

Focus Stock Report

March 30, 2011

Apple Inc.

Paul Danesi, CIM – Director, Portfolio Advisory Group

Company Description

Apple is one of the world's largest computer and electronic device makers and one of the great success stories in the realm of American business history.

History

Convinced there was a market for small computers, in 1976, Steve Jobs and Steve Wozniak founded Apple Computer Inc. Sales grew quickly enough for them to take the company public four years later. Wozniak left Apple in 1983, the year before the company launched the Macintosh, the first commercially successful personal computer. In 1985, Steve Jobs departed Apple to found NeXT, which specialized in applications for developing software.

Jobs returned to Apple twelve years later resuming his role as CEO after Apple acquired NeXT. Upon his return, Jobs forged a surprising Alliance with Microsoft whereby Apple released a Mac version of Microsoft Office. In 1998, Apple took a more aggressive stance in the PC market launching a colorful array of iMac computers and at the same time halting production of its personal digital assistant, Newton, essentially the first tablet platform developed by Apple. In 1999, Apple introduced its iBook laptop, which was targeted at the consumer and education markets.

Apple's true renaissance began in 2001 when Steve Jobs introduced the iPod digital music player, which ultimately changed the way people bought and listened to music. Apple's new streamlined all-in-one PC design was also revolutionary, and in 2005 the line began incorporating Intel-based processors. Over the next couple of years, the Company would launch new smaller versions of its iPod MP3 player; a device for streaming PC content to televisions (Apple TV); and with Motorola and Cingular Wireless, a mobile device with iTunes functionality. In 2007, it introduced the highly successful iPhone, and in May 2010, the iPad, its latest take on the tablet computer.

Apple's innovation, creative design, and marketing genius have collectively led to what is today one of the mightiest technology and consumer electronics companies on the planet.

Apple Today

Today, Apple's suite of products and services include personal computers (iMac, Mac Pro, MacBook, MacBook Pro and Air) and related peripherals, mobile

Apple Inc.
(AAPL-NASDAQ)

Rating: Outperform

Risk: Medium

Summary Data (U\$)

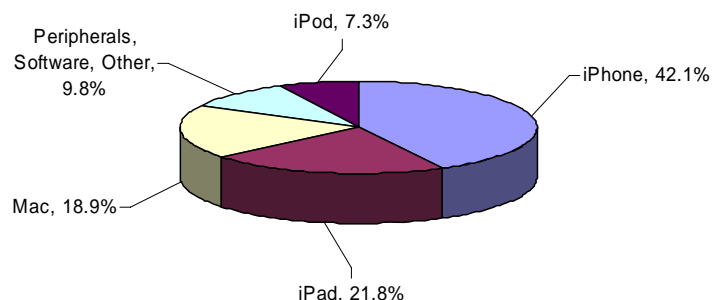
Price (Mar. 25/2011):	\$351.54	Fiscal Year-End:	Sept
12-Month Target:	\$500.00	Dividend:	\$0.00
Total Return:	42%	Yield:	0.0%
52-Week High:	\$364.90	52-Week Low:	\$199.25
Trailing ROE	35.3%	Market Value (\$mil)	\$323,863

Earnings Per Share (U\$)

Annual	2009A	2010A	2011E	2012E
EPS	\$9.08	\$15.15	\$25.11	\$32.49
P/E Multiple:	20.4x	18.7x	14.0x	10.8x

Source: Bloomberg; Credit Suisse

Forecast 2011 Revenue Breakdown



Source: Credit Suisse



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communications (iPhone), tablet computers (iPad), digital music players (iPod), and PC TV interface (Apple TV). It also sells operating systems, utilities, languages, developer tools, and database software. Apple operates an online store (App Store, iTunes, iBooks) as well as over 300 retail outlets, predominantly in the United States and Canada. Below are a few facts about the “store”.

- There are more than 350,000 apps available on the App Store
- There are more than 65,000 native iPad apps
- There are over 14 million songs, 50,000 TV episodes, and 10,000 films on the iTunes Store
- Customers have downloaded more than 10 billion apps so far

Apple has been on the U.S. recommended list since 2007 and has been a stellar performer ever since.

Key elements supporting this investment include:

Highly Differentiated Business Strategy: The Company’s highly differentiated business strategy is premised on operating at the high end of the Personal Computer, mobile phone, and portable media player market, offering leading-edge, innovative products while integrating and controlling software and services with hardware. As Credit Suisse analyst, Kulbinder Garcha, noted in a recent report, “Apple is the clear leader when it comes to service offering; given not only its content in the areas of mobile applications, music, video, and TV shows, but also its tight integration of all these services with its iTunes store”.

Diversified Product Offering: Apple benefits by having product offerings across multiple market segments – MP3 players, PCs, wireless communications. As well, Apple is a true innovator redefining and in some instances creating new product segments within the consumer electronics market. Apple’s brand and marketing prowess allow it to take existing products such as the MP3 player and turn it into a gargantuan market opportunity. Apple’s online iTunes music store was revolutionary and changed the way consumers bought and listened to music. Its comprehensive product suite offers visible benefits for users, notably compatibility.

Outsized Growth: Building on its track record over the last several years, Credit Suisse believes Apple is capable of delivering outsized revenue and earnings growth over the next two years. That growth will be driven by the ongoing penetration of their highly successful iPhone and iPad, peripheral services, as well as four other growth engines the market has yet to fully recognize or discount.

iPhone: The iPhone remains the core engine of growth at Apple. Since being launched in 2007, the device has reached almost cult like status supported by a developer ecosystem, which have created some 65,000 product specific applications. Credit Suisse forecast iPhone unit volume to reach 112 million in 2012, nearly triple the 40 million units sold in 2010. The addressable smartphone market could exceed 1 billion units by 2015. Based on their estimates the iPhone should account for 42% of Apple’s 2011 sales.

iPad: Following on the heels of the original product introduced only last April, the iPad 2 now features a faster processor to speed performance and improve graphics quality, and front and rear cameras that allow for videoconferencing. It’s also 15 percent lighter and 33 percent thinner than the previous model. After selling 7.5 million units in 2010, Credit Suisse forecast unit volume to jump to 51 million units in 2011, and then double again to 104 million units in 2012.

Apple Revenue Forecast (US\$ mlns)

	2010 A	2011 E	2012 E	2013 E	2014 E	2015 E
Mac	17,479	20,947	23,810	26,795	29,589	31,455
iPhone	25,179	46,601	67,470	77,841	78,744	79,408
iPad	4,958	24,169	34,200	43,861	58,068	82,453
iPod	8,274	8,107	7,425	6,451	6,232	5,955
Peripherals, Software & Other	<u>9,335</u>	<u>10,821</u>	<u>13,487</u>	<u>15,027</u>	<u>16,797</u>	<u>17,407</u>
Total	65,225	110,645	146,392	169,975	189,430	216,678
% Change Y/Y		70%	32%	16%	11%	14%

Source: Credit Suisse

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Four Additional Growth Engines: Credit Suisse has identified four additional sources of potential growth for Apple.

- 1) **Low-end iPhone:** with over 80% of the above U\$500 smartphone market, Apple needs to launch a less expensive version of the phone to maintain momentum. Credit Suisse estimates a low-end phone could generate an incremental U\$26 billion in sales by 2015.
- 2) **Emerging markets:** Emerging market distribution and brand awareness is a work in progress and Apple should launch more stores in emerging markets (currently only 4, all of which are in China). The incremental revenue opportunity is U\$19 billion by 2015 in Credit Suisse's opinion.
- 3) **Increased corporate penetration:** Results from a recent proprietary survey conducted by Credit Suisse suggest rapid corporate adoption of Apple products over the next 12 months.
- 4) **Home entertainment provider:** Apple currently has 200 million iTunes customers and Credit Suisse believe this could rise to 700 million by 2015. Advertising, subscriptions, and possibly an Apple TV would be ways of monetizing their massive installed base.

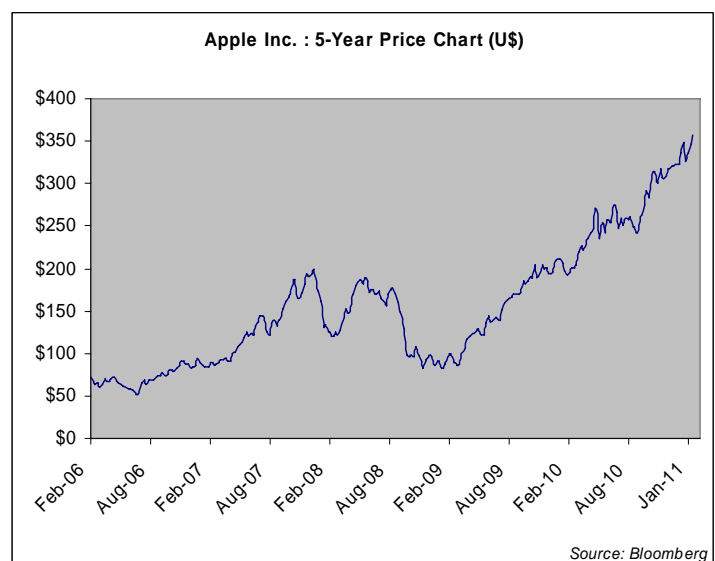
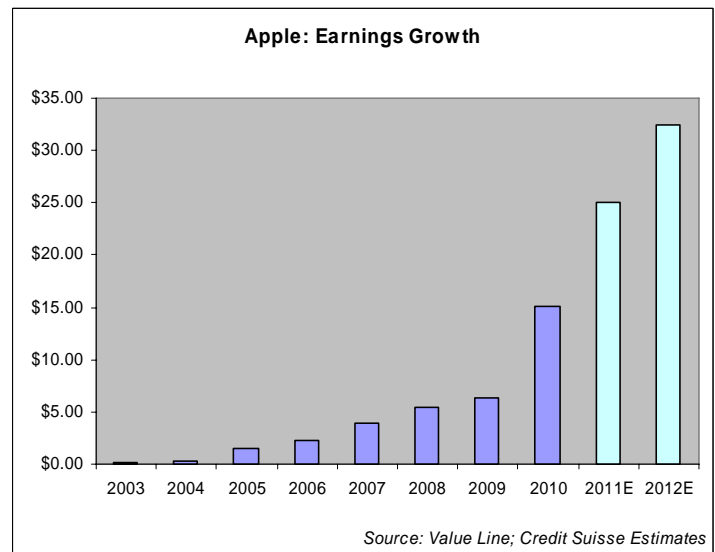
Unparalleled Earnings Growth: Apple Inc. offers investors an unparalleled earnings trajectory for a company of this size, driven by its sustained competitive advantage in hardware, software, service, and applications. Credit Suisse's 2011 and 2012 EPS estimates of U\$25.11 and U\$32.49, respectively imply growth of 66% in 2011 and 29% in 2012. Those estimates may prove conservative. The four opportunities discussed above could add an incremental U\$10 in earnings per share longer-term in their view.

Cash, Cash and More Cash: Apple has a clean balance sheet with no debt and currently sits on approximately U\$27 billion in cash, or more than U\$29 per share of cash, representing ~8% of the share price. Credit Suisse forecast free cash flow of U\$20.8 billion in 2011 rising to just over U\$25 billion in 2012.

All this for a Market Multiple: At its recent quotation, investors are buying one of the worlds fastest growing and most recognizable brands, incredible product momentum and innovation, along with superior earnings growth, all for less than the market multiple. Apple shares currently trade at 12.5 times Credit Suisse's calendarized 2011 EPS estimate of U\$28.12; a discount to the S&P 500 which is trading at a 14.6 times multiple based on Scotia Capital's U\$90 earnings estimate. We find the valuation compelling and encourage potential investors to look through the stock's lofty share price and focus on the fundamentals. A reminder that there is no minimum share order required to purchase the stock.

Risk Factors

The "Jobs" Factor: Steve Jobs is currently on a leave of absence for health reasons, (the third time in the past decade). Some commentators point to the potential risk of Job's permanent



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departure from the company; although we believe the stock would take a short term hit if such an announcement were to occur, we believe the company has demonstrated strong management depth in recent years that make that eventuality of only modest concern for the company in the future.

Competition: Although competition across the Company's various product lines is intense, we believe Apple remains well positioned given its proven product innovation and resulting market dominance in most categories outside the PC space.

Other Risks: Apple like other technology companies is exposed to disruptions in its supply chain and component availability; a risk underscored by the recent earthquake and tsunami in Japan. The Company is also dependent on worldwide economic conditions, the successful management of frequent product introductions and transitions, inventory management, and the support of third-party software developers.

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None.

The supervisors of the Portfolio Advisory Group own securities of the following companies.
None.

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