables	13,039	12,315	11,769	15,807	15,807	14,110	12,929	10,367	15,769	15,769	18,403	10,797	11,300	16,328	16,328
Allowance for doubtful accounts	86	86	55	53	53	53	53	53	53	53	53	53	53	53	53
Receivables, net	12,953	12,229	11,714	15,754	15,754	14,057	12,876	10,314	15,716	15,716	18,350	10,744	11,247	16,275	16,275
Inventories	2,451	2,281	1,831	2,132	2,132	2,712	2,517	1,832	2,690	2,690	3,204	1,840	2,244	2,813	2,813
Deferred Income Taxes , current	0	7,595	0	0	0	0	5,237	906	1,651	1,651	393	5,631	2,772	1,865	1,865
Other Current Assets	22,741	10,204	18,460	21,828	21,828	26,111	8,526	16,694	18,821	18,821	14,666	7,083	11,353	12,925	12,925
Total Current Assets	\$76,219	\$87,592	\$93,761	\$106,869	\$106,869	\$103,332	\$90,437	\$90,779	\$103,480	\$101,181	\$113,324	\$102,148	\$103,723	\$115,657	\$115,657
Long-Term Marketable Securities	177,665	177,645	169,794	170,430	170,430	185,638	185,638	185,638	185,638	185,638	185,638	185,638	185,638	185,638	185,638
Property and equipment, net	22,300	23,203	25,448	27,010	27,010	26,510	27,539	29,505	32,816	32,816	33,652	35,096	37,542	41,562	41,562
Goodwill	5,202	5,249	5,261	5,414	5,414	5,423	5,423	5,423	5,423	5,423	5,423	5,423	5,423	5,423	5,423
Acquired intangible assets, net	3,924	3,843	3,506	3,206	3,206	2,848	2,848	2,848	2,848	2,848	2,848	2,848	2,848	2,848	2,848
Other Long-Term Assets	7,974	7,745	7,862	8,757	8,757	7,390	7,402	5,036	6,677	6,677	5,482	5,741	3,670	5,400	5,400
Total Long-term Assets	\$217,065	\$217,685	\$211,871	\$214,817	\$214,817	\$227,809	\$228,850	\$228,451	\$233,402	\$233,402	\$233,043	\$234,746	\$235,121	\$240,870	\$240,870
Total Assets	\$293,284	\$305,277	\$305,632	\$321,686	\$321,686	\$331,141	\$319,287	\$319,230	\$336,882	\$334,583	\$346,367	\$336,895	\$338,844	\$356,527	\$356,527
Liabilities and Equity															
Short-Term Debt	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Accounts payable	33,312	25,098	26,318	37,294	37,294	38,510	26,372	25,379	39,330	39,330	34,630	27,191	26,791	36,353	36,353
Accrued expenses	24,032	23,208	20,820	22,027	22,027	23,739	20,347	20,987	22,443	22,443	28,300	22,706	24,991	30,817	30,817
Deferred revenue, current	8,989	9,461	8,352	8,080	8,080	7,889	8,156	7,825	7,712	7,712	7,565	7,816	7,200	7,175	7,175
Other Current Liabilities	9,759	10,498	15,996	11,605	11,605	13,992	7,720	13,232	17,589	17,589	12,079	9,515	15,575	18,898	18,898
Total Current Liabilities	\$76,092	\$68,265	\$71,486	\$79,006	\$79,006	\$84,130	\$62,595	\$67,424	\$87,075	\$87,075	\$82,575	\$67,228	\$74,556	\$93,242	\$93,242
Long-Term Debt	53,204	69,374	68,939	75,427	75,427	73,557	73,557	73,557	73,557	73,557	73,557	73,557	73,557	73,557	73,557
Deferred Revenue, non-current	3,546	3,322	3,064	2,930	2,930	3,163	3,104	2,942	3,295	3,295	3,094	2,906	2,717	3,043	3,043
Other Long-term liabilities	32,175	33,859	35,572	36,074	36,074	37,901	37,901	37,901	37,901	37,901	37,901	37,901	37,901	37,901	37,901
Total Liabilities	\$165,017	\$174,820	\$179,061	\$193,437	\$193,437	\$198,751	\$177,158	\$181,823	\$201,827	\$201,827	\$197,127	\$181,592	\$188,731	\$207,743	\$207,743
Common & Pfd. Stock & Add'l Paid-in Cap	28,253	29,484	30,106	31,251	31,251	32,144	32,144	32,144	32,144	32,144	32,144	32,144	32,144	32,144	32,144
Retained Earnings	101,494	102,021	96,542	96,364	96,364	100,001	111,582	120,468	130,553	130,553	149,592	161,138	170,041	180,052	180,052
Accumulated Other Comprehensive Income	(1,480)	(1,048)	(107)	634	634	245	(1,597)	(15,205)	(27,642)	(27,642)	(32,495)	(37,979)	(52,071)	(63,411)	(63,411)
Total Shareholders' Equity	\$128,267	\$130,457	\$126,541	\$128,249	\$128,249	\$132,390	\$142,129	\$137,406	\$135,055	\$135,055	\$149,240	\$155,303	\$150,113	\$148,784	\$148,784
Total Liabilities and Equity	\$293,284	\$305,277	\$305,632	\$321,686	\$321,686	\$331,141	\$319,287	\$319,230	\$336,882	\$336,882	\$346,367	\$336,895	\$338,844	\$356,527	\$356,527

Source: Company data and Mizuho Securities USA estimates

Price Target Calculation and Key Risks

Our price target is derived using an equally weighted three-pronged valuation approach, which includes a DCF, Enterprise Value (EV) to FCF, and EV to operating earnings analysis. Our assumptions are based on comparables in the information technology hardware universe.

Based on an EV to FCF multiple of 12.0x our FY17 estimate, we come up with a share price of \$146. For our EV to forward 12-month operating earnings analysis, we have calculated a share price of \$132 based on a 12x multiple on our FY17 EPS estimate. Finally, our DCF assumes a discount rate of 10% and a terminal FCF multiple of 12.0x, suggesting fair value 12 months hence of \$121. This implies a free cash flow perpetuity growth rate of about 1.5%. Given these inputs, we reach our 12-month price target of \$135.

On the downside, the biggest risk to Apple's stock could result from the company's inability to keep innovating. The current management team is very capable of delivering on Steve Jobs's vision, however, the stock could be materially impacted if the company were to lose some key executives. Additionally, more than expected slowdown in iPhone sales could push the stock materially lower.

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Investment Risks and Valuation Methods can be located in the following section of this research report - Price Target Calculation and Key Risks.

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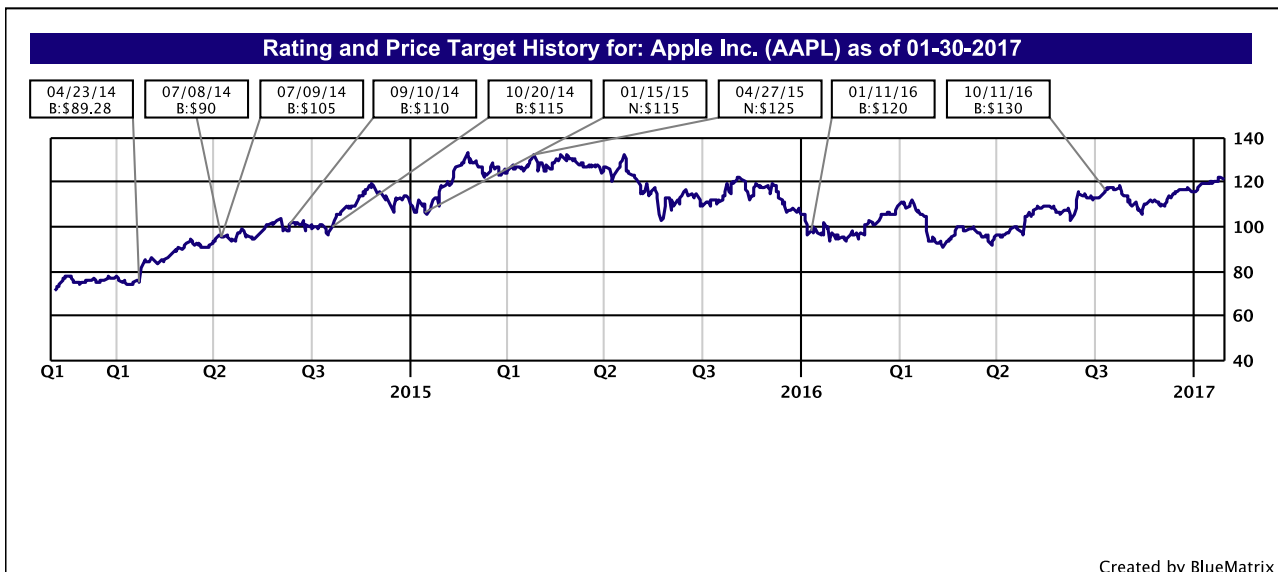
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(As of 1/31)	% of coverage	IB service past 12 mo
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Sell (Underperform)	3.18%	44.44%

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