

HEWLETT PACKARD CO  
Form 10-Q  
March 11, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the quarterly period ended: **January 31, 2011**

Or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-4423

**HEWLETT-PACKARD COMPANY**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**94-1081436**  
(I.R.S. employer  
identification no.)

**3000 Hanover Street, Palo Alto, California**  
(Address of principal executive offices)

**94304**  
(Zip code)

**(650) 857-1501**  
(Registrant's telephone number, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act") during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes  No

The number of shares of HP common stock outstanding as of February 28, 2011 was 2,163,931,073 shares.

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**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES  
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*This Quarterly Report on Form 10-Q, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2 of Part I of this report, contains forward-looking statements that involve risks, uncertainties and assumptions. If the risks or uncertainties ever materialize or the assumptions prove incorrect, the results of Hewlett-Packard Company and its consolidated subsidiaries ("HP") may differ materially from those expressed or implied by such forward-looking statements and assumptions. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including but not limited to any projections of revenue, margins, expenses, earnings, earnings per share, tax provisions, cash flows, benefit obligations, share repurchases, currency exchange rates, the impact of acquisitions or other financial items; any statements of the plans, strategies and objectives of management for future operations, including execution of cost reduction programs and restructuring plans; any statements concerning the expected development, performance or market share relating to products or services; any statements regarding current or future macroeconomic trends or events and the impact of those trends and events on HP and its financial performance; any statements regarding pending investigations, claims or disputes; any statements of expectation or belief; and any statements of assumptions underlying any of the foregoing. Risks, uncertainties and assumptions include the impact of macroeconomic and geopolitical trends and events; the competitive pressures faced by HP's businesses; the development and transition of new products and services (and the enhancement of existing products and services) to meet customer needs and respond to emerging technological trends; the execution and performance of contracts by HP and its suppliers, customers and partners; the protection of HP's intellectual property assets, including intellectual property licensed from third parties; integration and other risks associated with business combination and investment transactions; the hiring and retention of key employees; assumptions related to pension and other post-retirement costs; expectations and assumptions relating to the execution and timing of cost reduction programs and restructuring plans; the resolution of pending investigations, claims and disputes; and other risks that are described herein, including but not limited to the items discussed in "Factors that Could Affect Future Results" set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2 of Part I of this report, and that are otherwise described from time to time in HP's Securities and Exchange Commission reports, including HP's Annual Report on Form 10-K for the fiscal year ended October 31, 2010. HP assumes no obligation and does not intend to update these forward-looking statements.*

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Consolidated Condensed Statements of Earnings

(Unaudited)

|  | Three months ended<br>January 31         |               |
|--|--|---------------|
|  | 2011                                     | 2010          |
|  | In millions, except per<br>share amounts |               |
| Net revenue:   |  |               |
| Products   | \$ 22,194                                | \$ 21,003     |
| Services   | 10,002                                   | 10,067        |
| Financing income   | 106                                      | 107           |
| <b>Total net revenue</b>   | <b>32,302</b>                            | <b>31,177</b> |
| Costs and expenses:  |  |               |
| Cost of products   | 16,798                                   | 16,347        |
| Cost of services   | 7,535                                    | 7,601         |
| Financing interest   | 75                                       | 79            |
| Research and development   | 798                                      | 681           |
| Selling, general and administrative                                | 3,090                                    | 2,967         |
| Amortization of purchased<br>intangible assets                     | 425                                      | 330           |
| Restructuring charges  | 158                                      | 131           |
| Acquisition-related charges  | 29                                       | 38            |
| <b>Total operating expenses</b>                                    | <b>28,908</b>                            | <b>28,174</b> |
| Earnings from operations   | 3,394                                    | 3,003         |
| Interest and other, net  | (97)                                     | (199)         |
| Earnings before taxes  | 3,297                                    | 2,804         |
| Provision for taxes  | 692                                      | 554           |
| Net earnings   | \$ 2,605                                 | \$ 2,250      |
| Net earnings per share:  |  |               |
| Basic  | \$ 1.19                                  | \$ 0.95       |
| Diluted  | \$ 1.17                                  | \$ 0.93       |
| Cash dividends declared per share                                  | \$ 0.16                                  | \$ 0.16       |
| Weighted-average shares used to<br>compute net earnings per share: |  |               |
| Basic  | 2,182                                    | 2,358         |

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|         |       |       |
|---------|-------|-------|
| Diluted | 2,226 | 2,427 |
|---------|-------|-------|

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Consolidated Condensed Balance Sheets

January 31,      October 31,  
2011              2010

In millions, except par value  
(Unaudited)

| <b>ASSETS</b>                                    |            |            |
|--|------------|------------|
| Current assets:                                  |            |            |
| Cash and cash equivalents                        | \$ 9,934   | \$ 10,929  |
| Accounts receivable                              | 16,552     | 18,481     |
| Financing receivables                            | 2,982      | 2,986      |
| Inventory  | 6,747      | 6,466      |
| Other current assets                             | 15,189     | 15,322     |
| <br>   |            |            |
| Total current assets                             | 51,404     | 54,184     |
| <br>   |            |            |
| Property, plant and equipment                    | 11,575     | 11,763     |
| Long-term financing receivables and other assets | 11,017     | 12,225     |
| Goodwill   | 38,506     | 38,483     |
| Purchased intangible assets                      | 7,431      | 7,848      |
| <br>   |            |            |
| Total assets                                     | \$ 119,933 | \$ 124,503 |

**LIABILITIES AND STOCKHOLDERS' EQUITY**

|   |          |          |
|---|----------|----------|
| Current liabilities:  |          |          |
| Notes payable and short-term borrowings   | \$ 3,381 | \$ 7,046 |
| Accounts payable  | 13,453   | 14,365   |
| Employee compensation and benefits  | 2,976    | 4,256    |
| Taxes on earnings   | 789      | 802      |
| Deferred revenue  | 6,927    | 6,727    |
| Accrued restructuring   | 794      | 911      |
| Other accrued liabilities   | 15,290   | 15,296   |
| <br>  |          |          |
| Total current liabilities   | 43,610   | 49,403   |
| <br>  |          |          |
| Long-term debt  | 17,022   | 15,258   |
| Other liabilities   | 17,754   | 19,061   |
| Commitments and contingencies   |          |          |
| Stockholders' equity:   |          |          |
| HP stockholders' equity   |          |          |
| Preferred stock, \$0.01 par value (300 shares authorized; none issued)  |          |          |
| Common stock, \$0.01 par value (9,600 shares authorized; 2,174 and 2,204 shares issued and outstanding, respectively) | 22       | 22       |
| Additional paid-in capital  | 10,877   | 11,569   |
| Retained earnings   | 34,005   | 32,695   |
| Accumulated other comprehensive loss  | (3,698)  | (3,837)  |
| <br>  |          |          |
| Total HP stockholders' equity   | 41,206   | 40,449   |

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|  |            |            |
|--|------------|------------|
| Non-controlling interests                  | 341        | 332        |
| Total stockholders' equity                 | 41,547     | 40,781     |
| Total liabilities and stockholders' equity | \$ 119,933 | \$ 124,503 |

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Consolidated Condensed Statements of Cash Flows

(Unaudited)

Three months ended  
January 31

2011      2010

In millions

|   |          |          |
|---|----------|----------|
| Cash flows from operating activities:   |          |          |
| Net earnings  | \$ 2,605 | \$ 2,250 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |          |          |
| Depreciation and amortization   | 1,255    | 1,162    |
| Stock-based compensation expense  | 180      | 181      |
| Provision for doubtful accounts and financing receivables                           | 34       | 51       |
| Provision for inventory   | 52       | 41       |
| Restructuring charges   | 158      | 131      |
| Deferred taxes on earnings  | 632      | (192)    |
| Excess tax benefit from stock-based compensation                                    | (64)     | (128)    |
| Other, net  | (104)    | 87       |
| Changes in operating assets and liabilities:  |          |          |
| Accounts and financing receivables  | 1,752    | 1,875    |
| Inventory   | (333)    | (543)    |
| Accounts payable  | (912)    | (1,268)  |
| Taxes on earnings   | (242)    | 479      |
| Restructuring   | (272)    | (400)    |
| Other assets and liabilities  | (1,671)  | (1,319)  |
| Net cash provided by operating activities   | 3,070    | 2,407    |
| Cash flows from investing activities:   |          |          |
| Investment in property, plant and equipment   | (926)    | (821)    |
| Proceeds from sale of property, plant and equipment                                 | 543      | 112      |
| Purchases of available-for-sale securities and other investments                    | (19)     | (9)      |
| Maturities and sales of available-for-sale securities and other investments         | 53       |          |
| (Payments) in connection with business acquisitions, net of cash acquired           | (14)     | 7        |
| Net cash used in investing activities   | (363)    | (711)    |
| Cash flows from financing activities:   |          |          |
| (Repayment) issuance of commercial paper and notes payable, net                     | (3,710)  | 78       |
| Issuance of debt  | 2,117    | 29       |
| Payment of debt   | (138)    | (80)     |
| Issuance of common stock under employee stock plans                                 | 430      | 1,319    |
| Repurchase of common stock  | (2,290)  | (2,713)  |
| Excess tax benefit from stock-based compensation                                    | 64       | 128      |
| Dividends   | (175)    | (189)    |
| Net cash used in financing activities   | (3,702)  | (1,428)  |

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|  |        |        |
|--|--------|--------|
| (Decrease) increase in cash and cash equivalents | (995)  | 268    |
| Cash and cash equivalents at beginning of period | 10,929 | 13,279 |

Cash and cash equivalents at end of period                   \$   9,934   \$  13,547

Supplemental schedule of non-cash investing and financing activities:

|  |            |             |
|--|------------|-------------|
| Purchase of assets under capital lease | \$       5 | \$       53 |
|--|------------|-------------|

The accompanying notes are an integral part of these Consolidated Condensed Financial Statements.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements**

**(Unaudited)**

**Note 1: Basis of Presentation**

In the opinion of management, the accompanying Consolidated Condensed Financial Statements of Hewlett-Packard Company and its consolidated subsidiaries ("HP") contain all adjustments, including normal recurring adjustments, necessary to present fairly HP's financial position as of January 31, 2011, its results of operations and cash flows for the three months ended January 31, 2011 and January 31, 2010. The Consolidated Condensed Balance Sheet as of October 31, 2010 is derived from the October 31, 2010 audited consolidated financial statements.

The results of operations for the three months ended January 31, 2011 are not necessarily indicative of the results to be expected for the full year. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with "Risk Factors," "Legal Proceedings," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Quantitative and Qualitative Disclosures About Market Risk" and the Consolidated Financial Statements and notes thereto included in Items 1A, 3, 7, 7A and 8, respectively, of the Hewlett-Packard Company Annual Report on Form 10-K for the fiscal year ended October 31, 2010.

The preparation of financial statements in accordance with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the amounts reported in HP's Consolidated Condensed Financial Statements and accompanying notes. Actual results could differ materially from those estimates.

*Reclassifications and Segment Reorganization*

In connection with organizational realignments implemented in the first quarter of fiscal 2011, certain costs previously reported as Cost of services have been reclassified as Selling, general and administrative expenses to better align those costs with the functional areas that benefit from those expenditures. HP has made certain segment and business unit realignments in order to optimize its operating structure. Reclassifications of prior year financial information have been made to conform to the current year presentation. None of the changes impacts HP's previously reported consolidated net revenue, earnings from operations, net earnings or net earnings per share. See Note 16 for a further discussion of HP's segment reorganization.

**Note 2: Stock-Based Compensation**

HP's stock-based compensation plans include HP's principal equity plans as well as various equity plans assumed through acquisitions. HP's principal equity plans include performance-based restricted units ("PRU"), special incremental performance-based restricted units ("IPRU"), stock options and restricted stock awards.

Total stock-based compensation expense before income taxes for the three months ended January 31, 2011 and 2010 was \$180 million and \$181 million, respectively. The resulting income tax benefit for the three months ended January 31, 2011 and 2010 was \$43 million and \$58 million, respectively.

*Performance-based Restricted Units*

HP's PRU program provides for the issuance of PRUs representing hypothetical shares of HP common stock. Each PRU award reflects a target number of shares ("Target Shares") that may be

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 2: Stock-Based Compensation (Continued)**

issued to the award recipient before adjusting for performance and market conditions. The actual number of shares the recipient receives is determined at the end of a three-year performance period based on results achieved versus company performance goals and may range from 0% to 200% of the Target Shares granted. The performance goals are based on HP's annual cash flow from operations as a percentage of revenue and total shareholder return ("TSR") relative to the S&P 500 over the three-year performance period.

Recipients of PRU awards generally must remain employed by HP on a continuous basis through the end of the applicable three-year performance period in order to receive any portion of the shares subject to that award. Target Shares do not have dividend equivalent rights and do not have the voting rights of common stock until earned and issued following the end of the applicable performance period. The expense for these awards, net of estimated forfeitures, is recorded over the requisite service period based on the number of Target Shares that are expected to be earned and the achievement of the cash flow goals during the performance period.

HP estimates the fair value of a Target Share using a Monte Carlo simulation model, as the TSR modifier contains a market condition. The following weighted-average assumptions were used to determine the weighted-average fair values of the PRU awards:

|   | Three months ended      |                         |
|---|-------------------------|-------------------------|
|   | January 31              |                         |
|   | 2011                    | 2010                    |
| Weighted-average fair value of grants per share | \$ 27.59 <sup>(1)</sup> | \$ 57.13 <sup>(2)</sup> |
| Expected volatility <sup>(3)</sup>              | 30%                     | 38%                     |
| Risk-free interest rate                         | 0.38%                   | 0.73%                   |
| Dividend yield                                  | 0.75%                   | 0.64%                   |
| Expected life in months                         | 19                      | 22                      |

- (1) Reflects the weighted-average fair value for the third year of the three-year performance period applicable to PRUs granted in fiscal 2009, for the second year of the three-year performance period applicable to PRUs granted in fiscal 2010 and for the first year of the three-year performance period applicable to PRUs granted in the three months ended January 31, 2011. The estimated fair value of a Target Share for the third year for PRUs granted in fiscal 2010 and for the second and third years for PRUs granted in the three months ended January 31, 2011 will be determined on the measurement date applicable to those PRUs, which will be the date that the annual cash flow goals are approved for those PRUs, and the expense will be amortized over the remainder of the applicable three-year performance period.
- (2) Reflects the weighted-average fair value for the third year of the three-year performance period applicable to PRUs granted in fiscal 2008, for the second year of the three-year performance period applicable to PRUs granted in fiscal 2009 and for the first year of the three-year performance period applicable to PRUs granted in the three months ended January 31, 2010.
- (3) HP uses historic volatility for PRU awards as implied volatility cannot be used when simulating multivariate prices for companies in the S&P 500.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 2: Stock-Based Compensation (Continued)**

Non-vested PRUs as of January 31, 2011 and changes during the three months ended January 31, 2011 were as follows:

|  | Shares<br>(in thousands) |
|--|--------------------------|
| Outstanding Target Shares at October 31, 2010  | 18,508                   |
| Granted  | 5,738                    |
| Vested   |                          |
| Change in units due to performance and market conditions achievement for PRUs vested in the period |                          |
| Forfeited  | (311)                    |
| Outstanding Target Shares at January 31, 2011  | 23,935                   |
| Outstanding Target Shares assigned a fair value at January 31, 2011                                | 17,960 <sup>(1)</sup>    |

<sup>(1)</sup>

Excludes Target Shares for the third year for PRUs granted in fiscal 2010 and for the second and third years for PRUs granted in the three months ended January 31, 2011 as the measurement date has not yet been established. The measurement date and related fair value for the excluded PRUs will be established when the annual cash flow goals are approved.

At January 31, 2011, there was \$367 million of unrecognized pre-tax stock-based compensation expense related to PRUs with an assigned fair value, which HP expects to recognize over the remaining weighted-average vesting period of 1.5 years.

*Special Incremental Performance-Based Restricted Units*

HP granted IPRUs representing hypothetical shares of HP common stock to certain executive officers. IPRU awards contain performance and market conditions and vest over three years.

The amount of non-vested IPRUs granted and outstanding as of January 31, 2011 was 0.3 million units. At January 31, 2011, there was \$4 million of unrecognized pre-tax stock-based compensation expense related to IPRUs, which HP expects to recognize over the remaining weighted-average vesting period of 2.8 years.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 2: Stock-Based Compensation (Continued)

*Stock Options*

HP estimated the weighted-average fair value of stock options using the Black-Scholes option pricing model with the following weighted-average assumptions:

|  | Three months ended<br>January 31 |          |
|--|----------------------------------|----------|
|  | 2011                             | 2010     |
| Weighted-average fair value of grants per share <sup>(1)</sup> | \$ 11.42                         | \$ 14.42 |
| Implied volatility   | 29%                              | 30%      |
| Risk-free interest rate  | 1.75%                            | 2.34%    |
| Dividend yield   | 0.74%                            | 0.64%    |
| Expected life in months  | 60                               | 62       |

<sup>(1)</sup> The fair value calculation was based on stock options granted during the period.

Option activity as of January 31, 2011 and changes during the three months ended January 31, 2011 were as follows:

|   | Shares<br>(in thousands) | Weighted-<br>Average<br>Exercise<br>Price<br>Per Share | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term<br>(in years) | Aggregate<br>Intrinsic<br>Value<br>(in millions) |
|---|--------------------------|--|--|--|
| Outstanding at October 31, 2010                 | 142,916                  | \$ 28  |  |  |
| Granted   | 224                      | \$ 43  |  |  |
| Exercised                                       | (14,921)                 | \$ 27  |  |  |
| Forfeited/cancelled/expired                     | (1,419)                  | \$ 40  |  |  |
| Outstanding at January 31, 2011                 | 126,800                  | \$ 28  | 2.7  | \$ 2,337   |
| Vested and expected to vest at January 31, 2011 | 125,916                  | \$ 28  | 2.6  | \$ 2,322   |
| Exercisable at January 31, 2011                 | 118,277                  | \$ 28  | 2.2  | \$ 2,191   |

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value that option holders would have received had all option holders exercised their options on January 31, 2011. The aggregate intrinsic value is the difference between HP's closing stock price on the last trading day of the first quarter of fiscal 2011 and the exercise price, multiplied by the number of in-the-money options. Total intrinsic value of options exercised for the three months ended January 31, 2011 was \$258 million.

At January 31, 2011, there was \$234 million of unrecognized pre-tax stock-based compensation expense related to stock options, which HP expects to recognize over the remaining weighted-average vesting period of 1.9 years.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 2: Stock-Based Compensation (Continued)***Restricted Stock Awards*

Restricted stock awards are non-vested stock awards that include grants of restricted stock and grants of restricted stock units.

Non-vested restricted stock awards as of January 31, 2011 and changes during the three months ended January 31, 2011 were as follows:

|  | Shares (in<br>thousands) | Weighted-<br>Average<br>Grant<br>Date Fair<br>Value<br>Per Share |
|--|--------------------------|--|
| Outstanding at October 31, 2010        | 5,848                    | \$ 45  |
| Granted                                | 7,207                    | \$ 43  |
| Vested                                 | (800)                    | \$ 45  |
| Forfeited                              | (99)                     | \$ 45  |
| <b>Outstanding at January 31, 2011</b> | <b>12,156</b>            | <b>\$ 44</b>   |

At January 31, 2011, there was \$408 million of unrecognized pre-tax stock-based compensation expense related to non-vested restricted stock awards, which HP expects to recognize over the remaining weighted-average vesting period of 1.7 years.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 3: Net Earnings Per Share**

HP calculates basic earnings per share using net earnings and the weighted-average number of shares outstanding during the reporting period. Diluted EPS includes any dilutive effect of outstanding stock options, PRUs, IPRUs, restricted stock units, and restricted stock.

The reconciliation of the numerators and denominators of the basic and diluted EPS calculations was as follows:

|   | <b>Three months ended</b>  |             |
|---|----------------------------|-------------|
|   | <b>January 31</b>          |             |
|   | <b>2011</b>                | <b>2010</b> |
|   | <b>In millions, except</b> |             |
|   | <b>per share amounts</b>   |             |
| <b>Numerator:</b>                                   |                            |             |
| Net earnings <sup>(1)</sup>                         | \$ 2,605                   | \$ 2,250    |
| <b>Denominator:</b>                                 |                            |             |
| Weighted-average shares used to compute basic EPS   | 2,182                      | 2,358       |
| Dilutive effect of employee stock plans             | 44                         | 69          |
| Weighted-average shares used to compute diluted EPS | 2,226                      | 2,427       |
| <b>Net earnings per share:</b>                      |                            |             |
| Basic   | \$ 1.19                    | \$ 0.95     |
| Diluted   | \$ 1.17                    | \$ 0.93     |

(1) Net earnings available to participating securities were not significant for the first quarter of fiscal 2011 and 2010. HP considers restricted stock that provides the holder with a non-forfeitable right to receive dividends to be a participating security.

HP excludes options with exercise prices that are greater than the average market price from the calculation of diluted EPS because their effect would be anti-dilutive. In the first quarter of fiscal 2011 and 2010, HP excluded from the calculation of diluted EPS options to purchase 7 million shares and 21 million shares, respectively. HP also excluded from the calculation of diluted EPS options to purchase an additional 1 million shares and 2 million shares in the first quarter of fiscal 2011 and 2010, respectively, whose combined exercise price, unamortized fair value and excess tax benefits were greater in each of those periods than the average market price for HP's common stock because their effect would be anti-dilutive.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 4: Balance Sheet Details**

Balance sheet details were as follows:

*Accounts and Financing Receivables*

|                                 | January 31,<br>2011 | October 31,<br>2010 |
|---------------------------------|---------------------|---------------------|
| In millions                     |                     |                     |
| Accounts receivable             | \$ 17,056           | \$ 19,006           |
| Allowance for doubtful accounts | (504)               | (525)               |
|                                 | \$ 16,552           | \$ 18,481           |
| Financing receivables           | \$ 3,037            | \$ 3,050            |
| Allowance for doubtful accounts | (55)                | (64)                |
|                                 | \$ 2,982            | \$ 2,986            |

HP has revolving trade receivables-based facilities permitting it to sell certain trade receivables to third parties on a non-recourse basis. The aggregate maximum capacity under these programs was \$556 million as of January 31, 2011. HP sold \$463 million of trade receivables during the first three months of fiscal 2011. As of January 31, 2011, HP had \$261 million available under these programs.

*Inventory*

|   | January 31,<br>2011 | October 31,<br>2010 |
|---|---------------------|---------------------|
| In millions                               |                     |                     |
| Finished goods                            | \$ 4,527            | \$ 4,431            |
| Purchased parts and fabricated assemblies | 2,220               | 2,035               |
|   | \$ 6,747            | \$ 6,466            |

*Property, Plant and Equipment*

|                                      | January 31,<br>2011 | October 31,<br>2010 |
|--------------------------------------|---------------------|---------------------|
| In millions                          |                     |                     |
| Land                                 | \$ 521              | \$ 530              |
| Buildings and leasehold improvements | 8,307               | 8,523               |
| Machinery and equipment              | 14,871              | 13,874              |
|                                      | 23,699              | 22,927              |
| Accumulated depreciation             | (12,124)            | (11,164)            |
|                                      | \$ 11,575           | \$ 11,763           |

On November 16, 2010, HP sold certain land and buildings for approximately \$415 million, which resulted in a gain of approximately \$286 million reported under selling, general and administrative expenses in the Consolidated Condensed Statement of Earnings. The sale was

part of the company's multi-year program to consolidate real estate locations worldwide to reduce real estate costs.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 5: Goodwill and Purchased Intangible Assets

*Goodwill*

Goodwill allocated to HP's business segments as of January 31, 2011 and changes in the carrying amount of goodwill for the three months ended January 31, 2011 are as follows:

|                      | Enterprise<br>Servers,<br>Storage<br>and<br>Services | HP<br>Software | Personal<br>Systems<br>Group | Imaging<br>and<br>Printing<br>Group | HP<br>Financial<br>Services | Corporate<br>Investments | Total    |           |
|----------------------|--|----------------|------------------------------|-------------------------------------|-----------------------------|--------------------------|----------|-----------|
| In millions          |  |                |                              |                                     |                             |                          |          |           |
| Balance at           |  |                |                              |                                     |                             |                          |          |           |
| October 31, 2010     | \$ 16,967  | \$ 6,610       | \$ 7,545                     | \$ 2,500                            | \$ 2,456                    | \$ 144                   | \$ 2,261 | \$ 38,483 |
| Goodwill adjustments | 256  | 1,420          | (251)                        | (2)                                 | (1)                         |                          | (1,399)  | 23        |
| Balance at           |  |                |                              |                                     |                             |                          |          |           |
| January 31, 2011     | \$ 17,223  | \$ 8,030       | \$ 7,294                     | \$ 2,498                            | \$ 2,455                    | \$ 144                   | \$ 862   | \$ 38,506 |

In connection with certain fiscal 2011 organizational realignments, HP reclassified goodwill related to HP's networking business from Corporate Investments to Enterprise Servers, Storage and Networking ("ESSN") and goodwill related to the communications and media solutions business from HP Software to Services. Additionally, during the three months ended January 31, 2011, HP recorded an increase to goodwill as a result of currency translation related to a 3Com subsidiary whose functional currency is not the U.S. dollar. The increase to goodwill was partially offset by tax adjustments primarily related to tax deductible stock-based awards assumed in connection with acquisitions completed prior to the effective date of the current accounting standard for business combinations.

*Purchased Intangible Assets*

HP's purchased intangible assets associated with completed acquisitions are composed of:

|  | January 31, 2011 |                             |          | October 31, 2010 |                             |          |
|--|------------------|-----------------------------|----------|------------------|-----------------------------|----------|
|  | Gross            | Accumulated<br>Amortization | Net      | Gross            | Accumulated<br>Amortization | Net      |
| In millions  |                  |                             |          |                  |                             |          |
| Customer contracts, customer lists and distribution agreements | \$ 7,505         | \$ (4,092)                  | \$ 3,413 | \$ 7,503         | \$ (3,864)                  | \$ 3,639 |
| Developed and core technology and patents                      | 5,784            | (3,572)                     | 2,212    | 5,763            | (3,384)                     | 2,379    |
| Product trademarks   | 346              | (248)                       | 98       | 346              | (239)                       | 107      |
| Total amortizable purchased intangible assets                  | 13,635           | (7,912)                     | 5,723    | 13,612           | (7,487)                     | 6,125    |
| IPR&D  | 286              |                             | 286      | 301              |                             | 301      |
| Compaq trade name  | 1,422            |                             | 1,422    | 1,422            |                             | 1,422    |
| Total purchased intangible assets                              | \$ 15,343        | \$ (7,912)                  | \$ 7,431 | \$ 15,335        | \$ (7,487)                  | \$ 7,848 |

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 5: Goodwill and Purchased Intangible Assets (Continued)**

Estimated future amortization expense related to finite-lived purchased intangible assets at January 31, 2011 is as follows:

| Fiscal year:              | In millions |
|---------------------------|-------------|
| 2011 (remaining 9 months) | \$ 1,102    |
| 2012                      | 1,294       |
| 2013                      | 1,141       |
| 2014                      | 810         |
| 2015                      | 682         |
| 2016                      | 534         |
| Thereafter                | 160         |
| Total                     | \$ 5,723    |

**Note 6: Restructuring Charges**

HP records restructuring charges associated with management approved restructuring plans to either reorganize one or more of HP's business segments, or to remove duplicative headcount and infrastructure associated with one or more business acquisitions. Restructuring charges can include severance costs to eliminate a specified number of employees, infrastructure charges to vacate facilities and consolidate operations, and contract cancellation cost. Restructuring charges are recorded based upon planned employee termination dates and site closure and consolidation plans. The timing of associated cash payments is dependent upon the type of restructuring charge and can extend over a multi-year period. HP records the short-term portion of the restructuring liability in Accrued restructuring and the long-term portion in Other liabilities in the Consolidated Condensed Balance Sheets.

*Fiscal 2010 Acquisitions*

On July 1, 2010, HP completed the acquisition of Palm, Inc. ("Palm"). In connection with the acquisition, HP's management approved and initiated a plan to restructure the operations of Palm, including severance for Palm employees, contract cancellation costs and other items. The total expected cost of the plan is \$46 million. In fiscal 2010, HP recorded restructuring charges of approximately \$46 million related to the plan. No further restructuring charges are anticipated, subject to changes in the Palm integration plan. The majority of these costs are expected to be paid out by the second quarter of fiscal 2011.

On April 12, 2010, HP completed the acquisition of 3Com. In connection with the acquisition, HP's management approved and initiated a plan to restructure the operations of 3Com, including severance costs and costs to vacate duplicative facilities. The total expected cost of the plan is \$42 million. In fiscal 2010, HP recorded restructuring charges of approximately \$18 million related to the plan. HP expects to record the majority of the remaining cost of this restructuring plan by the second quarter of fiscal 2011 based upon the timing of planned terminations and facility closure dates. These costs are expected to be paid out through fiscal 2016.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 6: Restructuring Charges (Continued)**

*Fiscal 2010 ES Restructuring Plan*

On June 1, 2010, HP's management announced a plan to restructure its Enterprise Services business, which includes its Infrastructure Technology Outsourcing, Business Process Outsourcing and Application Services business units. The multi-year restructuring program includes plans to consolidate commercial data centers, tools and applications. The total expected cost of the plan that will be recorded as restructuring charges is approximately \$1.0 billion, including severance costs to eliminate approximately 9,000 positions and infrastructure charges. For the three months ended January 31, 2011, a restructuring charge of \$97 million was recorded primarily related to severance costs. HP expects to record the majority of the remaining severance costs by the second quarter of fiscal 2011 and the majority of the infrastructure charges through fiscal 2012. The timing of the charges is based upon planned termination dates and site closure and consolidation plans. The majority of the associated cash payments are expected to be paid out through the fourth quarter of fiscal 2012. As of January 31, 2011, approximately 2,900 positions have been eliminated.

*Fiscal 2009 Restructuring Plan*

In May 2009, HP's management approved and initiated a restructuring plan to structurally change and improve the effectiveness of the Imaging and Printing Group ("IPG"), the Personal Systems Group ("PSG"), and ESSN businesses. The total expected cost of the plan is \$292 million in severance-related costs associated with the planned elimination of approximately 4,400 positions. As of January 31, 2011, all planned eliminations had occurred, and the majority of the remaining restructuring costs are expected to be paid out through the second quarter of fiscal 2011.

*Fiscal 2008 HP/EDS Restructuring Plan*

In connection with the acquisition of Electronic Data Systems Corporation ("EDS") on August 26, 2008, HP's management approved and initiated a restructuring plan to combine and align HP's services businesses, eliminate duplicative overhead functions and consolidate and vacate duplicative facilities. The restructuring plan is expected to be implemented over four years from the acquisition date at a total expected cost of \$3.4 billion.

The restructuring plan includes severance cost to eliminate approximately 25,000 positions. As of January 31, 2011, all planned eliminations had occurred and the vast majority of the associated severance costs had been paid out. The infrastructure charges in the restructuring plan include facility closure and consolidation costs and the costs associated with early termination of certain contractual obligations. HP expects to record the majority of these costs through fiscal 2011 based upon the execution of site closure and consolidation plans. The associated cash payments are expected to be paid out through fiscal 2016.

Approximately \$1.5 billion of the expected costs were associated with pre-acquisition EDS and were reflected in the purchase price of EDS. These costs are subject to change based on the actual costs incurred. The remaining costs are primarily associated with HP and will be recorded as a restructuring charge.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 6: Restructuring Charges (Continued)***Summary of Restructuring Plans*

The adjustments to the accrued restructuring expenses related to all of HP's restructuring plans described above for the three months ended January 31, 2011 were as follows:

|                                      | Balance,<br>October 31,<br>2010 | Three<br>months<br>ended<br>January 31,<br>2011<br>charges | Cash<br>payments | Non-cash<br>settlements<br>and other<br>adjustments | Balance,<br>January 31,<br>2011 | As of January 31, 2011<br>Total costs<br>and<br>adjustments<br>to date | Total<br>expected<br>costs and<br>adjustments |
|--------------------------------------|---------------------------------|--|------------------|---|---------------------------------|--|---|
| <b>In millions</b>                   |                                 |  |                  |   |                                 |  |   |
| <i>Fiscal 2010<br/>acquisitions</i>  | \$ 44                           | \$   | \$ (21)          | \$  | \$ 23                           | \$ 64  | \$ 88   |
| <i>Fiscal 2010 ES<br/>Plan:</i>      |                                 |  |                  |   |                                 |  |   |
| Severance                            | \$ 620                          | \$ 85  | \$ (57)          | \$ (1)  | \$ 647                          | \$ 715   | \$ 761  |
| Infrastructure                       | 4                               | 12   | (12)             |   | 4                               | 32   | 231   |
| <b>Total ES Plan</b>                 | <b>\$ 624</b>                   | <b>\$ 97</b>   | <b>\$ (69)</b>   | <b>\$ (1)</b>                                       | <b>\$ 651</b>                   | <b>\$ 747</b>  | <b>\$ 992</b>                                 |
| <i>Fiscal 2009 Plan</i>              | \$ 57                           | \$   | \$ (33)          | \$ (1)  | \$ 23                           | \$ 292   | \$ 292  |
| <i>Fiscal 2008 HP/EDS<br/>Plan:</i>  |                                 |  |                  |   |                                 |  |   |
| Severance                            | \$ 75                           | \$ 14  | \$ (66)          | \$ (16)   | \$ 7                            | \$ 2,160   | \$ 2,160                                      |
| Infrastructure                       | 408                             | 47   | (83)             | 12  | 384                             | 740  | 1,225   |
| <b>Total HP/EDS Plan</b>             | <b>\$ 483</b>                   | <b>\$ 61</b>   | <b>\$ (149)</b>  | <b>\$ (4)</b>                                       | <b>\$ 391</b>                   | <b>\$ 2,900</b>  | <b>\$ 3,385</b>                               |
| <b>Total restructuring<br/>plans</b> | <b>\$ 1,208</b>                 | <b>\$ 158</b>  | <b>\$ (272)</b>  | <b>\$ (6)</b>                                       | <b>\$ 1,088</b>                 | <b>\$ 4,003</b>  | <b>\$ 4,757</b>                               |

At January 31, 2011 and October 31, 2010, HP included the long-term portion of the restructuring liability of \$294 million and \$297 million, respectively, in Other liabilities, and the short-term portion in Accrued restructuring in the accompanying Consolidated Condensed Balance Sheets.

**Note 7: Fair Value**

HP determines fair value based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants.

Valuation techniques used by HP are based upon observable and unobservable inputs. Observable or market inputs reflect market data obtained from independent sources, while unobservable inputs reflect HP's assumptions about market participant assumptions based on best information available. Observable inputs are the preferred source of values. These two types of inputs create the following fair value hierarchy:

Level 1 Quoted prices (unadjusted) for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

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Level 3 Prices or valuations that require management inputs that are both significant to the fair value measurement and unobservable.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 7: Fair Value (Continued)

The following section describes the valuation methodologies HP uses to measure its financial assets and liabilities at fair value.

**Cash Equivalents and Investments:** HP holds time deposits, money market funds, commercial paper, other debt securities primarily consisting of corporate and foreign government notes and bonds, and common stock and equivalents. Where applicable, HP uses quoted prices in active markets for identical assets to determine fair value. If quoted prices in active markets for identical assets are not available to determine fair value, HP uses quoted prices for similar assets and liabilities or inputs that are observable either directly or indirectly. If quoted prices for identical or similar assets are not available, HP uses internally developed valuation models, whose inputs include bid prices, and third-party valuations utilizing underlying assets assumptions.

**Derivative Instruments:** As discussed in Note 8, HP mainly holds non-speculative forwards, swaps and options to hedge certain foreign currency and interest rate exposures. When active market quotes are not available, HP uses industry standard valuation models. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit risk, foreign exchange rates, and forward and spot prices for currencies. In certain cases, market-based observable inputs are not available and, in those cases, HP uses management judgment to develop assumptions which are used to determine fair value.

The following table presents HP's assets and liabilities that are measured at fair value on a recurring basis:

|   | As of January 31, 2011    |          |          |               | As of October 31, 2010    |          |          |               |          |
|---|---------------------------|----------|----------|---------------|---------------------------|----------|----------|---------------|----------|
|   | Fair Value Measured Using |          |          | Total Balance | Fair Value Measured Using |          |          | Total Balance |          |
| Level 1                                   | Level 2                   | Level 3  | Level 1  |               | Level 2                   | Level 3  |          |               |          |
| <b>In millions</b>                        |                           |          |          |               |                           |          |          |               |          |
| <b>Assets</b>                             |                           |          |          |               |                           |          |          |               |          |
| Time deposits                             | \$                        | \$ 6,082 | \$       | \$ 6,082      | \$                        | \$ 6,598 | \$       | \$ 6,598      |          |
| Commercial paper                          |                           | 97       |          | 97            |                           |          |          |               |          |
| Money market funds                        |                           | 515      |          | 515           | 971                       |          |          | 971           |          |
| Marketable equity securities              |                           | 11       | 3        | 14            | 11                        | 3        |          | 14            |          |
| Foreign bonds                             |                           | 7        | 368      | 375           | 8                         | 365      |          | 373           |          |
| Corporate bonds and other debt securities |                           | 3        | 2        | 49            | 54                        | 3        | 6        | 50            |          |
| Derivatives:                              |                           |          |          |               |                           |          |          |               |          |
| Interest rate contracts                   |                           |          | 535      | 535           |                           | 735      |          | 735           |          |
| Foreign exchange contracts                |                           |          | 141      | 7             | 148                       | 150      | 32       | 182           |          |
| Other derivatives                         |                           |          | 4        | 7             | 11                        | 5        | 6        | 11            |          |
| Total Assets                              | \$                        | \$ 536   | \$ 7,232 | \$ 63         | \$ 7,831                  | \$ 993   | \$ 7,862 | \$ 88         | \$ 8,943 |
| <b>Liabilities</b>                        |                           |          |          |               |                           |          |          |               |          |
| Derivatives:                              |                           |          |          |               |                           |          |          |               |          |
| Interest rate contracts                   | \$                        | \$ 66    | \$       | \$ 66         | \$                        | \$ 89    | \$       | \$ 89         |          |
| Foreign exchange                          |                           |          | 775      | 9             | 784                       | 880      | 10       | 890           |          |

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contracts

|                   |   |   |
|-------------------|---|---|
| Other derivatives | 2 | 2 |
|-------------------|---|---|

|                   |    |    |     |    |   |    |     |    |    |     |    |    |    |     |
|-------------------|----|----|-----|----|---|----|-----|----|----|-----|----|----|----|-----|
| Total Liabilities | \$ | \$ | 843 | \$ | 9 | \$ | 852 | \$ | \$ | 969 | \$ | 10 | \$ | 979 |
|-------------------|----|----|-----|----|---|----|-----|----|----|-----|----|----|----|-----|

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## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments

*Cash Equivalents and Available-for-Sale Investments*

Cash equivalents and available-for-sale investments at fair value as of January 31, 2011 and October 31, 2010 were as follows:

|  | January 31, 2011 |                             |                             | October 31, 2010           |                 |                             |                             |                            |
|--|------------------|-----------------------------|-----------------------------|----------------------------|-----------------|-----------------------------|-----------------------------|----------------------------|
|  | Cost             | Gross<br>Unrealized<br>Gain | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value | Cost            | Gross<br>Unrealized<br>Gain | Gross<br>Unrealized<br>Loss | Estimated<br>Fair<br>Value |
| <b>In millions</b>   |                  |                             |                             |                            |                 |                             |                             |                            |
| <b>Cash Equivalents</b>  |                  |                             |                             |                            |                 |                             |                             |                            |
| Time deposits  | \$ 6,055         | \$                          | \$                          | \$ 6,055                   | \$ 6,590        | \$                          | \$                          | \$ 6,590                   |
| Commercial paper   | 97               |                             |                             | 97                         |                 |                             |                             |                            |
| Money market funds   | 515              |                             |                             | 515                        | 971             |                             |                             | 971                        |
| <b>Total cash equivalents</b>                                    | <b>6,667</b>     |                             |                             | <b>6,667</b>               | <b>7,561</b>    |                             |                             | <b>7,561</b>               |
| <b>Available-for-Sale Investments</b>                            |                  |                             |                             |                            |                 |                             |                             |                            |
| <b>Debt securities:</b>  |                  |                             |                             |                            |                 |                             |                             |                            |
| Time deposits  | 27               |                             |                             | 27                         | 8               |                             |                             | 8                          |
| Foreign bonds  | 310              | 65                          |                             | 375                        | 315             | 58                          |                             | 373                        |
| Corporate bonds and other debt securities                        | 76               |                             | (22)                        | 54                         | 89              |                             | (30)                        | 59                         |
| <b>Total debt securities</b>                                     | <b>413</b>       | <b>65</b>                   | <b>(22)</b>                 | <b>456</b>                 | <b>412</b>      | <b>58</b>                   | <b>(30)</b>                 | <b>440</b>                 |
| Equity securities in public companies                            | 5                | 4                           |                             | 9                          | 5               | 4                           |                             | 9                          |
| <b>Total cash equivalents and available-for-sale investments</b> | <b>\$ 7,085</b>  | <b>\$ 69</b>                | <b>\$ (22)</b>              | <b>\$ 7,132</b>            | <b>\$ 7,978</b> | <b>\$ 62</b>                | <b>\$ (30)</b>              | <b>\$ 8,010</b>            |

Cash equivalents consist of investments in time deposits, commercial paper and money market funds with original maturities of ninety days or less. Time deposits were primarily issued by institutions outside the U.S. as of January 31, 2011 and October 31, 2010. Available-for-sale securities consist of short-term investments which mature within twelve months or less and long-term investments with maturities longer than twelve months. Investments include primarily time deposits, fixed-interest securities, and institutional bonds. HP estimates the fair values of its investments based on quoted market prices or pricing models using current market rates. These estimated fair values may not be representative of actual values that will be realized in the future.

The gross unrealized loss as of January 31, 2011 was due primarily to declines in certain debt securities and included \$22 million that has been in a continuous loss position for more than twelve months. The gross unrealized loss as of October 31, 2010 was due primarily to declines in the fair value of certain debt securities and included \$28 million that has been in a continuous loss position for more than twelve months. HP does not intend to sell these debt securities, and it is not likely that HP will be required to sell these debt securities prior to the recovery of the amortized cost. For the three months ended January 31, 2011 and 2010, HP did not recognize any impairment charge associated with debt securities.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments (Continued)

Contractual maturities of short-term and long-term investments in available-for-sale debt securities at January 31, 2011 were as follows:

|                             | Available-for-Sale<br>Securities |                         |
|-----------------------------|----------------------------------|-------------------------|
|                             | Cost                             | Estimated<br>Fair Value |
|                             | January 31, 2011                 |                         |
|                             | In millions                      |                         |
| Due in 1-5 years            | \$ 30                            | \$ 30                   |
| Due in more than five years | 383                              | 426                     |
|                             | \$ 413                           | \$ 456                  |

A summary of the carrying values and balance sheet classification of all short-term and long-term investments in debt and equity securities as of January 31, 2011 and October 31, 2010 was as follows:

|  | January 31,<br>2011 | October 31,<br>2010 |
|--|---------------------|---------------------|
|  | In millions         |                     |
| Available-for-sale debt securities                           | \$                  | \$ 5                |
| Included in Other current assets                             |                     | 5                   |
| Available-for-sale debt securities                           | 456                 | 435                 |
| Available-for-sale equity securities                         | 9                   | 9                   |
| Equity securities in privately-held companies                | 54                  | 154                 |
| Other investments  | 9                   | 9                   |
| Included in long-term financing receivables and other assets | 528                 | 607                 |
| Total investments  | \$ 528              | \$ 612              |

Equity securities in privately held companies include cost basis and equity method investments. Other investments include marketable trading securities. HP includes gains or losses from changes in fair value of these securities, offset by losses or gains on the related liabilities, in Interest and other, net, in HP's Consolidated Condensed Statements of Earnings. The net impact associated with these securities were not material for the three months ended January 31, 2011 and 2010.

*Derivative Financial Instruments*

HP is a global company that is exposed to foreign currency exchange rate fluctuations and interest rate changes in the normal course of its business. As part of its risk management strategy, HP uses derivative instruments, primarily forward contracts, option contracts, interest rate swaps, and total return swaps, to hedge certain foreign currency, interest rate and, to a lesser extent, equity exposures. HP's objective is to offset gains and losses resulting from these exposures with losses and gains on the derivative contracts used to hedge them, thereby reducing volatility of earnings or protecting fair values of assets and liabilities. HP does not have any leveraged derivatives and does not use derivative contracts for speculative purposes. HP designates its derivatives as fair value hedges, cash flow hedges or hedges of the foreign currency exposure of a net investment in a foreign operation ("net investment

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 8: Financial Instruments (Continued)**

hedges"). Additionally, for derivatives not designated as hedging instruments, HP categorizes those economic hedges as other derivatives. HP recognizes all derivatives, on a gross basis, in the Consolidated Condensed Balance Sheets at fair value and reports them in Other current assets, Long-term financing receivables and other assets, Other accrued liabilities, or Other liabilities. HP classifies cash flows from the derivative programs as operating activities in the Consolidated Condensed Statements of Cash Flows.

As a result of the use of derivative instruments, HP is exposed to the risk that counterparties to derivative contracts will fail to meet their contractual obligations. To mitigate the counterparty credit risk, HP has a policy of only entering into contracts with carefully selected major financial institutions based upon their credit ratings and other factors, and HP maintains dollar and term limits that correspond to each institution's credit rating. HP's established policies and procedures for mitigating credit risk on principal transactions and short-term cash include reviewing and establishing limits for credit exposure and continually assessing the creditworthiness of counterparties. Master agreements with counterparties include master netting arrangements as further mitigation of credit exposure to counterparties. These arrangements permit HP to net amounts due from HP to a counterparty with amounts due to HP from the same counterparty.

To further mitigate credit exposure to counterparties, HP may enter into collateral security arrangements with its counterparties. These arrangements require HP to hold or post collateral, referred to as "restricted cash," when the derivative fair values exceed contractually established thresholds. The restricted cash is comprised of U.S. dollars, and it is held by a third party. HP reports all collateral arrangements on a gross basis and classifies restricted cash received from its counterparties in Other current assets on HP's Consolidated Condensed Balance Sheets with a corresponding amount recorded under Other accrued liabilities. As of January 31, 2011, the fair value of all derivative instruments under these collateralized arrangements were in a net asset position of approximately \$51 million for which \$41 million of restricted cash had been deposited by the counterparties.

Certain of HP's derivative instruments contain credit risk-related contingent features, such as provisions whereby HP and the counterparties to the derivative instruments could request collateralization on derivative instruments in net liability positions if HP's or the counterparties' credit ratings fall below certain thresholds. As of January 31, 2011 and 2010, HP was not required to post any collateral, and HP did not have any derivative instruments with credit risk-related contingent features that were in a significant net liability position.

*Fair Value Hedges*

HP enters into fair value hedges to reduce the exposure of its debt portfolio to interest rate risk. HP issues long-term debt in U.S. dollars based on market conditions at the time of financing. HP uses interest rate swaps to mitigate the market risk exposures in connection with the debt to achieve primarily U.S. dollar LIBOR-based floating interest expense. The swap transactions generally involve principal and interest obligations for U.S. dollar-denominated amounts. Alternatively, HP may choose not to swap fixed for floating interest payments or may terminate a previously executed swap if it believes a larger proportion of fixed-rate debt would be beneficial. When investing in fixed-rate instruments, HP may enter into interest rate swaps that convert the fixed interest returns into variable

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 8: Financial Instruments (Continued)**

interest returns and would classify these swaps as fair value hedges. For derivative instruments that are designated and qualify as fair value hedges, HP recognizes the gain or loss on the derivative instrument, as well as the offsetting loss or gain on the hedged item, in Interest and other, net in the Consolidated Condensed Statements of Earnings in the current period.

*Cash Flow Hedges*

HP uses a combination of forward contracts and options designated as cash flow hedges to protect against the foreign currency exchange rate risks inherent in its forecasted net revenue and, to a lesser extent, cost of sales, operating expense, and intercompany lease loan denominated in currencies other than the U.S. dollar. HP's foreign currency cash flow hedges mature generally within six to twelve months. However, certain leasing revenue-related forward contracts and intercompany lease loan forward contracts extend for the duration of the lease term, which can be up to five years. For derivative instruments that are designated and qualify as cash flow hedges, HP initially records the effective portion of the gain or loss on the derivative instrument in accumulated other comprehensive income or loss as a separate component of stockholders' equity and subsequently reclassifies these amounts into earnings in the period during which the hedged transaction is recognized in earnings. HP reports the effective portion of cash flow hedges in the same financial statement line item as the changes in value of the hedged item. During the three months ended January 31, 2011 and 2010, HP did not discontinue any cash flow hedge for which it was probable that a forecasted transaction would not occur.

*Net Investment Hedges*

HP uses forward contracts designated as net investment hedges to hedge net investments in certain foreign subsidiaries whose functional currency is the local currency. These derivative instruments are designated as net investment hedges and, as such, HP records the effective portion of the gain or loss on the derivative instrument together with changes in the hedged items in cumulative translation adjustment as a separate component of stockholders' equity.

*Other Derivatives*

Other derivatives not designated as hedging instruments consist primarily of forward contracts HP uses to hedge foreign currency balance sheet exposures. HP also uses total return swaps and, to a lesser extent, interest rate swaps, based on the equity and fixed income indices, to hedge its executive deferred compensation plan liability. For derivative instruments not designated as hedging instruments, HP recognizes changes in the fair values in earnings in the period of change. HP recognizes the gain or loss on foreign currency forward contracts used to hedge balance sheet exposures in Interest and other, net in the same period as the remeasurement gain and loss of the related foreign currency denominated assets and liabilities. HP recognizes the gain or loss on the total return swaps and interest rate swaps in Interest and other, net in the same period as the gain or loss from the change in market value of the executive deferred compensation plan liability.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments (Continued)

*Hedge Effectiveness*

For interest rate swaps designated as fair value hedges, HP measures effectiveness by offsetting the change in fair value of the hedged debt with the change in fair value of the derivative. For foreign currency options and forward contracts designated as cash flow or net investment hedges, HP measures effectiveness by comparing the cumulative change in the hedge contract with the cumulative change in the hedged item, both of which are based on forward rates. HP recognizes any ineffective portion of the hedge, as well as amounts not included in the assessment of effectiveness, in the Consolidated Condensed Statements of Earnings. As of January 31, 2011 and 2010, the portion of hedging instruments' gain or loss excluded from the assessment of effectiveness was not material for fair value, cash flow or net investment hedges. Hedge ineffectiveness for fair value, cash flow and net investment hedges was not material in the three months ended January 31, 2011 and 2010.

*Fair Value of Derivative Instruments in the Consolidated Condensed Balance Sheets*

As discussed in Note 7, HP estimates the fair values of derivatives primarily based on pricing models using current market rates and records all derivatives on the balance sheet at fair value. The gross notional and fair value of derivative financial instruments in the Consolidated Condensed Balance Sheets were recorded as follows:

|   | As of January 31, 2011        |                      |                                 |                           |                   | As of October 31, 2010        |                      |                                 |                           |                   |
|---|-------------------------------|----------------------|---------------------------------|---------------------------|-------------------|-------------------------------|----------------------|---------------------------------|---------------------------|-------------------|
|   | Gross Notional <sup>(1)</sup> | Other Current Assets | Other and Financing Receivables | Other Accrued Liabilities | Other Liabilities | Gross Notional <sup>(1)</sup> | Other Current Assets | Other and Financing Receivables | Other Accrued Liabilities | Other Liabilities |
| <b>In millions</b>                                      |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Derivatives designated as hedging instruments           |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Fair value hedges:                                      |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Interest rate contracts                                 | \$ 8,575                      | \$                   | \$ 478                          | \$                        | \$                | \$ 8,575                      | \$                   | \$ 656                          | \$                        | \$                |
| Cash flow hedges:                                       |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Foreign exchange contracts                              | 17,613                        | 72                   | 18                              | 405                       | 86                | 16,862                        | 98                   | 20                              | 503                       | 83                |
| Net investment hedges:                                  |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Foreign exchange contracts                              | 1,504                         | 8                    | 4                               | 58                        | 60                | 1,466                         | 8                    | 2                               | 58                        | 62                |
| Total derivatives designated as hedging instruments     | 27,692                        | 80                   | 500                             | 463                       | 146               | 26,903                        | 106                  | 678                             | 561                       | 145               |
| Derivatives not designated as hedging instruments       |                               |                      |                                 |                           |                   |                               |                      |                                 |                           |                   |
| Foreign exchange contracts                              | 11,177                        | 44                   | 2                               | 131                       | 44                | 13,701                        | 51                   | 3                               | 129                       | 55                |
| Interest rate contracts <sup>(2)</sup>                  | 2,200                         |                      | 57                              |                           | 66                | 2,200                         |                      | 79                              |                           | 89                |
| Other derivatives                                       | 415                           | 4                    | 7                               | 2                         |                   | 397                           | 5                    | 6                               |                           |                   |
| Total derivatives not designated as hedging instruments | 13,792                        | 48                   | 66                              | 133                       | 110               | 16,298                        | 56                   | 88                              | 129                       | 144               |

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Total derivatives      \$ 41,484   \$ 128   \$    566   \$ 596   \$ 256   \$ 43,201   \$ 162   \$    766   \$ 690   \$ 289

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- (1) Represents the face amounts of contracts that were outstanding as of January 31, 2011 and October 31, 2010, respectively.
- (2) Represents offsetting swaps acquired through a previous business combination that were not designated as hedging instruments.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments (Continued)

*Effect of Derivative Instruments on the Consolidated Condensed Statements of Earnings*

The before-tax effect of a derivative instrument and related hedged item in a fair value hedging relationship for the three months ended January 31, 2011 and 2010 was as follows:

| Derivative Instrument   | Location                | Gain (Loss) Recognized in Income on Derivative and Related Hedged Item |                 | Location                | Three months ended January 31, 2011 |
|-------------------------|-------------------------|--|-----------------|-------------------------|-------------------------------------|
|                         |                         | Three months ended January 31, 2011                                    | Hedged Item     |                         |                                     |
|                         |                         | In millions  |                 | In millions             |                                     |
| Interest rate contracts | Interest and other, net | \$ (178)   | Fixed-rate debt | Interest and other, net | \$ 174                              |

| Derivative Instrument   | Location                | Gain (Loss) Recognized in Income on Derivative and Related Hedged Item |                 | Location                | Three months ended January 31, 2010 |
|-------------------------|-------------------------|--|-----------------|-------------------------|-------------------------------------|
|                         |                         | Three months ended January 31, 2010                                    | Hedged Item     |                         |                                     |
|                         |                         | In millions  |                 | In millions             |                                     |
| Interest rate contracts | Interest and other, net | \$ 9   | Fixed-rate debt | Interest and other, net | \$ (9)                              |

The before-tax effect of derivative instruments in cash flow and net investment hedging relationships for the three months ended January 31, 2011 and 2010 was as follows:

|                            | Gain (Loss) Recognized in Other Comprehensive Income ("OCI") on Derivative (Effective Portion) |                          | Gain (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion) |                          | Gain Recognized in Income on Derivative <sup>(1)</sup> (Ineffective portion and Amount Excluded from Effectiveness Testing) |             |
|----------------------------|--|--------------------------|---|--------------------------|---|-------------|
|                            | Three months ended January 31, 2011  | Location                 | Three months ended January 31, 2011   | Location                 | Three months ended January 31, 2011   | Location    |
|                            |  | In millions              |   |                          | In millions   | In millions |
| Cash flow hedges:          |  |                          |   |                          |   |             |
| Foreign exchange contracts | \$ 100   | Net revenue              | \$ (24)   | Net revenue              | \$  |             |
| Foreign exchange contracts | (9)  | Cost of products         | 26  | Cost of products         |   |             |
| Foreign exchange contracts | (2)  | Other operating expenses | 1   | Other operating expenses |   |             |
| Foreign exchange contracts | 16   | Interest and other, net  | 7   | Interest and other, net  |   |             |
| Foreign exchange contracts | (13)   | Net revenue              | 4   | Interest and other, net  |   | 2           |
| Total cash flow hedges     | \$ 92  |                          | \$ 14   |                          | \$  | 2           |
| Net investment hedges:     |  |                          |   |                          |   |             |
| Foreign exchange contracts | \$ (6)   | Interest and other, net  | \$  | Interest and other, net  | \$  |             |

- (1) Amount of gain recognized in income on derivative represents a \$2 million gain related to the amount excluded from the assessment of hedge effectiveness in the three months ended January 31, 2011.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments (Continued)

|                            | Gain Recognized in OCI on Derivative (Effective Portion) |                          | Gain (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion) |                          | Gain Recognized in Income on Derivative <sup>(1)</sup> (Ineffective portion and Amount Excluded from Effectiveness Testing) |          |
|----------------------------|--|--------------------------|---|--------------------------|---|----------|
|                            | Three months ended January 31, 2010                      | Location                 | Three months ended January 31, 2010   | Location                 | Three months ended January 31, 2010   | Location |
|                            | In millions  |                          | In millions   |                          | In millions   |          |
| Cash flow hedges:          |  |                          |   |                          |   |          |
| Foreign exchange contracts | \$ 425   | Net revenue              | \$ (130)  | Net revenue              | \$  |          |
| Foreign exchange contracts | 5  | Cost of products         | 15  | Cost of products         |   |          |
| Foreign exchange contracts |  | Other operating expenses | 1   | Other operating expenses |   |          |
| Foreign exchange contracts | 6  | Interest and other, net  | 4   | Interest and other, net  |   |          |
| Foreign exchange contracts | 11   | Net revenue              | 8   | Interest and other, net  |   | 4        |
| Total cash flow hedges     | \$ 447   |                          | \$ (102)  |                          | \$  | 4        |
| Net investment hedges:     |  |                          |   |                          |   |          |
| Foreign exchange contracts | \$ 3   | Interest and other, net  | \$  | Interest and other, net  | \$  |          |

(1) Amount of gain recognized in income on derivative represents a \$4 million gain related to the amount excluded from the assessment of hedge effectiveness in the three months ended January 31, 2010.

HP expects to reclassify a net accumulated other comprehensive loss of approximately \$168 million, net of taxes, to earnings in the next twelve months along with the earnings effects of the related forecasted transactions in association with cash flow hedges.

The before-tax effect of derivative instruments not designated as hedging instruments on the Consolidated Condensed Statements of Earnings for the three months ended January 31, 2011 and 2010 was as follows:

|                            | Location                | Gain (Loss) Recognized in Income on Derivative<br>Three months ended<br>January 31,<br>2011<br>In millions |
|----------------------------|-------------------------|--|
| Foreign exchange contracts | Interest and other, net | \$ (77)  |
| Other derivatives          | Interest and other, net | (2)  |
| Interest rate contracts    | Interest and other, net | 2  |
| Total                      |                         | \$ (77)  |

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 8: Financial Instruments (Continued)

|                            | Location                | Gain (Loss) Recognized in Income on Derivative |
|----------------------------|-------------------------|--|
|                            |                         | Three months ended January 31, 2010            |
|                            |                         | In millions                                    |
| Foreign exchange contracts | Interest and other, net | \$ 66  |
| Other derivatives          | Interest and other, net | (11)   |
| Interest rate contracts    | Interest and other, net | (1)  |
| Total                      |                         | \$ 54  |

*Other Financial Instruments*

For the balance of HP's financial instruments, accounts receivable, financing receivables, notes payable and short-term borrowings, accounts payable and other accrued liabilities, the carrying amounts approximate fair value due to their short maturities. The estimated fair value and carrying value of HP's short- and long-term debt was approximately \$20.4 billion at January 31, 2011. The estimated fair value of HP's short- and long-term debt was approximately \$16.0 billion at January 31, 2010, compared to a carrying value of \$15.9 billion at that date. The estimated fair value of the debt is based primarily on quoted market prices, as well as borrowing rates currently available to HP for bank loans with similar terms and maturities.

## Note 9: Financing Receivables and Operating Leases

Financing receivables represent sales-type and direct-financing leases resulting from the placement of HP and third-party products. These receivables typically have terms from two to five years and are usually collateralized by a security interest in the underlying assets. Financing receivables also include billed receivables from operating leases. The components of net financing receivables, which are included in financing receivables and long-term financing receivables and other assets, were as follows:

|                                   | January 31, 2011 | October 31, 2010 |
|-----------------------------------|------------------|------------------|
| In millions                       |                  |                  |
| Minimum lease payments receivable | \$ 7,239         | \$ 7,094         |
| Allowance for doubtful accounts   | (124)            | (140)            |
| Unguaranteed residual value       | 213              | 212              |
| Unearned income                   | (615)            | (596)            |
| Financing receivables, net        | 6,713            | 6,570            |
| Less current portion              | (2,982)          | (2,986)          |
| Amounts due after one year, net   | \$ 3,731         | \$ 3,584         |

Equipment leased to customers under operating leases was \$3.6 billion and \$3.5 billion at January 31, 2011 and October 31, 2010, respectively, and is included in machinery and equipment. Accumulated depreciation on equipment under lease was \$1.0 billion at January 31, 2011 and at October 31, 2010.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 9: Financing Receivables and Operating Leases (Continued)**

In July 2010, the Financial Accounting Standards Board issued Accounting Standards Update No. 2010-20, "Disclosures about Credit Quality of Financing Receivables and the Allowance for Credit Losses." This update requires disclosures related to the credit risk inherent in an entity's portfolio of financing receivables and how that risk is analyzed and assessed in arriving at the allowance for credit losses. The new standard also requires enhanced disclosures related to changes in the allowance for credit losses and the reasons for those changes. HP adopted this new standard in the first quarter of fiscal 2011.

Due to the homogenous nature of the leasing transactions, HP manages its financing receivables on an aggregate basis when assessing and monitoring credit risk. Credit risk is generally diversified due to the large number of entities comprising HP's customer base and their dispersion across many different industries and geographical regions. The credit quality of an obligor is evaluated at lease inception and monitored over the term of a transaction. Risk ratings are assigned to each lease based on the creditworthiness of the obligor and other variables that augment or diminish the inherent credit risk of a particular transaction. Such variables include the underlying value and liquidity of the collateral, the essential use of the equipment, the term of the lease, and the inclusion of guarantees, letters of credit, security deposits or other credit enhancements.

The credit risk profile of the gross financing receivables, based on internally assigned ratings, was as follows:

|                    | January 31,<br>2011 | October 31,<br>2010 |
|--------------------|---------------------|---------------------|
|                    | In millions         |                     |
| <u>Risk Rating</u> |                     |                     |
| Low                | \$ 3,931            | \$ 3,793            |
| Moderate           | 2,847               | 2,829               |
| High               | 59                  | 88                  |
| <b>Total</b>       | <b>\$ 6,837</b>     | <b>\$ 6,710</b>     |

Accounts rated low risk typically have the equivalent of a Standard & Poor's rating of BBB- or higher, while accounts rated moderate risk would be the equivalent of BB+ or lower. HP closely monitors accounts rated high risk and based upon impairment analysis, specific reserves may have been established against a portion of these leases.

HP establishes an allowance for doubtful accounts to ensure financing receivables are not overstated due to uncollectability. The allowance balance is comprised of a general reserve, which is determined based on a percentage of the financing receivables balance, and a specific reserve, which is established for certain leases with identified exposures, such as customer default, bankruptcy or other events, that make it unlikely that HP will recover its investment in the lease. The general reserve percentages are maintained on a regional basis and are based on several factors, which include consideration of historical credit losses and portfolio delinquencies, trends in the overall weighted-average risk rating of the portfolio, and information derived from competitive benchmarking.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 9: Financing Receivables and Operating Leases (Continued)**

The allowance for doubtful accounts and the related financing receivables for the three months ended January 31, 2011 were as follows:

|   | Three months ended<br>January 31, 2011 |       |
|---|--|-------|
|   | In millions                            |       |
| <u>Allowance for doubtful accounts</u>                              |  |       |
| Balance, beginning of period  | \$                                     | 140   |
| Additions to allowance  |  | 12    |
| Deductions, net of recoveries                                       |  | (28)  |
| Balance, end of period  | \$                                     | 124   |
|   |  |       |
| Allowance for financing receivables individually evaluated for loss | \$                                     | 41    |
| Allowance for financing receivables collectively evaluated for loss |  | 83    |
| Total   | \$                                     | 124   |
|   |  |       |
| Gross financing receivables individually evaluated for loss         | \$                                     | 84    |
| Gross financing receivables collectively evaluated for loss         |  | 6,753 |
| Total   | \$                                     | 6,837 |

Accounts are generally put on non-accrual status (cessation of interest accrual) when they reach 90 days past due. Exceptions may be granted in certain circumstances such as when the delinquency is deemed to be of an administrative nature. A write-off or specific reserve is generally recorded when an account reaches 180 days past due. As of January 31, 2011, total financing receivables on non-accrual status were \$234 million, and total financing receivables greater than 90 days past due and still accruing interest were \$106 million.

**Note 10: Guarantees***Guarantees and Indemnifications*

In the ordinary course of business, HP may provide certain clients with subsidiary performance guarantees and/or financial performance guarantees, which may be backed by standby letters of credit or surety bonds. In general, HP would be liable for the amounts of these guarantees in the event HP or HP's subsidiaries' nonperformance permits termination of the related contract by the client, the likelihood of which HP believes is remote. HP believes that the company is in compliance with the performance obligations under all material service contracts for which there is a performance guarantee.

HP has certain service contracts supported by client financing or securitization arrangements. Under specific circumstances involving nonperformance resulting in service contract termination or failure to comply with terms under the financing arrangement, HP would be required

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to acquire certain assets. HP considers the possibility of its failure to comply to be remote and the asset amounts involved to be immaterial.

In the ordinary course of business, HP enters into contractual arrangements under which HP may agree to indemnify the third party to such arrangement from any losses incurred relating to the services

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 10: Guarantees (Continued)**

they perform on behalf of HP or for losses arising from certain events as defined within the particular contract, which may include, for example, litigation or claims relating to past performance. Such indemnification obligations may not be subject to maximum loss clauses. Historically, payments made related to these indemnifications have been immaterial.

*Warranty*

HP provides for the estimated cost of product warranties at the time it recognizes revenue. HP engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its component suppliers; however, product warranty terms offered to customers, ongoing product failure rates, material usage and service delivery costs incurred in correcting a product failure, as well as specific product class failures outside of HP's baseline experience, affect the estimated warranty obligation. If actual product failure rates, repair rates or any other post sales support costs differ from these estimates, revisions to the estimated warranty liability would be required.

The changes in HP's aggregate product warranty liabilities for the three months ended January 31, 2011 were as follows:

|   | <b>In millions</b> |
|---|--------------------|
| Product warranty liability at October 31, 2010                                  | \$ 2,447           |
| Accruals for warranties issued  | 700                |
| Adjustments related to pre-existing warranties (including changes in estimates) | (31)               |
| Settlements made (in cash or in kind)   | (659)              |
| Product warranty liability at January 31, 2011                                  | \$ 2,457           |

**Note 11: Borrowings***Notes Payable and Short-Term Borrowings*

Notes payable and short-term borrowings, including the current portion of long-term debt, were as follows:

|   | <b>January 31, 2011</b> |  | <b>October 31, 2010</b> |  |
|---|-------------------------|--|-------------------------|--|
|   | <b>Amount</b>           | <b>Weighted-<br/>Average<br/>Interest<br/>Rate</b> | <b>Amount</b>           | <b>Weighted-<br/>Average<br/>Interest<br/>Rate</b> |
|   | <b>Outstanding</b>      |  | <b>Outstanding</b>      |  |
|   | <b>In millions</b>      |  |                         |  |
| Current portion of long-term debt                 | \$ 2,240                | 2.2%   | \$ 2,216                | 2.2%   |
| Commercial paper                                  | 680                     | 0.6%   | 4,432                   | 0.3%   |
| Notes payable to banks, lines of credit and other | 461                     | 2.6%   | 398                     | 1.5%   |
|   | \$ 3,381                |  | \$ 7,046                |  |

Notes payable to banks, lines of credit and other includes deposits associated with HP's banking-related activities of approximately \$361 million and \$348 million at January 31, 2011 and October 31, 2010, respectively.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 11: Borrowings (Continued)

## Long-Term Debt

Long-term debt was as follows:

|  | January 31,<br>2011 | October 31,<br>2010 |
|--|---------------------|---------------------|
|  | In millions         |                     |
| U.S. Dollar Global Notes   |                     |                     |
| 2002 Shelf Registration Statement:   |                     |                     |
| \$500 issued at discount to par at a price of 99.505% in June 2002 at 6.5%, due July 2012            | \$ 500              | \$ 500              |
| 2006 Shelf Registration Statement:   |                     |                     |
| \$600 issued at par in February 2007 at three-month USD LIBOR plus 0.11%, due March 2012             | 600                 | 600                 |
| \$900 issued at discount to par at a price of 99.938% in February 2007 at 5.25%, due March 2012      | 900                 | 900                 |
| \$500 issued at discount to par at a price of 99.694% in February 2007 at 5.4%, due March 2017       | 499                 | 499                 |
| \$1,500 issued at discount to par at a price of 99.921% in March 2008 at 4.5%, due March 2013        | 1,499               | 1,499               |
| \$750 issued at discount to par at a price of 99.932% in March 2008 at 5.5%, due March 2018          | 750                 | 750                 |
| \$2,000 issued at discount to par at a price of 99.561% in December 2008 at 6.125%, due March 2014   | 1,995               | 1,994               |
| \$275 issued at par in February 2009 at three-month USD LIBOR plus 1.75%, paid February 2011         | 275                 | 275                 |
| \$1,000 issued at discount to par at a price of 99.956% in February 2009 at 4.25%, due February 2012 | 1,000               | 1,000               |
| \$1,500 issued at discount to par at a price of 99.993% in February 2009 at 4.75%, due June 2014     | 1,500               | 1,500               |
| 2009 Shelf Registration Statement:   |                     |                     |
| \$750 issued at par in May 2009 at three-month USD LIBOR plus 1.05%, due May 2011                    | 750                 | 750                 |
| \$1,000 issued at discount to par at a price of 99.967% in May 2009 at 2.25%, due May 2011           | 1,000               | 1,000               |
| \$250 issued at discount to par at a price of 99.984% in May 2009 at 2.95%, due August 2012          | 250                 | 250                 |
| \$800 issued at par in September 2010 at three-month USD LIBOR plus 0.125%, due September 2012       | 800                 | 800                 |
| \$1,100 issued at discount to par of 99.921% in September 2010 at 1.25% due September 2013           | 1,099               | 1,099               |
| \$1,100 issued at discount to par of 99.887% in September 2010 at 2.125% due September 2015          | 1,099               | 1,099               |
| \$650 issued at discount to par of 99.911% in December 2010 at 2.2% due December 2015                | 649                 |                     |
| \$1,350 issued at discount to par of 99.827% in December 2010 at 3.75% due December 2020             | 1,347               |                     |
|  | 16,512              | 14,515              |
| EDS Senior Notes   |                     |                     |
| \$1,100 issued June 2003 at 6.0%, due August 2013  | 1,128               | 1,130               |
| \$300 issued October 1999 at 7.45%, due October 2029   | 315                 | 315                 |
|  | 1,443               | 1,445               |
| Other, including capital lease obligations, at 0.60%-8.63%, due in calendar years 2011-2024          | 810                 | 845                 |
| Fair value adjustment related to hedged debt   | 497                 | 669                 |
| Less: current portion  | (2,240)             | (2,216)             |
| Total long-term debt   | \$ 17,022           | \$ 15,258           |

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 11: Borrowings (Continued)**

As disclosed in Note 8 to the Consolidated Financial Statements, HP uses interest rate swaps to mitigate the market risk exposures in connection with certain fixed interest global notes to achieve primarily U.S. dollar LIBOR-based floating interest expense. The table above does not reflect the interest rate swap impact on the interest rate.

HP may redeem some or all of the Global Notes set forth in the above table at any time at the redemption prices described in the prospectus supplements relating thereto. The Global Notes are senior unsecured debt.

In May 2009, HP filed a shelf registration statement (the "2009 Shelf Registration Statement") with the SEC to enable the company to offer for sale, from time to time, in one or more offerings, an unspecified amount of debt securities, common stock, preferred stock, depository shares and warrants. The 2009 Shelf Registration Statement replaced other registration statements filed in March 2002 and May 2006.

In May 2008, HP's Board of Directors approved an increase in the capacity of HP's U.S. commercial paper program by \$10.0 billion to \$16.0 billion. HP's subsidiaries are authorized to issue up to an additional \$1.0 billion of commercial paper, of which \$500 million of capacity is currently available to be used by Hewlett-Packard International Bank PLC, a wholly-owned subsidiary of HP, for its Euro Commercial Paper/Certificate of Deposit Programme.

HP has a \$3.0 billion five-year credit facility expiring in May 2012. In February 2010, HP entered into a \$3.5 billion 364-day credit facility. The February credit facility expired in February 2011, at which time HP entered into a new \$4.5 billion four-year credit facility, increasing the total amount available under its credit facilities to \$7.5 billion. Commitment fees, interest rates and other terms of borrowing under the credit facilities vary based on HP's external credit ratings. The credit facilities are senior unsecured committed borrowing arrangements primarily to support the issuance of U.S. commercial paper. HP's ability to have a U.S. commercial paper outstanding balance that exceeds the \$7.5 billion supported by these credit facilities is subject to a number of factors, including liquidity conditions and business performance.

Within Other, including capital lease obligations, are borrowings that are collateralized by certain financing receivable assets. As of January 31, 2011, the carrying value of the assets approximated the carrying value of the borrowings of \$170 million.

As of January 31, 2011, HP had the capacity to issue an unspecified amount of additional debt securities, common stock, preferred stock, depository shares and warrants under the 2009 Shelf Registration Statement. As of that date, HP also had up to approximately \$17.2 billion of available borrowing resources, including \$15.8 billion under its commercial paper programs and approximately \$1.4 billion relating to uncommitted lines of credit.

**Note 12: Income Taxes**

*Provision for Taxes*

HP's effective tax rate was 21.0% and 19.8% for the three months ended January 31, 2011 and January 31, 2010, respectively. HP's effective tax rate increased due to a decline in the percentage of total earnings earned in lower-tax jurisdictions. HP's effective tax rate generally differs from the U.S. federal statutory rate of 35% due to favorable tax rates associated with certain earnings from HP's

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 12: Income Taxes (Continued)**

operations in lower-tax jurisdictions throughout the world. HP has not provided U.S. taxes for all of such earnings because HP plans to reinvest some of those earnings indefinitely outside the United States.

In the three months ended January 31, 2011, HP recorded discrete items with a net tax benefit of \$101 million, decreasing the effective tax rate. These amounts included net tax benefits of \$58 million from restructuring and acquisition charges. In addition, in December 2010, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 was signed into law. HP recorded a tax benefit of \$43 million arising from the retroactive research and development credit provided by that legislation in the first quarter of fiscal 2011.

In the three months ended January 31, 2010, HP recorded discrete items with a net tax benefit of \$92 million, decreasing the effective tax rate. These amounts included net tax benefits of \$54 million from restructuring and acquisition charges, a tax benefit of \$19 million from settlement of a tax audit matter, a net tax benefit of \$19 million from adjustments to prior year foreign income tax accruals and credits, and other miscellaneous discrete items.

As of January 31, 2011, the amount of gross unrecognized tax benefits was \$1.7 billion, a decline of approximately \$400 million since October 31, 2010. The decline was primarily attributable to the settlement or resolution of various uncertain tax positions within a non-U.S. jurisdiction. The benefit from the reversal of related income tax reserves was accompanied by a corresponding increase in U.S. deferred tax expense recognized for the related unremitted earnings. Of the balance of \$1.7 billion at January 31, 2011, up to \$1.1 billion would affect HP's effective tax rate if realized. HP recognizes interest income and interest expense and penalties on tax overpayments and underpayments, respectively, within income tax expense. As of January 31, 2011, HP had accrued a net \$160 million payable for interest and penalties. In the three months ended January 31, 2011, HP recognized \$21 million of net interest income on tax overpayments, net of tax.

HP engages in continuous discussion and negotiation with taxing authorities regarding tax matters in various jurisdictions. HP does not expect complete resolution of any IRS audit cycle within the next 12 months. However, it is reasonably possible that certain federal, foreign and state tax issues may be concluded in the next 12 months, including issues involving transfer pricing and other matters. Accordingly, HP believes it is reasonably possible that its existing unrecognized tax benefits may be reduced by an amount up to \$138 million within the next 12 months.

HP is subject to income tax in the United States and approximately 80 foreign countries and is subject to routine corporate income tax audits in many of these jurisdictions. In addition, HP is subject to numerous ongoing audits by state and foreign tax authorities. HP has received from the IRS Notices of Deficiency for its fiscal 1999, 2000, 2003, 2004 and 2005 tax years, and Revenue Agent's Reports ("RAR") for its fiscal 2001, 2002 and 2006 tax years. The IRS began an audit of HP's 2007 income tax returns in 2009, and began its audit of HP's 2008 income tax returns during 2010. With respect to major foreign and state tax jurisdictions, HP is no longer subject to tax authority examinations for years prior to 1999. HP believes that adequate accruals have been provided for all open tax years.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 12: Income Taxes (Continued)**

The breakdown between current and long-term deferred tax assets and deferred tax liabilities was as follows:

|   | January 31,<br>2011 | October 31,<br>2010 |
|---|---------------------|---------------------|
|   | In millions         |                     |
| Current deferred tax assets                               | \$ 5,365            | \$ 5,833            |
| Current deferred tax liabilities                          | (37)                | (53)                |
| Long-term deferred tax assets                             | 2,190               | 2,070               |
| Long-term deferred tax liabilities                        | (5,572)             | (5,239)             |
| Total deferred tax assets net of deferred tax liabilities | \$ 1,946            | \$ 2,611            |

**Note 13: Stockholders' Equity***Share Repurchase Program*

HP's share repurchase program authorizes both open market and private repurchase transactions. In the first quarter of fiscal 2011, HP executed share repurchases of 51 million shares. Repurchases of 54 million shares were settled for \$2.3 billion in the first quarter of fiscal 2011, which included 4 million shares repurchased in transactions that were executed in fiscal 2010 but settled in the first quarter of fiscal 2011. HP had approximately 1 million shares repurchased in the first quarter of fiscal 2011 that will be settled in the second quarter of fiscal 2011. HP paid approximately \$2.7 billion in connection with repurchases of approximately 54 million shares during the three months ended January 31, 2010. As of January 31, 2011, HP had remaining authorization of \$8.6 billion for future share repurchases.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 13: Stockholders' Equity (Continued)

*Comprehensive Income*

The changes in the components of OCI, net of taxes, were as follows:

|  | Three months ended<br>January 31 |          |
|--|----------------------------------|----------|
|  | 2011                             | 2010     |
|  | In millions                      |          |
| Net earnings   | \$ 2,605                         | \$ 2,250 |
| Net change in unrealized gains on available-for-sale securities, net of tax of \$5 million in 2011 and \$1 million in 2010         | 10                               | 2        |
| Net change in unrealized gains/losses on cash flow hedges:   |                                  |          |
| Unrealized gains recognized in OCI, net of tax of \$32 million in 2011 and \$157 million in 2010                                   | 60                               | 290      |
| (Gains) losses reclassified into income, net of tax of \$1 million in 2011 and net of tax benefit of \$42 million in 2010          | (13)                             | 60       |
|  | 47                               | 350      |
| Net change in cumulative translation adjustment, net of tax of \$17 million in 2011 and net of tax benefit of \$14 million in 2010 | 51                               | (60)     |
| Net change in unrealized components of defined benefit plans, net of tax of \$10 million in 2011 and \$9 million in 2010           | 31                               | 11       |
| Comprehensive income   | \$ 2,744                         | \$ 2,553 |

The components of accumulated other comprehensive loss, net of taxes, were as follows:

|  | January 31,<br>2011 | October 31,<br>2010 |
|--|---------------------|---------------------|
|  | In millions         |                     |
| Net unrealized gain on available-for-sale securities | \$ 30               | \$ 20               |
| Net unrealized loss on cash flow hedges              | (154)               | (201)               |
| Cumulative translation adjustment                    | (380)               | (431)               |
| Unrealized components of defined benefit plans       | (3,194)             | (3,225)             |
| Accumulated other comprehensive loss                 | \$ (3,698)          | \$ (3,837)          |

## Note 14: Retirement and Post-Retirement Benefit Plans

*Modifications to Defined Contribution Plans*

HP offers various defined contribution plans for U.S. and non-U.S. employees. As disclosed in our Consolidated Financial Statements for the fiscal year ended October 31, 2010, HP matching contributions under both the HP 401(k) Plan and the EDS 401(k) Plan in fiscal 2010 were on a quarterly, discretionary, performance-based match of up to a maximum of 4% of eligible compensation for all U.S. employees to be determined each fiscal quarter based on business results. HP's matching contributions for each of the quarters in fiscal 2010 were 100% of the maximum 4% match. Effective in fiscal year 2011, the quarterly employer matching contributions in the HP 401(k) Plan and the EDS 401(k) Plan are no longer discretionary and are equal to 100% of an employee's contributions, up to a



## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 14: Retirement and Post-Retirement Benefit Plans (Continued)**

maximum of 4% of eligible compensation. In addition, effective December 31, 2010, the EDS 401(k) Plan was merged into the HP 401(k) Plan.

HP's net pension and post-retirement benefit costs were as follows:

|                                  | Three months ended January 31    |         |                                      |        |                                      |        |
|----------------------------------|----------------------------------|---------|--------------------------------------|--------|--------------------------------------|--------|
|                                  | U.S.<br>Defined<br>Benefit Plans |         | Non-U.S.<br>Defined<br>Benefit Plans |        | Post-<br>Retirement<br>Benefit Plans |        |
|                                  | 2011                             | 2010    | 2011                                 | 2010   | 2011                                 | 2010   |
|                                  | In millions                      |         |                                      |        |                                      |        |
| Service cost                     | \$                               | \$      | \$                                   | \$     | \$                                   | \$     |
| Interest cost                    | 148                              | 145     | 169                                  | 172    | 8                                    | 12     |
| Expected return on plan assets   | (186)                            | (166)   | (213)                                | (198)  | (9)                                  | (7)    |
| Amortization and deferrals:      |                                  |         |                                      |        |                                      |        |
| Actuarial loss                   | 9                                | 7       | 62                                   | 56     | 1                                    | 5      |
| Prior service benefit            |                                  |         | (3)                                  | (2)    | (21)                                 | (21)   |
| Net periodic benefit (gain) cost | \$ (29)                          | \$ (14) | \$ 100                               | \$ 114 | \$ (19)                              | \$ (8) |
| Special termination benefits     |                                  |         | 2                                    |        |                                      |        |
| Net benefit (gain) cost          | \$ (29)                          | \$ (14) | \$ 102                               | \$ 114 | \$ (19)                              | \$ (8) |

*Employer Contributions and Funding Policy*

HP previously disclosed in its Consolidated Financial Statements for the fiscal year ended October 31, 2010 that it expected to contribute approximately \$747 million to its pension plans and approximately \$30 million to cover benefit payments to U.S. non-qualified plan participants. HP expects to pay approximately \$40 million to cover benefit claims for HP's post-retirement benefit plans. HP's funding policy is to contribute cash to its pension plans so that it makes at least the minimum contribution required by local authorities.

During the three months ended January 31, 2011, HP made \$183 million of contributions to its pension plans, paid \$7 million to cover benefit payments to U.S. non-qualified plan participants, and paid \$6 million to cover benefit claims under post-retirement benefit plans. During the remainder of fiscal 2011, HP anticipates making additional contributions of approximately \$564 million to its pension plans and approximately \$23 million to its U.S. non-qualified plan participants and expects to pay up to \$34 million to cover benefit claims under post-retirement benefit plans. HP's pension and other post-retirement benefit costs and obligations are dependent on various assumptions. Differences between expected and actual returns on investments will be reflected as unrecognized gains or losses, and such gains or losses will be amortized and recorded in future periods. Poor financial performance of invested assets in any year could lead to increased contributions in certain countries and increased future pension plan expense. Asset gains or losses are determined at the measurement date and amortized over the remaining service life or life expectancy of plan participants. HP's next measurement date is October 31, 2011.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 15: Litigation and Contingencies**

HP is involved in lawsuits, claims, investigations and proceedings, including those identified below, consisting of intellectual property, commercial, securities, employment, employee benefits and environmental matters that arise in the ordinary course of business. HP records a provision for a liability when management believes that it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. HP believes it has adequate provisions for any such matters. HP reviews these provisions at least quarterly and adjusts these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Based on its experience, HP believes that any damage amounts claimed in the specific matters discussed below are not a meaningful indicator of HP's potential liability. Litigation is inherently unpredictable. However, HP believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies or because of the diversion of management's attention and the creation of significant expenses.

*Litigation, Proceedings and Investigations*

Copyright levies. As described below, proceedings are ongoing or have been concluded involving HP in certain European Union ("EU") member countries, including litigation in Germany, Belgium and Austria, seeking to impose or modify levies upon equipment (such as multifunction devices ("MFDs"), personal computers ("PCs") and printers) and alleging that these devices enable producing private copies of copyrighted materials. Descriptions of some of the ongoing proceedings are included below. The levies are generally based upon the number of products sold and the per-product amounts of the levies, which vary. Some EU member countries that do not yet have levies on digital devices are expected to implement similar legislation to enable them to extend existing levy schemes, while some other EU member countries are expected to limit the scope of levy schemes and applicability in the digital hardware environment. HP, other companies and various industry associations have opposed the extension of levies to the digital environment and have advocated alternative models of compensation to rights holders.

VerwertungsGesellschaft Wort ("VG Wort"), a collection agency representing certain copyright holders, instituted legal proceedings against HP in the Stuttgart Civil Court seeking levies on printers. On December 22, 2004, the court held that HP is liable for payments regarding all printers using ASCII code sold in Germany but did not determine the amount payable per unit. HP appealed this decision in January 2005 to the Stuttgart Court of Appeals. On May 11, 2005, the Stuttgart Court of Appeals issued a decision confirming that levies are due. On June 6, 2005, HP filed an appeal to the German Federal Supreme Court in Karlsruhe. On December 6, 2007, the German Federal Supreme Court issued a judgment that printers are not subject to levies under the existing law. The court issued a written decision on January 25, 2008, and VG Wort subsequently filed an application with the German Federal Supreme Court under Section 321a of the German Code of Civil Procedure contending that the court did not consider their arguments. On May 9, 2008, the German Federal Supreme Court denied VG Wort's application. VG Wort appealed the decision by filing a claim with the German Federal Constitutional Court challenging the ruling that printers are not subject to levies. On September 21, 2010, the Constitutional Court published a decision holding that the German Federal Supreme Court erred by not referring questions on interpretation of German copyright law to

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 15: Litigation and Contingencies (Continued)**

the Court of Justice of the EU and therefore revoked the German Federal Supreme Court decision and remitted the matter to it. The German Federal Supreme Court has set a hearing date of March 24, 2011.

In September 2003, VG Wort filed a lawsuit against Fujitsu Siemens Computer GmbH ("FSC") in the Munich Civil Court in Munich, Germany seeking levies on PCs. This is an industry test case in Germany, and HP has agreed not to object to the delay if VG Wort sues HP for such levies on PCs following a final decision against FSC. On December 23, 2004, the Munich Civil Court held that PCs are subject to a levy and that FSC must pay €12 plus compound interest for each PC sold in Germany since March 2001. FSC appealed this decision in January 2005 to the Munich Court of Appeals. On December 15, 2005, the Munich Court of Appeals affirmed the Munich Civil Court decision. FSC filed an appeal with the German Federal Supreme Court in February 2006. On October 2, 2008, the German Federal Supreme Court issued a judgment that PCs were not photocopiers within the meaning of the German copyright law that was in effect until December 31, 2007 and, therefore, not subject to the levies on photocopiers established by that law. VG Wort subsequently filed a claim with the German Federal Constitutional Court challenging that ruling. In January 2011, the Constitutional Court published a decision holding that the German Federal Supreme Court decision was inconsistent with the German Constitution and revoking the German Federal Supreme Court decision. The Constitutional Court remitted the matter to the German Federal Supreme Court for further action.

Reprobel, a cooperative society with the authority to collect and distribute the remuneration for reprography to Belgian copyright holders, requested HP by extra-judicial means to amend certain copyright levy declarations submitted for inkjet MFDs sold in Belgium from January 2005 to December 2009 to enable it to collect copyright levies calculated based on the generally higher copying speed when the MFDs are operated in draft print mode rather than when operated in normal print mode. In March 2010, HP filed a lawsuit against Reprobel in the French-speaking chambers of the Court of First Instance of Brussels seeking a declaratory judgment that no copyright levies are payable on sales of MFDs in Belgium or, alternatively, that copyright levies payable on such MFDs must be assessed based on the copying speed when operated in the normal print mode set by default in the device. The schedule for the court proceedings has been determined, and no decision from the court is expected before September 2012.

Based on industry opposition to the extension of levies to digital products, HP's assessments of the merits of various proceedings and HP's estimates of the units impacted and levies, HP has accrued amounts that it believes are adequate to address the matters described above. However, the ultimate resolution of these matters and the associated financial impact on HP, including the number of units impacted, the amount of levies imposed and the ability of HP to recover such amounts through increased prices, remains uncertain.

Skold, et al. v. Intel Corporation and Hewlett-Packard Company is a lawsuit in which HP was joined on June 14, 2004 that is pending in state court in Santa Clara County, California. The lawsuit alleges that HP (along with Intel Corporation) misled the public by suppressing and concealing the alleged material fact that systems that use the Intel Pentium 4 processor are less powerful and slower than systems using the Intel Pentium III processor and processors made by a competitor of Intel. The plaintiffs seek unspecified damages, restitution, attorneys' fees and costs, and certification of a

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 15: Litigation and Contingencies (Continued)**

nationwide class. On February 27, 2009, the court denied with prejudice plaintiffs' motion for nationwide class certification for a third time. The plaintiffs have appealed the court's decision.

*Inkjet Printer Litigation.* As described below, HP is involved in several lawsuits claiming breach of express and implied warranty, unjust enrichment, deceptive advertising and unfair business practices where the plaintiffs have alleged, among other things, that HP employed a "smart chip" in certain inkjet printing products in order to register ink depletion prematurely and to render the cartridge unusable through a built-in expiration date that is hidden, not documented in marketing materials to consumers, or both. The plaintiffs have also contended that consumers received false ink depletion warnings and that the smart chip limits the ability of consumers to use the cartridge to its full capacity or to choose competitive products.

A consolidated lawsuit captioned *In re HP Inkjet Printer Litigation* is pending in the United States District Court for the Northern District of California where the plaintiffs are seeking class certification, restitution, damages (including enhanced damages), injunctive relief, interest, costs, and attorneys' fees. On January 4, 2008, the court heard plaintiffs' motions for class certification and to add a class representative and HP's motion for summary judgment. On July 25, 2008, the court denied all three motions. On March 30, 2009, the plaintiffs filed a renewed motion for class certification. A hearing on the plaintiffs' motion for class certification scheduled for April 9, 2010 was postponed.

A lawsuit captioned *Blennis v. HP* was filed on January 17, 2007 in the United States District Court for the Northern District of California where the plaintiffs are seeking class certification, restitution, damages (including enhanced damages), injunctive relief, interest, costs, and attorneys' fees. A class certification hearing was scheduled for May 21, 2010 but was taken off the calendar.

A lawsuit captioned *Rich v. HP* was filed against HP on May 22, 2006 in the United States District Court for the Northern District of California. The suit alleges that HP designed its color inkjet printers to unnecessarily use color ink in addition to black ink when printing black and white images and text. The plaintiffs are seeking to certify a nationwide injunctive class and a California-only damages class. A class certification hearing was scheduled for May 7, 2010 but was taken off the calendar.

Four class actions against HP and its subsidiary, Hewlett-Packard (Canada) Co., are pending in Canada, one commenced in British Columbia in February 2006, two commenced in Quebec in April 2006 and May 2006, respectively, and one commenced in Ontario in June 2006, where the plaintiffs are seeking class certification, restitution, declaratory relief, injunctive relief and unspecified statutory, compensatory and punitive damages. In March 2010, one of the Quebec cases was voluntarily dismissed by the plaintiff. In February 2011, the other Quebec case was voluntarily dismissed by the plaintiff.

On August 25, 2010, HP and the plaintiffs in *In re HP Inkjet Printer Litigation*, *Blennis v. HP* and *Rich v. HP* entered into an agreement to settle those lawsuits on behalf of the proposed classes, which agreement is subject to approval of the court before it becomes final. Under the terms of the proposed settlement, the lawsuits will be consolidated, and eligible class members will each have the right to obtain e-credits not to exceed \$5 million in the aggregate for use in purchasing printers or printer

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 15: Litigation and Contingencies (Continued)**

supplies through HP's website. As part of the proposed settlement, HP also agreed to provide class members with additional information regarding HP inkjet printer functionality and to change the content of certain software and user guide messaging provided to users regarding the life of inkjet printer cartridges. In addition, class counsel and the class representatives will be paid attorneys' fees and expenses and stipends in an amount that is yet to be approved by the court. On October 1, 2010, the court granted preliminary approval of the proposed settlement. The court held a fairness hearing on January 28, 2011 to determine whether to grant final approval of the proposed settlement. The court has not yet issued a decision.

Baggett v. HP is a consumer class action filed against HP on June 6, 2007 in the United States District Court for the Central District of California alleging that HP employs a technology in its LaserJet color printers whereby the printing process shuts down prematurely, thus preventing customers from using the toner that is allegedly left in the cartridge. The plaintiffs also allege that HP fails to disclose to consumers that they will be unable to utilize the toner remaining in the cartridge after the printer shuts down. The complaint seeks certification of a nationwide class of purchasers of all HP LaserJet color printers and seeks unspecified damages, restitution, disgorgement, injunctive relief, attorneys' fees and costs. On September 29, 2009, the court granted HP's motion for summary judgment against the named plaintiff and denied plaintiff's motion for class certification as moot. On November 3, 2009, the court entered judgment against the named plaintiff. On November 17, 2009, plaintiff filed an appeal of the court's summary judgment ruling with the United States Court of Appeals for the Ninth Circuit. On August 25, 2010, HP and the plaintiff entered into an agreement to settle the lawsuit on behalf of the proposed class, which agreement is subject to approval of the court before it becomes final. Under the terms of the proposed settlement, eligible class members will each have the right to obtain e-credits not to exceed \$5 million in the aggregate for use in purchasing printers or printer supplies through HP's website. In addition, class counsel and the class representative will be paid attorneys' fees and expenses and stipends in an amount that is yet to be approved by the court. On October 13, 2010, the court granted preliminary approval of the proposed settlement. The court held a fairness hearing on February 14, 2011 to determine whether to grant final approval of the proposed settlement. The court has not yet issued a decision.

Fair Labor Standards Act Litigation. HP is involved in several lawsuits in which the plaintiffs are seeking unpaid overtime compensation and other damages based on allegations that various employees of EDS or HP have been misclassified as exempt employees under the Fair Labor Standards Act and/or in violation of the California Labor Code or other state laws. Those matters include the following:

Cunningham and Cunningham, et al. v. Electronic Data Systems Corporation is a purported collective action filed on May 10, 2006 in the U.S. District Court for the Southern District of New York claiming that current and former EDS employees involved in installing and/or maintaining computer software and hardware were misclassified as exempt employees. Another purported collective action, Steavens, et al. v. Electronic Data Systems Corporation, which was filed on October 23, 2007, is also now pending in the same court alleging similar facts. The Steavens case has been consolidated for pretrial purposes with the Cunningham case. On December 14, 2010, the court granted conditional certification of the class in the consolidated Cunningham and Steavens matter.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 15: Litigation and Contingencies (Continued)**

Heffelfinger, et al. v. Electronic Data Systems Corporation is a class action filed in November 2006 in California Superior Court claiming that certain EDS information technology workers in California were misclassified as exempt employees. The case was subsequently transferred to the U.S. District Court for the Central District of California, which, on January 7, 2008, certified a class of information technology workers in California. On June 6, 2008, the court granted the defendant's motion for summary judgment. The plaintiffs subsequently filed an appeal with the U.S. Court of Appeals for the Ninth Circuit, which is pending. Two other purported class actions originally filed in California Superior Court, Karl bom, et al. v. Electronic Data Systems Corporation, which was filed on March 16, 2009, and George, et al. v. Electronic Data Systems Corporation, which was filed on April 2, 2009, allege similar facts. The Karl bom case is pending in San Diego County Superior Court but has been temporarily stayed based on the pending motions in the Steavens consolidated matter. The George case is pending in the U.S. District Court for the Southern District of New York and has been consolidated for pretrial purposes with the Cunningham and Steavens cases.

India Directorate of Revenue Intelligence Proceedings. As described below, Hewlett-Packard India Sales Private Ltd ("HPI"), a subsidiary of HP, and certain current and former HP employees have received show cause notices from the India Directorate of Revenue Intelligence (the "DRI") alleging underpayment of certain customs duties:

On April 30 and May 10, 2010, the DRI issued show cause notices to HPI, seven current HP employees and one former HP employee alleging that HP has underpaid customs duties while importing products and spare parts into India and seeking to recover an aggregate of approximately \$370 million, plus penalties. On June 2, 2010, the DRI issued an additional show cause notice to HPI and three current HPI employees alleging that HP failed to pay customs duties on the appropriate value of recovery CDs containing Microsoft operating systems and seeking to recover approximately \$5.3 million, plus penalties. HP has deposited a total of approximately \$16.7 million with the DRI and agreed to post a provisional bond in exchange for the DRI's agreement not to seize HP products and spare parts and not to interrupt the transaction of business by HP in India.

On June 17, 2010, the DRI issued show cause notices to HPI and two current HPI employees regarding non-inclusion of the value of software contained in the products imported from third party original design manufacturers. The total amount of the alleged unpaid customs duties relating to such software, including the interest proposed to be demanded under these notices, is approximately \$130,000, which amount HPI has deposited with the DRI. The DRI is also seeking to impose penalties.

On October 1, 2010, in connection with an existing DRI investigation commenced against SAP AG, the DRI issued a show cause notice to HPI alleging underpayment of customs duties related to the importation of certain SAP software. The amount of the alleged duty differential is approximately \$38,000, which amount has been deposited with the DRI. The DRI is also seeking to impose interest and penalties.

HP intends to contest each of the show cause notices through the judicial process. HP has responded or is in the process of responding to the show cause notices.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 15: Litigation and Contingencies (Continued)**

Russia GPO and Related Investigations. The German Public Prosecutor's Office ("German PPO") has been conducting an investigation into allegations that current and former employees of HP engaged in bribery, embezzlement and tax evasion relating to a transaction between Hewlett-Packard ISE GmbH in Germany, a former subsidiary of HP, and the Chief Public Prosecutor's Office of the Russian Federation. The €35 million transaction, which was referred to as the Russia GPO deal, spanned the years 2001 to 2006 and was for the delivery and installation of an IT network.

The U.S. Department of Justice and the SEC have also been conducting an investigation into the Russia GPO deal and potential violations of the Foreign Corrupt Practices Act ("FCPA"). Under the FCPA, a person or an entity could be subject to fines, civil penalties of up to \$500,000 per violation and equitable remedies, including disgorgement and other injunctive relief. In addition, criminal penalties could range from the greater of \$2 million per violation or twice the gross pecuniary gain or loss from the violation.

In addition to information about the Russia GPO deal, the U.S. enforcement authorities have requested (i) information related to certain other transactions, including transactions in Russia, Serbia and in the Commonwealth of Independent States (CIS) subregion dating back to 2000, and (ii) information related to two former HP executives seconded to Russia and to whether HP personnel in Russia, Germany, Austria, Serbia, the Netherlands or CIS were involved in kickbacks or other improper payments to channel partners, or state owned or private entities.

HP is cooperating with these investigating agencies.

In addition, as described below, HP is involved in stockholder derivative litigation arising from the Russia GPO deal, the related investigations and other matters commenced against current and former members of the HP Board of Directors in which the plaintiffs are seeking to recover certain compensation paid by HP to the defendants and other damages:

Henrietta Klein v. Mark V. Hurd, et al., is a lawsuit filed on September 24, 2010 in California Superior Court alleging the individual defendants wasted corporate assets and breached their fiduciary duties by failing to implement and oversee HP's compliance with the FCPA.

Saginaw Police & Fire Pension Fund v. Marc L. Andreessen, et al., is a lawsuit filed on October 19, 2010 in United States District Court for the Northern District of California alleging, among other things, that the defendants breached their fiduciary duties and were unjustly enriched by consciously disregarding HP's alleged violations of the FCPA.

A.J. Copeland v. Raymond J. Lane, et al., is a lawsuit filed on March 7, 2011 in the United States District Court for the Northern District of California alleging, among other things, that the defendants breached their fiduciary duties in connection with HP's alleged violations of the FCPA, severance payments made to former Chairman and Chief Executive Officer Mark Hurd, and HP's acquisition of 3PAR Inc. The lawsuit also alleges violations of Section 14(a) of the Exchange Act in connection with HP's 2010 and 2011 proxy statements.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 15: Litigation and Contingencies (Continued)**

Leak Investigation Proceedings. As described below, HP is or has been the subject of various governmental inquiries concerning the processes employed in an investigation into leaks of HP confidential information to members of the media that concluded in May 2006:

In August 2006, HP was informally contacted by the Attorney General of the State of California requesting information concerning the processes employed in the leak investigation. On December 7, 2006, HP announced that it entered into an agreement with the California Attorney General to resolve civil claims arising from the leak investigation, including a claim made by the California Attorney General in a Santa Clara County Superior Court action filed on December 7, 2006, that HP committed unfair business practices under California law in connection with the leak investigation. As a result of this agreement, which includes an injunction, the California Attorney General will not pursue civil claims against HP or its current and former directors, officers and employees. Under the terms of the agreement, HP paid a total of \$14.5 million and agreed to implement and maintain for five years a series of measures designed to ensure that HP's corporate investigations are conducted in accordance with California law and the company's high ethical standards. Of the \$14.5 million, \$13.5 million has been used to create a Privacy and Piracy Fund to assist California prosecutors in investigating and prosecuting consumer privacy and information piracy violations, \$650,000 was used to pay statutory damages and \$350,000 reimbursed the California Attorney General's office for its investigation costs. There was no finding of liability against HP as part of the settlement.

Beginning in September 2006, HP received requests from the Committee on Energy and Commerce of the U.S. House of Representatives (the "Committee") for records and information concerning the leak investigation, securities transactions by HP officers and directors, including an August 25, 2006, securities transaction by Mark Hurd, HP's former Chairman and Chief Executive Officer, and related matters. HP has responded to those requests. In addition, Mr. Hurd voluntarily gave testimony to the Committee regarding the leak investigation on September 28, 2006.

In September 2006, HP was informally contacted by the U.S. Attorney for the Northern District of California requesting similar information concerning the processes employed in the leak investigation. HP has responded to that request.

Beginning in September 2006, HP has received requests from the Division of Enforcement of the Securities and Exchange Commission for records and information and interviews with current and former HP directors and officers relating to the leak investigation, the resignation of Thomas J. Perkins from HP's Board of Directors, HP's May 22, 2006 and September 6, 2006 filings with the SEC on Form 8-K, stock repurchases by HP and securities transactions by its officers and directors that occurred between May 1 and October 1, 2006, and HP's policies, practices and approval of securities transactions. In May 2007, HP consented to the entry of an order by the SEC ordering HP to cease and desist from committing or causing violations of the public reporting requirements of the Securities Exchange Act of 1934, as amended. HP has been advised by the staff of the Division of Enforcement that the staff has completed its investigation and does not intend to recommend that any other SEC enforcement action be brought in connection with these matters.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 15: Litigation and Contingencies (Continued)**

In September 2006, HP received a request from the U.S. Federal Communications Commission for records and information relating to the processes employed in the leak investigation. HP has responded to that request.

In addition, four stockholder derivative lawsuits have been filed in California purportedly on behalf of HP stockholders seeking to recover damages for alleged breach of fiduciary duty and to require HP to improve its corporate governance and internal control procedures as a result of the activities of the leak investigation: Staehr v. Dunn, et al. was filed in Santa Clara County Superior Court on September 18, 2006; Worsham v. Dunn, et al. was filed in Santa Clara County Superior Court on September 14, 2006; Tansey v. Dunn, et al. was filed in Santa Clara County Superior Court on September 20, 2006; and Hall v. Dunn, et al. was filed in Santa Clara County Superior Court on September 25, 2006. On October 19, 2006, the Santa Clara County Superior Court consolidated the four California cases under the caption In re Hewlett-Packard Company Derivative Litigation. The consolidated complaint filed on November 19, 2006, also seeks to recover damages in connection with sales of HP stock alleged to have been made by certain current and former HP officers and directors while in possession of material non-public information. Two additional stockholder derivative lawsuits, Pifko v. Babbio, et al., filed on September 19, 2006, and Gross v. Babbio, et al., filed on November 21, 2006, were filed in Chancery Court, County of New Castle, Delaware; both seek to recover damages for alleged breaches of fiduciary duty and to obtain an order instructing the defendants to refrain from further breaches of fiduciary duty and to implement corrective measures that will prevent future occurrences of the alleged breaches of fiduciary duty. On January 24, 2007, the Delaware court consolidated the two cases under the caption In re Hewlett-Packard Company Derivative Litigation and subsequently stayed the proceedings, as the parties had reached a tentative settlement. The HP Board of Directors appointed a Special Litigation Committee consisting of independent Board members authorized to investigate, review and evaluate the facts and circumstances asserted in these derivative matters and to determine how HP should proceed in these matters. On December 14, 2007, HP and the plaintiffs in the California and Delaware derivative actions entered into an agreement to settle those lawsuits. Under the terms of the settlement, HP agreed to continue certain corporate governance changes until December 31, 2012 and to pay the plaintiffs' attorneys' fees. The California court granted final approval to the settlement on March 11, 2008 and subsequently granted plaintiffs' counsel's fee application and dismissed the action. On June 12, 2008, the Delaware court granted final approval to the settlement and the plaintiffs' application for attorneys' fees and also dismissed the action. Because neither the dismissal of the California nor the Delaware derivative action was thereafter appealed, both cases are now concluded.

*Environmental*

Our operations and our products are subject to various federal, state, local and foreign laws and regulations concerning environmental protection, including laws addressing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, the cleanup of contaminated sites, the content of its products and the recycling, treatment and disposal of its products. In particular, HP faces increasing complexity in its product design and procurement operations as it adjusts to new and future requirements relating to the chemical and materials composition of its products, their safe use, the energy consumption associated with those products, including requirements relating to climate change. We also are subject to legislation in an increasing

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 15: Litigation and Contingencies (Continued)**

number of jurisdictions that makes producers of electrical goods, including computers and printers, financially responsible for specified collection, recycling, treatment and disposal of past and future covered products (sometimes referred to as "product take-back legislation"). HP could incur substantial costs, its products could be restricted from entering certain jurisdictions, and it could face other sanctions, if it were to violate or become liable under environmental laws or if its products become non-compliant with environmental laws. HP's potential exposure includes fines and civil or criminal sanctions, third-party property damage or personal injury claims and clean up costs. The amount and timing of costs under environmental laws are difficult to predict.

HP is party to, or otherwise involved in, proceedings brought by U.S. or state environmental agencies under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), known as "Superfund," or state laws similar to CERCLA. HP is also conducting environmental investigations or remediations at several current or former operating sites pursuant to administrative orders or consent agreements with state environmental agencies.

**Note 16: Segment Information**

*Description of Segments*

HP is a leading global provider of products, technologies, software, solutions and services to individual consumers, small- and medium-sized businesses, and large enterprises, including customers in the government, health and education sectors. HP's offerings span multi-vendor customer services, including infrastructure technology and business process outsourcing, technology support and maintenance, application development and support services, and consulting and integration services; enterprise information technology infrastructure, including enterprise server and storage technology, networking products and solutions, information management software and software that optimizes business technology investments; personal computing and other access devices; and imaging and printing-related products and services.

HP and its operations are organized into seven business segments for financial reporting purposes: Services, ESSN, HP Software, PSG, IPG, HP Financial Services ("HPFS"), and Corporate Investments. HP's organizational structure is based on a number of factors that management uses to evaluate, view and run its business operations, which include, but are not limited to, customer base, homogeneity of products and technology. The business segments are based on this organizational structure and information reviewed by HP's management to evaluate the business segment results. Services, ESSN and HP Software are reported collectively as a broader HP Enterprise Business. In order to provide a supplementary view of HP's business, aggregated financial data for the HP Enterprise Business is presented herein.

HP has reclassified segment operating results for fiscal 2010 to conform to certain fiscal 2011 organizational realignments. None of the changes impacts HP's previously reported consolidated net revenue, earnings from operations, net earnings or net earnings per share. Future changes to this organizational structure may result in changes to the business segments disclosed.

A description of the types of products and services provided by each business segment follows.

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 16: Segment Information (Continued)**

*HP Enterprise Business.*

Each of the business segments within the HP Enterprise Business is described in detail below.

*Services* provides consulting, outsourcing and technology services across infrastructure, applications and business process domains. *Services* is divided into four main business units: Infrastructure Technology Outsourcing, Applications Services, Business Process Outsourcing and Technology Services. Infrastructure Technology Outsourcing delivers comprehensive services that encompass the data center; networking; security, compliance, and business continuity; workplace (desktop); and enterprise service management. Applications Services help clients revitalize and manage their applications assets through flexible, project-based consulting services and longer-term outsourcing contracts. These full life cycle services encompass application development, testing, modernization, system integration, maintenance and management. Business Process Outsourcing solutions include a broad array of enterprise shared services, customer relationship management services, financial process management services, and administrative services. Technology Services include consulting and support services. Consulting services include strategic IT advisory services, cloud consulting services, energy efficiency services, converged infrastructure services, networking services, data center transformation services and critical facilities services. Support services include mission critical services, technical and deployment services, support services for servers, storage, networks and imaging and printing, and warranty support across HP's product lines.

*Enterprise Servers, Storage and Networking* provides server, storage and network infrastructure products. The various server offerings range from entry-level servers to high-end scalable servers, including Superdome servers. Industry Standard Servers include primarily entry-level and mid-range ProLiant servers, which run primarily Windows, Linux and Novell operating systems and leverage Intel Corporation ("Intel") and Advanced Micro Devices ("AMD") processors. The business spans a range of product lines, including pedestal-tower servers, density-optimized rack servers and HP's BladeSystem family of server blades. Business Critical Systems include HP Integrity servers based on the Intel Itanium-based processor that run HP-UX, Microsoft Windows and OpenVMS operating systems, as well as fault-tolerant HP Integrity NonStop solutions. Business Critical Systems' portfolio of server solutions includes Scale-up x86 ProLiant Servers, the BladeSystem architecture-based Integrity blade servers and the Superdome 2 server solution. HP's StorageWorks offerings include entry-level, mid-range and high-end arrays, storage area networks ("SANs"), network attached storage ("NAS"), storage management software, and virtualization technologies, as well as StoreOnce data deduplication solutions, tape drives, tape libraries and optical archival storage. HP's networking offering includes the network infrastructure product portfolios sold under the ProCurve, 3Com, H3C and Tipping Point brands.

*HP Software* provides enterprise IT management software, information management solutions, and security intelligence/risk management solutions. Solutions are delivered via traditional software licenses or as software as a service. Augmented by support and professional services, the solutions allow large IT organizations to manage infrastructure, operations, application lifecycles, application quality and security, IT services, and business processes. In addition, the

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 16: Segment Information (Continued)**

solutions help businesses proactively safeguard digital assets, comply with corporate and regulatory policy, and control internal and external security risks.

HP's business segments not included in HP Enterprise Business are described below.

*Personal Systems Group* provides commercial PCs, consumer PCs, workstations, calculators and other related accessories, software and services for the commercial and consumer markets. Commercial PCs are optimized for commercial uses, including enterprise and small and medium sized business ("SMB") customers, and for connectivity and manageability in networked environments. Commercial PCs include the HP Compaq, HP Pro, and HP Elite lines of business desktops and notebooks, as well as the All in One Touchsmart and Omni PCs, HP Mini-Note PC, HP Blade PCs, Retail POS systems, HP Thin Clients, and the HP Slate Tablet. Consumer PCs are targeted at the home user and include the HP Pavilion and Compaq Presario series of multi media consumer desktops and notebooks, as well as the HP Pavilion Elite desktops, HP Envy Premium notebooks, Touchsmart PCs, All in One PC, HP and Compaq Mini notebooks, and the Media Smart Home Server. HP's Z series desktop workstations and HP Elitebook Mobile Workstations provide advanced graphics, computing, and large modeling capabilities, certified with applications in a wide range of industries and running both Windows and Linux operating systems.

*Imaging and Printing Group* provides consumer and commercial printer hardware, supplies, media and scanning devices. IPG is also focused on imaging solutions in the commercial markets. These solutions range from managed print services and capturing high-value pages in areas such as industrial applications, outdoor signage, and the graphic arts business. Inkjet and Web Solutions delivers HP's consumer and SMB inkjet solutions (hardware, supplies, media, web-connected hardware and services) and develops HP's retail publishing and web businesses. It includes single function and all-in-one inkjet printers targeted toward consumers and SMBs as well as retail publishing solutions, Snapfish, and ePrintCenter. LaserJet and Enterprise Solutions deliver products, services and solutions to the medium-business and enterprise segments. It includes LaserJet printers and supplies, multi-function devices, scanners, web-connected hardware and services and enterprise software solutions such as Exstream Software and Web Jetadmin. Managed enterprise solutions include managed print services products and solutions delivered to enterprise customers partnering with third-party software providers to offer workflow solutions in the enterprise environment. Graphics solutions include large format printing (Designjet and Scitex), large format supplies, WebPress supplies, Indigo printing, specialty printing systems and inkjet high-speed production solutions. The graphic solutions business targets Print Service Providers, architects, engineers, designers and industrial solution providers. Printer supplies include LaserJet toner and inkjet printer cartridges and other printing-related media.

*HP Financial Services* supports and enhances HP's global product and services solutions, providing a broad range of value-added financial life cycle management services. HPFS enables HP's worldwide customers to acquire complete IT solutions, including hardware, software and services. HPFS offers leasing, financing, utility programs, and asset recovery services, as well as financial asset management services, for large global and enterprise customers. HPFS also provides an array of specialized financial services to SMBs and educational and governmental

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 16: Segment Information (Continued)**

entities. HPFS offers innovative, customized and flexible alternatives to balance unique customer cash flow, technology obsolescence and capacity needs.

*Corporate Investments* includes business intelligence solutions, HP Labs, mobile devices associated with the Palm acquisition, and certain business incubation projects. Business intelligence solutions enable businesses to standardize on consistent data management schemes, connect and share data across the enterprise and apply analytics. The segment also includes certain video collaboration products sold under the brand "Halo," and Palm smartphones, which are targeted at the consumer segment and include the Pixi and Pre models running on the WebOS operating system. This segment also derives revenue from licensing specific HP technology to third parties.

*Segment Data*

HP derives the results of the business segments directly from its internal management reporting system. The accounting policies HP uses to derive business segment results are substantially the same as those the consolidated company uses. Management measures the performance of each business segment based on several metrics, including earnings from operations. Management uses these results, in part, to evaluate the performance of, and to assign resources to, each of the business segments. HP does not allocate to its business segments certain operating expenses, which it manages separately at the corporate level. These unallocated costs include primarily restructuring charges and any associated adjustments related to restructuring actions, amortization of purchased intangible assets, stock-based compensation expense related to HP-granted employee stock options, PRUs, restricted stock awards and the employee stock purchase plan, certain acquisition-related charges and charges for purchased IPR&D, as well as certain corporate governance costs.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 16: Segment Information (Continued)

Selected operating results information for each business segment was as follows:

|   | Three months ended January 31 |                     |                                    |                     |
|---|-------------------------------|---------------------|------------------------------------|---------------------|
|   | Net Revenue                   |                     | Earnings (Loss)<br>from Operations |                     |
|   | 2011                          | 2010 <sup>(1)</sup> | 2011                               | 2010 <sup>(1)</sup> |
|   | In millions                   |                     |                                    |                     |
| Services  | \$ 8,607                      | \$ 8,790            | \$ 1,375                           | \$ 1,379            |
| Enterprise Servers, Storage and Networking <sup>(2)</sup> | 5,634                         | 4,610               | 828                                | 607                 |
| HP Software <sup>(3)</sup>                                | 697                           | 663                 | 123                                | 172                 |
| HP Enterprise Business                                    | 14,938                        | 14,063              | 2,326                              | 2,158               |
| Personal Systems Group                                    | 10,449                        | 10,584              | 672                                | 530                 |
| Imaging and Printing Group                                | 6,630                         | 6,206               | 1,129                              | 1,054               |
| HP Financial Services                                     | 827                           | 719                 | 79                                 | 67                  |
| Corporate Investments <sup>(4)</sup>                      | 78                            | 60                  | (183)                              | (56)                |
| Segment total   | \$ 32,922                     | \$ 31,632           | \$ 4,023                           | \$ 3,753            |

(1) Certain fiscal 2011 organizational reclassifications have been reflected retroactively to provide improved visibility and comparability. For the three months ended January 31, 2010, the reclassifications resulted in the transfer of revenue and operating profit among ESSN, HP Software and Corporate Investments. Reclassifications between segments included the transfer of the networking business from Corporate Investments to ESSN, the transfer of the communications and media solutions business from HP Software to Services, and the transfer of the business intelligence business from HP Software to Corporate Investments. There was no impact on the previously reported financial results for PSG, HPFS or IPG.

(2) Includes the results of 3Com and 3PAR Inc. ("3PAR") from the dates of acquisition in April 2010 and October 2010, respectively.

(3) Includes the results of ArcSight, Inc. ("ArcSight") from the date of acquisition in October 2010.

(4) Includes the results of Palm from the date of acquisition in July 2010.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

**Note 16: Segment Information (Continued)**

The reconciliation of segment operating results information to HP consolidated totals was as follows:

|   | Three months ended |           |
|---|--------------------|-----------|
|   | January 31         |           |
|   | 2011               | 2010      |
|   | In millions        |           |
| Net revenue:  |                    |           |
| Segment total   | \$ 32,922          | \$ 31,632 |
| Eliminations of inter-segment net revenue and other           | (620)              | (455)     |
| Total HP consolidated net revenue                             | \$ 32,302          | \$ 31,177 |
| Earnings before taxes:  |                    |           |
| Total segment earnings from operations                        | \$ 4,023           | \$ 3,753  |
| Corporate and unallocated costs, gains and eliminations       | 149                | (88)      |
| Unallocated costs related to stock-based compensation expense | (166)              | (163)     |
| Amortization of purchased intangible assets                   | (425)              | (330)     |
| Restructuring charges   | (158)              | (131)     |
| Acquisition-related charges                                   | (29)               | (38)      |
| Interest and other, net                                       | (97)               | (199)     |
| Total HP consolidated earnings before taxes                   | \$ 3,297           | \$ 2,804  |

In connection with certain fiscal 2011 organizational realignments, HP reclassified total assets of its networking business from Corporate Investments to ESSN and total assets of the communications and media solutions business from HP Software to Services. There have been no other material changes to the total assets of HP's segments.

## HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

## Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

## Note 16: Segment Information (Continued)

*Net revenue by segment and business unit*

|   | Three months ended |                     |
|---|--------------------|---------------------|
|   | January 31         |                     |
|   | 2011               | 2010 <sup>(1)</sup> |
|   | In millions        |                     |
| Net revenue:  |                    |                     |
| Infrastructure Technology Outsourcing               | \$ 3,636           | \$ 3,675            |
| Technology Services                                 | 2,602              | 2,631               |
| Application Services                                | 1,632              | 1,681               |
| Business Process Outsourcing                        | 658                | 734                 |
| Other   | 79                 | 69                  |
| Services  | 8,607              | 8,790               |
| Industry Standard Servers                           | 3,448              | 2,946               |
| Storage <sup>(2)</sup>                              | 1,012              | 889                 |
| HP Networking <sup>(3)</sup>                        | 619                | 219                 |
| Business Critical Systems                           | 555                | 556                 |
| Enterprise Servers, Storage and Networking          | 5,634              | 4,610               |
| HP Software <sup>(4)</sup>                          | 697                | 663                 |
| HP Enterprise Business                              | 14,938             | 14,063              |
| Notebooks   | 5,808              | 6,138               |
| Desktops  | 3,896              | 3,853               |
| Workstations  | 535                | 375                 |
| Other <sup>(5)</sup>                                | 210                | 218                 |
| Personal Systems Group                              | 10,449             | 10,584              |
| Supplies  | 4,358              | 4,081               |
| Commercial Hardware                                 | 1,464              | 1,291               |
| Consumer Hardware                                   | 808                | 834                 |
| Imaging and Printing Group                          | 6,630              | 6,206               |
| HP Financial Services                               | 827                | 719                 |
| Corporate Investments <sup>(6)</sup>                | 78                 | 60                  |
| Total segments                                      | 32,922             | 31,632              |
| Eliminations of inter-segment net revenue and other | (620)              | (455)               |
| Total HP consolidated net revenue                   | \$ 32,302          | \$ 31,177           |

- (1) Certain fiscal 2011 organizational reclassifications have been reflected retroactively to provide improved visibility and comparability. For the three months ended January 31, 2010, the reclassifications resulted in the transfer of revenue among ESSN, Services, HP Software and Corporate Investments. Reclassifications between segments included the transfer of the networking business from Corporate Investments to ESSN, the transfer of the communications and media

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

**Notes to Consolidated Condensed Financial Statements (Continued)**

**(Unaudited)**

**Note 16: Segment Information (Continued)**

solutions business from HP Software to Services, and the transfer of the business intelligence business from HP Software to Corporate Investments. Revenue was also transferred among the business units within Services and within PSG. In addition, net revenue reported for the Infrastructure Technology Outsourcing business unit and eliminations of inter-segment net revenue have both been reduced to reflect a change in our inter-segment reporting model. There was no impact on the previously reported financial results for HPFS and IPG or for the business units within IPG.

- (2) Includes the results of 3PAR from the date of acquisition in September 2010.
- (3) The networking business was added to ESSN in fiscal 2011. Also includes the results of 3Com from the date of acquisition in April 2010.
- (4) The Business Technology Optimization and Other Software business units were consolidated into a single business unit within the HP Software segment in fiscal 2011. Also includes the results of ArcSight from the date of acquisition in October 2010.
- (5) The Handhelds business unit, which includes devices that run on Windows Mobile software, was realigned into the Other business unit within PSG in fiscal 2011.
- (6) Includes the results of Palm from the date of acquisition in July 2010.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**

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

*The following discussion should be read in conjunction with the Consolidated Condensed Financial Statements and the related notes that appear elsewhere in this document.*

**OVERVIEW**

We are a leading global provider of products, technologies, software, solutions and services to individual consumers, small- and medium-sized businesses, and large enterprises, including customers in the government, health and education sectors. Our offerings span:

multi-vendor customer services, including infrastructure technology and business process outsourcing, technology support and maintenance, application development and support services, and consulting and integration services;

enterprise information technology infrastructure, including enterprise storage and server technology, networking products and solutions, information management software and software that optimizes business technology investments;

personal computing and other access devices; and

imaging and printing-related products and services.

We have seven business segments for financial reporting purposes: Services, Enterprise Servers, Storage and Networking ("ESSN"), HP Software, the Personal Systems Group ("PSG"), the Imaging and Printing Group ("IPG"), HP Financial Services ("HPFS"), and Corporate Investments. Services, ESSN and HP Software are reported collectively as a broader HP Enterprise Business. While the HP Enterprise Business is not an operating segment, we sometimes provide financial data aggregating the segments within it in order to provide a supplementary view of our business.

Our strategy and operations are currently focused on the following initiatives:

*Competitive Positioning*

We are positioning our businesses to take advantage of important trends in the markets for our products and services. For example, we are aligning our printing business to capitalize on key market trends such as the shift from analog to digital printing and the growth in printable content by developing innovative products for consumers such as the first web-connected home printer, working to enable web and mobile printing, expanding our presence in high-usage annuity businesses including graphics and retail publishing printing, and growing our managed print services business. We are also positioning our enterprise business to capitalize on the trend towards converged infrastructure products that integrate storage, networking, servers and management software, while also delivering services for that converged infrastructure in a manner that best fits each client's needs, be it at a client site, as an outsourced service via the Internet or via a hybrid approach. In addition, we have developed IT management software offerings that seek to satisfy the increasing demand for virtualization management and increased automation.

*Driving Operational Efficiency*

We are working to optimize efficiency across the company. As part of those efforts, we are continuing to execute on our multi-year program to consolidate real estate locations worldwide to fewer



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core sites in order to reduce our IT spending and real estate costs. We are also continuing to implement the restructuring plan announced in the fourth quarter of fiscal 2008 to optimize the cost structure of our Services business. In June 2010, we announced and started implementing a new restructuring plan that will consolidate data centers, systems and tools to better position our enterprise services business, including our infrastructure technology outsourcing, application services, and business process outsourcing business units, for growth. See Note 6 to the Consolidated Condensed Financial Statements in Item 1 for further discussion of these restructuring plans and the associated restructuring charges.

### *Investing for Growth*

We are investing for growth by strengthening our position in our core markets and accelerating growth in adjacent markets in anticipation of market trends, such as data center consolidation and automation, cloud computing and virtualization, digitization, IT security, and mobility and connectivity. For example, we are increasing our sales coverage and investing in our sales channels to better address the markets we cover, including further expansion in emerging markets. We are creating innovative new products and developing new channels to connect with our customers. In addition, we have been making focused investments in innovation to strengthen our portfolio of products and services that we can offer to our customers, both through acquisitions and through organic growth. These investments have enabled us to expand in high-margin and high-growth industry segments and have further strengthened our portfolio of hardware, software and services.

### *Leveraging our Portfolio and Scale*

We now offer one of the IT industry's broadest portfolios of products and services, and we leverage that portfolio to our strategic advantage. For example, in our enterprise business, we are able to provide servers, storage and networking products packaged with services that can be delivered to customers in the manner of their choosing, be it in-house, outsourced as a service via the Internet or via a hybrid environment. Our portfolio of management software completes the package by allowing our customers to manage their IT operations in an efficient and cost-effective manner. In addition, we are working to optimize our supply chain by eliminating complexity, reducing fixed costs, and leveraging our scale to ensure the availability of components at favorable prices even during shortages. We are also expanding our use of industry standard components in our enterprise products to further leverage our scale.

The following provides an overview of our key financial metrics in the first quarter of fiscal 2011 and demonstrates how our execution has translated into financial performance:

|  | HP Enterprise Business                |          |          |                |           |           |          |        |
|--|---------------------------------------|----------|----------|----------------|-----------|-----------|----------|--------|
|  | HP <sup>(1)</sup><br>Consolidated     | Services | ESSN     | HP<br>Software | Total     | PSG       | IPG      | HPFS   |
|  | In millions, except per share amounts |          |          |                |           |           |          |        |
| Net revenue                                      | \$ 32,302                             | \$ 8,607 | \$ 5,634 | \$ 697         | \$ 14,938 | \$ 10,449 | \$ 6,630 | \$ 827 |
| Year-over-year net revenue % increase (decrease) | 3.6%                                  | (2.1)%   | 22.2%    | 5.1%           | 6.2%      | (1.3)%    | 6.8%     | 15.0%  |
| Earnings from operations                         | \$ 3,394                              | \$ 1,375 | \$ 828   | \$ 123         | \$ 2,326  | \$ 672    | \$ 1,129 | \$ 79  |
| Earnings from operations as a % of net revenue   | 10.5%                                 | 16.0%    | 14.7%    | 17.6%          | 15.6%     | 6.4%      | 17.0%    | 9.6%   |
| Net earnings                                     | \$ 2,605                              |          |          |                |           |           |          |        |
| Net earnings per share                           |                                       |          |          |                |           |           |          |        |
| Basic  | \$ 1.19                               |          |          |                |           |           |          |        |
| Diluted  | \$ 1.17                               |          |          |                |           |           |          |        |

(1) Includes Corporate Investments and eliminations.

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Cash and cash equivalents at January 31, 2011 totaled \$9.9 billion, a decrease of \$1.0 billion from the October 31, 2010 balance of \$10.9 billion. The decrease for the first three months of fiscal 2011 was due primarily to \$2.3 billion of cash used to repurchase common stock and \$1.7 billion net payment of our debt, which were partially offset by \$3.1 billion of cash provided from operations.

We intend the discussion of our financial condition and results of operations that follows to provide information that will assist in understanding our Consolidated Condensed Financial Statements, the changes in certain key items in those financial statements from year to year, and the primary factors that accounted for those changes, as well as how certain accounting principles, policies and estimates affect our Consolidated Condensed Financial Statements.

The discussion of results of operations at the consolidated level is followed by a more detailed discussion of results of operations by segment.

For a further discussion of trends, uncertainties and other factors that could impact our operating results, see the section entitled "Factors That Could Affect Future Results."

### **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Consolidated Condensed Financial Statements, which we have prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Senior management has discussed the development, selection and disclosure of significant estimates with the Audit Committee of our Board of Directors. Actual results may differ from these estimates under different assumptions or conditions.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, if different estimates reasonably could have been used, or if changes in the estimate that are reasonably likely to occur could materially impact the financial statements. Management believes that there have been no significant changes during the three months ended January 31, 2011 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended October 31, 2010.

### **CONSTANT CURRENCY PRESENTATION**

Revenue from our international operations has historically represented, and we expect will continue to represent, a majority of our overall net revenue. As a result, our revenue growth has been impacted, and we expect will continue to be impacted, by fluctuations in foreign currency exchange rates. In order to provide a framework for assessing how each of our business segments performed excluding the impact of foreign currency fluctuations, we present the year-over-year percentage change in revenue performance on a constant currency basis, which assumes no change in the exchange rate from the prior-year period. This constant currency disclosure is provided in addition to, and not as a substitute for, the year-over-year percentage change in revenue on an as-reported basis.

**RESULTS OF OPERATIONS**

Set forth below is an analysis of our financial results comparing the three months ended January 31, 2011 to the three months ended January 31, 2010. Unless otherwise noted, all comparative performance data included below reflect year-over-year comparisons.

Results of operations in dollars and as a percentage of net revenue were as follows:

|   | <b>Three months ended January 31</b> |                         |                           |                         |
|---|--------------------------------------|-------------------------|---------------------------|-------------------------|
|   | <b>2011</b>                          |                         | <b>2010<sup>(1)</sup></b> |                         |
|   | <b>Dollars</b>                       | <b>% of<br/>Revenue</b> | <b>Dollars</b>            | <b>% of<br/>Revenue</b> |
| <b>In millions</b>                          |                                      |                         |                           |                         |
| Net revenue                                 | \$ 32,302                            | 100%                    | \$ 31,177                 | 100.0%                  |
| Cost of sales <sup>(2)</sup>                | 24,408                               | 75.6%                   | 24,027                    | 77.1%                   |
| <b>Gross profit</b>                         | <b>7,894</b>                         | <b>24.4%</b>            | <b>7,150</b>              | <b>22.9%</b>            |
| Research and development                    | 798                                  | 2.5%                    | 681                       | 2.2%                    |
| Selling, general and administrative         | 3,090                                | 9.5%                    | 2,967                     | 9.5%                    |
| Amortization of purchased intangible assets | 425                                  | 1.3%                    | 330                       | 1.1%                    |
| Restructuring charges                       | 158                                  | 0.5%                    | 131                       | 0.4%                    |
| Acquisition-related charges                 | 29                                   | 0.1%                    | 38                        | 0.1%                    |
| <b>Earnings from operations</b>             | <b>3,394</b>                         | <b>10.5%</b>            | <b>3,003</b>              | <b>9.6%</b>             |
| Interest and other, net                     | (97)                                 | (0.3)%                  | (199)                     | (0.6)%                  |
| <b>Earnings before taxes</b>                | <b>3,297</b>                         | <b>10.2%</b>            | <b>2,804</b>              | <b>9.0%</b>             |
| Provision for taxes                         | 692                                  | 2.1%                    | 554                       | 1.8%                    |
| <b>Net earnings</b>                         | <b>\$ 2,605</b>                      | <b>8.1%</b>             | <b>\$ 2,250</b>           | <b>7.2%</b>             |

(1) In connection with organizational realignments implemented in the first quarter of fiscal 2011, certain costs previously reported as Cost of sales have been reclassified as Selling, general and administrative expenses to better align those costs with the functional areas that benefit from those expenditures.

(2) Cost of products, cost of services and financing interest.

*Net Revenue*

The components of the weighted net revenue change were as follows:

|  | <b>Three months ended<br/>January 31, 2011</b> |
|--|--|
|  | <b>Percentage Points</b>                       |
| Enterprise Servers, Storage and Networking | 3.3  |
| Imaging and Printing Group                 | 1.4  |
| HP Financial Services                      | 0.3  |
| HP Software                                | 0.1  |
| Personal Systems Group                     | (0.4)  |
| Corporate Investments/Other                | (0.5)  |
| Services                                   | (0.6)  |
| <b>Total HP</b>                            | <b>3.6</b>                                     |

For the three months ended January 31, 2011, total HP net revenue increased 3.6% (4.3% on a constant currency basis). U.S. net revenue increased 4.7% to \$11.4 billion for the first quarter of fiscal



2011, while net revenue from outside of the United States increased 3.0% to \$20.9 billion. As reflected in the table above, the ESSN segment was the largest contributor to HP net revenue growth as a result of balanced growth across all regions. An analysis of the change in net revenue for each business segment is included under "Segment Information" below.

#### *Gross Margin*

Total HP gross margin increased by 1.5 percentage points for the three months ended January 31, 2011. The increase was as a result of a favorable mix from higher HP Networking revenue and a favorable commodity pricing environment.

Services gross margin increased due primarily to the continued focus on operating improvements and cost initiatives that favorably impacted the cost structure of our enterprise services business, delivery efficiencies and cost controls in Technology Services, the effect of which was partially offset by revenue declines.

ESSN gross margin increased primarily as a result of a product mix shift towards higher margin products and lower product costs.

HP Software gross margin increased due primarily to rate improvements in support and licenses.

PSG gross margin increased primarily as a result of lower component costs and warranty expenses, the effect of which was partially offset by pricing actions and increased logistics costs.

IPG gross margin decreased primarily due to a mix shift in hardware towards lower price point products, the effect of which was partially offset by improvements in supplies volume.

HPFS gross margin decreased primarily as a result of lower portfolio margin associated with higher non-accrual income activity and higher bad debt expense, the effect of which was partially offset by higher end of lease activity.

Corporate Investments gross margin decreased for the three months ended January 31, 2011 primarily as a result of the lower gross margin products associated with the acquisition of Palm, Inc. ("Palm").

#### *Operating Expenses*

##### Research and Development

Total research and development ("R&D") expense increased in the three months ended January 31, 2011 due primarily to additional expenses from acquired companies. R&D expense as a percentage of net revenue increased for Corporate Investments, HP Software, ESSN and PSG and decreased for IPG and Services.

##### Selling, General and Administrative

Selling, general and administrative ("SG&A") expense increased in the three months ended January 31, 2011 due primarily to higher field selling and marketing costs as a result of our investments in sales resources to grow revenue, the effect of which was offset by gains on the sale of real estate. SG&A expense as a percentage of net revenue increased for Corporate Investments, HP Software, ESSN and PSG, decreased for HPFS and IPG, and was flat for Services.

#### Amortization of Purchased Intangible Assets

The increase in amortization expense for the three months ended January 31, 2011 was due primarily to increased amortization of purchased intangible assets from acquisitions completed during fiscal 2010.

#### Restructuring

Restructuring charges for the three months ended January 31, 2011 were \$158 million. These charges included \$97 million of severance and facility costs related to our fiscal 2010 Enterprise Services restructuring plan and \$61 million of severance and facility costs related to our fiscal 2008 restructuring plan.

Restructuring charges for the three months ended January 31, 2010 were \$131 million. These charges included \$130 million of severance and facility costs related to our fiscal 2008 restructuring plan and \$1 million of severance costs associated with our fiscal 2009 restructuring plan.

As part of our ongoing business operations, we incurred workforce rebalancing charges for severance and related costs within certain business segments during the first three months of fiscal 2011. Workforce rebalancing activities are considered part of normal operations as we continue to optimize our cost structure. Workforce rebalancing costs are included in our business segment results, and we expect to incur additional workforce rebalancing costs in the future.

#### Acquisition-Related Charges

For the three months ended January 31, 2011, we recorded acquisition-related charges of \$29 million primarily for consulting and integration costs, acquisition costs and retention bonuses associated with the acquisition of Electronic Data Systems Corporation ("EDS") and acquisitions completed in fiscal 2010.

For the three months ended January 31, 2010, we recorded acquisition-related charges of \$38 million primarily for consulting and integration costs as well as retention bonuses associated with the EDS acquisition.

#### *Interest and Other, Net*

Interest and other, net improved by \$102 million for the three months ended January 31, 2011. The improvement was driven primarily by lower currency transaction losses and lower litigation accruals, the effect of which was partially offset by asset impairment charges.

#### *Provision for Taxes*

Our effective tax rate was 21.0% and 19.8% for the three months ended January 31, 2011 and January 31, 2010, respectively. Our effective tax rate increased due to a decline in the percentage of total earnings earned in lower-tax jurisdictions. Our effective tax rate generally differs from the U.S. federal statutory rate of 35% due to favorable tax rates associated with certain earnings from our operations in lower-tax jurisdictions throughout the world. We have not provided U.S. taxes for all of such earnings because we plan to reinvest some of those earnings indefinitely outside the United States.

In the three months ended January 31, 2011, we recorded discrete items with a net tax benefit of \$101 million, decreasing the effective tax rate. These amounts included net tax benefits of \$58 million from restructuring and acquisition charges. In addition, in December 2010, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 was signed into law. We recorded a tax benefit of \$43 million arising from the retroactive research and development credit provided by that legislation in the first quarter of fiscal 2011.

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In the three months ended January 31, 2010, we recorded discrete items with a net tax benefit of \$92 million, decreasing the effective tax rate. These amounts included net tax benefits of \$54 million from restructuring and acquisition charges, a tax benefit of \$19 million from settlement of a tax audit matter, a net tax benefit of \$19 million from adjustments to prior year foreign income tax accruals and credits, and other miscellaneous discrete items.

### Segment Information

A description of the products and services for each segment can be found in Note 16 to the Consolidated Condensed Financial Statements. Future changes to this organizational structure may result in changes to the business segments disclosed.

#### *HP Enterprise Business*

Services, ESSN and HP Software are reported collectively as a broader HP Enterprise Business. We describe the results of the business segments of the HP Enterprise Business in more detail below.

#### *Services*

|  | <b>Three months ended January 31</b> |             |                   |
|--|--------------------------------------|-------------|-------------------|
|  | <b>2011</b>                          | <b>2010</b> | <b>% Decrease</b> |
|  | <b>In millions</b>                   |             |                   |
| Net revenue                                    | \$ 8,607                             | \$ 8,790    | (2.1)%            |
| Earnings from operations                       | \$ 1,375                             | \$ 1,379    | (0.3)%            |
| Earnings from operations as a % of net revenue | 16.0%                                | 15.7%       |                   |

The components of the weighted net revenue change by business unit were as follows:

|                                       | <b>Three months ended<br/>January 31, 2011<br/>Percentage Points</b> |
|---------------------------------------|--|
| Technology Services                   | (0.3)  |
| Infrastructure Technology Outsourcing | (0.4)  |
| Application Services                  | (0.6)  |
| Business Process Outsourcing          | (0.9)  |
| Other                                 | 0.1  |
| <b>Total Services</b>                 | <b>(2.1)</b>   |

Services net revenue decreased 2.1% (1.4% when adjusted for currency) for the three months ended January 31, 2011. Net revenue in Technology Services declined by 1% due primarily to reduced sales of third-party hardware, the effect of which was partially offset by revenue growth in our support business. Infrastructure Technology Outsourcing net revenue decreased by 1% due to a lower mix of short-term deal signings and unfavorable currency impacts. Application Services net revenue declined by 3% due primarily to a decline in signings for short-term project work and unfavorable currency impacts. Business Process Outsourcing net revenue decreased by 10% due primarily to the ExcellerateHRO divestiture completed at the end of the third quarter of fiscal 2010.

Services earnings from operations as a percentage of net revenue increased by 0.3 percentage points in the three months ended January 31, 2011. Operating margin increased primarily due to continued focus on operating improvements and cost initiatives that favorably impacted the cost structure of our enterprise services business, delivery efficiencies and cost controls in Technology Services. Further operating margin expansion was limited by revenue declines.

*Enterprise Servers, Storage and Networking*

|  | Three months ended January 31 |          |            |
|--|-------------------------------|----------|------------|
|  | 2011                          | 2010     | % Increase |
|  | In millions                   |          |            |
| Net revenue                                    | \$ 5,634                      | \$ 4,610 | 22.2%      |
| Earnings from operations                       | \$ 828                        | \$ 607   | 36.4%      |
| Earnings from operations as a % of net revenue | 14.7%                         | 13.2%    |            |

The components of the weighted net revenue change by business unit were as follows:

|                                   | Three months ended<br>January 31, 2011 |  |
|-----------------------------------|--|--|
|                                   | Percentage Points                      |  |
| Industry Standard Servers ("ISS") | 10.9                                   |  |
| HP Networking                     | 8.7                                    |  |
| Storage                           | 2.7                                    |  |
| Business Critical Systems ("BCS") | (0.1)                                  |  |
| <b>Total ESSN</b>                 | <b>22.2</b>                            |  |

ESSN net revenue increased 22.2% (23.4% when adjusted for currency) for the three months ended January 31, 2011. Total revenue from server and storage blades increased by 23%. ISS net revenue increased by 17%, driven primarily by unit volume growth coupled with increased average unit prices due to improved market conditions and demand for the latest generation of ISS products. HP Networking net revenue increased by 183% for the three months ended January 31, 2011, driven primarily by our acquisition of 3Com in April 2010, improved market demand for our core data center products, and continued investment in sales coverage. Storage net revenue increased by 14%, driven primarily by strong performance in products related to our acquisition of 3PAR in September 2010 and continued growth in scale-out and storage networking products. Business Critical Systems net revenue was flat for the three months ended January 31, 2011, due primarily to competitive pressures, the effect of which was offset by higher demand for the latest generation of BCS products.

ESSN earnings from operations as a percentage of net revenue increased by 1.5 percentage points for the three months ended January 31, 2011, driven by an increase in gross margin resulting from a product mix shift towards higher margin products and lower product costs. The favorable effect on operating margin from higher gross margin was partially offset by an increase in operating expenses as a percentage of net revenue, due primarily to additional expenses associated with acquisitions and investments in R&D and sales coverage.

*HP Software*

|  | Three months ended January 31 |        |                          |
|--|-------------------------------|--------|--------------------------|
|  | 2011                          | 2010   | % Increase<br>(Decrease) |
|  | In millions                   |        |                          |
| Net revenue                                    | \$ 697                        | \$ 663 | 5.1%                     |
| Earnings from operations                       | \$ 123                        | \$ 172 | (28.5)%                  |
| Earnings from operations as a % of net revenue | 17.6%                         | 25.9%  |                          |

HP Software net revenue increased 5.1% (6.0% when adjusted for currency) for the three months ended January 31, 2011. The net revenue increase was primarily due to revenues resulting from the acquisitions of Fortify Software Inc. and ArcSight, which HP completed in September 2010 and

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October 2010, respectively. Net revenue from services, support and licenses increased by 10%, 5% and 3%, respectively.

HP Software earnings from operations as a percentage of net revenue decreased by 8.3 percentage points for the three months ended January 31, 2011. The operating margin decline was primarily due to impacts from acquisitions and investments in R&D and sales coverage.

### *Personal Systems Group*

|  | Three months ended January 31 |           |                          |
|--|-------------------------------|-----------|--------------------------|
|  | 2011                          | 2010      | % Increase<br>(Decrease) |
|  | In millions                   |           |                          |
| Net revenue                                    | \$ 10,449                     | \$ 10,584 | (1.3)%                   |
| Earnings from operations                       | \$ 672                        | \$ 530    | 26.8%                    |
| Earnings from operations as a % of net revenue | 6.4%                          | 5.0%      |                          |

The components of the weighted net revenue change by business unit were as follows:

|                  | Three months ended<br>January 31, 2011<br>Percentage Points |
|------------------|---|
| Workstations     | 1.5   |
| Desktop PCs      | 0.4   |
| Notebook PCs     | (3.1)   |
| Other            | (0.1)   |
| <b>Total PSG</b> | <b>(1.3)</b>  |

PSG net revenue decreased 1.3% (0.3% when adjusted for currency) for the three months ended January 31, 2011. The revenue decrease was primarily due to softness in the consumer markets and weakness in PCs in China offset by strength in commercial markets. PSG net revenue was also impacted by a 6% decline in average selling prices ("ASPs"). ASPs declined due primarily to a competitive pricing environment and a product mix shift toward lower-end models. PSG unit volume increased across all business units except for the consumer PC business unit. Workstations revenue increased by 43%. Net revenue for Desktop PCs increased by 1%, while net revenue for Notebook PCs decreased by 5%. Commercial clients net revenue increased by 11%, while consumer clients decreased by 12%. The net revenue decline in Other was related primarily to decreased sales of support services, extended warranties and third-party options.

PSG earnings from operations as a percentage of net revenue increased 1.4 percentage points for the three months ended January 31, 2011, due to an increase in gross margin resulting primarily from component cost declines and lower warranty expenses, the effect of which was partially offset by pricing actions and increased logistics costs. Offsetting the increase in gross margin was an increase in operating expenses as a percentage of net revenue due primarily to increased marketing expenses and investments in sales coverage.

### *Imaging and Printing Group*

|  | Three months ended January 31 |          |            |
|--|-------------------------------|----------|------------|
|  | 2011                          | 2010     | % Increase |
|  | In millions                   |          |            |
| Net revenue                                    | \$ 6,630                      | \$ 6,206 | 6.8%       |
| Earnings from operations                       | \$ 1,129                      | \$ 1,054 | 7.1%       |
| Earnings from operations as a % of net revenue | 17.0%                         | 17.0%    |            |

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The components of the weighted net revenue change as compared to the prior-year period by business unit were as follows:

| <b>Three months ended<br/>January 31, 2011</b> |            |
|--|------------|
| <b>Percentage Points</b>                       |            |
| Supplies                                       | 4.4        |
| Commercial Hardware                            | 2.8        |
| Consumer Hardware                              | (0.4)      |
| <b>Total IPG</b>                               | <b>6.8</b> |

IPG net revenue increased 6.8% (6.9% when adjusted for currency) for the three months ended January 31, 2011, reflecting an improvement in market conditions. Supplies net revenue increased 6.8% in the first quarter of fiscal 2011, driven by improved volume. Net revenue for Commercial Hardware increased 13.4% in the first quarter of fiscal 2011 due primarily to laser unit volume growth of 33% as a result of improved product availability. Net revenue for Consumer Hardware decreased 3.1% in the first quarter of fiscal 2011 due to a mix shift toward lower price point products.

IPG earnings from operations as a percentage of net revenue was flat for the three months ended January 31, 2011 due primarily to a decrease in gross margin, the effect of which was offset by a decrease in operating expenses as a percentage of net revenue. The decline in gross margin in the first quarter of fiscal 2011 was due to a mix shift in Consumer Hardware and Commercial Hardware toward lower price point products, the effect of which was partially offset by improvements in supplies volume. The decrease in operating expense as a percentage of net revenue in the first quarter of fiscal 2011 was due to continued cost management.

### *HP Financial Services*

| <b>Three months ended January 31</b>           |             |             |                   |
|--|-------------|-------------|-------------------|
|  | <b>2011</b> | <b>2010</b> | <b>% Increase</b> |
| <b>In millions</b>                             |             |             |                   |
| Net revenue                                    | \$ 827      | \$ 719      | 15.0%             |
| Earnings from operations                       | \$ 79       | \$ 67       | 17.9%             |
| Earnings from operations as a % of net revenue | 9.6%        | 9.3%        |                   |

HPFS net revenue increased by 15.0% for the three months ended January 31, 2011. The net revenue increase was due primarily to portfolio growth from higher customer demand, a higher operating lease mix due to higher service-led financing volume, and higher end of lease revenue from residual expirations in line with portfolio growth, the effect of which was partially offset by unfavorable currency movements.

HPFS earnings from operations as a percentage of net revenue increased by 0.3 percentage points for the three months ended January 31, 2011 due primarily to a decrease in operating expenses as a percentage of net revenue, the effect of which was partially offset by a slight decline in gross margin. The decrease in operating expenses as a percentage of net revenue was driven primarily by improved cost efficiencies. The gross margin decrease was primarily due to lower portfolio margin associated with higher non-accrual income activity and higher bad debt expense, the effect of which was partially offset by higher end of lease activity.

*Financing Originations***Three months ended  
January 31****2011      2010****In millions**

|                              |    |       |    |       |
|------------------------------|----|-------|----|-------|
| Total financing originations | \$ | 1,543 | \$ | 1,403 |
|------------------------------|----|-------|----|-------|

New financing originations, which represent the amounts of financing provided to customers for equipment and related software and services and include intercompany activity, increased 10% in the three months ended January 31, 2011. The increase was driven by higher financing associated with HP product sales resulting from improved integration and engagement with HP's sales efforts, the effect of which was partially offset by an unfavorable currency impact.

*Portfolio Assets and Ratios*

HPFS maintains a strategy to generate a competitive return on equity by effectively leveraging its portfolio against the risks associated with interest rates and credit. The HPFS business model is asset-intensive and uses certain internal metrics to measure its performance against other financial services companies, including a segment balance sheet that is derived from our internal management reporting system. The accounting policies used to derive these amounts are substantially the same as those used by the consolidated company. However, certain intercompany loans and accounts that are reflected in the segment balances are eliminated in our Consolidated Condensed Financial Statements.

The portfolio assets and ratios derived from the segment balance sheet for HPFS were as follows:

|  |    | <b>January 31,<br/>2011</b> | <b>October 31,<br/>2010</b> |
|--|----|-----------------------------|-----------------------------|
|  |    | <b>In millions</b>          |                             |
| Portfolio assets <sup>(1)</sup>                | \$ | 11,644                      | \$ 11,418                   |
| Allowance for doubtful accounts <sup>(2)</sup> |    | 124                         | 140                         |
| Operating lease equipment reserve              |    | 83                          | 83                          |
| Total reserves                                 |    | 207                         | 223                         |
| Net portfolio assets                           | \$ | 11,437                      | \$ 11,195                   |
| Reserve coverage                               |    | 1.8%                        | 2.0%                        |
| Debt to equity ratio <sup>(3)</sup>            |    | 7.0x                        | 7.0x                        |

(1) Portfolio assets include gross financing receivables of approximately \$6.8 billion and \$6.7 billion at January 31, 2011 and October 31, 2010, respectively, and net equipment under operating leases of \$2.6 billion at January 31, 2011 and \$2.5 billion at October 31, 2010, respectively. Portfolio assets also include capitalized profit on intercompany equipment transactions of approximately \$800 million at January 31, 2011 and October 31, 2010, respectively, and intercompany leases of approximately \$1.4 billion at January 31, 2011 and \$1.3 billion at October 31, 2010, both of which are eliminated in consolidation.

(2) Allowance for doubtful accounts includes both the short-term and the long-term portions of the allowance on financing receivables.

(3) HPFS debt consists of intercompany equity that is treated as debt for segment reporting purposes, intercompany debt and debt issued directly by HPFS.

Net portfolio assets at January 31, 2011 increased 2.2% from October 31, 2010. The increase resulted from higher levels of financing originations and a favorable currency impact during the first three months of fiscal 2011. The overall percentage of portfolio asset reserves decreased as a percentage of the portfolio assets.

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For the three months ended January 31, 2011 and 2010, HPFS recorded net bad debt expenses of \$18 million and \$12 million, respectively.

### *Corporate Investments*

|  | Three months ended January 31 |         |                          |
|--|-------------------------------|---------|--------------------------|
|  | 2011                          | 2010    | % Increase<br>(Decrease) |
| In millions                                |                               |         |                          |
| Net revenue                                | \$ 78                         | \$ 60   | 30.0%                    |
| Loss from operations                       | \$ (183)                      | \$ (56) | (226.8)%                 |
| Loss from operations as a % of net revenue | (234.6)%                      | (93.3)% |                          |

Net revenue in Corporate Investments relates primarily to business intelligence solutions, HP Labs, mobile devices associated with the Palm acquisition, and certain business incubation projects. The revenue increase in Corporate Investments was primarily due to revenue resulting from the acquisition of Palm which HP completed in July 2010.

Corporate Investments reported a loss from operations for the three months ended January 31, 2011 due primarily to the impact from the Palm acquisition. The loss from operations in Corporate Investments was also due to expenses carried in the segment associated with corporate development, global alliances and HP Labs, which expenses increased for the three months ended January 31, 2011.

### **LIQUIDITY AND CAPITAL RESOURCES**

Our cash balances are held in numerous locations throughout the world, including substantial amounts held outside of the United States. Most of the amounts held outside of the United States could be repatriated to the United States but, under current law, would be subject to U.S. federal income taxes, less applicable foreign tax credits. Repatriation of some foreign balances is restricted by local laws. We have provided for the U.S. federal tax liability on these amounts for financial statement purposes, except for foreign earnings that are considered indefinitely reinvested outside of the United States. Repatriation could result in additional U.S. federal income tax payments in future years. Where local restrictions prevent an efficient intercompany transfer of funds, our intent is that cash balances would remain outside of the United States, and we would meet U.S. liquidity needs through ongoing cash flows, external borrowings, or both. We utilize a variety of tax planning and financing strategies in an effort to ensure that our worldwide cash is available in the locations in which it is needed.

#### *FINANCIAL CONDITION (Sources and Uses of Cash)*

|  | Three months ended<br>January 31 |          |
|--|----------------------------------|----------|
|  | 2011                             | 2010     |
| In millions  |                                  |          |
| Net cash provided by operating activities            | \$ 3,070                         | \$ 2,407 |
| Net cash used in investing activities                | (363)                            | (711)    |
| Net cash used in financing activities                | (3,702)                          | (1,428)  |
| Net (decrease) increase in cash and cash equivalents | \$ (995)                         | \$ 268   |

#### *Operating Activities*

Compared to the corresponding period in 2010, net cash provided by operating activities increased by approximately \$663 million for the three months ended January 31, 2011. The increase was due primarily to higher net earnings and lower reduction in accounts payable, the impact of which was partially offset by a smaller reduction of accounts and financing receivables.

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Our key working capital metrics are as follows:

|  | Three months ended |      |
|--|--------------------|------|
|  | January 31         |      |
|  | 2011               | 2010 |
| Days of sales outstanding in accounts receivable   | 46                 | 42   |
| Days of supply in inventory                        | 25                 | 25   |
| Days of purchases outstanding in accounts payable. | (50)               | (51) |
| Cash conversion cycle                              | 21                 | 16   |

Days of sales outstanding in accounts receivable ("DSO") is calculated by dividing ending accounts receivable, net of allowance for doubtful accounts, by a 90-day average net revenue.

Days of supply in inventory ("DOS") measures the average number of days from procurement to sale of our product. DOS is calculated by dividing ending inventory by a 90-day average cost of goods sold.

Days of purchases outstanding in accounts payable ("DPO") is calculated by dividing ending accounts payable by a 90-day average cost of goods sold.

Our working capital requirements depend upon our effective management of the cash conversion cycle, which represents effectively the number of days that elapse from the day we pay for the purchase of raw materials to the collection of cash from our customers. The cash conversion cycle is the sum of DSO and DOS less DPO.

The increase in DSO was due primarily to lower collections as a result of revenue linearity during the quarter. The DOS remained flat year over year. The decrease in DPO was due primarily to the timing of supplier purchases and payments in the first quarter. These changes contributed to the increase in the cash conversion cycle for the three months ended January 31, 2011.

### *Investing Activities*

Compared to the corresponding period in fiscal 2010, net cash used in investing activities decreased by approximately \$348 million for the three months ended January 31, 2011 due primarily to proceeds from the sale of land and buildings as part of our multi-year program to consolidate real estate locations worldwide to reduce real estate costs.

### *Financing Activities*

Compared to the corresponding period in fiscal 2010, net cash used in financing activities increased by approximately \$2.3 billion for the three months ended January 31, 2011. The increase was due primarily to higher net repayments of commercial paper and debt and the decrease in cash received as a result of lower issuances of common stock under employee stock plans, the impact of which was partially offset by decreased repurchases of common stock.

For more information on our share repurchase programs, see Note 13 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

## **CAPITAL RESOURCES**

### *Debt Levels*

We maintain debt levels that we establish through consideration of a number of factors, including cash flow expectations, cash requirements for operations, investment plans (including acquisitions), share repurchase activities, overall cost of capital, and targeted capital structure. Outstanding borrowings decreased to \$20.4 billion as of January 31, 2011 as compared to \$22.3 billion at

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October 31, 2010, bearing weighted average interest rates of 2.3% and 2.0%, respectively. During the first three months of fiscal 2011, we issued \$4.8 billion and repaid \$8.5 billion of commercial paper.

Our weighted-average interest rate reflects the average effective rate on our borrowings prevailing during the period; it factors in the impact of swapping some of our global notes with fixed interest rates for global notes with floating interest rates. For more information on our interest rate swaps, see Note 8 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

For more information on our borrowings, see Note 11 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

### *Available Borrowing Resources*

At January 31, 2011, we had the following resources available to obtain short-term or long-term financings if we need additional liquidity:

| <b>At January 31, 2011</b>                                  |             |
|---|-------------|
| <b>In millions</b>  |             |
| 2009 Shelf Registration Statement <sup>(1)</sup>            | Unspecified |
| Commercial paper programs <sup>(1)</sup>                    | \$ 15,800   |
| Uncommitted lines of credit <sup>(1)</sup>                  | \$ 1,400    |
| Revolving trade receivables-based facilities <sup>(2)</sup> | \$ 261      |

(1) For more information on our available borrowings resources, see Note 11 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

(2) For more information on our revolving trade receivables-based facilities, see Note 4 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

### *Credit Ratings*

Our credit risk is evaluated by three independent rating agencies based upon publicly available information as well as information obtained in our ongoing discussions with them. The ratings as of January 31, 2011 were:

|                         | <b>Standard &amp; Poor's<br/>Ratings Services</b> | <b>Moody's Investors<br/>Service</b> | <b>Fitch Ratings<br/>Services</b> |
|-------------------------|---|--------------------------------------|-----------------------------------|
| Short-term debt ratings | A-1   | Prime-1                              | F1                                |
| Long-term debt ratings  | A   | A2                                   | A+                                |

We do not have any rating downgrade triggers that would accelerate the maturity of a material amount of our debt. However, a downgrade in our credit rating would increase the cost of borrowings under our credit facilities. Also, a downgrade in our credit rating could limit our ability to issue commercial paper under our current programs. If this occurs, we would seek alternative sources of funding, including drawdowns under our credit facilities or the issuance of notes under our existing shelf registration statement.

## **CONTRACTUAL AND OTHER OBLIGATIONS**

### *Income Tax Obligations*

At January 31, 2011, we had approximately \$1.5 billion of recorded liabilities and related interest and penalties pertaining to uncertainty in income tax positions, which will be partially offset by \$90 million of deferred tax assets and interest receivable. The decline of approximately \$500 million since October 31, 2010 was due primarily to the settlement or resolution of various uncertain tax

positions within a non-U.S. jurisdiction. These liabilities and related interest and penalties include \$67 million expected to be paid within one year. For the remaining amount, we are unable to make a reasonable estimate as to when cash settlement with the tax authorities might occur due to the uncertainties related to these tax matters. See Note 12 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference, for additional information on taxes.

*Guarantees and Indemnifications*

For more information on liabilities that may arise from guarantees and indemnification, see Note 10 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

*Litigation and Contingencies*

For more information on liabilities that may arise from litigation and contingencies, see Note 15 to the Consolidated Condensed Financial Statements in Item 1, which is incorporated herein by reference.

*Off-Balance Sheet Arrangements*

As part of our ongoing business, we have not participated in transactions that generate material relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities ("SPEs"), which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of January 31, 2011, we are not involved in any material unconsolidated SPEs.

**FACTORS THAT COULD AFFECT FUTURE RESULTS**

Because of the following factors, as well as other variables affecting our operating results, past financial performance may not be a reliable indicator of future performance, and historical trends should not be used to anticipate results or trends in future periods.

*Competitive pressures could harm our revenue, gross margin and prospects.*

We encounter aggressive competition from numerous and varied competitors in all areas of our business, and our competitors may target our key market segments. We compete primarily on the basis of technology, performance, price, quality, reliability, brand, reputation, distribution, range of products and services, ease of use of our products, account relationships, customer training, service and support, security, availability of application software, and Internet infrastructure offerings. If our products, services, support and cost structure do not enable us to compete successfully based on any of those criteria, our operations, results and prospects could be harmed.

Unlike many of our competitors, we have a portfolio of businesses and must allocate resources across these businesses while competing with companies that specialize in one or more of these product lines. As a result, we may invest less in certain areas of our businesses than our competitors do, and these competitors may have greater financial, technical and marketing resources available to them than our businesses that compete against them. Industry consolidation also may affect competition by creating larger, more homogeneous and potentially stronger competitors in the markets in which we compete, and our competitors also may affect our business by entering into exclusive arrangements with existing or potential customers or suppliers. In addition, companies with whom we have strategic alliances in some areas may be competitors in other areas. Those companies also may acquire or form alliances with our competitors, thereby reducing their business with us. Any inability to effectively manage these complicated relationships with strategic alliance partners could have an adverse effect on our results of operations.

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We may have to continue to lower the prices of many of our products and services to stay competitive, while at the same time trying to maintain or improve revenue and gross margin. The markets in which we do business, particularly the personal computer and printing markets, are highly competitive, and we encounter aggressive price competition for all of our products and services from numerous companies globally. Over the past several years, price competition in the market for personal computers, printers and related products has been particularly intense as competitors have aggressively cut prices and lowered their product margins for these products. In addition, competitors in some of the markets in which we compete with a greater presence in lower-cost jurisdictions may be able to offer lower prices than we are able to offer. Our results of operations and financial condition may be adversely affected by these and other industry-wide pricing pressures.

Because our business model is based on providing innovative and high quality products, we may spend a proportionately greater amount on research and development than some of our competitors. If we cannot proportionately decrease our cost structure on a timely basis in response to competitive price pressures, our gross margin and, therefore, our profitability could be adversely affected. In addition, if our pricing and other factors are not sufficiently competitive, or if there is an adverse reaction to our product decisions, we may lose market share in certain areas, which could adversely affect our revenue and prospects.

Even if we are able to maintain or increase market share for a particular product, revenue could decline because the product is in a maturing industry. Revenue and margins also could decline due to increased competition from other types of products. For example, growing demand for an increasing array of mobile computing devices and the development of cloud-based solutions may reduce demand for some of our existing hardware products. In addition, refill and remanufactured alternatives for some of HP's LaserJet toner and inkjet cartridges compete with HP's supplies business. Other companies have also developed and marketed new compatible cartridges for HP's LaserJet and inkjet products, particularly in jurisdictions outside of the United States where adequate intellectual property protection may not exist.

*If we cannot continue to develop, manufacture and market products and services that meet customer requirements for innovation and quality, our revenue and gross margin may suffer.*

The process of developing new high technology products and services and enhancing existing products and services is complex, costly and uncertain, and any failure by us to anticipate customers' changing needs and emerging technological trends accurately could significantly harm our market share and results of operations. For example, we must successfully address the increasing market demand for mobile computing devices in a variety of form factors that provide a compelling user experience. We must also attract and retain developers to ensure the continued availability and development of appealing and innovative software applications for our mobile computing devices. In addition, we are transitioning to an environment characterized by cloud-based computing and software being delivered as a service, and we must continue to successfully develop and deploy cloud-based solutions for our customers. We must make long-term investments, develop or obtain appropriate intellectual property and commit significant resources before knowing whether our predictions will accurately reflect customer demand for our products and services. After we develop a product, we must be able to manufacture appropriate volumes quickly and at low costs. To accomplish this, we must accurately forecast volumes, mixes of products and configurations that meet customer requirements, and we may not succeed at doing so at all or within a given product's life cycle. Any delay in the development, production or marketing of a new product could result in us not being among the first to market, which could further harm our competitive position.

In the course of conducting our business, we must adequately address quality issues associated with our products and services, including defects in our engineering, design and manufacturing processes, as well as defects in third-party components included in our products. In order to address quality issues, we work extensively with our customers and suppliers and engage in product testing to determine the cause of the problem and to determine appropriate solutions. However, we may have limited ability to control quality issues, particularly with respect to faulty components manufactured by third parties. If we are unable to determine the cause, find an appropriate solution or offer a temporary fix (or "patch"), we may delay shipment to customers, which would delay revenue recognition and could adversely affect our revenue and reported results. Finding solutions to quality issues can be expensive and may result in additional warranty, replacement and other costs, adversely affecting our profits. If new or existing customers have difficulty operating our products, our operating margins could be adversely affected, and we could face possible claims if we fail to meet our customers' expectations. In addition, quality issues can impair our relationships with new or existing customers and adversely affect our brand and reputation, which could adversely affect our operating results.

*Economic weakness and uncertainty could adversely affect our revenue, gross margin and expenses.*

Our revenue and gross margin depend significantly on worldwide economic conditions and the demand for computing and imaging products and services in the markets in which we compete. Economic weakness and uncertainty have resulted, and may result in the future, in decreased revenue, gross margin, earnings or growth rates and difficulty managing inventory levels. Sustained uncertainty about current global economic conditions may adversely affect demand for our products and services. Economic weakness and uncertainty also make it more difficult for us to make accurate forecasts of revenue, gross margin and expenses.

We also have experienced, and may experience in the future, gross margin declines in certain businesses, reflecting the effect of items such as competitive pricing pressures, inventory write downs and increases in component and manufacturing costs resulting from higher labor and material costs borne by our manufacturers and suppliers that, as a result of competitive pricing pressures or other factors, we are unable to pass on to our customers. In addition, our business may be disrupted if we are unable to obtain equipment, parts or components from our suppliers and our suppliers from their suppliers due to the insolvency of key suppliers or the inability of key suppliers to obtain credit.

Economic weakness and uncertainty could cause our expenses to vary materially from our expectations. Any renewed financial turmoil affecting the banking system and financial markets or any significant financial services institution failures could negatively impact our treasury operations, as the financial condition of such parties may deteriorate rapidly and without notice in times of market volatility and disruption. Poor financial performance of asset markets could lead to increased pension and post-retirement benefit expenses. Other income and expense could vary materially from expectations depending on changes in interest rates, borrowing costs, currency exchange rates, hedging expenses and the fair value of derivative instruments. Economic downturns also may lead to restructuring actions and associated expenses.

*We depend on third-party suppliers, and our revenue and gross margin could suffer if we fail to manage suppliers properly.*

Our operations depend on our ability to anticipate our needs for components, products and services and our suppliers' ability to deliver sufficient quantities of quality components, products and services at reasonable prices in time for us to meet critical schedules. Given the wide variety of systems, products and services that we offer, the large number of our suppliers and contract manufacturers that are dispersed across the globe, and the long lead times that are required to manufacture, assemble and deliver certain components and products, problems could arise in planning production and managing inventory levels that could seriously harm us. In addition, our ongoing project to improve the efficiency

of our supply chain could cause supply disruptions and be more expensive, time consuming and resource-intensive than expected. Other supplier problems that we could face include component shortages, excess supply, risks related to the terms of our contracts with suppliers, risks associated with contingent workers, and risks related to our relationships with single source suppliers, as described below.

*Shortages.* Occasionally we may experience a shortage of, or a delay in receiving, certain components as a result of strong demand, capacity constraints, supplier financial weaknesses, inability of suppliers to borrow funds in the credit markets, disputes with suppliers (some of whom are also customers), disruptions in the operations of component suppliers, other problems experienced by suppliers or problems faced during the transition to new suppliers. In particular, our PC business relies heavily upon Outsourced Manufacturers ("OMs") to manufacture its products and is therefore dependent upon the continuing operations of those OMs to fulfill demand for our PC products. HP represents a substantial portion of the business of some of these OMs, and any changes to the nature or volume of business transacted by HP with a particular OM could adversely affect the operations and financial condition of the OM and lead to shortages or delays in receiving products from that OM. If shortages or delays persist, the price of these components may increase, we may be exposed to quality issues or the components may not be available at all. We may not be able to secure enough components at reasonable prices or of acceptable quality to build products or provide services in a timely manner in the quantities or according to the specifications needed. Accordingly, our revenue and gross margin could suffer as we could lose time-sensitive sales, incur additional freight costs or be unable to pass on price increases to our customers. If we cannot adequately address supply issues, we might have to reengineer some products or service offerings, resulting in further costs and delays.

*Oversupply.* In order to secure components for the provision of products or services, at times we may make advance payments to suppliers or enter into non-cancelable commitments with vendors. In addition, we may purchase components strategically in advance of demand to take advantage of favorable pricing or to address concerns about the availability of future components. If we fail to anticipate customer demand properly, a temporary oversupply could result in excess or obsolete components, which could adversely affect our gross margin.

*Contractual terms.* As a result of binding price or purchase commitments with vendors, we may be obligated to purchase components or services at prices that are higher than those available in the current market and be limited in our ability to respond to changing market conditions. In the event that we become committed to purchase components or services for prices in excess of the current market price, we may be at a disadvantage to competitors who have access to components or services at lower prices, and our gross margin could suffer. In addition, many of our competitors obtain products or components from the same OMs and suppliers that we utilize. Our competitors may obtain better pricing and other terms and more favorable allocations of products and components during periods of limited supply, and our ability to engage in relationships with certain OMs and suppliers could be limited. The practice employed by our PC business of purchasing product components and transferring those components to its OMs may create large supplier receivables with the OMs that, depending on the financial condition of the OMs, may have risk of uncollectability. In addition, certain of our OMs and suppliers may decide in the future to discontinue conducting business with us. Any of these actions by our competitors, OMs or suppliers could adversely affect our future operating results and financial condition.

*Contingent workers.* We also rely on third-party suppliers for the provision of contingent workers, and our failure to manage our use of such workers effectively could adversely affect our results of operations. We have been exposed to various legal claims relating to the status of contingent

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workers in the past and could face similar claims in the future. We may be subject to shortages, oversupply or fixed contractual terms relating to contingent workers, as described above. Our ability to manage the size of, and costs associated with, the contingent workforce may be subject to additional constraints imposed by local laws.

*Single source suppliers.* Our use of single source suppliers for certain components could exacerbate our supplier issues. We obtain a significant number of components from single sources due to technology, availability, price, quality or other considerations. For example, we rely on Intel Corporation to provide us with a sufficient supply of processors for many of our PCs, workstations, handheld computing devices and servers, and some of those processors are customized for our products. New products that we introduce may utilize custom components obtained from only one source initially until we have evaluated whether there is a need for additional suppliers. Replacing a single source supplier could delay production of some products as replacement suppliers initially may be subject to capacity constraints or other output limitations. For some components, such as customized components and some of the processors that we obtain from Intel, alternative sources may not exist or those alternative sources may be unable to produce the quantities of those components necessary to satisfy our production requirements. In addition, we sometimes purchase components from single source suppliers under short-term agreements that contain favorable pricing and other terms but that may be unilaterally modified or terminated by the supplier with limited notice and with little or no penalty. The performance of such single source suppliers under those agreements (and the renewal or extension of those agreements upon similar terms) may affect the quality, quantity or price of components to HP. The loss of a single source supplier, the deterioration of our relationship with a single source supplier, or any unilateral modification to the contractual terms under which we are supplied components by a single source supplier could adversely affect our revenue and gross margins.

*Business disruptions could seriously harm our future revenue and financial condition and increase our costs and expenses.*

Our worldwide operations could be subject to earthquakes, power shortages, telecommunications failures, water shortages, tsunamis, floods, hurricanes, typhoons, fires, extreme weather conditions, medical epidemics or pandemics and other natural or manmade disasters or business interruptions, for which we are predominantly self-insured. The occurrence of any of these business disruptions could seriously harm our revenue and financial condition and increase our costs and expenses. Our corporate headquarters, and a portion of our research and development activities, are located in California, and other critical business operations and some of our suppliers are located in California and Asia, near major earthquake faults. In addition, all six of our principal worldwide IT data centers are located in the southern United States, making our operations more vulnerable to natural disasters or other business disruptions occurring in that geographical area. The manufacture of product components, the final assembly of our products and other critical operations are concentrated in certain geographic locations, including Shanghai, Singapore and India. We also rely on major logistics hubs primarily in Asia to manufacture and distribute our products and in the southwestern United States to import products into the Americas region. Our operations could be adversely affected if manufacturing, logistics or other operations in these locations are disrupted for any reason, including natural disasters, information technology system failures, military actions or economic, business, labor, environmental, public health, regulatory or political issues. The ultimate impact on us, our significant suppliers and our general infrastructure of being located near major earthquake faults and being consolidated in certain geographical areas is unknown, but our revenue, profitability and financial condition could suffer in the event of a major earthquake or other natural disaster.

*System security risks, data protection breaches and systems integration issues could disrupt our internal operations or information technology services provided to customers, and any such disruption could reduce our expected revenue, increase our expenses, damage our reputation and adversely affect our stock price.*

Experienced computer programmers and hackers may be able to penetrate our network security and misappropriate our confidential information or that of third parties, create system disruptions or cause shutdowns. Computer programmers and hackers also may be able to develop and deploy viruses, worms, and other malicious software programs that attack our products or otherwise exploit any security vulnerabilities of our products. In addition, sophisticated hardware and operating system software and applications that we produce or procure from third parties may contain defects in design or manufacture, including "bugs" and other problems that could unexpectedly interfere with the operation of the system. The costs to us to eliminate or alleviate security problems, bugs, viruses, worms, malicious software programs and security vulnerabilities could be significant, and the efforts to address these problems could result in interruptions, delays, cessation of service and loss of existing or potential customers that may impede our sales, manufacturing, distribution or other critical functions.

We manage and store various proprietary information and sensitive or confidential data relating to our business. In addition, our outsourcing services business routinely processes, stores and transmits large amounts of data for our clients, including sensitive and personally identifiable information. Breaches of our security measures or the accidental loss, inadvertent disclosure or unapproved dissemination of proprietary information or sensitive or confidential data about us or our clients, including the potential loss or disclosure of such information or data as a result of fraud, trickery or other forms of deception, could expose us, our customers or the individuals affected to a risk of loss or misuse of this information, result in litigation and potential liability for us, damage our brand and reputation or otherwise harm our business. We also could lose existing or potential customers for outsourcing services or other information technology solutions or incur significant expenses in connection with our customers' system failures or any actual or perceived security vulnerabilities in our products. In addition, the cost and operational consequences of implementing further data protection measures could be significant.

Portions of our IT infrastructure also may experience interruptions, delays or cessations of service or produce errors in connection with systems integration or migration work that takes place from time to time. We may not be successful in implementing new systems and transitioning data which could cause business disruptions and be more expensive, time consuming, disruptive and resource-intensive. Such disruptions could adversely impact our ability to fulfill orders and interrupt other processes. Delayed sales, lower margins or lost customers resulting from these disruptions have adversely affected in the past, and in the future could adversely affect, our financial results, stock price and reputation.

*The revenue and profitability of our operations have historically varied, which makes our future financial results less predictable.*

Our revenue, gross margin and profit vary among our products and services, customer groups and geographic markets and therefore will likely be different in future periods than our current results. Our revenue depends on the overall demand for our products and services. Delays or reductions in IT spending could materially adversely affect demand for our products and services, which could result in a significant decline in revenues. Overall gross margins and profitability in any given period are dependent partially on the product, customer and geographic mix reflected in that period's net revenue. Competition, lawsuits, investigations and other risks affecting those businesses therefore may have a significant impact on our overall gross margin and profitability. Certain segments have a higher fixed cost structure and more variation in gross margins across their business units and product portfolios than others and may therefore experience significant operating profit volatility on a quarterly basis. In addition, newer geographic markets may be relatively less profitable due to investments associated with entering those markets and local pricing pressures, and we may have difficulty establishing and

maintaining the operating infrastructure necessary to support the high growth rate associated with some of those markets. Market trends, competitive pressures, commoditization of products, seasonal rebates, increased component or shipping costs, regulatory impacts and other factors may result in reductions in revenue or pressure on gross margins of certain segments in a given period, which may necessitate adjustments to our operations.

*HP's stock price has historically fluctuated and may continue to fluctuate, which may make future prices of HP's stock difficult to predict.*

HP's stock price, like that of other technology companies, can be volatile. Some of the factors that could affect our stock price are:

speculation in the press or investment community about, or actual changes in, our business, strategic position, market share, organizational structure, operations, financial condition, financial reporting and results, effectiveness of cost cutting efforts, value or liquidity of our investments, exposure to market volatility, prospects, business combination or investment transactions, or executive team;

the announcement of new products, services, technological innovations or acquisitions by HP or its competitors;

quarterly increases or decreases in revenue, gross margin, earnings or cash flow from operations, changes in estimates by the investment community or guidance provided by HP, and variations between actual and estimated financial results;

announcements of actual and anticipated financial results by HP's competitors and other companies in the IT industry; and

the timing and amount of share repurchases by HP.

General or industry specific market conditions or stock market performance or domestic or international macroeconomic and geopolitical factors unrelated to HP's performance also may affect the price of HP common stock. For these reasons, investors should not rely on recent trends to predict future stock prices, financial condition, results of operations or cash flows. In addition, following periods of volatility in a company's securities, securities class action litigation against a company is sometimes instituted. If instituted against HP, this type of litigation could result in substantial costs and the diversion of management time and resources.

*Our revenue, cost of sales, and expenses may suffer if we cannot continue to license or enforce the intellectual property rights on which our businesses depend or if third parties assert that we violate their intellectual property rights.*

We rely upon patent, copyright, trademark and trade secret laws in the United States, similar laws in other countries, and agreements with our employees, customers, suppliers and other parties, to establish and maintain intellectual property rights in the technology and products we sell, provide or otherwise use in our operations. However, any of our direct or indirect intellectual property rights could be challenged, invalidated or circumvented, or such intellectual property rights may not be sufficient to permit us to take advantage of current market trends or otherwise to provide competitive advantages, either of which could result in costly product redesign efforts, discontinuance of certain product offerings or other competitive harm. Further, the laws of certain countries do not protect proprietary rights to the same extent as the laws of the United States. Therefore, in certain jurisdictions we may be unable to protect our proprietary technology adequately against unauthorized third-party copying or use; this too could adversely affect our competitive position.

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Because of the rapid pace of technological change in the information technology industry, much of our business and many of our products rely on key technologies developed or licensed by third parties. We may not be able to obtain or continue to obtain licenses and technologies from these third parties at all or on reasonable terms, or such third parties may demand cross-licenses to our intellectual property. In addition, it is possible that as a consequence of a merger or acquisition, third parties may obtain licenses to some of our intellectual property rights or our business may be subject to certain restrictions that were not in place prior to the transaction. Consequently, we may lose a competitive advantage with respect to these intellectual property rights or we may be required to enter into costly arrangements in order to terminate or limit these rights.

Third parties also may claim that we or customers indemnified by us are infringing upon their intellectual property rights. For example, individuals and groups frequently purchase intellectual property assets for the sole purpose of asserting claims of infringement and attempting to extract settlements from large companies such as HP. The number of these claims has increased significantly in recent periods and may continue to increase in the future. If we cannot or do not license the infringed technology at all or on reasonable terms, or substitute similar technology from another source, our operations could be adversely affected. Even if we believe that the claims are without merit, they can be time-consuming and costly to defend and may divert management's attention and resources away from our business. Claims of intellectual property infringement also might require us to redesign affected products, enter into costly settlement or license agreements, pay costly damage awards, or face a temporary or permanent injunction prohibiting us from importing, marketing or selling certain of our products. Even if we have an agreement to indemnify us against such costs, the indemnifying party may be unable to uphold its contractual obligations to us.

Finally, our results of operations and cash flows have been and could continue to be affected in certain periods and on an ongoing basis by the imposition, accrual and payment of copyright levies or similar fees. In certain countries (primarily in Europe), proceedings are ongoing or have been concluded involving HP in which groups representing copyright owners sought to impose upon and collect from HP levies upon equipment (such as PCs, MFDs and printers) alleged to be copying devices under applicable laws. Other such groups have also sought to modify existing levy schemes to increase the amount of the levies that can be collected from HP. Other countries that have not imposed levies on these types of devices are expected to extend existing levy schemes, and countries that do not currently have levy schemes may decide to impose copyright levies on these types of devices. The total amount of the copyright levies will depend on the types of products determined to be subject to the levy, the number of units of those products sold during the period covered by the levy, and the per unit fee for each type of product, all of which are affected by several factors, including the outcome of ongoing litigation involving HP and other industry participants and possible action by the legislative bodies in the applicable countries, and could be substantial. Consequently, the ultimate impact of these copyright levies or similar fees, and the ability of HP to recover such amounts through increased prices, remain uncertain.

*Due to the international nature of our business, political or economic changes or other factors could harm our future revenue, costs and expenses and financial condition.*

Sales outside the United States make up approximately 65% of our net revenue. In addition, an increasing portion of our business activity is being conducted in emerging markets, including Brazil, Russia, India and China. Our future revenue, gross margin, expenses and financial condition could suffer due to a variety of international factors, including:

ongoing instability or changes in a country's or region's economic or political conditions, including inflation, recession, interest rate fluctuations and actual or anticipated military or political conflicts;

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longer accounts receivable cycles and financial instability among customers;

trade regulations and procedures and actions affecting production, pricing and marketing of products;

local labor conditions and regulations, including local labor issues faced by specific HP suppliers and OMs;

managing a geographically dispersed workforce;

changes in the regulatory or legal environment;

differing technology standards or customer requirements;

import, export or other business licensing requirements or requirements relating to making foreign direct investments, which could increase our cost of doing business in certain jurisdictions, prevent us from shipping products to particular countries or markets, affect our ability to obtain favorable terms for components, increase our operating costs or lead to penalties or restrictions;

difficulties associated with repatriating cash generated or held abroad in a tax-efficient manner and changes in tax laws; and

fluctuations in freight costs, limitations on shipping and receiving capacity, and other disruptions in the transportation and shipping infrastructure at important geographic points of exit and entry for our products and shipments.

The factors described above also could disrupt our product and component manufacturing and key suppliers located outside of the United States. For example, we rely on manufacturers in Taiwan for the production of notebook computers and other suppliers in Asia for product assembly and manufacture.

As approximately 65% of our sales are from countries outside of the United States, other currencies, particularly the euro, the British pound, Chinese yuan renminbi and the Japanese yen, can have an impact on HP's results (expressed in U.S. dollars). Currency variations also contribute to variations in sales of products and services in impacted jurisdictions. Accordingly, fluctuations in foreign currency rates, most notably the strengthening of the dollar against the euro, could adversely affect our revenue growth in future periods. In addition, currency variations can adversely affect margins on sales of our products in countries outside of the United States and margins on sales of products that include components obtained from suppliers located outside of the United States. We use a combination of forward contracts and options designated as cash flow hedges to protect against foreign currency exchange rate risks. The effectiveness of our hedges depends on our ability to accurately forecast future cash flows, which is particularly difficult during periods of uncertain demand for our products and services and highly volatile exchange rates. As a result, we could incur significant losses from our hedging activities if our forecasts are incorrect. In addition, our hedging activities may be ineffective or may not offset any or more than a portion of the adverse financial impact resulting from currency variations. Gains or losses associated with hedging activities also may impact our revenue and to a lesser extent our cost of sales and financial condition.

In many foreign countries, particularly in those with developing economies, it is common to engage in business practices that are prohibited by laws and regulations applicable to us, such as the Foreign Corrupt Practices Act. For example, as discussed in Note 15 to the Consolidated Condensed Financial Statements, the German Public Prosecutor's Office, the U.S. Department of Justice and the SEC have been investigating allegations that certain current and former employees of HP engaged in bribery, embezzlement and tax evasion or were involved in kickbacks or other improper payments. Although we implement policies and procedures designed to facilitate compliance with these laws, our employees, contractors and agents, as well as those companies to which we outsource certain of our business

operations, may take actions in violation of our policies. Any such violation, even if prohibited by our policies, could have an adverse effect on our business and reputation.

*If we fail to manage the distribution of our products and services properly, our revenue, gross margin and profitability could suffer.*

We use a variety of distribution methods to sell our products and services, including third-party resellers and distributors and both direct and indirect sales to both enterprise accounts and consumers. Successfully managing the interaction of our direct and indirect channel efforts to reach various potential customer segments for our products and services is a complex process. Moreover, since each distribution method has distinct risks and gross margins, our failure to implement the most advantageous balance in the delivery model for our products and services could adversely affect our revenue and gross margins and therefore our profitability. Other distribution risks are described below.

Our financial results could be materially adversely affected due to channel conflicts or if the financial conditions of our channel partners were to weaken.

Our future operating results may be adversely affected by any conflicts that might arise between our various sales channels, the loss or deterioration of any alliance or distribution arrangement or the loss of retail shelf space. Moreover, some of our wholesale and retail distributors may have insufficient financial resources and may not be able to withstand changes in business conditions, including economic weakness and industry consolidation. Many of our significant distributors operate on narrow product margins and have been negatively affected by business pressures. Considerable trade receivables that are not covered by collateral or credit insurance are outstanding with our distribution and retail channel partners. Revenue from indirect sales could suffer, and we could experience disruptions in distribution if our distributors' financial conditions, abilities to borrow funds in the credit markets or operations weaken.

Our inventory management is complex as we continue to sell a significant mix of products through distributors.

We must manage inventory effectively, particularly with respect to sales to distributors, which involves forecasting demand and pricing issues. Distributors may increase orders during periods of product shortages, cancel orders if their inventory is too high or delay orders in anticipation of new products. Distributors also may adjust their orders in response to the supply of our products and the products of our competitors and seasonal fluctuations in end-user demand. Our reliance upon indirect distribution methods may reduce visibility to demand and pricing issues, and therefore make forecasting more difficult. If we have excess or obsolete inventory, we may have to reduce our prices and write down inventory. Moreover, our use of indirect distribution channels may limit our willingness or ability to adjust prices quickly and otherwise to respond to pricing changes by competitors. We also may have limited ability to estimate future product rebate redemptions in order to price our products effectively.

*If we do not effectively manage our product and services transitions, our revenue may suffer.*

Many of the markets in which we compete are characterized by rapid technological advances in hardware performance and software features and functionality; frequent introduction of new products; short product life cycles; and continual improvement in product price characteristics relative to product performance. To maintain our competitive position in these markets, we must successfully develop and introduce new products and services. For example, our Palm business unit recently announced the introduction of several new products to address the growing demand for mobile computing devices in a variety of form factors. Among the risks associated with the introduction of new products and services are delays in development or manufacturing, variations in costs, delays in customer purchases or reductions in price of existing products in anticipation of new introductions, difficulty in predicting

customer demand for the new offerings and effectively managing inventory levels so that they are in line with anticipated demand, risks associated with customer qualification and evaluation of new products and the risk that new products may have quality or other defects or may not be supported adequately by application software. If we do not make an effective transition from existing products and services to future offerings, our revenue may decline.

Our revenue and gross margin also may suffer due to the timing of product or service introductions by our suppliers and competitors. This is especially challenging when a product has a short life cycle or a competitor introduces a new product just before our own product introduction. Furthermore, sales of our new products and services may replace sales, or result in discounting of some of our current offerings, offsetting the benefit of even a successful introduction. There also may be overlaps in the current products and services of HP and portfolios acquired through mergers and acquisitions that we must manage. In addition, it may be difficult to ensure performance of new customer contracts in accordance with our revenue, margin and cost estimates and to achieve operational efficiencies embedded in our estimates. Given the competitive nature of our industry, if any of these risks materializes, future demand for our products and services and our results of operations may suffer.

*Our revenue and profitability could suffer if we do not manage the risks associated with our IT services business properly.*

The size and significance of the IT services portion of our business have increased in recent periods. The risks that accompany that business differ from those of our other businesses and include the following:

The pricing and other terms of some of our IT services agreements, particularly our long-term IT outsourcing services agreements, require us to make estimates and assumptions at the time we enter into these contracts that could differ from actual results. Any increased or unexpected costs or unanticipated delays in connection with the performance of these engagements, including delays caused by factors outside our control, could make these agreements less profitable or unprofitable, which would have an adverse affect on the profit margin of our IT services business.

Some of our IT services agreements require significant investment in the early stages that is expected to be recovered through billings over the life of the agreement. These agreements often involve the construction of new IT systems and communications networks and the development and deployment of new technologies. Substantial performance risk exists in each agreement with these characteristics, and some or all elements of service delivery under these agreements are dependent upon successful completion of the development, construction and deployment phases. Any failure to perform satisfactorily under these agreements may expose us to legal liability, result in the loss of customers and harm our reputation, which could decrease the revenues and profitability of our IT services business.

Some of our outsourcing services agreements contain pricing provisions that permit a client to request a benchmark study by a mutually acceptable third party. The benchmarking process typically compares the contractual price of our services against the price of similar services offered by other specified providers in a peer comparison group, subject to agreed upon adjustment and normalization factors. Generally, if the benchmarking study shows that our pricing has a difference outside a specified range, and the difference is not due to the unique requirements of the client, then the parties will negotiate in good faith any appropriate adjustments to the pricing. This may result in the reduction of our rates for the benchmarked services performed after the implementation of those pricing adjustments, which could decrease the revenues and profitability of our IT services business.

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*If we fail to comply with our customer contracts or government contracting regulations, our revenue could suffer.*

Our contracts with our customers may include unique and specialized performance requirements. In particular, our contracts with federal, state, provincial and local governmental customers are subject to various procurement regulations, contract provisions and other requirements relating to their formation, administration and performance. Any failure by us to comply with the specific provisions in our customer contracts or any violation of government contracting regulations could result in the imposition of various civil and criminal penalties, which may include termination of contracts, forfeiture of profits, suspension of payments and, in the case of our government contracts, fines and suspension from future government contracting. In addition, we have in the past been, and may in the future be, subject to *qui tam* litigation brought by private individuals on behalf of the government relating to our government contracts, which could include claims for up to treble damages. Further, any negative publicity related to our customer contracts or any proceedings surrounding them, regardless of its accuracy, may damage our business by affecting our ability to compete for new contracts. If our customer contracts are terminated, if we are suspended from government work, or if our ability to compete for new contracts is adversely affected, we could suffer a reduction in expected revenue.

*We make estimates and assumptions in connection with the preparation of HP's Consolidated Condensed Financial Statements, and any changes to those estimates and assumptions could adversely affect our results of operations.*

In connection with the preparation of HP's Consolidated Condensed Financial Statements, we use certain estimates and assumptions based on historical experience and other factors. Our most critical accounting estimates are described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this report. In addition, as discussed in Note 15 to the Consolidated Condensed Financial Statements, we make certain estimates, including decisions related to provisions for legal proceedings and other contingencies. While we believe that these estimates and assumptions are reasonable under the circumstances, they are subject to significant uncertainties, some of which are beyond our control. Should any of these estimates and assumptions change or prove to have been incorrect, it could adversely affect our results of operations.

*Unanticipated changes in HP's tax provisions, the adoption of new tax legislation or exposure to additional tax liabilities could affect our profitability.*

We are subject to income and other taxes in the United States and numerous foreign jurisdictions. Our tax liabilities are affected by the amounts we charge for inventory, services, licenses, funding and other items in intercompany transactions. We are subject to ongoing tax audits in various jurisdictions. Tax authorities may disagree with our intercompany charges, cross-jurisdictional transfer pricing or other matters and assess additional taxes. We regularly assess the likely outcomes of these audits in order to determine the appropriateness of our tax provision. However, there can be no assurance that we will accurately predict the outcomes of these audits, and the amounts ultimately paid upon resolution of audits could be materially different from the amounts previously included in our income tax expense and therefore could have a material impact on our tax provision, net income and cash flows. In addition, our effective tax rate in the future could be adversely affected by changes to our operating structure, changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in tax laws and the discovery of new information in the course of our tax return preparation process. In particular, the carrying value of deferred tax assets, which are predominantly in the United States, is dependent on our ability to generate future taxable income in the United States. In addition, President Obama's administration has announced proposals for other U.S. tax legislation that, if adopted, could adversely affect our tax rate. There are also other tax proposals that have been introduced, that are being considered, or that have

been enacted by the United States Congress or the legislative bodies in foreign jurisdictions that could affect our tax rate, the carrying value of deferred tax assets, or our other tax liabilities. Any of these changes could affect our profitability.

*Our sales cycle makes planning and inventory management difficult and future financial results less predictable.*

In some of our segments, our quarterly sales often have reflected a pattern in which a disproportionate percentage of each quarter's total sales occurs towards the end of such quarter. This uneven sales pattern makes prediction of revenue, earnings, cash flow from operations and working capital for each financial period difficult, increases the risk of unanticipated variations in quarterly results and financial condition and places pressure on our inventory management and logistics systems. If predicted demand is substantially greater than orders, there will be excess inventory. Alternatively, if orders substantially exceed predicted demand, we may not be able to fulfill all of the orders received in the last few weeks of each quarter. Other developments late in a quarter, such as a systems failure, component pricing movements, component shortages or global logistics disruptions, could adversely impact inventory levels and results of operations in a manner that is disproportionate to the number of days in the quarter affected.

We experience some seasonal trends in the sale of our products that also may produce variations in quarterly results and financial condition. For example, sales to governments (particularly sales to the U.S. government) are often stronger in the third calendar quarter, consumer sales are often stronger in the fourth calendar quarter, and many customers whose fiscal and calendar years are the same spend their remaining capital budget authorizations in the fourth calendar quarter prior to new budget constraints in the first calendar quarter of the following year. European sales are often weaker during the summer months. Demand during the spring and early summer also may be adversely impacted by market anticipation of seasonal trends. Moreover, to the extent that we introduce new products in anticipation of seasonal demand trends, our discounting of existing products may adversely affect our gross margin prior to or shortly after such product launches. Typically, our third fiscal quarter is our weakest and our fourth fiscal quarter is our strongest. Many of the factors that create and affect seasonal trends are beyond our control.

*Any failure by us to execute on our strategy for operational efficiency successfully could result in total costs and expenses that are greater than expected.*

We have adopted an operating framework that includes a disciplined focus on operational efficiency. As part of this framework, we have adopted several initiatives, including a multi-year program announced in 2006 to reduce real estate costs by consolidating several hundred HP real estate locations worldwide to fewer core sites, and a multi-year process of examining every function and every one of our businesses and functions in order to optimize efficiency and reduce cost. We have also implemented a workforce restructuring program in fiscal 2008 relating to our acquisition of EDS, a workforce restructuring program in fiscal 2009 relating to our product businesses and a multi-year restructuring plan in the third quarter of fiscal 2010 relating to our enterprise services business.

Our ability to achieve the anticipated cost savings and other benefits from these initiatives within the expected time frame is subject to many estimates and assumptions, including estimates and assumptions regarding the cost of consolidating real estate locations, the amount of accelerated depreciation or asset impairment to be incurred when we vacate facilities or cease using equipment before the end of their respective lease term or asset life, and the costs and timing of other activities in connection with these initiatives. These estimates and assumptions are subject to significant economic, competitive and other uncertainties, some of which are beyond our control. In addition, there are significant risks associated with our workforce restructuring programs, including potential delays in the implementation of those programs in highly regulated locations outside of the United States,

particularly in Europe and Asia, decreases in employee morale, and the failure to meet operational targets due to the loss of employees. If these estimates and assumptions are incorrect, if we experience delays, or if other unforeseen events occur, our business and results of operations could be adversely affected.

*In order to be successful, we must attract, retain and motivate key employees, and failure to do so could seriously harm us.*

In order to be successful, we must attract, retain and motivate executives and other key employees, including those in managerial, technical, sales, marketing and IT support positions. Hiring and retaining qualified executives, engineers, skilled solutions providers in the IT support business and qualified sales representatives are critical to our future, and competition for experienced employees in the IT industry can be intense. In order to attract and retain executives and other key employees in a competitive marketplace, we must provide a competitive compensation package, including cash and share-based compensation. Our primary forms of share-based incentive awards are restricted stock units and performance-based restricted stock units, which contain conditions relating to HP's stock price performance and, in the case of performance-based restricted stock units, HP's long-term financial performance that make the future value of those awards uncertain. If the anticipated value of such share-based incentive awards does not materialize, if our share-based compensation otherwise ceases to be viewed as a valuable benefit, or if our total compensation package is not viewed as being competitive, our ability to attract, retain, and motivate executives and key employees could be weakened. The failure to successfully hire executives and key employees or the loss of any executives and key employees could have a significant impact on our operations.

*Terrorist acts, conflicts and wars may seriously harm our business and revenue, costs and expenses and financial condition and stock price.*

Terrorist acts, conflicts or wars (wherever located around the world) may cause damage or disruption to HP, our employees, facilities, partners, suppliers, distributors, resellers or customers. The potential for future attacks, the national and international responses to attacks or perceived threats to national security, and other actual or potential conflicts or wars, including the ongoing military operations in Iraq and Afghanistan have created many economic and political uncertainties. In addition, as a major multinational company with headquarters and significant operations located in the United States, actions against or by the United States may impact our business or employees. Although it is impossible to predict the occurrences or consequences of any such events, they could result in a decrease in demand for our products, make it difficult or impossible to deliver products to our customers or to receive components from our suppliers, create delays and inefficiencies in our supply chain and result in the need to impose employee travel restrictions. We are predominantly uninsured for losses and interruptions caused by terrorist acts, conflicts and wars.

*Any failure by us to identify, manage, complete and integrate acquisitions, divestitures and other significant transactions successfully could harm our financial results, business and prospects, and the costs, expenses and other financial and operational effects associated with managing, completing and integrating acquisitions may result in financial results that are different than expected.*

As part of our business strategy, we frequently acquire complementary companies or businesses, divest non-core businesses or assets, enter into strategic alliances and joint ventures and make investments to further our business (collectively, "business combination and investment transactions"). In order to pursue this strategy successfully, we must identify suitable candidates for and successfully complete business combination and investment transactions, some of which may be large and complex, and manage post-closing issues such as the integration of acquired companies or employees. We may not fully realize all of the anticipated benefits of any business combination and investment transaction,

and the timeframe for achieving benefits of a business combination and investment transaction may depend partially upon the actions of employees, suppliers or other third parties. In addition, the pricing and other terms of our contracts for business combination and investment transactions require us to make estimates and assumptions at the time we enter into these contracts, and, during the course of our due diligence, we may not identify all of the factors necessary to estimate our costs accurately. Any increased or unexpected costs, unanticipated delays or failure to meet contractual obligations could make these transactions less profitable or unprofitable. Moreover, if we fail to identify and successfully complete business combination and investment transactions that further our strategic objectives, we may be required to expend resources to develop products and technology internally, we may be at a competitive disadvantage or we may be adversely affected by negative market perceptions, any of which could adversely affect our revenue, gross margin and profitability.

Integration issues are complex, time-consuming and expensive and, without proper planning and implementation, could significantly disrupt our business. The challenges involved in integration include:

combining product offerings and entering into new markets in which we are not experienced;

convincing customers and distributors that the transaction will not diminish client service standards or business focus, preventing customers and distributors from deferring purchasing decisions or switching to other suppliers (which could result in our incurring additional obligations in order to address customer uncertainty), minimizing sales force attrition and coordinating sales, marketing and distribution efforts;

consolidating and rationalizing corporate IT infrastructure, which may include multiple legacy systems from various acquisitions and integrating software code;

minimizing the diversion of management attention from ongoing business concerns;

persuading employees that business cultures are compatible, maintaining employee morale and retaining key employees, engaging with employee works councils representing an acquired company's non-U.S. employees, integrating employees into HP, correctly estimating employee benefit costs and implementing restructuring programs;

coordinating and combining administrative, manufacturing, research and development and other operations, subsidiaries, facilities and relationships with third parties in accordance with local laws and other obligations while maintaining adequate standards, controls and procedures;

achieving savings from supply chain integration; and

managing integration issues shortly after or pending the completion of other independent transactions.

Managing business combination and investment transactions requires varying levels of management resources, which may divert our attention from other business operations. These business combination and investment transactions also have resulted, and in the future may result, in significant costs and expenses and charges to earnings, including those related to severance pay, early retirement costs, employee benefit costs, asset impairment charges, charges from the elimination of duplicative facilities and contracts, in-process research and development charges, inventory adjustments, assumed litigation and other liabilities, legal, accounting and financial advisory fees, and required payments to executive officers and key employees under retention plans. Moreover, HP has incurred and will incur additional depreciation and amortization expense over the useful lives of certain assets acquired in connection with business combination and investment transactions, and, to the extent that the value of goodwill or intangible assets with indefinite lives acquired in connection with a business combination and investment transaction becomes impaired, we may be required to incur additional material charges relating to the impairment of those assets. In order to complete an acquisition, we may issue common stock, potentially creating dilution for existing stockholders. In addition, we may borrow to finance an



acquisition, and the amount and terms of any potential future acquisition-related borrowings, as well as other factors, could affect our liquidity and financial condition and potentially our credit ratings. Any potential future downgrades in our credit rating associated with an acquisition could adversely affect our ability to borrow and cost of borrowing and result in more restrictive borrowing terms. In addition, HP's effective tax rate on an ongoing basis is uncertain, and business combination and investment transactions could impact our effective tax rate. We also may experience risks relating to the challenges and costs of closing a business combination and investment transaction and the risk that an announced business combination and investment transaction may not close. As a result, any completed, pending or future transactions may contribute to financial results that differ from the investment community's expectations in a given quarter.

*Unforeseen environmental costs could impact our future net earnings.*

We are subject to various federal, state, local and foreign laws and regulations concerning environmental protection, including laws addressing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, the cleanup of contaminated sites, the content of our products and the recycling, treatment and disposal of our products, including batteries. In particular, we face increasing complexity in our product design and procurement operations as we adjust to new and future requirements relating to the chemical and materials composition of our products, their safe use, the energy consumption associated with those products, climate change laws and regulations, and product take-back legislation. We could incur substantial costs, our products could be restricted from entering certain jurisdictions, and we could face other sanctions, if we were to violate or become liable under environmental laws or if our products become non-compliant with environmental laws. Our potential exposure includes fines and civil or criminal sanctions, third-party property damage, personal injury claims and clean up costs. Further, liability under some environmental laws relating to contaminated sites can be imposed retroactively, on a joint and several basis, and without any finding of noncompliance or fault. The amount and timing of costs under environmental laws are difficult to predict.

*Some anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.*

We have provisions in our certificate of incorporation and bylaws, each of which could have the effect of rendering more difficult or discouraging an acquisition of HP deemed undesirable by our Board of Directors. These include provisions:

authorizing blank check preferred stock, which HP could issue with voting, liquidation, dividend and other rights superior to our common stock;

limiting the liability of, and providing indemnification to, HP's directors and officers;

specifying that HP stockholders may take action only at a duly called annual or special meeting of stockholders and otherwise in accordance with our bylaws and limiting the ability of our stockholders to call special meetings;

requiring advance notice of proposals by HP stockholders for business to be conducted at stockholder meetings and for nominations of candidates for election to our Board of Directors;

requiring a vote by the holders of two-thirds of HP's outstanding shares to amend certain bylaws relating to HP stockholder meetings, the Board of Directors and indemnification; and

controlling the procedures for conduct of HP Board and stockholder meetings and election, appointment and removal of HP directors.

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These provisions, alone or together, could deter or delay hostile takeovers, proxy contests and changes in control or management of HP. As a Delaware corporation, HP also is subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which prevents some stockholders from engaging in certain business combinations without approval of the holders of substantially all of HP's outstanding common stock.

Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control of HP could limit the opportunity for our stockholders to receive a premium for their shares of HP common stock and also could affect the price that some investors are willing to pay for HP common stock.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

For quantitative and qualitative disclosures about market risk affecting HP, see "Quantitative and Qualitative Disclosures About Market Risk" in Item 7A of Part II of our Annual Report on Form 10-K for the fiscal year ended October 31, 2010, which is incorporated herein by reference. Our exposure to market risk has not changed materially since October 31, 2010.

### **Item 4. Controls and Procedures.**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this report (the "Evaluation Date"). Based on this evaluation, our principal executive officer and principal financial officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective such that the information relating to HP, including our consolidated subsidiaries, required to be disclosed in our SEC reports (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to HP's management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our most recently completed fiscal quarter. Based on that evaluation, our principal executive officer and principal financial officer concluded that there has not been any change in our internal control over financial reporting during that quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings.**

The information set forth above under Note 15 contained in the "Notes to Consolidated Condensed Financial Statements" is incorporated herein by reference.

**Item 1A. Risk Factors.**

A description of factors that could materially affect our business, financial condition or operating results is included under "Factors that Could Affect Future Results" in "Management's Discussion and Analysis of Financial Condition and Results of Operations," contained in Item 2 of Part I of this report. This description includes any material changes to the risk factor disclosure in Item 1A of Part I of our 2010 Annual Report on Form 10-K and is incorporated herein by reference.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.****Recent Sales of Unregistered Securities**

There were no unregistered sales of equity securities during the period covered by this report.

**Issuer Purchases of Equity Securities**

| Period                                 | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased under the Plans or Programs |
|--|----------------------------------|------------------------------|--|--|
| In thousands, except per share amounts |                                  |                              |  |  |
| <b>Month #1</b>                        |                                  |                              |  |  |
| (November 2010)                        | 23,893                           | \$ 42.91                     | 23,893   | \$ 9,887,091   |
| <b>Month #2</b>                        |                                  |                              |  |  |
| (December 2010)                        | 23,347                           | \$ 42.10                     | 23,347   | \$ 8,904,197   |
| <b>Month #3</b>                        |                                  |                              |  |  |
| (January 2011)                         | 6,323                            | \$ 44.67                     | 6,323  | \$ 8,621,762   |
| <b>Total</b>                           | <b>53,563</b>                    | <b>\$ 42.76</b>              | <b>53,563</b>  |  |

HP repurchased shares in the first quarter of fiscal 2011 under an ongoing program to manage the dilution created by shares issued under employee stock plans as well as to repurchase shares opportunistically. This program, which does not have a specific expiration date, authorizes repurchases in the open market or in private transactions. All shares repurchased in the first quarter of fiscal 2011 were purchased in open market transactions. As of January 31, 2011, HP had remaining authorization of \$8.6 billion for future share repurchases.

**Item 6. Exhibits.**

The Exhibit Index beginning on page 84 of this report sets forth a list of exhibits.

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HEWLETT-PACKARD COMPANY

/s/ CATHERINE A. LESJAK

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Catherine A. Lesjak  
*Executive Vice President and Chief Financial Officer*  
*(Principal Financial Officer and Authorized Signatory)*

Date: March 10, 2011

**HEWLETT-PACKARD COMPANY AND SUBSIDIARIES**  
**EXHIBIT INDEX**

| Exhibit<br>Number | Exhibit Description   | Form | Incorporated by Reference |                          | Filing Date          |
|-------------------|---|------|---------------------------|--------------------------|----------------------|
|                   |   |      | File No.                  | Exhibit(s)               |                      |
| 3(a)              | Registrant's Certificate of Incorporation.  | 10-Q | 001-04423                 | 3(a)                     | June 12, 1998        |
| 3(b)              | Registrant's Amendment to the Certificate of Incorporation.   | 10-Q | 001-04423                 | 3(b)                     | March 16,<br>2001    |
| 3(c)              | Registrant's Amended and Restated By-Laws effective January 21, 2011.   |      |                           |                          |                      |
| 4(a)              | Form of Senior Indenture.   | S-3  | 333-30786                 | 4.1                      | March 17,<br>2000    |
| 4(b)              | Form of Registrant's Fixed Rate Note and Floating Rate Note and related Officers' Certificate.  | 8-K  | 001-04423                 | 4.1, 4.2 and<br>4.4      | May 24, 2001         |
| 4(c)              | Form of Registrant's 6.50% Global Note due July 1, 2012, and form of related Officers' Certificate.   | 8-K  | 001-04423                 | 4.2 and 4.3              | June 27, 2002        |
| 4(d)              | Form of Registrant's Fixed Rate Note and form of Floating Rate Note.  | 8-K  | 001-04423                 | 4.1 and 4.2              | December 11,<br>2002 |
| 4(e)              | Indenture, dated as of June 1, 2000, between the Registrant and J.P. Morgan Trust Company, National Association (formerly Chase Manhattan Bank), as Trustee.                                      | S-3  | 333-134327                | 4.9                      | June 7, 2006         |
| 4(f)              | Form of Registrant's Floating Rate Global Note due March 1, 2012, form of 5.25% Global Note due March 1, 2012 and form of 5.40% Global Note due March 1, 2017.                                    | 8-K  | 001-04423                 | 4.1, 4.2 and<br>4.3      | February 28,<br>2007 |
| 4(g)              | Form of Registrant's Floating Rate Global Note due September 3, 2009, 4.50% Global Note due March 1, 2013 and 5.50% Global Note due March 1, 2018.  | 8-K  | 001-04423                 | 4.1, 4.2 and<br>4.3      | February 29,<br>2008 |
| 4(h)              | Form of Registrant's 6.125% Global Note due March 1, 2014 and form of related Officers' Certificate.  | 8-K  | 001-04423                 | 4.1 and 4.2              | December 8,<br>2008  |
| 4(i)              | Form of Registrant's Floating Rate Global Note due February 24, 2011, 4.250% Global Note due February 24, 2012 and 4.750% Global Note due June 2, 2014 and form of related Officers' Certificate. | 8-K  | 001-04423                 | 4.1, 4.2, 4.3<br>and 4.4 | February 27,<br>2009 |

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| Exhibit Number | Exhibit Description  | Form  | Incorporated by Reference File No. | Exhibit(s)            | Filing Date        |
|----------------|--|-------|------------------------------------|-----------------------|--------------------|
| 4(j)           | Form of Registrant's Floating Rate Global Note due May 27, 2011, 2.25% Global Note due May 27, 2011 and 2.95% Global Note due August 15, 2012 and form of related Officers' Certificate.                   | 8-K   | 001-04423                          | 4.1, 4.2, 4.3 and 4.4 | May 28, 2009       |
| 4(k)           | Form of Registrant's Floating Rate Global Note due September 13, 2012, 1.250% Global Note due September 13, 2013, and 2.125% Global Note due September 13, 2015 and form of related Officers' Certificate. | 8-K   | 001-04423                          | 4.1, 4.2, 4.3 and 4.4 | September 13, 2010 |
| 4(l)           | Form of Registrant's 2.200% Global Note due December 1, 2015 and 3.750% Global Note due December 1, 2020 and form of related Officers' Certificate.  | 8-K   | 001-04423                          | 4.1, 4.2 and 4.3      | December 2, 2010   |
| 4(m)           | Speciman certificate for the Registrant's common stock.  | 8-A/A | 001-04423                          | 4.1                   | June 23, 2006      |
| 9              | None.  |       |                                    |                       |                    |
| 10(a)          | Registrant's 2004 Stock Incentive Plan.*   | S-8   | 333-114253                         | 4.1                   | April 7, 2004      |
| 10(b)          | Registrant's 2000 Stock Plan, amended and restated effective September 17, 2008.*  | 10-K  | 001-04423                          | 10(b)                 | December 18, 2008  |
| 10(c)          | Registrant's 1997 Director Stock Plan, amended and restated effective November 1, 2005.*   | 8-K   | 001-04423                          | 99.4                  | November 23, 2005  |
| 10(d)          | Registrant's 1995 Incentive Stock Plan, amended and restated effective May 1, 2007.*   | 10-Q  | 001-04423                          | 10(d)                 | June 8, 2007       |
| 10(e)          | Registrant's 1990 Incentive Stock Plan, amended and restated effective May 1, 2007.*   | 10-Q  | 001-04423                          | 10(e)                 | June 8, 2007       |
| 10(f)          | Compaq Computer Corporation 2001 Stock Option Plan, amended and restated effective November 21, 2002.*   | 10-K  | 001-04423                          | 10(f)                 | January 21, 2003   |
| 10(g)          | Compaq Computer Corporation 1998 Stock Option Plan, amended and restated effective November 21, 2002.*   | 10-K  | 001-04423                          | 10(g)                 | January 21, 2003   |

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| Exhibit Number | Exhibit Description  | Form | Incorporated by Reference File No. | Exhibit(s) | Filing Date        |
|----------------|--|------|------------------------------------|------------|--------------------|
| 10(h)          | Compaq Computer Corporation 1995 Equity Incentive Plan, amended and restated effective November 21, 2002.*                         | 10-K | 001-04423                          | 10(h)      | January 21, 2003   |
| 10(i)          | Compaq Computer Corporation 1989 Equity Incentive Plan, amended and restated effective November 21, 2002.*                         | 10-K | 001-04423                          | 10(i)      | January 21, 2003   |
| 10(j)          | Compaq Computer Corporation 1985 Nonqualified Stock Option Plan for Non-Employee Directors.*                                       | S-3  | 333-86378                          | 10.5       | April 18, 2002     |
| 10(k)          | Amendment of Compaq Computer Corporation Non-Qualified Stock Option Plan for Non-Employee Directors, effective September 3, 2001.* | S-3  | 333-86378                          | 10.11      | April 18, 2002     |
| 10(l)          | Compaq Computer Corporation 1998 Former Nonemployee Replacement Option Plan.*  | S-3  | 333-86378                          | 10.9       | April 18, 2002     |
| 10(m)          | Registrant's Excess Benefit Retirement Plan, amended and restated as of January 1, 2006.*  | 8-K  | 001-04423                          | 10.2       | September 21, 2006 |
| 10(n)          | Hewlett-Packard Company Cash Account Restoration Plan, amended and restated as of January 1, 2005.*                                | 8-K  | 001-04423                          | 99.3       | November 23, 2005  |
| 10(o)          | Registrant's 2005 Pay-for-Results Plan.*   | 8-K  | 001-04423                          | 99.5       | November 23, 2005  |
| 10(p)          | Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.*                        | 8-K  | 001-04423                          | 10.1       | September 21, 2006 |
| 10(q)          | First Amendment to the Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.* | 10-Q | 001-04423                          | 10(q)      | June 8, 2007       |
| 10(r)          | Employment Agreement, dated June 9, 2005, between Registrant and R. Todd Bradley.*   | 10-Q | 001-04423                          | 10(x)      | September 8, 2005  |
| 10(s)          | Employment Agreement, dated July 11, 2005, between Registrant and Randall D. Mott.*  | 10-Q | 001-04423                          | 10(y)      | September 8, 2005  |
| 10(t)          | Registrant's Amended and Restated Severance Plan for Executive Officers.*  | 8-K  | 001-04423                          | 99.1       | July 27, 2005      |

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| <b>Exhibit Number</b> | <b>Exhibit Description</b>   | <b>Form</b> | <b>Incorporated by Reference File No.</b> | <b>Reference Exhibit(s)</b> | <b>Filing Date</b> |
|-----------------------|--|-------------|---|-----------------------------|--------------------|
| 10(u)                 | Form letter to participants in the Registrant's Pay-for-Results Plan for fiscal year 2006.*  | 10-Q        | 001-04423                                 | 10(w)                       | March 10, 2006     |
| 10(v)                 | Registrant's Executive Severance Agreement.*   | 10-Q        | 001-04423                                 | 10(u)(u)                    | June 13, 2002      |
| 10(w)                 | Registrant's Executive Officers Severance Agreement.*  | 10-Q        | 001-04423                                 | 10(v)(v)                    | June 13, 2002      |
| 10(x)                 | Form letter regarding severance offset for restricted stock and restricted units.*   | 8-K         | 001-04423                                 | 10.2                        | March 22, 2005     |
| 10(y)                 | Form of Indemnity Agreement between Compaq Computer Corporation and its executive officers.*   | 10-Q        | 001-04423                                 | 10(x)(x)                    | June 13, 2002      |
| 10(z)                 | Form of Stock Option Agreement for Registrant's 2004 Stock Incentive Plan, Registrant's 2000 Stock Plan, as amended, Registrant's 1995 Incentive Stock Plan, as amended, the Compaq Computer Corporation 2001 Stock Option Plan, as amended, the Compaq Computer Corporation 1998 Stock Option Plan, as amended, the Compaq Computer Corporation 1995 Equity Incentive Plan, as amended and the Compaq Computer Corporation 1989 Equity Incentive Plan, as amended.* | 10-Q        | 001-04423                                 | 10(a)(a)                    | June 8, 2007       |
| 10(a)(a)              | Form of Restricted Stock Agreement for Registrant's 2004 Stock Incentive Plan, Registrant's 2000 Stock Plan, as amended, and Registrant's 1995 Incentive Stock Plan, as amended.*  | 10-Q        | 001-04423                                 | 10(b)(b)                    | June 8, 2007       |
| 10(b)(b)              | Form of Restricted Stock Unit Agreement for Registrant's 2004 Stock Incentive Plan.*   | 10-Q        | 001-04423                                 | 10(c)(c)                    | June 8, 2007       |
| 10(c)(c)              | Form of Stock Option Agreement for Registrant's 1990 Incentive Stock Plan, as amended.*  | 10-K        | 001-04423                                 | 10(e)                       | January 27, 2000   |
| 10(d)(d)              | Form of Common Stock Payment Agreement and Option Agreement for Registrant's 1997 Director Stock Plan, as amended.*  | 10-Q        | 001-04423                                 | 10(j)(j)                    | March 11, 2005     |
| 10(e)(e)              | Form of Restricted Stock Grant Notice for the Compaq Computer Corporation 1989 Equity Incentive Plan.*   | 10-Q        | 001-04423                                 | 10(w)(w)                    | June 13, 2002      |

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| Exhibit Number | Exhibit Description  | Form | Incorporated by Reference File No. | Exhibit(s) | Filing Date       |
|----------------|--|------|------------------------------------|------------|-------------------|
| 10(f)(f)       | Forms of Stock Option Notice for the Compaq Computer Corporation Non-Qualified Stock Option Plan for Non-Employee Directors, as amended.*    | 10-K | 001-04423                          | 10(r)(r)   | January 14, 2005  |
| 10(g)(g)       | Form of Long-Term Performance Cash Award Agreement for Registrant's 2004 Stock Incentive Plan and Registrant's 2000 Stock Plan, as amended.* | 10-K | 001-04423                          | 10(t)(t)   | January 14, 2005  |
| 10(h)(h)       | Amendment One to the Long-Term Performance Cash Award Agreement for the 2004 Program.*   | 10-Q | 001-04423                          | 10(q)(q)   | September 8, 2005 |
| 10(i)(i)       | Form of Long-Term Performance Cash Award Agreement for the 2005 Program.*  | 10-Q | 001-04423                          | 10(r)(r)   | September 8, 2005 |
| 10(j)(j)       | Form of Long-Term Performance Cash Award Agreement.*   | 10-Q | 001-04423                          | 10(o)(o)   | March 10, 2006    |
| 10(k)(k)       | Second Amendment to the Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.*          | 10-K | 001-04423                          | 10(l)(l)   | December 18, 2007 |
| 10(l)(l)       | Form of Stock Notification and Award Agreement for awards of performance-based restricted units.*  | 8-K  | 001-04423                          | 10.1       | January 24, 2008  |
| 10(m)(m)       | Form of Agreement Regarding Confidential Information and Proprietary Developments (California).*   | 8-K  | 001-04423                          | 10.2       | January 24, 2008  |
| 10(n)(n)       | Form of Agreement Regarding Confidential Information and Proprietary Developments (Texas).*  | 10-Q | 001-04423                          | 10(o)(o)   | March 10, 2008    |
| 10(o)(o)       | Form of Restricted Stock Agreement for Registrant's 2004 Stock Incentive Plan.*  | 10-Q | 001-04423                          | 10(p)(p)   | March 10, 2008    |
| 10(p)(p)       | Form of Restricted Stock Unit Agreement for Registrant's 2004 Stock Incentive Plan.*   | 10-Q | 001-04423                          | 10(q)(q)   | March 10, 2008    |
| 10(q)(q)       | Form of Stock Option Agreement for Registrant's 2004 Stock Incentive Plan.*  | 10-Q | 001-04423                          | 10(r)(r)   | March 10, 2008    |
| 10(r)(r)       | Form of Special Performance-Based Cash Incentive Notification Letter.*   | 8-K  | 001-04423                          | 10.1       | May 20, 2008      |
| 10(s)(s)       | Form of Option Agreement for Registrant's 2000 Stock Plan.*  | 10-Q | 001-04423                          | 10(t)(t)   | June 6, 2008      |

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| <b>Exhibit Number</b> | <b>Exhibit Description</b>  | <b>Form</b> | <b>Incorporated by Reference File No.</b> | <b>Exhibit(s)</b> | <b>Filing Date</b> |
|-----------------------|---|-------------|---|-------------------|--------------------|
| 10(t)(t)              | Form of Common Stock Payment Agreement for Registrant's 2000 Stock Plan.*   | 10-Q        | 001-04423                                 | 10(u)(u)          | June 6, 2008       |
| 10(u)(u)              | Third Amendment to the Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.*  | 10-K        | 001-04423                                 | 10(v)(v)          | December 18, 2008  |
| 10(v)(v)              | Form of Stock Notification and Award Agreement for awards of restricted stock units.*   | 10-K        | 001-04423                                 | 10(w)(w)          | December 18, 2008  |
| 10(w)(w)              | Form of Stock Notification and Award Agreement for awards of performance-based restricted units.*                                   | 10-K        | 001-04423                                 | 10(x)(x)          | December 18, 2008  |
| 10(x)(x)              | Form of Stock Notification and Award Agreement for awards of non-qualified stock options.*  | 10-K        | 001-04423                                 | 10(y)(y)          | December 18, 2008  |
| 10(y)(y)              | Form of Stock Notification and Award Agreement for awards of restricted stock.*   | 10-K        | 001-04423                                 | 10(z)(z)          | December 18, 2008  |
| 10(z)(z)              | Form of Restricted Stock Unit Agreement for Registrant's 2004 Stock Incentive Plan.*  | 10-Q        | 001-04423                                 | 10(a)(a)(a)       | March 10, 2009     |
| 10(a)(a)(a)           | First Amendment to the Hewlett-Packard Company Excess Benefit Retirement Plan.*   | 10-Q        | 001-04423                                 | 10(b)(b)(b)       | March 10, 2009     |
| 10(b)(b)(b)           | Fourth Amendment to the Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.* | 10-Q        | 001-04423                                 | 10(c)(c)(c)       | June 5, 2009       |
| 10(c)(c)(c)           | Fifth Amendment to the Registrant's 2005 Executive Deferred Compensation Plan, as amended and restated effective October 1, 2006.*  | 10-Q        | 001-04423                                 | 10(d)(d)(d)       | September 4, 2009  |
| 10(d)(d)(d)           | Amended and Restated Hewlett-Packard Company 2004 Stock Incentive Plan.*  | 8-K         | 001-04423                                 | 10.2              | March 23, 2010     |
| 10(e)(e)(e)           | Employment Agreement, dated September 29, 2010, between the Registrant and Léo Apotheker.*  | 8-K         | 001-04423                                 | 10.1              | October 1, 2010    |
| 10(f)(f)(f)           | Form of Stock Notification and Award Agreement for awards of restricted stock units.*   | 10-K        | 001-04423                                 | 10(f)(f)(f)       | December 15, 2010  |
| 10(g)(g)(g)           | Form of Stock Notification and Award Agreement for awards of performance-based restricted units.*                                   | 10-K        | 001-04423                                 | 10(g)(g)(g)       | December 15, 2010  |

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| Exhibit Number | Exhibit Description  | Form | Incorporated by Reference File No. | Exhibit(s)  | Filing Date       |
|----------------|--|------|------------------------------------|-------------|-------------------|
| 10(h)(h)(h)    | Form of Stock Notification and Award Agreement for awards of restricted stock.*  | 10-K | 001-04423                          | 10(h)(h)(h) | December 15, 2010 |
| 10(i)(i)(i)    | Form of Stock Notification and Award Agreement for awards of non-qualified stock options.*   | 10-K | 001-04423                          | 10(i)(i)(i) | December 15, 2010 |
| 10(j)(j)(j)    | Form of Agreement Regarding Confidential Information and Proprietary Developments (California new hires).*   | 10-K | 001-04423                          | 10(j)(j)(j) | December 15, 2010 |
| 10(k)(k)(k)    | Form of Agreement Regarding Confidential Information and Proprietary Developments (California current employees).*   | 10-K | 001-04423                          | 10(k)(k)(k) | December 15, 2010 |
| 10(l)(l)(l)    | Letter Agreement, dated December 15, 2010, between the Registrant and Catherine A. Lesjak.*  | 10-K | 001-04423                          | 10(l)(l)(l) | December 15, 2010 |
| 11             | None.  |      |                                    |             |                   |
| 12             | Statement of Computation of Ratio of Earnings to Fixed Charges.  |      |                                    |             |                   |
| 15             | None.  |      |                                    |             |                   |
| 18-19          | None.  |      |                                    |             |                   |
| 22-24          | None.  |      |                                    |             |                   |
| 31.1           | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.                             |      |                                    |             |                   |
| 31.2           | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.                             |      |                                    |             |                   |
| 32             | Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |      |                                    |             |                   |
| 101.INS        | XBRL Instance Document.§   |      |                                    |             |                   |
| 101.SCH        | XBRL Taxonomy Extension Schema Document.§  |      |                                    |             |                   |
| 101.CAL        | XBRL Taxonomy Extension Calculation Linkbase Document.§  |      |                                    |             |                   |
| 101.DEF        | XBRL Taxonomy Extension Definition Linkbase Document.§   |      |                                    |             |                   |

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| <b>Exhibit Number</b> | <b>Exhibit Description</b>                               | <b>Form</b> | <b>Incorporated by Reference</b> |                   | <b>Filing Date</b> |
|-----------------------|--|-------------|----------------------------------|-------------------|--------------------|
|                       |  |             | <b>File No.</b>                  | <b>Exhibit(s)</b> |                    |
| 101.LAB               | XBRL Taxonomy Extension Label Linkbase Document.§        |             |                                  |                   |                    |
| 101.PRE               | XBRL Taxonomy Extension Presentation Linkbase Document.§ |             |                                  |                   |                    |

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\*  
Indicates management contract or compensatory plan, contract or arrangement.

Filed herewith.

Furnished herewith.

§  
Furnished herewith. In accordance with Rule 406T of Regulation S-T, the information in these exhibits shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to liability under that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as expressly set forth by specific reference in such filing.

The registrant agrees to furnish to the Commission supplementally upon request a copy of (1) any instrument with respect to long-term debt not filed herewith as to which the total amount of securities authorized thereunder does not exceed 10 percent of the total assets of the registrant and its subsidiaries on a consolidated basis and (2) any omitted schedules to any material plan of acquisition, disposition or reorganization set forth above.

QuickLinks

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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SIGNATURE

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES EXHIBIT INDEX