HEWLETT PACKARD CO
Form 10-Q
September 09, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: July 31, 2010

Or

o **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)

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 ý No o

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 ý No o

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

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

The number of shares of HP common stock outstanding as of August 31, 2010 was 2,267,742,673 shares.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES
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Forward-Looking Statements

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, tax provisions, earnings, 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 the execution of cost reduction programs and restructuring plans; any statements concerning expected development, performance or market share relating to products or services; any statements regarding future economic conditions or 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 macroeconomic and geopolitical trends and events; the execution and performance of contracts by HP and its customers, suppliers and partners; the challenge of managing asset levels, including inventory; the difficulty of aligning expense levels with revenue changes; 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, 2009. 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 July 31		Nine months ended July 31	
	2010	**2009**	**2010**	**2009**
	In millions, except per share amounts			
Net revenue:				
Products	$ 20,547	$ 17,693	$ 62,120	$ 53,740
Services	10,078	9,796	30,317	29,760
Financing income	104	96	318	275
Total net revenue	30,729	27,585	92,755	83,775
Costs and expenses:				
Cost of products	15,730	13,598	47,936	41,127
Cost of services	7,597	7,352	22,902	22,671
Financing interest	75	81	227	251
Research and development	742	667	2,145	2,115
Selling, general and administrative	3,154	2,874	9,150	8,647
Amortization of purchased intangible assets	383	379	1,060	1,171
In-process research and development charges				6
Restructuring charges	598	362	909	602
Acquisition-related charges	127	59	242	182
Total operating expenses	28,406	25,372	84,571	76,772
Earnings from operations	2,323	2,213	8,184	7,003
Interest and other, net	(134)	(177)	(424)	(589)
Earnings before taxes	2,189	2,036	7,760	6,414
Provision for taxes	416	365	1,537	1,166
Net earnings	$ 1,773	$ 1,671	$ 6,223	$ 5,248
Net earnings per share:				
Basic	$ 0.76	$ 0.70	$ 2.66	$ 2.19
Diluted	$ 0.75	$ 0.69	$ 2.60	$ 2.15
Cash dividends declared per share	$ 0.16	$ 0.16	$ 0.32	$ 0.32
Weighted-average shares used to compute net earnings per share:				
Basic	2,322	2,382	2,342	2,395

Diluted	2,376	2,436	2,398	2,442

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

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Consolidated Condensed Balance Sheets

	July 31, 2010	October 31, 2009
	In millions, except par value	
	(Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 14,718	$ 13,279
Short-term investments	5	55
Accounts receivable	15,621	16,537
Financing receivables	2,799	2,675
Inventory	7,206	6,128
Other current assets	14,016	13,865
Total current assets	54,365	52,539
Property, plant and equipment	11,477	11,262
Long-term financing receivables and other assets	11,681	11,289
Goodwill	35,409	33,109
Purchased intangible assets	7,085	6,600
Total assets	$ 120,017	$ 114,799
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable and short-term borrowings	$ 7,842	$ 1,850
Accounts payable	14,885	14,809
Employee compensation and benefits	3,703	4,071
Taxes on earnings	947	910
Deferred revenue	6,583	6,182
Accrued restructuring	985	1,109
Other accrued liabilities	14,343	14,072
Total current liabilities	49,288	43,003
Long-term debt	12,204	13,980
Other liabilities	15,690	17,052(1)
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; 2,296 and 2,365 shares issued and outstanding, respectively)	23	24
Additional paid-in capital	13,668	13,804
Retained earnings	31,784	29,936
Accumulated other comprehensive loss	(2,940)	(3,247)
Total HP stockholders' equity	42,535	40,517
Noncontrolling interests	300	247(1)

Total stockholders' equity		42,835		40,764
Total liabilities and stockholders' equity	$	120,017	$	114,799

(1) Reflects the adoption of the accounting standard related to the presentation of noncontrolling interests in consolidated financial statements.

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)

	Nine months ended July 31 2010	Nine months ended July 31 2009
	In millions	
Cash flows from operating activities:		
Net earnings	$ 6,223	$ 5,248
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	3,556	3,546
Stock-based compensation expense	547	501
Provision for doubtful accounts accounts and financing receivables	122	273
Provision for inventory	127	189
In-process research and development charges		6
Restructuring charges	909	602
Deferred taxes on earnings	(191)	272
Excess tax benefit from stock-based compensation	(283)	(67)
Other, net	193	47
Changes in operating assets and liabilities:		
Accounts and financing receivables	845	1,635
Inventory	(981)	1,843
Accounts payable	(128)	(2,228)
Taxes on earnings	641	826
Restructuring	(1,053)	(844)
Other assets and liabilities	(1,756)	(1,903)
Net cash provided by operating activities	8,771	9,946
Cash flows from investing activities:		
Investment in property, plant and equipment	(2,901)	(2,749)
Proceeds from sale of property, plant and equipment	353	401
Purchases of available-for-sale securities and other investments	(50)	(105)
Maturities and sales of available-for-sale securities and other investments	197	103
Payments made in connection with business acquisitions, net	(4,017)	(348)
Proceeds from business divestiture, net	125	
Net cash used in investing activities	(6,293)	(2,698)
Cash flows from financing activities:		
Issuance (payments) of commercial paper and notes payable, net	4,993	(6,866)
Issuance of debt	121	6,778
Payment of debt	(1,274)	(1,181)
Issuance of common stock under employee stock plans	2,507	936
Repurchase of common stock	(7,079)	(3,038)
Excess tax benefit from stock-based compensation	283	67
Dividends	(590)	(576)
Net cash used in financing activities	(1,039)	(3,880)

Increase in cash and cash equivalents		1,439		3,368
Cash and cash equivalents at beginning of period		13,279		10,153
Cash and cash equivalents at end of period	$	14,718	$	13,521
Supplemental schedule of non-cash investing and financing activities:				
Issuance of common stock and stock awards assumed in business acquisitions	$	62	$	(3)
Purchase of assets under financing arrangement	$		$	283
Purchase of assets under capital lease	$	105	$	74

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 and Changes in Significant Accounting Policies

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 July 31, 2010, its results of operations for the three and nine months ended July 31, 2010 and 2009 and its cash flows for the nine months ended July 31, 2010 and 2009. The Consolidated Condensed Balance Sheet as of October 31, 2009 is derived from the October 31, 2009 audited consolidated financial statements. Certain reclassifications have been made to prior-period amounts in order to conform to the current period presentation.

The results of operations for the three and nine months ended July 31, 2010 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, 2009.

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.

Accounting Pronouncements

The following disclosure on accounting pronouncements includes those that may apply to the historical financial statements.

In December 2007, the Financial Accounting Standards Board ("FASB") issued a new accounting standard related to business combinations that expands the definition of a "business" and a "business combination"; requires recognition of assets acquired, liabilities assumed, and contingent consideration at their fair value on the acquisition date and through the defined measurement period with subsequent changes recognized in earnings; requires acquisition-related expenses and restructuring costs to be recognized separately from the business combination and expensed as incurred; requires in-process research and development ("IPR&D") to be capitalized initially at fair value as an indefinite-lived intangible asset; and requires that changes in accounting for deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period be recognized as a component of provision for taxes. The standard also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. In November 2008, the FASB issued a new accounting standard related to defensive intangible assets. Defensive intangible assets are acquired intangible assets that the acquirer does not intend to actively use but intends to hold to prevent its competitors from obtaining access to them. Under this standard, defensive intangible assets must be initially recognized at fair value and amortized over the benefit period. In April 2009, the FASB issued an accounting standard which clarified the accounting for pre-acquisition contingencies. HP adopted all of these standards in the first quarter of fiscal 2010. The impact of these standards depends on the size and nature of the business combinations completed after the effective date.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 1: Basis of Presentation and Changes in Significant Accounting Policies (Continued)

In December 2007, the FASB issued a new accounting standard related to noncontrolling interests. The standard establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interests, changes in a parent's ownership interest, and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The standard also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. In January 2010, the FASB issued Accounting Standards Update No. 2010-02, "Consolidation: Accounting and Reporting for Decreases in Ownership of a Subsidiary a Scope Clarification." This update clarifies the scope of the decrease in ownership provisions and also requires expanded disclosures. HP adopted these standards in the first quarter of fiscal 2010 with retrospective application of the presentation and disclosure requirements. Noncontrolling interests of $247 million at October 31, 2009 were reclassified from Other liabilities to Stockholders' equity in the Consolidated Condensed Balance Sheet as of October 31, 2009. Income attributable to noncontrolling interests was immaterial for the three and nine months ended July 31, 2010 and July 31, 2009.

In June 2008, the FASB issued a new accounting standard that clarifies when instruments granted in share-based payment transactions should be included in computing earnings per share ("EPS"). Under the new standard, companies are required to include unvested share-based payment awards that contain non-forfeitable rights to receive dividends in their calculation of EPS and are required to calculate EPS using the "two-class method." The two-class method of computing EPS is an earnings allocation formula that determines EPS for each class of common stock and participating securities according to dividends declared (or accumulated) and participation rights in undistributed earnings. HP adopted this new accounting standard on a retrospective basis in the first quarter of fiscal 2010. The adoption did not have a material impact on EPS for the three and nine months ended July 31, 2010 and July 31, 2009.

Note 2: Stock-Based Compensation

HP's stock-based compensation plans include incentive compensation plans and an employee stock purchase plan. Incentive compensation plans include principal equity plans as well as various equity plans assumed through acquisitions. Principal equity plans include performance-based restricted units ("PRU"), stock options and restricted stock awards.

Total stock-based compensation expense before income taxes for the three and nine months ended July 31, 2010 was $166 million and $547 million, respectively. The resulting income tax benefit for the three and nine months ended July 31, 2010 was $54 million and $176 million, respectively. Total stock-based compensation expense before income taxes for the three and nine months ended July 31, 2009 was $150 million and $501 million, respectively. The resulting income tax benefit for the three and nine months ended July 31, 2009 was $51 million and $158 million, respectively.

Performance-based Restricted Units

In fiscal 2008, HP implemented a program that provides for the issuance of PRUs representing hypothetical shares of HP common stock. Under the PRU program, HP annually awards a target number of units at the beginning of each three-year performance period. The number of shares released at the end of the performance period will range from zero to two times the target number

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

depending on performance during the period. 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. 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 PRU share using the 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:

	Nine months ended July 31	
	2010	**2009**
Weighted-average fair value of grants per share	$ 57.13(1)	$ 40.56(2)
Expected volatility(3)	38%	35%
Risk-free interest rate	0.73%	1.34%
Dividend yield	0.64%	0.88%
Expected life in months	22	30

(1) 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 fiscal 2010. The estimated fair value of a target share for the third year for PRUs granted in fiscal 2009 and for the second and third years for PRUs granted in fiscal 2010 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 second year of the three-year performance period applicable to PRUs granted in fiscal 2008 and for the first year of the three-year performance period applicable to PRUs granted in fiscal 2009.

(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 July 31, 2010 and changes during the nine months ended July 31, 2010 were as follows:

	Shares (in thousands)
Outstanding at October 31, 2009	24,723
Granted	7,388
Vested	
Change in units due to performance and market conditions	(4,409)
Forfeited	(1,541)
Outstanding at July 31, 2010	26,161
Outstanding PRUs assigned a fair value at July 31, 2010	17,382[(1)]

(1) Excludes target shares for the third year for PRUs granted in fiscal 2009 and for the second and third years for PRUs granted in fiscal 2010 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 July 31, 2010, there was $362 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 1.3 years.

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 July 31		Nine months ended July 31	
	2010	2009	2010	2009
Weighted-average fair value of grants per share[(1)]	$ 13.66	$ 11.57	$ 14.04	$ 12.89
Implied volatility	32%	36%	29%	45%
Risk-free interest rate	1.96%	2.43%	2.29%	2.01%
Dividend yield	0.69%	0.91%	0.64%	0.95%
Expected life in months	60	61	61	61

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

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

Option activity as of July 31, 2010 and changes during the nine months ended July 31, 2010 were as follows:

	Shares (in thousands)	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Outstanding at October 31, 2009	233,214	$ 33		
Granted and assumed through acquisitions	3,068	$ 43		
Exercised	(70,693)	$ 34		
Forfeited/cancelled/expired	(23,234)	$ 55		
Outstanding at July 31, 2010	142,355	$ 29	2.5	$ 2,498
Vested and expected to vest at July 31, 2010	141,313	$ 29	2.5	$ 2,493
Exercisable at July 31, 2010	132,312	$ 28	2.3	$ 2,452

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 July 31, 2010. The aggregate intrinsic value is the difference between HP's closing stock price on the last trading day of the third quarter of fiscal 2010 and the exercise price, multiplied by the number of in-the-money options. Total intrinsic value of options exercised for the three months and nine months ended July 31, 2010 was $0.1 billion and $1.2 billion, respectively.

At July 31, 2010, there was $95 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 1.4 years.

Restricted Stock Awards

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

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 2: Stock-Based Compensation (Continued)

Non-vested restricted stock awards as of July 31, 2010 and changes during the nine months ended July 31, 2010 were as follows:

	Shares (in thousands)	Weighted-Average Grant Date Fair Value Per Share
Outstanding at October 31, 2009	6,864	$ 44
Granted and assumed through acquisitions	3,293	$ 51
Vested	(4,699)	$ 45
Forfeited	(482)	$ 46
Outstanding at July 31, 2010	4,976	$ 47

At July 31, 2010, there was $133 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 1.4 years.

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, restricted stock units, and restricted stock.

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

	Three months ended July 31		Nine months ended July 31	
	2010	2009	2010	2009
	In millions, except per share amounts			
Numerator:				
Net earnings[(1)]	$ 1,773	$ 1,671	$ 6,223	$ 5,248
Denominator:				
Weighted-average shares used to compute basic EPS	2,322	2,382	2,342	2,395
Dilutive effect of employee stock plans	54	54	56	47
Weighted-average shares used to compute diluted EPS	2,376	2,436	2,398	2,442
Net earnings per share:				
Basic	$ 0.76	$ 0.70	$ 2.66	$ 2.19
Diluted	$ 0.75	$ 0.69	$ 2.60	$ 2.15

(1) Net earnings available to participating securities were not significant for the three and nine months ended July 31, 2010 and 2009. HP considers restricted stock that provides the holder with a non-forfeitable right to receive dividends to be a participating security.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 3: Net Earnings Per Share (Continued)

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. For the three and nine months ended July 31, 2010, HP excluded from the calculation of diluted EPS options to purchase 8 million shares and 5 million shares, respectively, compared to 96 million shares and 100 million shares, respectively, in the prior-year comparable periods. HP also excluded from the calculation of diluted EPS options to purchase an additional 2 million shares and 3 million shares in the third quarter and the first nine months of fiscal 2010, respectively, compared to an additional 2 million shares in the prior-year comparable periods, 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.

As discussed in Note 2, HP implemented the PRU program in fiscal 2008. Accordingly, for the three and nine months ended July 31, 2010, HP has included 9 million shares and 8 million shares, respectively, underlying the PRU awards granted in fiscal 2009 and 2008 when calculating diluted EPS as those shares became contingently issuable upon the satisfaction of the cash flow from operations condition with respect to the first year of the three-year performance period applicable to the fiscal 2009 awards and the first and second years of the three-year performance period applicable to the fiscal 2008 awards. HP has excluded all other shares underlying the fiscal 2010, 2009 and 2008 PRU awards when calculating diluted EPS as those shares are not contingently issuable. For the three and nine months ended July 31, 2009, HP has included 4 million shares and 3 million shares, respectively, underlying the PRU awards granted in fiscal 2008 when calculating diluted EPS as those shares became contingently issuable upon the satisfaction of the cash flow from operations condition with respect to the first year of the three-year performance period applicable to the fiscal 2008 awards. HP has excluded all other shares underlying the fiscal 2009 and 2008 PRU awards when calculating diluted EPS as those shares were not contingently issuable.

Note 4: Balance Sheet Details

Balance sheet details were as follows:

Accounts and Financing Receivables

	July 31, 2010	October 31, 2009
	In millions	
Accounts receivable	$ 16,157	$ 17,166
Allowance for doubtful accounts	(536)	(629)
	$ 15,621	$ 16,537
Financing receivables	$ 2,855	$ 2,723
Allowance for doubtful accounts	(56)	(48)
	$ 2,799	$ 2,675

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

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 4: Balance Sheet Details (Continued)

$493 million as of July 31, 2010. HP sold $1.3 billion of trade receivables during the first nine months of fiscal 2010. As of July 31, 2010, HP had $209 million available under these programs.

Inventory

	July 31, 2010	October 31, 2009
	In millions	
Finished goods	$ 4,887	$ 4,092
Purchased parts and fabricated assemblies	2,319	2,036
	$ 7,206	$ 6,128

Property, Plant and Equipment

	July 31, 2010	October 31, 2009
	In millions	
Land	$ 529	$ 513
Buildings and leasehold improvements	8,252	7,472
Machinery and equipment	13,652	12,959
	22,433	20,944
Accumulated depreciation	(10,956)	(9,682)
	$ 11,477	$ 11,262

Note 5: Acquisitions

In fiscal 2010, HP adopted a new accounting standard related to business combinations. HP has included the results of operations of the businesses that it acquired in fiscal 2010 in HP's consolidated results as of the respective dates of acquisitions. HP allocates the purchase price of its acquisitions to the tangible assets, liabilities and intangible assets acquired, including IPR&D, based on their estimated fair values. The excess of the purchase price over those fair values is recorded as goodwill. IPR&D is initially capitalized at fair value as an intangible asset with an indefinite life and assessed for impairment thereafter. When the IPR&D project is complete, it is reclassified as an amortizable purchased intangible asset and is amortized over its estimated useful life. If an IPR&D project is abandoned, HP will record a charge for the value of the related intangible asset to HP's Consolidated Statement of Earnings in the period it is abandoned. Acquisition-related expenses and restructuring costs are recognized separately from the business combination and are expensed as incurred.

In the first nine months of fiscal 2010, HP completed seven acquisitions. The purchase price allocation for these acquisitions as set forth in the table below reflects various preliminary fair value estimates and analyses, including preliminary work performed by third-party valuation specialists, which are subject to change within the measurement period as valuations are finalized. The primary areas of the preliminary purchase price allocations that are not yet finalized relate to the fair values of certain tangible assets and liabilities acquired, the valuation of intangible assets acquired, certain legal matters, income and non-income based taxes and residual goodwill. We expect to continue to obtain information

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 5: Acquisitions (Continued)

to assist us in determining the fair value of the net assets acquired at the acquisition date during the measurement period. Measurement period adjustments that HP determines to be material will be applied retrospectively to the period of acquisition in HP's consolidated financial statements and, depending on the nature of the adjustments, other periods subsequent to the period of acquisition could also be affected.

Pro forma results of operations for these acquisitions have not been presented because they are not material to HP's consolidated results of operations, either individually or in the aggregate. Goodwill, which represents the excess of the purchase price over the net tangible and intangible assets acquired, is not deductible for tax purposes.

	In millions
Net assets	$ 1,380
Amortizable intangible assets	1,377
In-process research and development	186
Goodwill	2,217
Total purchase price	$ 5,160

Acquisition of 3Com Corporation ("3Com")

On April 12, 2010, HP completed its acquisition of 3Com, a global enterprise provider of networking switching, routing and security solutions, at a price of $7.90 per share in cash. HP reports the financial results of the 3Com business in the Corporate Investments segment. The aggregate purchase price of $3.3 billion consisted of cash paid for outstanding common stock, vested in-the-money stock awards and the estimated fair value of earned unvested stock awards assumed by HP. In connection with this acquisition, HP recorded approximately $1.3 billion of goodwill, amortizable purchased intangible assets of $987 million and IPR&D assets of $106 million. HP is amortizing the purchased intangible assets on a straight-line basis over an estimated weighted-average life of 5.1 years.

Acquisition of Palm, Inc. ("Palm")

On July 1, 2010, HP completed the acquisition of Palm, a provider of smartphones powered by the Palm webOS mobile operating systems. HP reports the financial results of the Palm business in the Corporate Investments segment. The aggregate purchase price was $1.8 billion, which included cash paid for common stock, vested-in-the-money stock awards, the estimated fair value of earned unvested stock awards assumed as well as certain debt that was repaid at the acquisition date. In connection with this acquisition, HP recorded approximately $917 million of goodwill, amortizable purchased intangible assets of $344 million and IPR&D assets of $80 million. HP is amortizing the purchased intangible assets on a straight-line basis over an estimated weighted-average life of 6.2 years.

Pending Acquisition

On September 2, 2010, HP entered into a definitive agreement to acquire 3PAR Inc., a provider of utility storage, through a cash tender offer of $33.00 per share or an enterprise value of approximately

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 5: Acquisitions (Continued)

$2.3 billion. The transaction is subject to customary closing conditions and is expected to be completed by the end of the calendar year.

Note 6: Goodwill and Purchased Intangible Assets

Goodwill

Goodwill allocated to HP's business segments as of July 31, 2010 and changes in the carrying amount of goodwill for the nine months ended July 31, 2010 are as follows:

	Services	Enterprise Storage and Servers	HP Software	Personal Systems Group	Imaging and Printing Group	HP Financial Services	Corporate Investments	Total
	In millions							
Balance at October 31, 2009	$ 16,829	$ 5,005	$ 6,140	$ 2,487	$ 2,460	$ 144	$ 44	$ 33,109
Goodwill acquired during the period				18			2,199	2,217
Goodwill adjustments	124	(30)	(2)	(5)	(4)			83
Balance at July 31, 2010	$ 16,953	$ 4,975	$ 6,138	$ 2,500	$ 2,456	$ 144	$ 2,243	$ 35,409

During the first nine months of fiscal 2010, HP recorded approximately $2.2 billion of goodwill related to acquisitions based on its preliminary purchase price allocations. HP recorded goodwill adjustments primarily related to an increase to the deferred tax liability on outside basis differences of Electronic Data Systems Corporation ("EDS") foreign subsidiaries at acquisition. The increase to goodwill was partially offset by adjustments to goodwill primarily for tax adjustments related to tax deductible stock-based awards for certain acquisitions for which the acquisition date preceded the effective date of the new accounting standard for business combinations.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 6: Goodwill and Purchased Intangible Assets (Continued)

Purchased Intangible Assets

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

	July 31, 2010			October 31, 2009		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
	In millions					
Customer contracts, customer lists and distribution agreements	$ 7,191	$ (3,643)	$ 3,548	$ 6,763	$ (3,034)	$ 3,729
Developed and core technology and patents	5,040	(3,187)	1,853	4,171	(2,747)	1,424
Product trademarks	310	(233)	77	247	(222)	25
Total amortizable purchased intangible assets	12,541	(7,063)	5,478	11,181	(6,003)	5,178
IPR&D	185		185			
Compaq trade name	1,422		1,422	1,422		1,422
Total purchased intangible assets	$ 14,148	$ (7,063)	$ 7,085	$ 12,603	$ (6,003)	$ 6,600

During the first nine months of fiscal 2010, HP recorded approximately $1.6 billion of purchased intangible assets related to acquisitions based on its preliminary purchase price allocations.

Under the revised accounting standard adopted in the first quarter of fiscal 2010, IPR&D is initially capitalized at fair value as an intangible asset with an indefinite life and assessed for impairment thereafter. When the IPR&D project is complete, it is reclassified as an amortizable purchased intangible asset and is amortized over its estimated useful life. If an IPR&D project is abandoned, HP will record a charge for the value of the related intangible asset to HP's Consolidated Statement of Earnings in the period it is abandoned.

Estimated future amortization expense related to finite-lived purchased intangible assets at July 31, 2010 is as follows:

Fiscal year:	In millions
2010 (remaining 3 months)	$ 395
2011	1,326
2012	1,121
2013	984
2014	647
2015	530
Thereafter	475
Total	$ 5,478

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 7: Restructuring Charges

Fiscal 2010 Acquisitions

On July 1, 2010, HP completed the acquisition of Palm. In connection with the acquisition, HP's management approved and initiated a $40 million plan to restructure the operations of Palm, including severance for Palm employees, contract cancellation costs and other items. HP recorded restructuring charges of approximately $40 million for the three months ended July 31, 2010. No further restructuring charges are anticipated, subject to changes in the Palm integration plan. HP expects the majority of these costs to be paid out by the fourth quarter of fiscal 2010.

On April 12, 2010, HP completed the acquisition of 3Com. In connection with the acquisition, HP's management approved and initiated a $39 million plan to restructure the operation of 3Com, including severance costs and costs to vacate duplicative facilities. HP expects to record the majority of the 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.

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 is approximately $1 billion, including severance costs to eliminate approximately 9,000 positions and infrastructure charges. For the three and nine months ended July 31, 2010, a restructuring charge of $520 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 main 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 July 31, 2010, approximately 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 Enterprise Storage and Servers ("ESS") businesses. The total expected cost of the plan is $303 million in severance-related costs associated with the planned elimination of approximately 5,000 positions. As of July 31, 2010, approximately 3,900 positions have been eliminated. HP expects a majority of the remaining positions to be eliminated and a majority of the restructuring costs to be paid out through the fourth quarter of fiscal 2010.

Fiscal 2008 HP/EDS Restructuring Plan

In connection with the acquisition of EDS on August 26, 2008, HP's management approved and initiated a restructuring plan to streamline the combined company's services business and to better align the structure and efficiency of that business with HP's operating model. The restructuring plan is

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 7: Restructuring Charges (Continued)

expected to be implemented over four years from the acquisition date and includes changes to the combined company's workforce as well as changes to corporate overhead functions such as real estate and information technology ("IT").

The total expected cost of this restructuring plan is $3.1 billion, consisting mainly of severance costs to eliminate approximately 25,000 positions, costs to vacate duplicative facilities and costs associated with early termination of certain contractual obligations. As of July 31, 2010, the vast majority of the positions had been eliminated. In future quarters, as part of this action, HP expects to record charges of approximately $333 million related to the cost to vacate duplicative facilities.

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.

Summary of Restructuring Plans

The adjustments to the accrued restructuring expenses related to all of HP's restructuring plans described above for the nine months ended July 31, 2010 were as follows:

							As of July 31, 2010	
	Balance, October 31, 2009	Three months ended July 31, 2010 charges	Nine months ended July 31, 2010 charges	Cash payments	Non-cash settlements and other adjustments	Balance, July 31, 2010	Total costs and adjustments to date	Total expected costs and adjustments
	In millions							
Fiscal 2010 acquisitions	$	$ 42	$ 57	$ (3)	$	$ 54	$ 57	$ 79
Fiscal 2010 ES Plan:								
Severance	$	$ 509	$ 509	$ (5)	$ 22	$ 526	$ 509	$ 761
Infrastructure		11	11		(11)		11	231
Total ES Plan	$	$ 520	$ 520	$ (5)	$ 11	$ 526	$ 520	$ 992
Fiscal 2009 Plan	$ 248	$	$ 4	$ (150)	$ (12)	$ 90	$ 303	$ 303
Fiscal 2008 HP/EDS Plan:								
Severance	$ 747	$	$ 226	$ (789)	$ (43)	$ 141	$ 2,136	$ 2,136
Infrastructure	419	36	102	(89)	(20)	412	602	935
Total HP/EDS Plan	$ 1,166	$ 36	$ 328	$ (878)	$ (63)	$ 553	$ 2,738	$ 3,071
Total restructuring plans	$ 1,414	$ 598	$ 909	$ (1,036)	$ (64)	$ 1,223	$ 3,618	$ 4,445

At July 31, 2010 and October 31, 2009, HP had $30 million and $51 million, respectively, of restructuring liabilities associated with previous restructuring actions that are complete but have cash payouts anticipated to occur through 2012. For the nine months ended July 31, 2010, cash payouts of $17 million and other adjustments of $4 million were recorded against these liabilities.

At July 31, 2010 and October 31, 2009, HP included the long-term portion of the restructuring liability of $268 million and $356 million, respectively, in Other liabilities, and the short-term portion in Accrued restructuring in the accompanying Consolidated Condensed Balance

Sheets.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 8: Fair Value

HP adopted the provisions related to the fair value of nonfinancial assets and nonfinancial liabilities in the first quarter of fiscal 2010 for the following major categories of nonfinancial items from the Consolidated Condensed Balance Sheet: Property, plant and equipment; Goodwill; Purchased intangible assets; Accrued restructuring; and the asset retirement obligations within Other accrued liabilities and Other liabilities. The provisions of the accounting standard related to measuring fair value and related disclosures are applied to nonfinancial assets and nonfinancial liabilities whenever they are required to be measured at fair value, such as when accounting for a business combination, when evaluating and/or determining impairment, or in accordance with certain other accounting pronouncements. Except for assets and liabilities acquired in business combinations as discussed in Note 5, HP did not measure any material nonfinancial assets and nonfinancial liabilities at fair value on a non-recurring basis for the three and nine months ended July 31, 2010.

Except for the provisions noted above, the accounting standard relating to fair value measurements and disclosures became effective for HP since the beginning of fiscal 2009. This standard establishes a new framework for measuring fair value and expands related disclosures. The framework requires fair value to be determined 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.

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

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.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 8: Fair Value (Continued)

Derivative Instruments: As discussed in Note 9, 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 July 31, 2010				As of October 31, 2009			
	Fair Value Measured Using				Fair Value Measured Using			
	Level 1	Level 2	Level 3	Total Balance	Level 1	Level 2	Level 3	Total Balance
	In millions							
Assets								
Time deposits	$	$ 9,363	$	$ 9,363	$	$ 8,925	$	$ 8,925
Commercial paper		1,774		1,774		1,388		1,388
Money market funds	763			763	262			262
U.S. Treasury securities	3			3	5			5
Marketable equity securities	9	3		12	7	3		10
Foreign bonds	7	342		349	10	367		377
Corporate bonds and other debt securities		7	48	55		5	36	41
Derivatives:								
Interest rate contracts		652		652		375		375
Foreign exchange contracts		416	61	477		379	1	380
Other derivatives		17	4	21		1		1
Total Assets	$ 782	$ 12,574	$ 113	$ 13,469	$ 284	$ 11,443	$ 37	$ 11,764
Liabilities								
Derivatives:								
Interest rate contracts	$	$ 81	$	$ 81	$	$ 51	$	$ 51
Foreign exchange contracts		531	17	548		720	1	721
Other derivatives						2		2
	$	$ 612	$ 17	$ 629	$	$ 773	$ 1	$ 774

Total Liabilities

The following table presents the changes in Level 3 instruments for the nine months ended July 31, 2010 that are measured at fair value on a recurring basis. The majority of the Level 3 balances

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 8: Fair Value (Continued)

consist of investment securities classified as available-for-sale with changes in fair value recorded in other comprehensive income ("OCI").

	Fair Value Measured Using Significant Unobservable Inputs (Level 3)		
Nine months ended July 31, 2010	**Other Debt Securities**	**Derivative Instruments**	**Total**
	In millions		
Beginning balance at November 1, 2009	$ 36	$	$ 36
Total (losses) gains (realized/unrealized):			
Included in earnings[1]	(8)		(8)
Included in OCI	12	62	74
Purchases, issuances, and settlements	8	(14)	(6)
Ending balance at July 31, 2010	$ 48	$ 48	$ 96
The amount of total losses for the period included in earnings attributable to the change in unrealized losses relating to assets still held as of July 31, 2010	$ (8)	$	$ (8)

(1) Included in Interest and other, net in the accompanying Consolidated Condensed Statements of Earnings.

The changes in Level 3 instruments for the three months ended July 31, 2010 that were measured at fair value on a recurring basis resulted in a total loss of $5 million. The loss for the period was included in earnings attributable to the changes in unrealized losses relating to assets still held as of July 31, 2010.

The changes in Level 3 instruments for the three months ended July 31, 2009 that were measured at fair value on a recurring basis did not result in any gain or loss. The changes in Level 3 instruments for the nine months ended July 31, 2009 that were measured at fair value on a recurring basis resulted in a total loss of $3 million. The losses for the periods were included in earnings attributable to the changes in unrealized losses relating to assets still held as of July 31, 2009.

HP measures certain assets including cost and equity method investments at fair value on a non-recurring basis. These assets are recognized at fair value when they are deemed to be other-than-temporarily impaired. In both the three and nine months ended July 31, 2010, HP recorded an impairment charge of $1 million. In the three and nine months ended July 31, 2009, HP recorded an impairment charge of $3 million and $4 million, respectively.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments

Cash Equivalents and Available-for-Sale Investments

Cash equivalents and available-for-sale investments at fair value as of July 31, 2010 and October 31, 2009 were as follows:

	July 31, 2010				October 31, 2009			
	Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value	Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
	In millions							
Cash Equivalents								
Time deposits	$ 9,356	$	$	$ 9,356	$ 8,870	$	$	$ 8,870
Commercial paper	1,774			1,774	1,388			1,388
Money market funds	763			763	262			262
Total cash equivalents	11,893			11,893	10,520			10,520
Available-for-Sale Investments								
Debt securities:								
Time deposits	7			7	55			55
U.S. Treasury securities	3			3	5			5
Foreign bonds	295	54		349	329	49		378
Corporate bonds and other debt securities	87		(32)	55	85		(45)	40
Total debt securities	392	54	(32)	414	474	49	(45)	478
Equity securities in public companies	5	2		7	3	2		5
Total cash equivalents and available-for-sale investments	$ 12,290	$ 56	$ (32)	$ 12,314	$ 10,997	$ 51	$ (45)	$ 11,003

Cash equivalents consist of investments with original maturities of ninety days or less. 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 July 31, 2010 was due primarily to declines in the fair value of certain debt securities and included $30 million that has been in a continuous loss position for more than twelve months. The gross unrealized loss as of October 31, 2009 was due primarily to declines in the fair value of certain debt securities and included $20 million that had 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. In the three and nine months ended July 31, 2010, HP recognized an impairment charge of $6 million and $8 million, respectively, on total investments. In the three and nine months ended July 31, 2009, HP recognized an impairment charge of $4 million and $6 million, respectively, on total investments.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

Contractual maturities of short-term and long-term investments in available-for-sale debt securities at July 31, 2010 were as follows:

	July 31, 2010	
	Cost	Estimated Fair Value
	In millions	
Due in less than one year	$ 5	$ 5
Due in 1-5 years	21	21
Due in more than five years	366	388
	$ 392	$ 414

Proceeds from sales and maturities of available-for-sale and other securities were $94 million and $197 million in the three and nine months ended July 31, 2010, respectively. There were $1 million and $8 million of gross realized gains on total investments in the three and nine months ended July 31, 2010, respectively. There were no sales or maturities of available-for-sale and other securities for the three months ended July 31, 2009. Proceeds from sales or maturities of available-for-sale and other securities were $103 million for the nine months ended July 31, 2009. There were no realized gains or losses on available-for-sale and other securities for the three and nine months ended July 31, 2009. The specific identification method is used to account for gains and losses on available-for-sale securities.

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 July 31, 2010 and October 31, 2009 was as follows:

	July 31, 2010	October 31, 2009
	In millions	
Time deposits	$	$ 55
Available-for-sale debt securities	5	
Short-term investments	5	55
Time deposits	7	
Available-for-sale debt securities	402	423
Available-for-sale equity securities	7	5
Equity securities in privately-held companies	164	129
Other investments	9	13
Included in long-term financing receivables and other assets	589	570
Total investments	$ 594	$ 625

Equity securities in privately held companies include cost basis and equity method investments. Other investments include marketable trading securities held to generate returns that HP expects to offset changes in certain liabilities related to deferred compensation arrangements. 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. There were no net losses or gains associated with these securities for the three months ended July 31, 2010. The net losses associated with these securities were $5 million for the nine months ended July 31, 2010.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

The net losses associated with these securities were $4 million and $11 million for the three and nine months ended July 31, 2009, respectively.

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. HP 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 hedges"). Additionally, for derivatives not designated as hedging instruments, HP categorizes those economic hedges as other derivatives. HP recognizes all derivatives 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 a counterparty, which reduces the maximum loss from credit risk in the event of counterparty default.

Certain of HP's derivative instruments contain credit-risk-related contingent features, such as a provision 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 rating falls below certain thresholds. As of July 31, 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

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

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 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 nine months ended July 31, 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 9: 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 July 31, 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 and nine months ended July 31, 2010.

Fair Value of Derivative Instruments in the Consolidated Condensed Balance Sheets

As discussed in Note 8, 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 July 31, 2010					As of October 31, 2009				
	Gross Notional[(1)]	Other Current Assets	Long-term Financing Receivables and Other Assets	Other Accrued Liabilities	Other Liabilities	Gross Notional[(1)]	Other Current Assets	Long-term Financing Receivables and Other Assets	Other Accrued Liabilities	Other Liabilities
	In millions									
Derivatives designated as hedging instruments										
Fair value hedges:										
Interest rate contracts	$ 8,575	$	$ 583	$	$	$ 7,575	$	$ 346	$	$ 5
Cash flow hedges:										
Foreign exchange contracts	15,148	313	53	235	34	15,056	116	12	389	33
Net investment hedges:										
Foreign exchange contracts	1,454	17	7	40	34	1,350	13	12	47	39
Total derivatives designated as hedging instruments	25,177	330	643	275	68	23,981	129	370	436	77
Derivatives not designated as hedging instruments										
Foreign exchange contracts	10,725	70	17	170	35	16,104	206	20	163	51
Interest rate contracts[(2)]	2,200		69		81	2,211		29		45
Other derivatives	362	17	4			268	2		2	
Total derivatives not designated as hedging instruments	13,287	87	90	170	116	18,583	208	49	165	96

Total derivatives	$ 38,464	$ 417	$ 733	$ 445	$ 184	$ 42,564	$ 337	$ 419	$ 601	$ 173

(1) Represents the face amounts of contracts that were outstanding as of July 31, 2010 and October 31, 2009, respectively.

(2) Represents offsetting swaps acquired through previous business combination that were not designated as hedging instruments.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: 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 and nine months ended July 31, 2010 and July 31, 2009 was as follows:

Gain (Loss) Recognized in Income on Derivative and Related Hedged Item							
Derivative Instrument	Location	Three months ended July 31, 2010	Nine months ended July 31, 2010	Hedged Item	Location	Three months ended July 31, 2010	Nine months ended July 31, 2010
		In millions				In millions	
Interest rate contracts	Interest and other, net	$ 215	$ 242	Fixed-rate debt	Interest and other, net	$ (206)	$ (230)

Gain (Loss) Recognized in Income on Derivative and Related Hedged Item							
Derivative Instrument	Location	Three months ended July 31, 2009	Nine months ended July 31, 2009	Hedged Item	Location	Three months ended July 31, 2009	Nine months ended July 31, 2009
		In millions				In millions	
Interest rate contracts	Interest and other, net	$ (94)	$ 155	Fixed-rate debt	Interest and other, net	$ 91	$ (161)

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

The before-tax effect of derivative instruments in cash flow and net investment hedging relationships for the three and nine months ended July 31, 2010 and July 31, 2009 was as follows:

	Gain (Loss) Recognized in OCI on Derivative (Effective Portion)		Gain (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion)			Gain Recognized in Income on Derivative[(1)] (Ineffective Portion and Amount Excluded from Effectiveness Testing)		
	Three months ended July 31, 2010	Nine months ended July 31, 2010	Location	Three months ended July 31, 2010	Nine months ended July 31, 2010	Location	Three months ended July 31, 2010	Nine months ended July 31, 2010
	In millions			In millions			In millions	
Cash flow hedges:								
Foreign exchange contracts	$ 114	$ 769	Net revenue	$ 375	$ 433	Net revenue	$	$
Foreign exchange contracts	45	38	Cost of products	17	44	Cost of products		
Foreign exchange contracts	(1)	(1)	Other operating expenses	(1)		Other operating expenses		
Foreign exchange contracts	11	12	Interest and other, net			Interest and other, net		
Foreign exchange contracts	(26)	10	Net revenue	5	20	Interest and other, net	1	7
Total cash flow hedges	$ 143	$ 828		$ 396	$ 497		$ 1	$ 7
Net investment hedges:								
Foreign exchange contracts	$ 25	$ (19)	Interest and other, net	$	$	Interest and other, net	$	$

(1) Amount of gain recognized in income on derivative represents a $1 million gain and $7 million gain related to the amount excluded from the assessment of hedge effectiveness in the three and nine months ended July 31, 2010, respectively.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

	Gain (Loss) Recognized in OCI on Derivative (Effective Portion)		Gain (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion)			Gain Recognized in Income on Derivative[1] (Ineffective Portion and Amount Excluded from Effectiveness Testing)		
	Three months ended July 31, 2009	Nine months ended July 31, 2009	Location	Three months ended July 31, 2009	Nine months ended July 31, 2009	Location	Three months ended July 31, 2009	Nine months ended July 31, 2009
	In millions			In millions			In millions	
Cash flow hedges:								
Foreign exchange contracts	$ (612)	$ (743)	Net revenue	$ (162)	$ 713	Net revenue	$	$
Foreign exchange contracts	38	72	Cost of products	43	124	Cost of products		
Foreign exchange contracts	5	(4)	Other operating expenses	(1)	(5)	Other operating expenses		
Foreign exchange contracts	(5)	(6)	Interest and other, net	(2)	(4)	Interest and other, net		
Foreign exchange contracts	14	19	Net revenue	2	7	Interest and other, net	2	4
Total cash flow hedges	$ (560)	$ (662)		$ (120)	$ 835		$ 2	$ 4
Net investment hedges:								
Foreign exchange contracts	$ (96)	$ (127)	Interest and other, net	$	$	Interest and other, net	$	$

(1) Amount of gain recognized in income on derivative represents a $2 million gain and a $4 million gain related to the amount excluded from the assessment of hedge effectiveness in the three and nine months ended July 31, 2009, respectively.

HP expects to reclassify an estimated net accumulated other comprehensive gain of $42 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.

HEWLETT-PACKARD COMPANY AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements (Continued)

(Unaudited)

Note 9: Financial Instruments (Continued)

The before-tax effect of derivative instruments not designated as hedging instruments on the Consolidated Condensed Statements of Earnings for the three and nine months ended July 31, 2010 and July 31, 2009 was as follows:

	Gain (Loss) Recognized in Income on Derivative		
	Location	Three months ended July 31, 2010	Nine months ended July 31, 2010
		In millions	
Foreign exchange contracts	Interest and other, net	$ (142)	$ (205)
Other derivatives	Interest and other, net	15	17
Interest rate contracts	Interest and other, net		5
Total		$ (127)	$ (183)

Gain (Loss) Recognized in Income on Derivative		
Location	Three months ended July 31, 2009	Nine months ended July 31, 2009