Financial Statement

Dell Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Dell–through its direct business model–designs, develops, manufactures, markets, sells, and supports a wide range of computer systems and services that are customized to customer requirements. These include enterprise systems (servers, storage, workstations, and networking products), client systems (notebook and desktop computer systems), printing and imaging systems, software and peripherals, and global services. Dell markets and sells its products and services directly to its customers, which include large corporate, government, healthcare, and education accounts, as well as small-to-medium businesses and individual customers. Dell conducts operations worldwide and is managed in three geographic segments: the Americas, Europe, and Asia Pacific–Japan regions. Within the Americas, Dell is further segmented into Business and U.S. Consumer.

The following table summarizes Dell's consolidated results of operations for each of the past three fiscal years:

	FISCAL YEAR ENDED				
(dollars in millions)	January 28, 2005	Percentage Change	January 30, 2004	Percentage Change	January 31, 2003
Net revenue	$49,205	19%	$41,444	17%	$35,404
Gross margin	$ 9,015	19%	$ 7,552	19%	$ 6,349
% of net revenue	18.3%		18.2%		17.9%
Operating expenses	$ 4,761	19%	$ 4,008	14%	$ 3,505
% of net revenue	9.7%		9.7%		9.9%
Operating income	$ 4,254	20%	$ 3,544	25%	$ 2,844
% of net revenue	8.6%		8.6%		8.0%
Tax provision before repatriation charge	$ 1,122		$ 1,079		$ 905
% of income before income taxes	25.2%		29.0%		29.9%
Tax repatriation charge	$ 280		$ —		$ —
% of Income before income taxes	6.3%		—		—
Income tax provision	$ 1,402		$ 1,079		$ 905
% of Income before income taxes	31.5%		29.0%		29.9%
Net income	$ 3,043	15%	$ 2,645	25%	$ 2,122
% of net revenue	6.2%		6.4%		6.0%

During fiscal 2005, Dell maintained its position as the world's number one supplier of personal computer systems with performance that continued to outpace the industry. Dell's consolidated net unit shipments increased 21% as the company increased its

share of worldwide personal computer sales by 1.1 percentage points during the calendar year to 17.8%. Consolidated net revenue increased 19% to $49.2 billion during fiscal 2005, with Dell's strong international performance being a key driver of this growth even as the company expanded its number one position in the U.S. During fiscal 2005, component costs continued to decline at a moderate pace that was relatively comparable to fiscal 2004. Dell utilized these cost declines to pass on cost savings to its customers and improve gross profit margin to 18.3% for the year. Dell's focus on balancing growth and profitability resulted in record operating and net income of $4.3 billion and $3.0 billion, respectively. Net income for fiscal 2005 includes a tax repatriation charge of $280 million pursuant to a favorable tax incentive provided by the American Jobs Creation Act of 2004. This tax charge is related to Dell's decision to repatriate $4.1 billion in foreign earnings. Dell's efficient direct business model and cash conversion cycle have allowed the company to generate annual cash flows from operating activities that typically exceed net income. During fiscal 2005, Dell continued to deliver strong liquidity with record operating cash flow of $5.3 billion and ended the year with record cash and investments of $14.1 billion.

Dell's objective is to maximize stockholder value while maintaining a balance of three key financial metrics: liquidity, profitability, and growth. Dell's strategy combines its direct business model with a highly efficient manufacturing and supply chain management organization and an emphasis on standards-based technologies. Dell's business model provides the company with a constant flow of information about trends in customers' plans and requirements. These trends have shown an increased use of standards-based technologies as well as a push towards standardization of services. Unlike proprietary technologies promoted by some of Dell's top competitors, standards-based technologies provide customers with flexibility and choice while allowing their purchasing decisions to be based on performance, cost, and customer service. Dell's business strategy continues to focus on the company's enterprise business and expanding its capabilities in that product group. Dell is also expanding into consumer electronics products such as plasma televisions while maintaining its leadership position in desktops and notebooks. Dell's superior execution in all product and service offerings has been demonstrated by progress in customer satisfaction ratings during the year, which is a key performance metric for the company.

Management believes that growth opportunities exist for Dell as the use of standards-based technologies becomes more prevalent and the company increases its presence in existing geographical regions, expands into new regions, and pursues additional product and service opportunities. During the year, Dell opened new facilities in the U.S., Canada, India, and El Salvador and expects to continue its global expansion in years ahead. Dell's investment in international growth opportunities contributed to an increase in Dell's non-U.S. revenue, as a percentage of consolidated net revenue, from 36% in fiscal 2004 to 38% during fiscal 2005.

While the current competitive environment continues to be challenging, management believes that there has been a steady improvement in business technology spending since the end of fiscal 2004. Management expects that the competitive pricing environment will continue to be challenging, and expects to continue to reduce its pricing as necessary in response to future competitive and economic conditions. Management is also focused on attracting and retaining key personnel as well as further investing in

the company's global information technology infrastructure in order to address challenges that may arise with Dell's rapid global growth and the increased complexity of the company's product and service offerings.

Results of Operations

Net Revenue

During fiscal 2005, Dell's strategy and execution extended the company's number one worldwide position for the calendar year. Dell produced net revenue of $49.2 billion in fiscal 2005, compared to $41.4 billion in fiscal 2004 and $35.4 billion in fiscal 2003. The year-over-year increases in net revenue during both fiscal 2005 and 2004 were driven by strong unit growth across most regions and product lines. Specifically, Dell's Europe and Asia Pacific–Japan segments produced revenue growth in excess of 25% during fiscal 2005, while notebooks produced consolidated revenue growth of 24%. During fiscal 2005, Dell's net unit growth continued to exceed industry growth as consolidated net unit shipments increased 21% while total PC industry growth increased only 15% for the calendar year. During fiscal 2004, Dell produced net unit growth of 26%, while the total PC industry increased only 12% for the calendar year.

During fiscal 2005, management continued to focus on Dell's enterprise business. Net revenue for enterprise systems increased 16% and 31% during fiscal 2005 and 2004, respectively, with fiscal 2005 growth being led by 18% server growth. Dell gained 1.5 share percentage points in shipments of x86 servers (based on standard Intel architecture) and improved its number two position to 24.8% for calendar 2004. Dell's four-year running partnership with EMC Corporation, and management's continued focus on mid-range Dell/EMC storage area network ("SAN") products, produced year-over-year Clariion revenue growth of 41% during fiscal 2005. However, total external storage revenue growth of 16% during fiscal 2005 was lower than fiscal 2004 growth of 58%. The higher growth rate during fiscal 2004 was due, in part, to the relatively low base of storage revenue in fiscal 2003. In addition, the fiscal 2005 growth rate declined due to a planned product shift associated with Dell's increased focus on scaling its mid-range SAN business. This product shift included the launch of the Dell/EMC AX100 storage array during the second quarter of fiscal 2005 to meet demand for smaller business enterprises.

In client systems, Dell continues to capitalize on the growth of mobile computing with notebooks producing net unit growth in excess of 30% during both fiscal 2005 and 2004. This net unit growth was partially offset by a 9% decline in average revenue per-unit sold during fiscal 2005, producing net revenue growth for notebooks of 24% in this highly competitive space. During fiscal 2004, average revenue per-unit sold for notebooks decreased by 13%. Dell's notebook products continue to carry higher growth rates than desktops as consumer trends continue to shift more toward mobile computing. Dell's desktop product group produced net unit and revenue growth of 17% during fiscal 2005. During fiscal 2004, desktops delivered net unit and revenue growth of 23% and 11%, respectively.

Dell continues to expand its service offerings with revenue growth for enhanced services of 35% and 37% during fiscal 2005 and 2004, respectively. In addition, software and peripherals, which includes Dell's printing and imaging business that was launched in early fiscal 2004, continued to contribute to Dell's core business with fiscal 2005 and 2004 revenue growth of 35% and 27%, respectively. The growth of Dell's printing and imaging business has been particularly strong with over five million Dell-branded printers shipped during fiscal 2005.

The following table summarizes Dell's net revenue and annual share of personal computer sales by reportable segment for each of the past three fiscal years:

	FISCAL YEAR ENDED				
(dollars in millions)	January 28, 2005	Change	January 30, 2004	Change	January 31, 2003
Net Revenue					
Americas					
Business	$25,339	16%	$21,888	13%	$19,394
U.S. Consumer	7,601	13%	6,715	19%	5,653
Total Americas	32,940	15%	28,603	14%	25,047
Europe	10,787	27%	8,495	23%	6,912
Asia Pacific–Japan	5,478	26%	4,346	26%	3,445
Total net revenue	$49,205	19%	$41,444	17%	$35,404
Annual Share of Personal Computer Sales[a]					
Americas	29.1%	1.4	27.7%	2.9	24.8%
Europe	11.7%	1.2	10.5%	0.9	9.6%
Asia Pacific–Japan	8.3%	1.1	7.2%	1.4	5.8%
Worldwide	17.8%	1.1	16.7%	1.7	15.0%

[a] Represents personal computer units for the full calendar year and is based upon information provided by IDC.

Americas. Dell increased its number one share position in personal computers sales in the Americas region by 1.4 percentage points to 29.1% during calendar 2004. Net unit growth was 17% during fiscal 2005, compared to 23% in fiscal 2004, while net revenue increased 15% and 14% during fiscal 2005 and 2004, respectively. Notebooks led the fiscal 2005 revenue growth, supported by an improvement in corporate spending during the year. Fiscal 2004 revenue growth was broad-based, but primarily led by growth in enterprise systems of 28%.

In the Americas Business segment, which includes sales to small and medium businesses, government, and corporate accounts, net revenue increased 16% and 13% during fiscal 2005 and 2004, respectively, as business technology spending steadily improved since the end of fiscal 2004. Specifically, Dell's small and medium business customers led the revenue growth during fiscal 2005 while notebook systems provided about one-third of the revenue growth for the segment. Enterprise revenue growth during fiscal 2005 was 11%, with servers providing the majority of the product group growth. Enterprise systems provided the majority of the growth in Dell's Americas Business segment during fiscal 2004, with servers contributing more than one-half of the increase during that fiscal year.

Dell's U.S. Consumer segment includes sales primarily to individual consumers. Net revenue grew 13% and 19% during fiscal 2005 and 2004, respectively, and was led by Dell's printing and imaging products during fiscal 2005. The decrease in revenue growth during fiscal 2005, compared to fiscal 2004, was partially due to relatively weak demand in the overall U.S. consumer segment toward the second half of fiscal 2005. Dell produced strong net unit growth in consumer notebooks of 29% during fiscal 2005; however, this growth was partially offset by an 11% decline in average revenue per-unit

sold as product mix continued to shift toward lower-priced products. Revenue growth during fiscal 2004 was led by notebooks with net unit growth of 67%.

Europe. Dell produced strong performance in Europe, which includes the Middle East and Africa, maintaining its number two share position of personal computer sales with 11.7% share during calendar 2004, compared to 10.5% during calendar 2003. Net unit shipments grew at a rate of 31% during fiscal 2005 in a market that grew at a robust rate of 19% during calendar year 2004. The appreciation of the Euro and British Pound helped stimulate overall market demand in Europe, as Dell and other companies generally passed on these foreign currency benefits to customers through lower pricing of products and services. Net revenue during fiscal 2005 and 2004 increased by 27% and 23%, respectively. Revenue during fiscal 2005 included combined net revenue growth of 30% in the United Kingdom and France. Dell's enterprise business produced revenue growth of 29% and 35% during fiscal 2005 and 2004, respectively.

Asia Pacific–Japan. Dell's strong revenue growth in Asia Pacific–Japan of 26% during fiscal 2005 was supported by the company's strength and demand growth in China. During calendar 2004, Dell generated share gains in Asia Pacific–Japan of 1.1 percentage points to 8.3% share of personal computer sales, achieving the number three share position. During fiscal 2005, Dell's net unit growth was 29%, in an industry with overall growth that increased only 13%. Dell's enterprise business produced revenue growth of 23% and 32% during fiscal 2005 and 2004, respectively.

For additional information regarding Dell's segments, see Note 9 of "Notes to Consolidated Financial Statements" included in "Item 8–Financial Statements and Supp1ementary Data."

Gross Margin

Gross margin as a percentage of net revenue improved slightly to 18.3% during fiscal 2005, compared to 18.2% in fiscal 2004 and 17.9% in fiscal 2003. The year-over-year improvement during fiscal 2005 and 2004 was primarily driven by Dell's continued cost savings initiatives. During fiscal 2005, component costs continued to decline at a moderate pace that was relatively comparable to fiscal 2004. Management utilized these cost declines to balance profitable growth while passing on cost savings to its customers. Management expects the component cost environment to continue to be favorable during the first quarter of fiscal 2006. As part of management's focus on improving margins, Dell remains committed to reducing costs through four primary cost reduction initiatives: manufacturing costs, warranty costs, structural or design costs, and overhead or operating expenses. These cost savings initiatives also include providing certain customer technical support and back-office functions from cost effective locations as well as driving more efficient processes and tools globally. Dell's general practice is to aggressively pass on declines in costs to its customers in order to add customer value while increasing global market share. Management believes that the strength of Dell's direct business model, as well as its strong liquidity position, makes Dell better positioned than its competitors to continue profitable growth in any business climate.

Operating Expenses

The following table presents information regarding Dell's operating expenses during each of the past three fiscal years:

(dollars in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Operating Expenses			
Selling, general, and administrative	$4,298	$3,544	$3,050
Research, development, and engineering	463	464	455
Total operating expenses	$4,761	$4,008	$3,505
Operating Expenses as a percentage of net revenue:			
Selling, general, and administrative	8.7%	8.6%	8.6%
Research, development, and engineering	0.9	1.1	1.3
Total operating expenses	9.7%	9.7%	9.9%

Selling, General, and Administrative. During fiscal 2005, selling, general, and administrative expenses, as a percentage of net revenue, increased slightly compared to fiscal 2004 and 2003. This increase is primarily due to Dell's global expansion efforts and a greater mix of business outside the U.S. during fiscal 2005, which typically carries a slightly higher operating expense. The primary component of the overall increase is compensation costs as management focuses on attracting and retaining key personnel in order to support the company's growth. Selling, general, and administrative expenses as a percentage of net revenue remained relatively flat in fiscal 2004 compared to fiscal 2003, but increased in absolute dollars commensurate with the increase in net revenue.

Research, Development, and Engineering. During fiscal 2005, research, development, and engineering expenses continued to decrease slightly, as a percentage of net revenue, compared to fiscal 2004 and 2003. The efficiencies are a result of Dell's continued utilization of its streamlined infrastructure and strategic relationships with its vendor partners. Dell expects to continue to invest in research, development, and engineering activity to develop and introduce new products and has received 1,128 U.S. patents and has 719 U.S. patent applications pending as of January 28, 2005.

Investment and Other Income, Net

The following table summarizes Dell's investment and other income, net for each of the past three fiscal years:

(in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Investment income, primarily interest	$226	$200	$227
Gains (losses) on investments, net	6	16	(6)
Interest expense	(16)	(14)	(17)
Other	(25)	(22)	(21)
Investment and other income, net	$191	$180	$183

Investment income increased from fiscal 2004 to fiscal 2005 primarily due to an increase in investment income earned on higher average balances of cash equivalents and investments. Investment income decreased from fiscal 2003 to fiscal 2004 primarily from

a decline in interest rates on investments, which was partially offset by an increase in cash equivalents and investments during the year.

Income Taxes

Dell's reported effective tax rate was 31.5% in fiscal 2005, compared to 29.0% for fiscal 2004 and 29.9% for fiscal 2003. The fiscal 2005 effective tax rate includes a tax repatriation charge of $280 million pursuant to a favorable tax incentive provided by the American Jobs Creation Act of 2004 (the "Act"), which was signed into law on October 22, 2004. This tax repatriation charge increased Dell's effective tax rate by 6.3% for fiscal 2005. The increase in Dell's fiscal 2005 effective tax rate, compared to fiscal 2004 and fiscal 2003, is due to the aforementioned tax repatriation charge, partially offset by a higher proportion of operating profits attributable to foreign jurisdictions.

Among other items, the Act creates a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the U.S. at a tax rate of 5.25%, versus the U.S. federal statutory rate of 35%. Although the Act contains a number of limitations related to the repatriation and some uncertainty remains, as of January 28, 2005, Dell believes that it has the information necessary to make an informed decision regarding the impact of the Act on its repatriation plans. Based on this new legislation, and subsequent guidance issued by the Department of Treasury, Dell determined during the fourth quarter of fiscal 2005 that it will repatriate $4.1 billion in foreign earnings. Accordingly, Dell recognized a tax repatriation charge of $280 million in accordance with *Statement of Financial Accounting Standards ("SFAS") No.109, Accounting for Income Taxes.* This tax charge includes an amount relating to an apparent drafting oversight that Congressional leaders indicate will be fixed by a Technical Corrections Bill sometime during calendar year 2005. The fiscal 2005 tax repatriation charge will be reduced in the quarter that the Technical Corrections Bill becomes law. In addition, at the time of repatriation further adjustment may be required depending upon a number of factors, including geographic location of cash, mix of foreign earnings, and statutory tax rates in effect at the time of the repatriation. The repatriation is required to be completed by the end of fiscal 2006.

Differences between Dell's fiscal 2005 effective tax rate and the U.S. federal statutory rate of 35% principally result from Dell's geographical distribution of taxable income and losses, partially offset by the impact of the Act. During fiscal 2004 and 2003, the differences between Dell's effective and statutory tax rates were attributable to the geographic distribution of taxable income and losses. Dell's effective tax rate may decline in future periods as the company's business outside the U.S. continues to expand and contribute an increasing portion of Dell's consolidated operating profits.

Off-Balance Sheet Arrangements

Consolidation of Leasing Affiliate. Dell is currently a partner in DFS, a joint venture with CIT. The joint venture allows Dell to provide its customers with various financing alternatives while CIT generally provides the financing between DFS and the customer for certain transactions. Dell began consolidating DFS's financial results at the beginning of the third quarter of fiscal 2004 due to the adoption of Financial Accounting Standards Board ("FASB") Interpretation No. 46R ("FIN 46R"). See Note 6 of "Notes to Consolidated Financial Statements" included in "Item 8–Financial Statements and Supplementary Data."

Securitized Lending Transactions. During the third quarter of fiscal 2005, Dell and CIT executed an agreement that extended the term of the joint venture to January 29,

2010 and modified certain terms of the relationship. Prior to the execution of that agreement, CIT provided all of the financing for transactions between DFS and the customer. The extension agreement gives Dell the right, but not the obligation, to participate in such financings. During the fourth quarter of fiscal 2005, Dell began financing certain loan and lease transactions through securitized lending arrangements. Specifically, Dell began selling certain loan and lease finance receivables to an unconsolidated qualifying special purpose entity that is wholly owned by Dell. The qualifying special purpose entity is a separate legal entity with assets and liabilities separate from those of Dell. The qualifying special purpose entity has entered into a financing arrangement with a multiseller conduit that in turn issues asset-backed debt securities to the capital markets. The sale of these loan and lease financing receivables did not have a material impact on Dell's consolidated results of operations, financial position, or cash flows for fiscal 2005. Dell expects that its participation in securitized lending transactions may increase in future periods.

Master Lease Facilities. Dell historically maintained master lease facilities which provided the company with the ability to lease certain real property, buildings, and equipment to be constructed or acquired. These leases were accounted for as operating leases by Dell. During fiscal 2004, Dell paid $636 million to purchase all of the assets covered by its master lease facilities. Accordingly, the assets formerly covered by these facilities are included in Dell's consolidated statement of financial position and Dell has no remaining lease commitments under these master lease facilities.

Liquidity, Capital Commitments, and Contractual Cash Obligations

Liquidity

During fiscal 2005, Dell continued to maintain strong liquidity with cash flow from operations of $5.3 billion, compared to $3.7 billion in fiscal 2004. Dell ended fiscal 2005 with a record $14.1 billion in cash and investments, an increase of $2.2 billion over the prior fiscal year end. The following table summarizes Dell's ending cash, cash equivalents, and investments and the results of Dell's consolidated statements of cash flows for the past three fiscal years:

(in millions)	January 28, 2005	January 30, 2004	January 31, 2003
Cash, cash equivalents, and investments			
Cash and cash equivalents	$ 4,747	$ 4,317	$ 4,232
Debt securities	9,253	7,454	5,442
Equity and other securities	126	151	231
Cash, cash equivalents and investments	$14,126	$11,922	$ 9,905
Net cash flow provided by (used in)			
Operating activities	$ 5,310	$ 3,670	$ 3,538
Investing activities	(2,317)	(2,814)	(1,381)
Financing activities	(3,128)	(1,383)	(2,025)
Effect of exchange rate changes on cash and cash equivalents	565	612	459
Net increase in cash and cash equivalents	$ 430	$ 85	$ 591

Operating Activities. Cash flows from operating activities during fiscal 2005, 2004, and 2003 resulted primarily from net income, which represents Dell's principal source of cash. The increase in operating cash flows during fiscal 2005 was primarily led by an increase in operating income and the improvement in Dell's cash conversion cycle. In addition, operating cash flows have historically been impacted by income tax benefits that result from the exercise of employee stock options. These tax benefits totaled $249 million, $181 million, and $260 million in fiscal 2005, 2004, and 2003, respectively. These benefits represent corporate tax deductions (that are considered taxable income to the employee) that represent the amount by which the fair value of Dell's stock exceeds the option strike price on the day the employee exercises a stock option.

Dell's direct business model allows the company to maintain a leading asset management system in comparison to its major competitors. Dell is capable of minimizing inventory risk while collecting amounts due from customers before paying vendors, thus allowing the company to generate annual cash flows from operating activities that typically exceed net income. The following table presents the components of Dell's cash conversion cycle for each of the past three fiscal years:

	FISCAL YEAR ENDED		
	January 28, 2005	January 30, 2004	January 31, 2003
Days of sales outstanding[a]	32	31	28
Days of supply in inventory	4	3	3
Days in accounts payable	73	70	68
Cash conversion cycle	(37)	(36)	(37)

[a] Dell defers the cost of shipped products awaiting revenue recognition until the goods are delivered and revenue is recognized. Days of sales outstanding include these product costs, which are classified in other current assets. At January 28, 2005, January 30, 2004, and January 31. 2003, days of sales outstanding included days of sales in accounts receivable and days of in-transit customer shipments of 29 and 3 days; 28 and 3 days; and 24 and 4 days, respectively.

The increase in days of sales outstanding at January 28, 2005, from the end of fiscal 2004, was partially due to an increase in non-U.S. revenues where collection periods tend to be longer. Dell defers the cost of shipped products awaiting revenue recognition until the goods are delivered and revenue is recognized. These deferred costs are included in Dell's reported days of sales outstanding because management believes it illustrates a more conservative and accurate presentation of Dell's days of sales outstanding and cash conversion cycle. These deferred costs are recorded in other current assets in Dell's consolidated statement of financial position and totaled $430 million, $387 million, and $423 million as of January 28, 2005, January 30, 2004, and January 31, 2003, respectively.

Investing Activities. Cash used in investing activities during fiscal 2005 was $2.3 billion, as compared to $2.8 billion in fiscal 2004 and $1.4 billion in fiscal 2003. Cash used in investing activities principally consists of net purchases of investments and capital expenditures for property, plant, and equipment. The decrease in cash used in investing activities during fiscal 2005, compared to fiscal 2004, was primarily due to the purchase of $636 million in assets during fiscal 2004 that were held in master lease facilities and previously classified as operating leases. This was partially offset by an increase in

capital expenditures during fiscal 2005 as Dell continued to focus on investing in the company's global information technology infrastructure in order to support Dell's rapid global growth and the increased complexity of its product and service offerings. The increase in cash used in investing activities during fiscal 2004, when compared to fiscal 2003, was primarily due to the increase in purchases of investments, net of maturities and sales, as Dell continues to invest its cash provided by operating activities.

Financing Activities. Cash used in financing activities during fiscal 2005 was $3.1 billion, as compared to $1.4 billion in fiscal 2004 and $2.0 billion in fiscal 2003. Financing activities primarily consist of the repurchase of Dell common stock, partially offset by the issuance of common stock under employee stock option plans. The increase in share repurchases in fiscal 2005, compared to fiscal 2004, drove the year-over-year increase in cash used in financing activities. Dell repurchased 119 million shares during fiscal 2005, compared to 63 million in fiscal 2004. The decrease in cash used during fiscal 2004, compared to fiscal 2003, was primarily due to an increase in the number of shares issued under employee plans and an increase in the weighted average exercise price of stock options exercised. In addition, the aggregate value of common stock repurchased by Dell declined during fiscal 2004, which was primarily due to a respective decrease in the weighted average share price of common stock repurchased by Dell.

Management currently believes that Dell's fiscal 2006 cash flows from operations will continue to exceed net income and will be more than sufficient to support Dell's operations and capital requirements. Dell currently anticipates that it will continue to utilize its strong liquidity and cash flows from operations to repurchase its common stock, invest in systems and processes, invest in the growth of the company with an emphasis on enterprise products, make capital investments, and make a limited number of strategic equity investments.

Capital Commitments

Share Repurchase Program. Dell has a share repurchase program that authorizes the company to purchase shares of common stock in order to both distribute cash to stockholders and manage dilution resulting from shares issued under Dell's equity compensation plans. However, Dell does not currently have a policy that requires the repurchase of common stock in conjunction with share-based payment arrangements. As of January 28, 2005, Dell's share repurchase program authorized the purchase of up to 1.25 billion shares of common stock at an aggregate cost not to exceed $20 billion. Subsequent to fiscal 2005, on March 3, 2005, the Board of Directors of Dell approved an amendment to the plan to increase the number of authorized shares available for repurchase by 250 million to 1.5 billion, and the aggregate dollar cost threshold by $10 billion to $30 billion.

Dell expects to continue to repurchase shares of common stock through a systematic program of open market purchases. As of the end of fiscal 2005, Dell had cumulatively repurchased 1.2 billion shares for an aggregate cost of approximately $18.3 billion. During fiscal 2005, Dell repurchased 119 million shares of common stock for an aggregate cost of $4.2 billion. Through the fourth quarter of fiscal 2003, Dell previously utilized equity instrument contracts to facilitate its repurchase of common stock. All remaining put and call contracts were settled in full during the fourth quarter of fiscal 2003. Dell now effects its share repurchases entirely through open market transactions. As of March 3, 2005, Dell has spent approximately $1.3 billion in share repurchases for the first quarter of fiscal 2006.

Capital Expenditures. During fiscal 2005, Dell spent $525 million on property, plant, and equipment. Capital expenditures increased during fiscal 2005, compared to recent fiscal years, primarily due to the company's global expansion efforts and infrastructure investments in order to support the company's future growth. Product demand and mix, as well as ongoing efficiencies in operating and information technology infrastructure, influence the level and prioritization of Dell's capital expenditures. Capital expenditures for fiscal 2006 are currently expected to be up to approximately $700 million. Capital expenditures during fiscal 2006 are expected to be funded by cash flows from operating activities and are estimated to increase compared to recent years due to Dell's continued expansion worldwide and the need for additional capacity.

Restricted Cash. Pursuant to the joint venture agreement between DFS and CIT, DFS is required to maintain certain escrow cash accounts. Due to the consolidation of DFS, $438 million in restricted cash is included in other current assets on Dell's consolidated statement of financial position as of January 28, 2005.

Contractual Cash Obligations

The following table summarizes Dell's contractual cash obligations as of January 28, 2005.

	PAYMENTS DUE BY PERIOD				
(in millions)	Total	Fiscal 2006	Fiscal 2007–2008	Fiscal 2009–2010	Beyond
Long-term debt, including current portion	$ 507	$ 2	$ 3	$204	$298
Operating leases	257	52	76	46	83
Advances under credit facilities	158	29	129	—	—
Purchase obligations	107	56	23	28	—
DFS purchase commitment	100	—	—	100	—
Total contractual cash obligations	$1,129	$139	$231	$378	$381

Operating Leases. Dell leases property and equipment, manufacturing facilities, and office space under noncancellable leases. Certain of these leases obligate Dell to pay taxes, maintenance, and repair costs.

Advances under Credit Facilities. DFS maintains credit facilities with CIT which provide DFS with a funding capacity of up to $1.0 billion. Outstanding advances under these facilities totaled $158 million and are included in other current and non-current liabilities on Dell's consolidated statement of financial position as of January 28, 2005.

Long-Term Debt. As of January 28, 2005, Dell had outstanding $200 million in Senior Notes due April 15, 2008 and $300 million in Senior Debentures due April 15, 2028. For additional information regarding these issuances, see Note 2 of Notes to Consolidated Financial Statements included in "Item 8–Financial Statements and Supplementary Data."

Concurrent with the issuance of the Senior Notes and Senior Debentures, Dell entered into interest rate swap agreements converting Dell's interest rate exposure from a fixed rate to a floating rate basis to better align the associated interest rate

characteristics to its cash and investments portfolio. The interest rate swap agreements have an aggregate notional amount of $200 million maturing April 15, 2008 and $300 million maturing April 15, 2028. The floating rates are based on three-month London Interbank Offered Rates plus 0.41% and 0.79% for the Senior Notes and Senior Debentures, respectively. As a result of the interest rate swap agreements, Dell's effective interest rates for the Senior Notes and Senior Debentures were 2.059% and 2.392%, respectively, for fiscal 2005.

Purchase Obligations. Purchase obligations are defined as contractual obligations to purchase goods or services that are enforceable and legally binding on Dell and that specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum, or variable price provisions; and the approximate timing of the transaction. Purchase obligations do not include contracts that may be canceled without penalty.

Dell utilizes several suppliers to manufacture sub-assemblies for the company's products. Dell's highly efficient supply chain management allows the company to enter into flexible and mutually beneficial purchase arrangements with its suppliers in order to minimize inventory risk. Consistent with industry practice, Dell acquires raw materials or other goods and services, including product components, by issuing suppliers authorizations to purchase based on Dell's projected demand and manufacturing needs. These purchase orders are typically fulfilled within 30 days and are entered into during the ordinary course of business in order to establish best pricing and continuity of supply for Dell's production. Purchase orders are not included in the table above as they typically represent Dell's authorization to purchase rather than binding purchase obligations.

DFS Purchase Commitment. Included in the table above is Dell's minimum purchase obligation to purchase CIT's 30% interest in DFS at the expiration of the joint venture on January 29, 2010, for a purchase price ranging from $100 million to $345 million. See Note 6 of "Notes to Consolidated Financial Statements" included in "Item 8–Financial Statements and Supplementary Data."

Market Risk

Dell is exposed to a variety of risks, including foreign currency exchange rate fluctuations and changes in the market value of its investments. In the normal course of business, Dell employs established policies and procedures to manage these risks.

Foreign Currency Hedging Activities

Dell's objective in managing its exposure to foreign currency exchange rate fluctuations is to reduce the impact of adverse fluctuations on earnings and cash flows associated with foreign currency exchange rate changes. Accordingly, Dell utilizes foreign currency option contracts and forward contracts to hedge its exposure on forecasted transactions and firm commitments in most of the foreign countries in which it operates. The principal currencies hedged during fiscal 2005 were the Euro, British Pound, Japanese Yen, and Canadian Dollar. Dell monitors its foreign currency exchange exposures to ensure the overall effectiveness of its foreign currency hedge positions. However, there can be no assurance Dell's foreign currency hedging activities will substantially offset the impact of fluctuations in currency exchange rates on its results of operations and financial position.

Based on Dell's foreign currency cash flow hedge instruments outstanding at January 28, 2005 and January 30, 2004, Dell estimates a maximum potential one-day loss in fair value of approximately $43 million and $53 million, respectively, using a Value-at-Risk ("VAR") model. The VAR model estimates were made assuming normal market conditions and a 95% confidence level. Dell used a Monte Carlo simulation type model that valued its foreign currency instruments against a thousand randomly generated market price paths. Forecasted transactions, firm commitments, fair value hedge instruments, and accounts receivable and payable denominated in foreign currencies were excluded from the model. The VAR model is a risk estimation tool, and as such, is not intended to represent actual losses in fair value that will be incurred by Dell. Additionally, as Dell utilizes foreign currency instruments for hedging forecasted and firmly committed transactions, a loss in fair value for those instruments is generally offset by increases in the value of the underlying exposure. As a result of Dell's hedging activities, foreign currency fluctuations did not have a material impact on Dell's results of operations and financial position during fiscal 2005, 2004, and 2003.

Cash and Investments

At January 28, 2005, Dell had $14.1 billion of total cash and investments (including investments in equity securities discussed below), all of which are stated at fair value. Dell's investment policy is to manage its total cash and investments balances to preserve principal and liquidity while maximizing the return on the investment portfolio through the full investment of available funds. Dell diversifies its investment portfolio by investing in multiple types of investment-grade securities and through the use of third-party investment managers. Based on Dell's investment portfolio and interest rates at January 28, 2005 and January 30, 2004, a 100 basis point increase or decrease in interest rates would result in a decrease or increase of approximately $97 million and $140 million, respectively, in the fair value of the investment portfolio. Changes in interest rates may affect the fair value of the investment portfolio; however, Dell will not recognize such gains or losses unless the investments are sold.

At January 28, 2005, the fair value of investments in equity securities of privately and publicly held technology companies was $43 million. These investments were made in order to enhance and extend Dell's direct business model and core business initiatives. Because these companies are typically early-stage companies with products or services that are not yet fully developed or that have not yet achieved market acceptance, these investments are inherently risky. Dell currently anticipates that it will continue to make minimal additional investments in fiscal 2006 and will focus on managing its current investments.

Debt

Dell has entered into interest rate swap arrangements that convert its fixed interest rate expense to a floating rate basis to better align the associated interest rate characteristics to its cash and investments portfolio. The interest rate swaps qualify for hedge accounting treatment pursuant to *SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities*, as amended. Dell has designated the issuance of the Senior Notes and Senior Debentures and the related interest rate swap agreements as an integrated transaction. The difference between Dell's carrying amounts and fair value of its long-term debt and related interest rate swaps was not material at January 28, 2005 and January 30, 2004. The differential to be paid or received on the interest rate swap agreements is accrued and recognized as an adjustment to interest expense as interest rates change.

Critical Accounting Policies

Dell prepares its financial statements in conformity with generally accepted accounting principles in the United States of America ("GAAP"). The preparation of GAAP financial statements requires certain estimates, assumptions, and judgments to be made that may affect Dell's consolidated statement of financial position and results of operations. Dell believes its most critical accounting policies relate to revenue recognition, warranty accruals, and income taxes. Management has discussed the development, selection, and disclosure of its critical accounting policies with the Audit Committee of Dell's Board of Directors. These critical accounting policies and Dell's other accounting policies are described in Note 1 of "Notes to Consolidated Financial Statements" included in "Item 8–Financial Statements and Supplementary Data."

Revenue Recognition. Dell frequently enters into sales arrangements with customers that contain multiple elements or deliverables such as hardware, software, peripherals, and services. Judgments and estimates are critical to ensure compliance with GAAP. These judgments relate to the allocation of the proceeds received from an arrangement to the multiple elements, the determination of whether any undelivered elements are essential to the functionality of the delivered elements, and the appropriate timing of revenue recognition. Dell offers extended warranty and service contracts to customers that extend and/or enhance the technical support, parts, and labor coverage offered as part of the base warranty included with the product. Revenue from extended warranty and service contracts, for which Dell is obligated to perform, is recorded as deferred revenue and subsequently recognized over the term of the contract or when the service is completed. Revenue from sales of third-party extended warranty and service contracts, for which Dell is not obligated to perform, is recognized on a net basis at the time of sale.

Estimates that further impact revenue recognition relate primarily to customer sales returns and allowance for doubtful accounts. Both estimates are relatively predictable based on historical experience. The primary factors affecting Dell's accrual for estimated customer returns include estimated return rates as well as the number of units shipped that still have a right of return as of the balance sheet date. During recent fiscal years, customer returns as a percentage of revenues have declined to approximately 1%. Factors affecting Dell's allowance for doubtful accounts include historical and anticipated customer default rates of the various aging categories of accounts receivable. Each quarter, Dell reevaluates its estimates to assess the adequacy of its recorded accruals for customer returns and allowance for doubtful accounts and adjusts the amounts as necessary.

Warranty. Dell records warranty liabilities at the time of sale for the estimated costs that may be incurred under its basic limited warranty. The specific warranty terms and conditions vary depending upon the product sold and country in which Dell does business, but generally includes technical support, repair parts, labor, and a period ranging from 90 days to three years. Factors that affect Dell's warranty liability include the number of installed units currently under warranty, historical and anticipated rates of warranty claims on those units, and cost per claim to satisfy Dell's warranty obligation. The anticipated rate of warranty claims is the primary factor impacting Dell's estimated warranty obligation. The other factors are relatively insignificant because the average remaining aggregate warranty period of the covered installed base is approximately 20 months, repair parts are generally already in stock or available at pre-determined

prices, and labor rates are generally arranged at pre-established amounts with service providers. Warranty claims are relatively predictable based on historical experience of failure rates. Each Quarter, Dell reevaluates its estimates to assess the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Income Taxes. Dell calculates a provision for income taxes using the asset and liability method, under which deferred tax assets and liabilities are recognized by identifying the temporary differences arising from the different treatment of items for tax and accounting purposes. In determining the future tax consequences of events that have been recognized in Dell's financial statements or tax returns, judgment is required. Differences between the anticipated and actual outcomes of these future tax consequences could have a material impact on Dell's consolidated results of operations or financial position.

MANAGEMENT'S DISCUSSION OF BUSINESS

General

Dell Inc., with fiscal 2005 net revenue of $49.2 billion, is a premier provider of products and services worldwide that enable customers to build their information-technology and Internet infrastructures. Dell offers a broad range of enterprise systems (servers, storage, workstations, and networking products), client systems (notebook and desktop computer systems), printing and imaging systems, software and peripherals, and global services. During calendar 2004, Dell was the number one supplier of personal computer systems worldwide as well as in the United States. Dell's global market leadership is the result of a persistent focus on delivering the best possible customer experience by selling products and services directly to customers.

Dell, a Delaware corporation, was founded in 1984 by Michael Dell on a simple concept: by selling computer systems directly to customers, Dell could best understand their needs and efficiently provide the most effective computing solutions to meet those needs. Dell is based in Round Rock, Texas, and conducts operations worldwide through its subsidiaries. Unless otherwise specified, references to Dell include its consolidated subsidiaries. Dell operates principally in one industry and is managed in three geographic segments: the Americas, Europe, and Asia Pacific–Japan regions. See "Item 1–Business–Geographic Areas of Operations."

Business Strategy

Dell's business strategy combines its direct customer model with a highly efficient manufacturing and supply chain management organization and an emphasis on standards-based technologies. This strategy enables Dell to provide customers with superior value; high-quality, relevant technology; customized systems; superior service and support; and products and services that are easy to buy and use. The key tenets of Dell's business strategy are:

- *A direct relationship is the most efficient path to the customer.* A direct customer relationship, also referred to as Dell's "direct business model," eliminates wholesale and retail dealers that add unnecessary time and cost or diminish Dell's understanding of customer expectations. As a result, Dell is able to offer customers

superior value by avoiding expenditures associated with the retail channel such as higher inventory carrying costs, obsolescence associated with technology products, and retail mark-ups. In addition, direct customer relationships provide a constant flow of information about customers' plans and requirements and enable Dell to continually refine its product offerings. At www.dell.com, customers may review, configure and price systems within Dell's entire product line; order systems online; and track orders from manufacturing through shipping.

- *Customers can purchase custom-built products and custom-tailored services.* Dell believes the direct business model is the most effective model for providing solutions that address customer needs. In addition, Dell's flexible, build-to-order manufacturing process enables Dell to turn over inventory every four days on average, and reduce inventory levels. This allows Dell to rapidly introduce the latest relevant technology more quickly than companies with slow-moving, indirect distribution channels, and to rapidly pass on component cost savings directly to customers.
- *Dell is the low-cost leader.* Dell's highly efficient supply chain management and manufacturing organization, efficient direct business model, and concentration on standards-based technologies allow Dell to maintain the lowest cost structure among its major competitors, and to pass those savings to its customers. Dell's relentless focus on reducing its costs allows it to consistently provide customers with superior value.
- *Dell provides a single point of accountability for its customers.* Dell recognizes that as technology needs become more complex, it becomes more challenging for customers to efficiently address their information technology needs. Dell therefore strives to be the single point of accountability for customers with complex technological challenges. Dell offers an array of services designed to provide customers the ability to maximize system performance, efficiency, and return on investment.
- *Non-proprietary standards-based technologies deliver the best value to customers.* Dell believes that non-proprietary standards-based technologies are critical to providing customers with relevant, high-value products and services. Focusing on standards gives customers the benefit of extensive research and development from Dell and its entire supply chain, rather than a single company. Unlike proprietary technologies, standards provide customers with flexibility and choice while allowing their purchasing decisions to be based on performance, cost, and customer service.

Products

Dell designs, develops, manufactures, markets, sells, and supports a wide range of products that are customized to customer requirements. These include enterprise systems, client systems, printing and imaging systems, software and peripherals.

- *Servers.* Dell's standards-based PowerEdge™ line of servers is designed to provide customers affordable performance, reliability, and scalability. Options include high performance rack and tower servers for enterprise customers and aggressively priced tower servers for small organizations and networks. Dell ranks number one in the U.S. and number two worldwide in shipments of x86 servers (based on standard Intel architecture). During calendar 2004, Dell increased its share of worldwide x86 server sales by 1.5 percentage points and maintained its number two position in that category at 24.8%.

- *Storage*. Dell/EMC and Dell's PowerVault™ lines of storage products offer customers a comprehensive portfolio of cost-effective hardware and software products to store, serve, and protect customer data. Dell offers external storage, tape backup products, network attached storage, fibre channel arrays, storage area networks, and rack solutions. Total storage revenue grew 16% during fiscal 2005 and continues to be supported by Dell's four-year running partnership with EMC Corporation.
- *Workstations*. Dell Precision™ desktop and mobile workstations are intended for professional users who demand exceptional performance to run sophisticated applications, such as three-dimensional computer-aided design, digital content creation, geographic information systems, computer animation, software development, and financial analysis. In calendar 2004, Dell held the number one position in the U.S. and worldwide for branded workstation unit shipments.
- *Networking Products*. Dell's PowerConnect™ switches connect computers and servers in small- to medium-sized networks. PowerConnect products offer customers enterprise-class features and reliability at a low cost.
- *Notebook Computers*. Dell offers two lines of notebook computer systems. The Latitude™ line is designed to address a wide range of business and organizational needs, including powerful performance, portability, and flexibility. Latitude offerings range from wireless-ready, highly expandable full-featured models to thin, light ultra-portable models. The Inspiron™ line is targeted to customers who require high-performance computer systems at competitive prices. Typical customers are individuals or small-to-medium sized businesses that require optimum performance for their investment. Dell ranked number one in the U.S. and worldwide in notebook computer shipments in calendar 2004.
- *Desktop Computer Systems*. Dell customers can select from two lines of desktop computer systems. The OptiPlex™ line is designed for corporate, institutional, and small business customers who demand highly-reliable, stable, manageable, and easily serviced systems within networked environments. The Dimension™ line is designed for small businesses and home users requiring fast technology turns and high-performance computing. The Dimension line typically features the latest high-performance components. Dimension customers include corporate and institutional customers as well as small businesses and home users. Dell ranked number one in the U.S. and worldwide in desktop shipments in calendar 2004.
- *Printing and Imaging Systems*. Dell offers a wide array of Dell-branded printers, ranging from photo printers for consumers to large multifunction lasers for corporate workgroups. The Dell printer product line is focused on making printing easier to buy, own, and use. All Dell printers feature the Dell Ink Management System™ or Dell Toner Management System™, which simplifies the purchasing process for supplies by displaying ink or toner levels on the status window during every print job and proactively prompting users to order replacement cartridges directly from Dell. During fiscal 2005, Dell shipped more than five million Dell-branded printers.
- *Software and Peripherals*. Dell offers a multitude of competitively priced software and peripherals products, including a wide range of software titles, monitors, plasma and LCD televisions, MP3 players, handhelds, notebook accessories, networking and wireless products, memory, digital cameras, projectors, power

adapters and scanners. Dell introduced several new peripherals products in fiscal 2005, including a new line of plasma televisions.

Services

By applying the direct business model to its global services business, Dell seeks to simplify customers' computing experience by offering a full range of flexible, tailored solutions. Dell offers a portfolio of services that help customers maximize the value of their information technology investments, rapidly deploy systems, and educate IT professionals and consumers.

- *Managed Services.* Dell's wide range of IT management services allows customers to lower annual service costs and enhance performance without sacrificing control of their systems. Dell Managed Services assists customers in planning, deployment, maintenance, asset management, on-site field services, and other related services.
- *Professional Services.* Dell Professional Services helps businesses utilize emerging technology, enhance efficiencies, reduce business risk, and maximize return on technology investment. Using its expertise and best practices in technology consulting, application development, solutions integration, and infrastructure design, Dell designs, develops, and implements end-to-end technology solutions.
- *Deployment Services.* Dell's deployment services are designed to rapidly configure and deploy Dell systems and products into IT environments. Dell's custom factory integration services allow customers to configure systems to meet their specific hardware and software needs. Additional deployment services include asset management and recovery services, custom delivery services, installation services, managed deployment services, and image management services.
- *Support Services.* Dell offers a variety of customized services and support programs tailored to meet specific customer requirements. Dell operates Enterprise Command Centers in the United States, Ireland, China, and Japan to provide rapid, around-the-clock support for critical enterprise systems. Additionally, Dell provides a limited warranty for all computer systems and offers limited 24-hour telephone and online technical support. Dell also offers warranty upgrades and services such as CompleteCare™ accidental damage service, At Home Service for technical support service at home (provided via third-party contract with the customer), Helpdesk for all software and peripherals support, and Gold Technical Support for advanced technical service.
- *Training and Certification Services.* Dell offers training and certification programs for business and consumer customers worldwide. Dell's online training programs feature over 1,200 courses for consumer, business, and IT professionals. The courses are designed for all skill levels and range from personal finance to business productivity to IT certification.

Financial Services

Dell offers various financing alternatives, asset management services, and other customer financial services for its business and consumer customers in the U.S. through Dell Financial Services L.P. ("DFS"), a joint venture between Dell and CIT Group, Inc.

("CIT"). For additional information about Dell's financing arrangements, see "Item 7–Management's Discussion and Analysis of Financial Condition and Results of Operations–Off-Balance Sheet Arrangements" and Note 6 of Notes to Consolidated Financial Statements included In "Item 8–Financial Statements and Supplementary Data." Also see "Item 1–Business–Factors Affecting Dell's Business and Prospects" for information about the risks associated with DFS.

Sales and Marketing

Dell sells its products and services directly to its customers through dedicated sales representatives, telephone-based sales, and online sales through www.dell.com. Dell's customers include large corporate, government, healthcare, and education accounts, as well as small-to-medium businesses and individual customers. Within each of Dell's geographic regions, Dell has divided its sales and marketing resources among these various customer groups. No single customer accounted for more than 10% of Dell's consolidated net revenue during any of the last three fiscal years. See "Item 1–Business–Factors Affecting Dell's Business and Prospects" for information about the risk associated with government contracts.

Dell's sales and marketing efforts are organized around the needs, trends, and characteristics of Dell's customers. Dell's direct business model provides direct and continuous feedback from its customers, thereby allowing the company to develop and refine its products and marketing programs for specific customer groups. This constant flow of communication, which is unique to the direct business model, also allows Dell to rapidly gauge customer satisfaction and target new or existing products.

For large business and institutional customers, Dell maintains a field sales force throughout the world. Dedicated account teams, which include field-based system engineers and consultants, form long-term relationships to provide our largest customers with a single source of assistance and develop specific marketing programs for these customers. For large, multinational customers, Dell offers several programs designed to provide single points of contact and accountability with global account specialists, special global pricing, consistent service and support programs across global regions, and access to central purchasing facilities. Dell also maintains specific sales and marketing programs targeted at federal, state, and local governmental agencies as well as specific healthcare and educational markets.

Dell markets its products and services to small-to-medium businesses and consumers primarily by advertising on television and the Internet. advertising in a variety of print media, and by mailing a broad range of direct marketing publications, such as promotional pieces, catalogs, and customer newsletters. In certain states as well as non-U.S. locations. Dell also operates Dell Direct Stores, which are kiosks typically located within shopping centers, that allow customers to view Dell products in person and purchase online from Dell with the assistance of a Dell expert.

SELECTED FINANCIAL DATA

(in millions, except per share data)	FISCAL YEAR ENDED January 28, 2005[a]	January 30, 2004	January 31, 2003	February 1, 2002[b]	February 2, 2001[c]
Results of Operations					
Net revenue	$49,205	$41,444	$35,404	$31,168	$31,888
Gross margin	9,015	7,552	6,349	5,507	6,443
Operating income	4,254	3,544	2,844	1,789	2,663
Income before cumulative effect of change in accounting principle[d]	3,043	2,645	2,122	1,246	2,236
Net income	$ 3,043	$ 2,645	$ 2,122	$ 1,246	$ 2,177
Earnings per common share:					
Before cumulative effect of change in accounting principle:					
Basic	$ 1.21	$ 1.03	$ 0.82	$ 0.48	$ 0.87
Diluted	$ 1.18	$1.01	$ 0.80	$ 0.46	$ 0.81
After cumulative effect of change in accounting principle:					
Basic	$ 1.21	$ 1.03	$ 0.82	$ 0.48	$ 0.84
Diluted	$ 1.18	$ 1.01	$ 0.80	$ 0.46	$ 0.79
Number of weighted average shares outstanding:					
Basic	2,509	2,565	2,584	2,602	2,582
Diluted	2,568	2,619	2,644	2,726	2,746
Cash Flow and Balance Sheet Data					
Net cash provided by operating activities	$ 5,310	$ 3,670	$3,538	$3,797	$ 4,195
Cash, cash equivalents and investments	14,126	11,922	9,905	8,287	7,853
Total assets	23,215	19,311	15,470	13,535	13,670
Long-term debt	505	505	506	520	509
Total stockholders' equity	$ 6,485	$ 6,280	$4,873	$4,694	$ 5,622

[a] During the fourth quarter of fiscal 2005, Dell recorded a tax repatriation charge of $280 million pursuant to a favorable tax incentive provided by the American Jobs Creation Act of 2004. This tax charge is related to Dell's decision to repatriate $4.1 billion in foreign earnings.

[b] Includes a pre-tax charge of $742 million. Approximately $482 million relates to employee termination benefits, facilities closure costs, and other asset impairments and exit costs, while the balance of $260 million relates to other-than-temporary declines in the fair value of equity securities.

[c] Includes a pre-tax charge of $105 million related to employee termination benefits and facilities closure costs.

[d] Effective January 29, 2000, Dell changed its accounting for revenue recognition in accordance with the SEC's Staff Accounting Bulletin ("SAB") No. 101, *Revenue Recognition in Financial Statements*. The cumulative effect of the change on retained earnings as of the beginning of fiscal 2001 resulted in a charge to fiscal 2001 income of $59 million (net of income taxes of $25 million). With the exception of the cumulative effect adjustment, the effect of the change on net income for the fiscal year ended February 2, 2001 was not material.

Certification by (1) Kevin B. Rollins, President and Chief Executive Officer, and (2) James M. Schneider, Senior Vice President and Chief Financial Officer

1. I have reviewed this Annual Report on Form 10-K of Dell Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of interna1 control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 7, 2005

/s/ KEVIN B. ROLLINS	/s/ JAMES M. SCHNEIDER
Kevin B. Rollins	James M. Schneider
President and Chief Executive Officer	*Senior Vice President and Chief Financial Officer*

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Dell Inc.

We have completed an integrated audit of Dell Inc.'s January 28, 2005 consolidated financial statements and of its internal control over financial reporting as of January 28, 2005 and audits of its January 30, 2004 and January 31, 2003 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated Financial Statements and Financial Statement Schedule

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Dell Inc. and its subsidiaries at January 28, 2005 and January 30, 2004, and the results of their operations and their cash flows for each of the three years in the period ended January 28, 2005 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Internal Control over Financial Reporting

Also, in our opinion, management's assessment, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A–Controls and Procedures, that the company maintained effective internal control over financial reporting as of January 28, 2005, based on criteria established in *Internal Control–Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly stated, in all material respects, based on those criteria. Furthermore, in our opinion, the company maintained, in all material respects, effective internal control over financial reporting as of January 28, 2005, based on criteria established in *Internal Control–Integrated Framework* issued by the COSO. The company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PRICEWATERHOUSECOOPERS LLP

Austin, Texas
March 3, 2005

DELL INC.
Consolidated Statements of Financial Position

(in millions)	January 28, 2005	January 30, 2004
Assets		
Current assets		
Cash and cash equivalents	$ 4,747	$4,317
Short-term investments	5,060	835
Accounts receivable, net	4,414	3,635
Inventories	459	327
Other	2,217	1,519
Total current assets	16,897	10,633
Property, plant, and equipment, net	1,691	1,517
Investments	4,319	6,770
Other non-current assets	308	391
Total assets	$ 23,215	$19,311
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$ 8,895	$ 7,316
Accrued and other	5,241	3,580
Total current liabilities	14,136	10,896
Long-term debt	505	505
Other non-current liabilities	2,089	1,630
Total liabilities	16,730	13,031
Commitments and contingent liabilities (Note 8)	—	—
Stockholders' equity		
Preferred stock and capital in excess of $.01 par value; shares issued and outstanding: none	—	—
Common stock and capital in excess of $.01 par value; shares authorized: 7,000; shares issued: 2,769 and 2,721, respectively	8,195	6,823
Treasury stock, at cost; 284 and 165 shares, respectively	(10,758)	(6,539)
Retained earnings	9,174	6,131
Other comprehensive loss	(82)	(83)
Other	(44)	(52)
Total stockholders' equity	6,485	6,280
Total liabilities and stockholders' equity	$ 23,215	$19,311

DELL INC.
Consolidated Statements of Income

(in millions, except per share amounts)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Net revenue	$49,205	$41,444	$35,404
Cost of revenue	40,190	33,892	29,055
Gross margin	9,015	7,552	6,349
Operating expenses			
Selling, general, and administrative	4,298	3,544	3,050
Research, development, and engineering	463	464	455
Total operating expenses	4,761	4,008	3,505
Operating income	4,254	3,544	2,844
Investment and other income, net	191	180	183
Income before income taxes	4,445	3,724	3,027
Income tax provision	1,402	1,079	905
Net income	$ 3,043	$ 2,645	$ 2,122
Earnings per common share:			
Basic	$ 1.21	$ 1.03	$ 0.82
Diluted	$ 1.18	$ 1.01	$ 0.80
Weighted average shares outstanding:			
Basic	2,509	2,565	2,584
Diluted	2,568	2,619	2,644

DELL INC.
Consolidated Statements of Cash Flows

(in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Cash flows from operating activities			
Net income	$ 3,043	$ 2,645	$2,122
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	334	263	211
Tax benefits of employee stock plans	249	181	260
Effects of exchange rate changes on monetary assets and liabilities denominated in foreign currencies	(602)	(677)	(537)
Other	78	113	60
Changes in:			
Operating working capital	1,755	872	1,210
Non-current assets and liabilities	453	273	212
Net cash provided by operating activities	5,310	3,670	3,538
Cash flows from investing activities			
Investments:			
Purchases	(12,261)	(12,099)	(8,736)
Maturities and sales	10,469	10,078	7,660
Capital expenditures	(525)	(329)	(305)
Purchase of assets held in master lease facilities	—	(636)	—
Cash assumed in consolidation of Dell Financial Services L.P.	—	172	—
Net cash used in investing activities	(2,317)	(2,814)	(1,381)
Cash flows from financing activities			
Repurchase of common stock	(4,219)	(2,000)	(2,290)
Issuance of common stock under employee plans and other	1,091	617	265
Net cash used in financing activities	(3,128)	(1,383)	(2,025)
Effect of exchange rate changes on cash and cash equivalents	565	612	459
Net increase in cash and cash equivalents	430	85	591
Cash and cash equivalents at beginning of period	4,317	4,232	3,641
Cash and cash equivalents at end of period	$ 4,747	$ 4,317	$4,232

DELL INC.
Consolidated Statements of Stockholders' Equity

(in millions)	Common Stock and Capital in Excess of Par Value		Treasury Stock		Retained Earnings	Other Comprehensive Income (Loss)	Other	Total
	Shares	Amount	Shares	Amount				
Balances at February 1, 2002	2,654	$5,605	52	$ (2,249)	$1,364	$ 38	$(64)	$ 4,694
Net income	—	—	—	—	2,122	—	—	2,122
Change in net unrealized gain on investments, net of taxes of $14	—	—	—	—	—	26	—	26
Foreign currency translation adjustments	—	—	—	—	—	4	—	4
Change in net unrealized loss on derivative instruments, net of taxes of $42	—	—	—	—	—	(101)	—	(101)
Total comprehensive income								2,051
Stock issuances under employee plans, including tax benefits	27	410	—	—	—	—	6	416
Repurchases	—	—	50	(2,290)	—	—	—	(2,290)
Other	—	3	—	—	—	—	(1)	2
Balances at January 31, 2003	2,681	6,018	102	(4,539)	3,486	(33)	(59)	4,873
Net income	—	—	—	—	2,645	—	—	2,645
Change in net unrealized gain on investments, net of taxes of $19	—	—	—	—	—	(35)	—	(35)
Foreign currency translation adjustments	—	—	—	—	—	6	—	6
Change in net unrealized loss on derivative instruments, net of taxes of $5	—	—	—	—	—	(21)	—	(21)
Total comprehensive income								2,595
Stock issuances under employee plans, including tax benefits	40	805	—	—	—	—	—	805
Repurchases	—	—	63	(2,000)	—	—	—	(2,000)
Other	—	—	—	—	—	—	7	7
Balances at January 30, 2004	2,721	6,823	165	(6,539)	6,131	(83)	(52)	6,280
Net income	—	—	—	—	3,043	—	—	3,043
Change in net unrealized gain on investments, net of taxes of $16	—	—	—	—	—	(52)	—	(52)
Foreign currency translation adjustments	—	—	—	—	—	1	—	1
Change in net unrealized loss on derivative instruments, net of taxes of $21	—	—	—	—	—	52	—	52
Total comprehensive income								3,044
Stock issuances under employee plans, including tax benefits	48	1,372	—	—	—	—	—	1,372
Repurchases	—	—	119	(4,219)	—	—	—	(4,219)
Other	—	—	—	—	—	—	8	8
Balances at January 28, 2005	2,769	$8,195	284	$(10,758)	$9,174	$ (82)	$(44)	$ 6,485

DELL INC.
Notes to Consolidated Financial Statements

NOTE 1—DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business. Dell Inc., a Delaware corporation, and its consolidated subsidiaries (collectively referred to as "Dell") designs, develops, manufactures, markets, sells, and supports a wide range of computer systems and services that are customized to customer requirements. These include enterprise systems (servers, storage, workstations, and networking products), client systems (notebook and desktop computer systems), printing and imaging systems, software and peripherals, and global services. Dell markets and sells its products and services directly to its customers, which include large corporate, government, healthcare, and education accounts, as well as small-to-medium businesses and individual customers.

Fiscal Year. Dell's fiscal year is the 52- or 53-week period ending on the Friday nearest January 31. Fiscal 2005, 2004, and 2003 all included 52 weeks.

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of Dell and its wholly-owned and controlled majority-owned subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). All significant intercompany transactions and balances have been eliminated.

Dell is currently a partner in Dell Financial Services L.P. ("DFS"), a joint venture with CIT Group Inc. ("CIT"). The joint venture allows Dell to provide its customers with various financing alternatives while CIT provides the financing between DFS and the customer for certain transactions. Dell began consolidating DFS's financial results at the beginning of the third quarter of fiscal 2004 due to the adoption of Financial Accounting Standards Board ("FASB") Interpretation No. 46R ("FIN 46R"). The consolidation of DFS had no impact on Dell's net income or earnings per share because Dell had historically been recording its 70% equity interest in DFS under the equity method. See Note 6 of "Notes to Consolidated Financial Statements."

Use of Estimates. The preparation of financial statements in accordance with GAAP requires the use of management's estimates. These estimates are subjective in nature and involve judgments that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at fiscal year end, and the reported amounts of revenues and expenses during the fiscal year. Actual results could differ from those estimates.

Cash and Cash Equivalents. All highly liquid investments with original maturities of three months or less at date of purchase are carried at cost plus accrued interest, which approximates fair value, and are considered to be cash equivalents. All other investments not considered to be cash equivalents are separately categorized as investments.

Investments. Dell's investments in debt securities and publicly traded equity securities are classified as available-for-sale and are reported at fair market value (based on quoted

market prices) using the specific identification method. Unrealized gains and losses, net of taxes, are reported as a component of stockholders' equity. Realized gains and losses on investments are included in investment and other income, net when realized. All other investments are initially recorded at cost and charged against income when a decline in the fair market value of an individual security is determined to be other-than-temporary.

Inventories. Inventories are stated at the lower of cost or market with cost being determined on a first-in, first-out basis.

Property, Plant, and Equipment. Property, plant, and equipment are carried at depreciated cost. Depreciation is provided using the straight-line method over the estimated economic lives of the assets, which range from 10 to 30 years for buildings and two to five years for all other assets. Leasehold improvements are amortized over the shorter of five years or the lease term. Gains or losses related to retirements or disposition of fixed assets are recognized in the period incurred. Dell performs reviews for the impairment of fixed assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Dell capitalizes eligible internal-use software development costs incurred subsequent to the completion of the preliminary project stage. Development costs are amortized over the shorter of the expected useful life of the software or five years.

Foreign Currency Translation. The majority of Dell's international sales are made by international subsidiaries, most of which have the U.S. dollar as their functional currency. Local currency transactions of international subsidiaries, which have the U.S. dollar as the functional currency are remeasured into U.S. dollars using current rates of exchange for monetary assets and liabilities and historical rates of exchange for nonmonetary assets. Gains and losses from remeasurement of monetary assets and liabilities are included in investment and other income, net. Dell's subsidiaries that do not have the U.S. dollar as their functional currency translate assets and liabilities at current rates of exchange in effect at the balance sheet date. Revenue and expenses from these international subsidiaries are translated using the monthly average exchange rates in effect for the period in which the items occur. The resulting gains and losses from translation are included as a component of stockholders' equity.

Hedging Instruments. Dell applies *Statement of Financial Accounting Standards ("SFAS") No. 133, Accounting for Derivative Instruments and Hedging Activities,* as amended, which establishes accounting and reporting standards for derivative instruments and hedging activities. SFAS No. 133 requires Dell to recognize all derivatives as either assets or liabilities in its consolidated statement of financial position and measure those instruments at fair value.

Treasury Stock. Effective with the beginning of the second quarter of fiscal 2002, Dell began holding repurchased shares of its common stock as treasury stock. Prior to that date, Dell retired all such repurchased shares which were recorded as a reduction to retained earnings. Dell accounts for treasury stock under the cost method and includes treasury stock as a component of stockholders' equity.

Revenue Recognition. Net revenue includes sales of hardware, software and peripherals, and services (including extended service contracts and professional services). These products and services are sold either separately or as part of a multiple-element

arrangement. Dell allocates fees from multiple-element arrangements to the elements based on the relative fair value of each element, which is generally based on the relative list price of each element. For sales of extended warranties with a separate contract price, Dell defers revenue equal to the separately stated price. Revenue associated with undelivered elements is deferred and recorded when delivery occurs. Product revenue is recognized, net of an allowance for estimated returns, when both title and risk of loss transfer to the customer, provided that no significant obligations remain. Revenue from extended warranty and service contracts, for which Dell is obligated to perform, is recorded as deferred revenue and subsequently recognized over the term of the contract or when the service is completed. Revenue from sales of third-party extended warranty and service contracts, for which Dell is not obligated to perform, is recognized on a net basis at the time of sale.

Dell defers the cost of shipped products awaiting revenue recognition until the goods are delivered and revenue is recognized. In-transit product shipments to customers totaled $430 million and $387 million as of January 28, 2005 and January 30, 2004, respectively, and are included in other current assets on Dell's consolidated statement of financial position.

Sale of Finance Receivables. Dell sells certain loan and lease finance receivables to a special purpose entity in securitization transactions. The receivables are removed from the statement of financial position at the time they are sold. Receivables are considered sold when the receivables are transferred beyond the reach of Dell's creditors, the transferee has the right to pledge or exchange the assets, and Dell has surrendered control over the rights and obligations of the receivables. Gains and losses from the sale of certain loan and lease finance receivables are recognized in the period the sale occurs, based upon the relative fair value of the portion sold and the portion allocated to retained interests.

Warranty. Dell records warranty liabilities at the time of sale for the estimated costs that may be incurred under its basic limited warranty. The specific warranty terms and conditions vary depending upon the product sold and country in which Dell does business, but generally includes technical support, repair parts, labor, and a period ranging from 90 days to three years. Factors that affect Dell's warranty liability include the number of installed units currently under warranty, historical and anticipated rates of warranty claims on those units, and cost per claim to satisfy Dell's warranty obligation. Each quarter, Dell reevaluates its estimates to assess the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Shipping Costs. Dell's shipping and handling costs are included in cost of sales in the accompanying consolidated statement of income for all periods presented.

Selling, General, and Administrative. Selling expenses include items such as sales commissions, marketing and advertising costs, and contractor services. Advertising costs are expensed as incurred and were $576 million, $473 million, and $426 million during fiscal 2005, 2004, and 2003, respectively. General and administrative expenses include items for Dell's administrative functions, such as Finance, Legal, Human Resources, and information technology support. These functions include costs for items such as salaries, maintenance and supplies, insurance, depreciation expense, and allowance for doubtful accounts.

Research, Development, and Engineering Costs. Research, development, and engineering costs are expensed as incurred, in accordance with *SFAS No. 2, Accounting for Research and Development Costs*. Research, development, and engineering expenses primarily include payroll and headcount related costs, contractor fees, infrastructure costs, and administrative expenses directly related to research and development support.

Website Development Costs. Dell expenses the costs of maintenance and minor enhancements to the features and functionality of its websites.

Income Taxes. Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

Earnings Per Common Share. Basic earnings per share is based on the weighted effect of all common shares issued and outstanding, and is calculated by dividing net income by the weighted average shares outstanding during the period. Diluted earnings per share is calculated by dividing net income by the weighted average number of common shares used in the basic earnings per share calculation plus the number of common shares that would be issued assuming exercise or conversion of all potentially dilutive common shares outstanding. Dell excludes equity instruments from the calculation of diluted weighted average shares outstanding if the effect of including such instruments is antidilutive to earnings per share. Accordingly, certain employee stock options and equity put contracts (during fiscal 2003) have been excluded from the calculation of diluted weighted average shares totaling 103 million, 138 million, and 192 million shares during fiscal 2005, 2004, and 2003, respectively.

The following table sets forth the computation of basic and diluted earnings per share for each of the past three fiscal years:

	FISCAL YEAR ENDED		
(in millions, except per share amounts)	January 28, 2005	January 30, 2004	January 31, 2003
Numerator:			
Net income	$3,043	$2,645	$2,122
Denominator:			
Weighted average shares outstanding			
Basic	2,509	2,565	2,584
Employee stock options and other	59	54	60
Diluted	2,568	2,619	2,644
Earnings per common share:			
Basic	$ 1.21	$ 1.03	$ 0.82
Diluted	$ 1.18	$ 1.01	$ 0.80

Pro Forma Effects of Stock-Based Compensation. As of January 28, 2005, Dell had four stock-based compensation plans and an employee stock purchase plan where stock options or purchase rights were outstanding. See Note 5 of "Notes to Consolidated Financial Statements." Dell currently applies the recognition and measurement principles of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees,* and related Interpretations in accounting for those plans.

Under *SFAS No. 123, Accounting for Stock-Based Compensation,* the value of each option is estimated on the date of grant using the Black-Scholes option pricing model, which was developed for use in estimating the value of freely traded options. Similar to other option pricing models, it requires the input of highly subjective assumptions, including stock price volatility. Because (1) Dell's employee stock options have characteristics significantly different from those of traded options and (2) changes in the subjective input assumptions can materially affect the estimated fair value, management's opinion is that the existing option pricing models (including Black-Scholes and Binomial) do not provide a reliable measure of the fair value of Dell's employee stock options.

The following table illustrates the effect on net income and earnings per share for each of the past three fiscal years as if Dell had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation:

	FISCAL YEAR ENDED		
(in millions, except per share amounts)	**January 28, 2005**	**January 30, 2004**	**January 31, 2003**
Net income—as reported	$3,043	$2,645	$2,122
Deduct: Total stock-based employee compensation determined under fair value method for all awards, net of related tax effects	(812)	(829)	(723)
Net income—pro forma	$2,231	$1,816	$1,399
Earnings per common share			
Basic—as reported	$ 1.21	$ 1.03	$ 0.82
Basic—pro forma	$ 0.89	$ 0.71	$ 0.54
Diluted—as reported	$ 1.18	$ 1.01	$ 0.80
Diluted—pro forma	$ 0.88	$ 0.68	$ 0.51

Under the Black-Scholes option pricing model, the weighted average fair value of stock options at date of grant was $10.72, $10.25, and $11.41 per option for options granted during fiscal 2005, 2004, and 2003, respectively. Additionally, the weighted average fair value of the purchase rights under the employee stock purchase plan granted in fiscal 2005, 2004, and 2003 was $9.77, $7.88, and $7.39 per right, respectively. The weighted average fair value of options and purchase rights under the employee stock purchase plan was determined based on the Black-Scholes model weighted for all grants during the period, utilizing the following assumptions:

	FISCAL YEAR ENDED		
	January 28, 2005	**January 30, 2004**	**January 31, 2003**
Expected term			
Stock options	3.8 years	3.8 years	5 years
Employee stock purchase plan	6 months	6 months	6 months
Risk-free interest rate	2.89%	2.99%	3.76%
Volatility	36%	43%	43%
Dividends	0%	0%	0%

During fiscal 2005 and 2004, Dell evaluated the historical stock option exercise behavior of its employees, among other relevant factors, and determined that the best estimate of expected term of stock options granted in fiscal 2005 and 2004 was 3.8 years, compared to the previous expected term of 5 years. Dell used expected volatility, as well as other economic data, to estimate the volatility for fiscal 2005, 2004, and 2003 option grants, because management believes such volatility is more representative of prospective trends.

Comprehensive Income. Dell's comprehensive income is comprised of net income, foreign currency translation adjustments, unrealized gains and losses on derivative financial instruments related to foreign currency hedging, and unrealized gains and losses on marketable securities classified as available-for-sale.

Recently Issued Accounting Pronouncements. On December 16, 2004, the FASB issued *SFAS No. 123R, Share-Based Payment. SFAS No. 123R* addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise or (b) liabilities that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using Accounting Principles Board Opinion No. 25 and generally requires that such transactions be accounted for using a fair-value-based method. Dell expects to adopt this standard on its effective date, which is the beginning of Dell's third quarter of fiscal 2006. Dell is currently assessing the final impact of this standard on the company's consolidated results of operations, financial position, and cash flows. This assessment includes evaluating option valuation methodologies and assumptions as well as potential changes to Dell's compensation strategies.

On November 24, 2004, the FASB issued *SFAS No. 151, Inventory Costs–an amendment of ARB No. 43. SFAS No. 151* requires idle facility expenses, freight, handling costs, and wasted material (spoilage) costs to be excluded from the cost of inventory and expensed when incurred. It also requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. *SFAS No. 151* will be effective at the beginning of Dell's fiscal 2007. *SFAS No. 151* is not expected to have a material impact on Dell's consolidated results of operations or financial position.

Reclassifications. Certain prior year amounts have been reclassified to conform to the fiscal 2005 presentation.

NOTE 2—FINANCIAL INSTRUMENTS

Disclosures about Fair Values of Financial Instruments

The fair value of investments, long-term debt, and related interest rate derivative instruments has been estimated based upon market quotes from brokers. The fair value of foreign currency forward contracts has been estimated using market quoted rates of foreign currencies at the applicable balance sheet date. The estimated fair value of foreign currency purchased option contracts is based on market quoted rates at the applicable balance sheet date and the Black-Scholes option pricing model. The estimates presented herein are not necessarily indicative of the amounts that Dell could realize in a current market exchange. Changes in assumptions could significantly affect the estimates.

Cash and cash equivalents, accounts receivable, accounts payable, and accrued and other liabilities are reflected in the accompanying consolidated statement of financial position at cost, which approximates fair value because of the short-term maturity of these instruments.

Investments

The following table summarizes by major security type the fair market value and cost of Dell's investments. All investments with remaining maturities in excess of one year are recorded as long-term investments in the accompanying consolidated statement of financial position.

	JANUARY 28, 2005			JANUARY 30, 2004		
(in millions)	Fair Market Value	Cost	Unrealized Gain (Loss)	Fair Market Value	Cost	Unrealized Gain
Debt securities						
U.S. government and agencies	$7,973	$8,012	$(39)	$5,115	$5,108	$ 7
U.S. corporate	1,012	1,021	(9)	2,175	2,169	6
International corporate	243	245	(2)	159	159	—
State and municipal governments	25	25	—	5	5	—
Total debt securities	9,253	9,303	(50)	7,454	7,441	13
Equity and other securities	126	123	3	151	138	13
Total investments	$9,379	$9,426	$(47)	$7,605	$7,579	$26
Short-term	$5,060	$5,068	$ (8)	$ 835	$ 835	$—
Long-term	4,319	4,358	(39)	6,770	6,744	26
Total investments	$9,379	$9,426	$(47)	$7,605	$7,579	$26

As of January 28, 2005, Dell had approximately 1,290 debt investment positions that had fair market values below their carrying values for a period of less than 12 months. The fair market value and unrealized losses on these investment positions totaled $10 billion and $49 million, respectively, as of January 28, 2005. The unrealized losses are due to changes in interest rates and are expected to be temporary in nature.

The following table summarizes Dell's recognized gains and losses on investments, including impairments of certain investments:

	FISCAL YEAR ENDED		
(in millions)	January 28, 2005	January 30, 2004	January 31, 2003
Gains	$ 40	$ 94	$ 86
Losses	(34)	(78)	(92)
Net recognized gains (losses)	$ 6	$ 16	$ (6)

Dell routinely enters into securities lending agreements with financial institutions in order to enhance investment income. Dell requires that the loaned securities be collateralized in the form of cash or securities for values which generally exceed the value of the loaned security. As of January 28, 2005, securities on loan and the related collateral amounts were not material.

Foreign Currency Instruments

Dell uses purchased option contracts and forward contracts designated as cash flow hedges to protect against the foreign currency exchange risk inherent in its forecasted transactions denominated in currencies other than the U.S. dollar. Hedged transactions include international sales by U.S. dollar functional currency entities, foreign currency denominated purchases of certain components and intercompany shipments to some international subsidiaries. The risk of loss associated with purchased options is limited to premium amounts paid for the option contracts. The risk of loss associated with forward contracts is equal to the exchange rate differential from the time the contract is entered into until the time it is settled. These contracts generally expire in twelve months or less.

Dell also uses forward contracts to hedge monetary assets and liabilities, primarily receivables and payables, denominated in a foreign currency. These contracts are not designated as hedging instruments under GAAP, and therefore, the change in the instrument's fair value is recognized currently in earnings and is reported as a component of investment and other income, net. The change in the fair value of these instruments represents a natural hedge as their gains and losses offset the changes in the underlying fair value of the monetary assets and liabilities due to movements in currency exchange rates. These contracts generally expire in three months or less.

If the derivative is designated as a cash flow hedge, the effective portion of the change in the fair value of the derivative is initially deferred in other comprehensive income. These amounts are subsequently recognized in income as a component of net revenue or cost of revenue in the same period the hedged transaction affects earnings. The ineffective portion of the change in the fair value of cash flow hedge is recognized currently in earnings and is reported as a component of investment and other income, net. Hedge effectiveness is measured by comparing the hedging instrument's cumulative change in fair value from inception to maturity to the forecasted transaction's terminal value. During fiscal years 2005, 2004, and 2003, Dell did not discontinue any cash flow hedges as substantially all forecasted foreign currency transactions were realized in Dell's actual results. Furthermore, hedge ineffectiveness was not material.

At January 28. 2005, Dell held purchased option contracts with a notional amount of approximately $2.0 billion, a net asset value of $53 million and a net unrealized deferred loss of $52 million, net of taxes. At January 28, 2005, Dell held forward contracts with a notional amount of approximately $3.0 billion, a net liability value of $146 million and a net unrealized gain of $21 million, net of taxes.

At January 30, 2004, Dell held purchased option contracts with a notional amount of approximately $2.0 billion, a net asset value of $41 million and a net unrealized deferred loss of $58 million, net of taxes. At January 30, 2004, Dell held forward contracts with a notional amount of approximately $3.0 billion, a net liability value of $185 million and a net unrealized loss of $24 million, net of taxes.

Long-Term Debt and Interest Rate Risk Management

In April 1998, Dell issued $200 million 6.55% fixed rate senior notes due April 15, 2008 (the "Senior Notes") and $300 million 7.10% fixed rate senior debentures due April 15, 2028 (the "Senior Debentures"). Interest on the Senior Notes and Senior Debentures is paid semi-annually, on April 15 and October 15. The Senior Notes and Senior Debentures rank pari passu and are redeemable, in whole or in part, at the election of Dell for principal, any accrued interest and a redemption premium based on the present value of interest to be paid over the term of the debt agreements. The Senior Notes and Senior Debentures generally contain no restrictive covenants, other than a limitation on liens on Dell's assets and a limitation on sale-leaseback transactions.

Concurrent with the issuance of the Senior Notes and Senior Debentures, Dell entered into interest rate swap agreements converting Dell's interest rate exposure from a fixed rate to a floating rate basis to better align the associated interest rate characteristics to its cash and investments portfolio. The interest rate swap agreements have an aggregate notional amount of $200 million maturing April 15, 2008 and $300 million maturing April 15, 2028. The floating rates are based on three-month London Interbank Offered Rates plus 0.41 % and 0.79% for the Senior Notes and Senior Debentures, respectively. As a result of the interest rate swap agreements, Dell's effective interest rates for the Senior Notes and Senior Debentures were 2.059% and 2.392%, respectively, for fiscal 2005.

The interest rate swap agreements are designated as fair value hedges, and the terms of the swap agreements and hedged items are such that effectiveness can be measured using the short-cut method defined in SFAS No. 133. The differential to be paid or received on the interest rate swap agreements is accrued and recognized as an adjustment to interest expense as interest rates change. The difference between Dell's carrying amounts and fair value of its long-term debt and related interest rate swaps was not material at January 28, 2005 and January 30, 2004.

NOTE 3—INCOME TAXES

The provision for income taxes consists of the following:

	FISCAL YEAR ENDED		
(In millions)	January 28, 2005	January 30, 2004	January 31, 2003
Current			
Domestic	$ 984	$ 969	$702
Foreign	209	132	94
Tax repatriation charge	280	—	—
Deferred	(71)	(22)	109
Provision for income taxes	$1,402	$1,079	$905

Income before income taxes included approximately $2.4 billion, $1.6 billion, and $968 million related to foreign operations in fiscal 2005, 2004, and 2003, respectively. On October 22, 2004, the American Jobs Creation Act of 2004 (the "Act") was signed into law. Among other items, the Act creates a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the U.S. at a tax rate of 5.25%, versus the U.S. federal statutory rate of 35%. Although the Act contains a number of

limitations related to the repatriation and some uncertainty remains, as of January 28, 2005, Dell believes that it has the information necessary to make an informed decision regarding the impact of the Act on its repatriation plans. Based on this new legislation, and subsequent guidance issued by the Department of Treasury, Dell determined during the fourth quarter of fiscal 2005 that it will repatriate $4.1 billion in foreign earnings. Accordingly, Dell recognized a tax repatriation charge of $280 million in accordance with SFAS No. 109, *Accounting for Income Taxes*. This tax charge includes an amount relating to an apparent drafting oversight that Congressional leaders indicate will be fixed by a Technical Corrections Bill sometime during calendar year 2005. The fiscal 2005 tax repatriation charge will be reduced in the quarter that the Technical Corrections Bill becomes law. In addition, at the time of repatriation further adjustment may be required depending upon a number of factors, including geographic location of cash, mix of foreign earnings, and statutory tax rates in effect at the time of the repatriation. The repatriation is required to be completed by the end of fiscal 2006. This tax repatriation charge increased Dell's effective tax rate by 6.3% for fiscal 2005.

Deferred taxes have not been provided on excess book basis in the amount of approximately $2.9 billion in the shares of certain foreign subsidiaries because these basis differences are not expected to reverse in the foreseeable future and are essentially permanent in duration. These basis differences arose primarily through the undistributed book earnings of the subsidiaries that Dell intends to reinvest indefinitely. The basis differences could reverse through a sale of the subsidiaries, the receipt of dividends from the subsidiaries as well as various other events. Net of available foreign tax credits, residual income tax of approximately $740 million would be due upon a reversal of this excess book basis. The excess book basis of $2.9 billion excludes the $4.1 billion to be repatriated under the Act.

The components of Dell's net deferred tax asset are as follows:

(in millions)	January 28, 2005	January 30, 2004
Deferred tax assets		
Deferred revenue	$ 241	$ 86
Inventory and warranty provisions	232	260
Investment impairments and unrealized gains	23	39
Provisions for product returns and doubtful accounts	22	21
Capital loss	6	96
Leasing	—	69
Other	99	104
	623	675
Deferred tax liabilities		
Fixed assets	(156)	(129)
Leasing	(10)	—
Other	(26)	(74)
	(192)	(203)
Net deferred tax asset	$ 431	$ 472
Current portion (included in other current assets)	$ 425	$ 339
Non-current portion (included in other non-current assets)	6	133
Net deferred tax asset	$ 431	$ 472

A portion of Dell's operations operate at a reduced tax rate or free of tax under various tax holidays which expire in whole or in part during fiscal 2012 through 2019. Many of these holidays may be extended when certain conditions are met. The income tax benefits attributable to the tax status of these subsidiaries were estimated to be approximately $280 million ($0.11 per share) in fiscal 2005, $210 million ($0.08 per share) in fiscal 2004, and $137 million ($0.05 per share) in fiscal 2003.

The effective tax rate differed from the statutory U.S. federal income tax rate as follows:

	FISCAL YEAR ENDED		
	January 28, 2005	January 30, 2004	January 31, 2003
U.S. federal statutory rate	35.0%	35.0%	35.0%
Foreign income taxed at different rates	(11.6)	(7.3)	(7.9)
Tax repatriation charge	6.3	—	—
Other	1.8	1.3	2.8
Effective tax rate	31.5%	29.0%	29.9%

The increase in Dell's fiscal 2005 effective tax rate, compared to fiscal 2004 and fiscal 2003, is due to the aforementioned tax repatriation charge, partially offset by a higher proportion of operating profits attributable to foreign jurisdictions.

NOTE 4—CAPITALIZATION

Preferred Stock

Authorized Shares. Dell has the authority to issue five million shares of preferred stock, par value $.01 per share. At January 28, 2005 and January 30, 2004, no shares of preferred stock were issued or outstanding.

Series A Junior Participating Preferred Stock. In conjunction with the distribution of Preferred Share Purchase Rights (see below), Dell's Board of Directors designated 200,000 shares of preferred stock as Series A Junior Participating Preferred Stock ("Junior Preferred Stock") and reserved such shares for issuance upon exercise of the Preferred Share Purchase Rights. At January 28, 2005 and January 30, 2004, no shares of Junior Preferred Stock were issued or outstanding.

Common Stock

Authorized Shares. As of January 28, 2005, Dell is authorized to issue seven billion shares of common stock, par value $.01 per share.

Share Repurchase Program. Dell has a share repurchase program that authorizes the company to purchase shares of common stock in order to both distribute cash to stockholders and manage dilution resulting from shares issued under Dell's equity compensation plans. However, Dell does not currently have a policy that requires the repurchase of common stock in conjunction with share-based payment arrangements. As of

January 28, 2005, Dell's share repurchase program authorized the purchase of up to 1.25 billion shares of common stock at an aggregate cost not to exceed $20 billion. Dell expects to repurchase shares of common stock through a systematic program of open market purchases. As of the end of fiscal 2005, Dell had cumulatively repurchased 1.2 billion shares for an aggregate cost of approximately $18.3 billion. During fiscal 2005, Dell repurchased 119 million shares of common stock for an aggregate cost of $4.2 billion.

Dell historically utilized equity instrument contracts to facilitate its repurchase of common stock; however, all remaining put and call contracts were settled in full during the fourth quarter of fiscal 2003.

Preferred Share Purchase Rights

In December 1995, Dell distributed a dividend of one Preferred Share Repurchase Right (a "Right") for each outstanding share of common stock, and since that distribution, shares of common stock have been issued with accompanying Rights. Each Right entitles the holder to purchase shares of Junior Preferred Stock at specified prices and rates. The Rights become exercisable when a person or group acquires 15% or more of Dell's outstanding common stock. When it becomes exercisable, a Right will entitle the holder (other than the acquiring person or group) to purchase, at the Right's then current exercise price, the number of shares of common stock having a market value of twice the exercise price of the Right. The Rights also contain provisions relating to mergers or other business combinations.

In certain circumstances, the Board of Directors may, at its option, exchange Rights (other than Rights held by the acquiring person or group) for shares of common stock or shares of Junior Preferred Stock at specified exchange rates. In addition, Dell will be entitled to redeem the Rights at $.001 per Right at any time before a person or group has acquired 15% or more of Dell's outstanding common stock. The Rights expire on November 29, 2005. The Board of Directors may amend the terms of the Rights to lower the 15% acquisition threshold to not less than the greater of (a) any percentage greater than the largest percentage of common stock known by Dell to be owned by any person (other than Michael S. Dell) or (b) 10%.

Neither the ownership nor the further acquisition of common stock by Michael S. Dell will cause the Rights to become exercisable or nonredeemable or will trigger the other features of the Rights.

NOTE 5—BENEFIT PLANS

Stock Option Plans. Dell has the following four stock option plans (collectively referred to as the "Option Plans") under which options were outstanding as of January 28, 2005:

- The Dell Computer Corporation 1989 Stock Option Plan (the "1989 Option Plan")
- The Dell Computer Corporation Incentive Plan (the "1994 Incentive Plan")
- The Dell Computer Corporation 1998 Broad-Based Stock Option Plan (the "1998 Broad-Based Plan"), and
- The Dell Computer Corporation 2002 Long-Term Incentive Plan (the "2002 Incentive Plan")

The Option Plans are administered by the Compensation Committee of Dell's Board of Directors.

The 1989 Option Plan, the 1994 Incentive Plan, and the 1998 Broad-Based Plan have been terminated (except for options previously granted under those plans that are still outstanding). Consequently, awards are currently only being made under the 2002 Incentive Plan.

The 2002 Incentive Plan provides for the granting of stock-based incentive awards to Dell's employees, nonemployee directors, and certain consultants and advisors to Dell. Awards may be either incentive stock options within the meaning of Section 422 of the Internal Revenue Code or nonqualified options. The right to purchase shares pursuant to existing stock option agreements typically vests pro-rata at each option anniversary date over a five-year period. The options are generally granted at fair market value and must be exercised within ten years from the date of grant. Dell has not issued any options to consultants or advisors to the company since fiscal 1999.

There were 291 million, 327 million, and 365 million options to purchase Dell's common stock available for future grants under the Option Plans as of January 28, 2005, January 30, 2004, and January 31, 2003, respectively. All of the shares available for future grants as of January 28, 2005 are under the 2002 Incentive Plan.

The following table summarizes stock option activity for the Option Plans:

	FISCAL YEAR ENDED					
	January 28, 2005		January 30, 2004		January 31, 2003	
(share data in millions)	Number of Options	Weighted-Average Exercise Price	Number of Options	Weighted-Average Exercise Price	Number of Options	Weighted-Average Exercise Price
Options outstanding—beginning of year	378	$28.30	387	$27.09	350	$26.36
Granted	52	34.35	51	30.01	84	26.37
Exercised	(45)	22.30	(35)	14.92	(22)	7.69
Canceled	(16)	32.39	(25)	31.62	(25)	31.75
Options outstanding—end of year	369	29.70	378	28.30	387	27.09
Options exercisable—end of year	171	$28.99	154	$26.74	130	$22.59

The following is additional information relating to options for the Option Plans outstanding as of January 28, 2005:

	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
(share data in millions)	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (Years)	Number of Shares	Weighted-Average Exercise Price
$0.01–$1.49	7	$ 1.17	1.11	7	$ 1.17
$1.50–$14.99	17	$ 7.74	2.42	17	$ 7.74
$15.00–$24.99	74	$22.41	6.14	37	$21.93
$25.00–$34.99	145	$29.04	7.56	40	$28.38
$35.00 and over	126	$39.27	6.22	70	$41.07
	369			171	

Employee Stock Purchase Plan. Dell has an employee stock purchase plan that qualifies under Section 423 of the Internal Revenue Code and permits substantially all employees to purchase shares of Dell's common stock. Participating employees may purchase common stock through payroll deductions at the end of each participation period at a purchase price equal to 85% of the lower of the fair market value of the common stock at the beginning or the end of the participation period. Common stock reserved for future employee purchases under the plan aggregated 21 million shares at January 28, 2005, 25 million shares at January 30, 2004 and 29 million shares at January 31, 2003. Common stock issued under this plan totaled 4 million shares in fiscal 2005, 4 million shares in fiscal 2004, and 4 million shares in fiscal 2003.

Restricted Stock Grants. During fiscal 2005, 2004, and 2003, Dell granted 0.4 million shares, 0.6 million shares, and 0.3 million shares of restricted stock, respectively. The weighted average fair value of restricted stock granted in fiscal 2005, 2004, and 2003 was $35.14, $27.92, and $25.43, respectively. For substantially all restricted stock grants, at the date of grant, the recipient has all rights of a stockholder, subject to certain restrictions on transferability and a risk of forfeiture. Restricted shares typically vest over a seven-year period beginning on the date of grant. Dell records unearned compensation in stockholders' equity equal to the market value of the restricted shares on the date of grant and charges the unearned compensation to expense over the vesting period.

401(k) Plan. Dell has a defined contribution retirement plan that complies with Section 401(k) of the Internal Revenue Code. Substantially all employees in the U.S. are eligible to participate in the plan. During calendar 2004, Dell matched 100% of each participant's voluntary contributions, subject to a maximum contribution of 3% of the participant's compensation. Beginning January 1, 2005, Dell began matching 100% of each participant's voluntary contributions, subject to a maximum contribution of 4% of the participant's compensation, and participants vest immediately in all company contributions to the Plan. Dell's contributions during fiscal 2005, 2004, and 2003 were $48 million, $42 million, and $38 million, respectively. Dell's contributions are invested proportionate to each participant's voluntary contributions in the investment options provided under the plan. Investment options include Dell stock, but neither participant nor Dell contributions are required to be invested in Dell stock.

NOTE 6—FINANCIAL SERVICES

Dell is currently a partner in DFS, a joint venture with CIT. The joint venture allows Dell to provide its customers with various financing alternatives while CIT usually provides the financing for the transaction between DFS and the customer for certain transactions. In general, DFS facilitates customer financing transactions through either loan or lease financing. For customers who desire loan financing, Dell sells equipment directly to customers who, in turn, enter into loans with CIT to finance their purchases. For customers who desire lease financing, Dell sells the equipment to DFS, and DFS enters into direct financing lease arrangements with the customers. Dell recognized revenue from the sale of products pursuant to loan and lease financing transactions of $5.6 billion, $4.5 billion, and $3.6 billion during fiscal 2005, 2004, and 2003, respectively.

Dell currently owns a 70% equity interest in DFS. During the third quarter of fiscal 2004, Dell began consolidating DFS's financial results due to the adoption of FIN 46R. FIN 46R provides that if an entity is the primary beneficiary of a Variable Interest Entity ("VIE"), the assets, liabilities, and results of operations of the VIE should be consolidated

in the entity's financial statements. Based on the guidance in FIN 46R, Dell concluded that DFS is a VIE and Dell is the primary beneficiary of DFS's expected cash flows. Prior to consolidating DFS's financial results, Dell's investment in DFS was accounted for under the equity method because the company historically did not exercise control over DFS. Accordingly, the consolidation of DFS had no impact on Dell's net income or earnings per share. CIT's equity ownership in the net assets of DFS as of January 28, 2005 was $13 million, which is recorded as minority interest and included in other non-current liabilities on Dell's consolidated statement of financial position. The consolidation did not alter the partnership agreement or risk sharing arrangement between Dell and CIT.

During the third quarter of fiscal 2005, Dell and CIT executed an agreement that extended the term of the joint venture to January 29, 2010 and modified certain terms of the relationship. In accordance with the extension agreement, net income and losses generated by DFS are currently allocated 70% to Dell and 30% to CIT. CIT has no recourse or rights of return to Dell, except that end-user customers may return equipment in accordance with Dell's standard return policy. The extension agreement provides Dell with the option to purchase CIT's 30% interest in DFS in February 2008 for a purchase price ranging from $100 million to $345 million, depending upon DFS's profitability. If Dell does not exercise this purchase option, Dell is obligated to purchase CIT's 30% interest upon the occurrence of certain termination events, or expiration of the joint venture on January 29, 2010 for a purchase price ranging from $100 million to $345 million.

Prior to execution of the extension agreement, CIT provided all of the financing for transactions between DFS and the customer. The extension agreement also gives Dell the right, but not the obligation, to participate in such financings beginning in the fourth quarter of fiscal 2005. During the fourth quarter of fiscal 2005, Dell began selling certain loan and lease finance receivables to an unconsolidated qualifying special purpose entity that is wholly owned by Dell. The qualifying special purpose entity is a separate legal entity with assets and liabilities separate from those of Dell. The qualifying special purpose entity has entered into a financing arrangement with a multiseller conduit that in turn issues asset-backed debt securities to the capital markets. Transfers of financing receivables are recorded in accordance with the provisions of SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities.* The sale of these loan and lease financing receivables did not have a material impact on Dell's consolidated financial position, results of operations, or cash flows for fiscal 2005.

DFS maintains credit facilities with CIT which provide DFS with a funding capacity of up to $1.0 billion. As of January 28, 2005, outstanding advances under these facilities totaled $158 million and are included in other current and non-current liabilities on Dell's consolidated statement of financial position. Dell is dependent upon DFS to provide financing for a significant number of customers who elect to finance Dell products, and DFS is dependent upon CIT to access the capital markets to provide funding for these transactions. If CIT is unable to access the capital markets, Dell would find additional alternative sources for financing for its customers or self-finance these activities.

NOTE 7—DEFERRED REVENUE AND WARRANTY LIABILITY

Revenue from extended warranty and service contracts, for which Dell is obligated to perform, is recorded as deferred revenue and subsequently recognized over the term of the contract or when the service is completed. Dell records warranty liabilities at the

time of sale for the estimated costs that may be incurred under its basic limited warranty. Changes in Dell's aggregate deferred revenue and warranty liability (basic and extended warranties), which are included in other current and non-current liabilities on Dell's consolidated statement of financial position, are presented in the following table:

	FISCAL YEAR ENDED	
(in millions)	January 28, 2005	January 30, 2004
Aggregate deferred revenue and warranty liability at beginning of period	$ 2,694	$2,042
Revenue deferred and costs accrued for new warranties	3,435	2,547
Service obligations honored	(1,176)	(983)
Amortization of deferred revenue	(1,359)	(912)
Aggregate deferred revenue and warranty liability at end of period	$ 3,594	$2,694
Current portion	$ 1,893	$1,333
Non-current portion	1,701	1,361
Aggregate deferred revenue and warranty liability at end of period	$ 3,594	$2,694

NOTE 8—COMMITMENTS, CONTINGENCIES, AND CERTAIN CONCENTRATIONS

Lease Commitments. Dell leases property and equipment, manufacturing facilities, and office space under noncancellable leases. Certain of these leases obligate Dell to pay taxes, maintenance, and repair costs. As of January 28, 2005, future minimum lease payments under these noncancellable leases were as follows: $52 million in fiscal 2006; $40 million in fiscal 2007; $36 million in fiscal 2008; $28 million in fiscal 2009; $18 million in fiscal 2010; and $83 million thereafter.

Dell historically maintained master lease facilities which provided the company with the ability to lease certain real property, buildings, and equipment to be constructed or acquired. These leases were accounted for as operating leases by Dell. During fiscal 2004, Dell paid $636 million to purchase all of the assets covered by its master lease facilities. Accordingly, the assets formerly covered by these facilities are included in Dell's consolidated statement of financial position and Dell has no remaining lease commitments under these master lease facilities.

Rent expense under all leases totaled $60 million, $76 million, and $96 million for fiscal 2005, 2004, and 2003, respectively.

DFS Purchase Commitment. Pursuant to the joint venture agreement between DFS and CIT, Dell has a minimum purchase obligation to purchase CIT's 30% interest in DFS at the expiration of the joint venture on January 29, 2010, for a purchase price ranging from $100 million to $345 million. See Note 6 of "Notes to Consolidated Financial Statements."

Restricted Cash. Pursuant to the joint venture agreement between DFS and CIT, DFS is required to maintain certain escrow cash accounts. Due to the consolidation of DFS,

$438 million in restricted cash is included in other current assets on Dell's consolidated statement of financial position as of January 28, 2005.

Legal Matters. Dell is subject to various legal proceedings and claims arising in the ordinary course of business. Dell's management does not expect that the outcome in any of these legal proceedings, individually or collectively, will have a material adverse effect on Dell's financial condition, results of operations, or cash flows.

Certain Concentrations. All of Dell's foreign currency exchange and interest rate derivative instruments involve elements of market and credit risk in excess of the amounts recognized in the consolidated financial statements. The counterparties to the financial instruments consist of a number of major financial institutions. In addition to limiting the amount of agreements and contracts it enters into with any one party, Dell monitors its positions with and the credit quality of the counterparties to these financial instruments. Dell does not anticipate nonperformance by any of the counterparties.

Dell's investments in debt securities are placed with high quality financial institutions and companies. Dell's investments in debt securities primarily have maturities of less than five years. Management believes that no significant concentration of credit risk for investments exists for Dell.

Dell markets and sells its products and services to large corporate clients, governments, healthcare and education accounts, as wel1 as small-to-medium businesses and individuals. Dell's receivables from such parties are well diversified.

Dell purchases a number of components from single sources. In some cases, alternative sources of supply are not available. In other cases, Dell may establish a working relationship with a single source if Dell believes it is advantageous due to performance, quality, support, delivery, capacity or price considerations. If the supply of a critical single-source material or component were delayed or curtailed, Dell's ability to ship the related product in desired quantities and in a timely manner could be adversely affected. Even where alternative sources of supply are available, qualification of the alternative suppliers and establishment of reliable supplies could result in delays and a possible loss of sales, which may have an adverse effect on Dell's operating results.

NOTE 9—SEGMENT INFORMATION

Dell conducts operations worldwide and is managed in three geographic segments: the Americas, Europe, and Asia Pacific–Japan regions. The Americas region, which is based in Round Rock, Texas, covers the U.S., Canada, and Latin America. Within the Americas, Dell is further segmented into Business and U.S. Consumer. The Americas Business segment includes sales to corporate, government, healthcare, education, and small and medium business customers while the U.S. Consumer segment includes sales primarily to individual consumers. The European region, which is based in Bracknell, England, covers Europe, the Middle East, and Africa. The Asia Pacific–Japan region covers the Pacific Rim, including Australia and New Zealand, and is based in Singapore.

The accounting policies of Dell's reportable segments are the same as those described in the summary of significant accounting policies. Dell allocates resources to and evaluates the performance of its segments based on operating income. Corporate expenses are included in Dell's measure of segment operating income for management

reporting purposes. The asset totals disclosed by geography are directly managed by those regions and include accounts receivable, inventory, certain fixed assets, and certain other assets. Assets are not allocated specifically to the Business and U.S. Consumer segments within the Americas. Corporate assets primarily include cash and cash equivalents, investments, deferred tax assets, and other assets.

The table below presents information about Dell's reportable segments:

	FISCAL YEAR ENDED		
(in millions)	January 28, 2005	January 30, 2004	January 31, 2003
Net revenue			
Americas:			
Business	$25,339	$21,888	$19,394
U.S. consumer	7,601	6,715	5,653
Total Americas	32,940	28,603	25,047
Europe	10,787	8,495	6,912
Asia Pacific–Japan	5,478	4,346	3,445
Total net revenue	$49,205	$41,444	$35,404
Operating income			
Americas:			
Business	$ 2,579	$ 2,194	$ 1,945
U.S. consumer	399	400	308
Total Americas	2,978	2,594	2,253
Europe	818	637	388
Asia Pacific–Japan	458	313	203
Total operating income	$ 4,254	$ 3,544	$ 2,844
Depreciation and amortization expense			
Americas:			
Business	$ 125	$ 102	$ 97
U.S. consumer	53	41	38
Total Americas	178	143	135
Europe	88	71	47
Asia Pacific–Japan	68	49	29
Total depreciation and amortization expense	$ 334	$ 263	$ 211
Assets			
Americas	$ 3,724	$ 3,134	$ 2,847
Europe	1,817	1,510	1,302
Asia Pacific–Japan	1,075	860	634
Corporate assets	16,599	13,807	10,687
Total assets	$23,215	$19,311	$15,470

The following is net revenue and long-lived asset information by geographic region:

(in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Net revenue			
United States	$30,338	$26,510	$23,355
Foreign countries	18,867	14,934	12,049
Total net revenue	$49,205	$41,444	$35,404
Long-lived assets			
United States	$ 1,267	$ 1,145	$ 613
Foreign countries	425	372	300
Total long-lived assets	$ 1,691	$ 1,517	$ 913

The allocation between domestic and foreign net revenue is based on the location of the customers. Net revenue and long-lived assets from no single foreign country comprised more than 10% of Dell's consolidated net revenues or long-lived assets during fiscal 2005, 2004, and 2003.

The following is net revenue by product groups:

(in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Desktop computer systems	$24,631	$21,026	$18,865
Notebook computers	14,057	11,380	9,638
Enterprise systems	10,517	9,038	6,901
Total net revenue	$49,205	$41,444	$35,404

Net revenue by product group includes associated revenue from printing and imaging systems, software and peripherals, and global services. No single customer accounted for more than 10% of Dell's consolidated net revenue during fiscal 2005, 2004 and 2003.

NOTE 10—SUPPLEMENTAL CONSOLIDATED FINANCIAL INFORMATION

(in millions)	January 28, 2005	January 30, 2004
Supplemental Consolidated Statements of Financial Position Information		
Accounts receivable:		
Gross accounts receivable	$ 4,492	$ 3,719
Allowance for doubtful accounts	(78)	(84)
	$ 4,414	$ 3,635
Inventories:		
Production materials	$ 228	$ 161
Work-in-process	58	69
Finished goods	173	97
	$ 459	$ 327
Property, plant, and equipment:		
Land and buildings	$ 1,207	$ 1,158
Computer equipment	1,053	898
Machinery and other equipment	757	594
Total property, plant, and equipment	3,017	2,650
Accumulated depreciation and amortization	(1,326)	(1,133)
	$ 1,691	$ 1,517
Accrued and other current liabilities:		
Deferred revenue	$ 1,389	$ 961
Compensation	753	603
Other	3,099	2,016
	$ 5,241	$ 3,580
Other non-current liabilities:		
Deferred revenue	$ 1,415	$ 1,092
Other	674	538
	$ 2,089	$ 1,630

	FISCAL YEAR ENDED		
(in millions)	January 28, 2005	January 30, 2004	January 31, 2003
Supplemental Consolidated Statements of Income Information			
Investment and other income, net:			
Investment income, primarily interest	$226	$200	$227
Gains (losses) on investments, net	6	16	(6)
Interest expense	(16)	(14)	(17)
Other	(25)	(22)	(21)
	$191	$180	$183

(in millions)	FISCAL YEAR ENDED January 28, 2005	January 30, 2004	January 31, 2003
Supplemental Consolidated Statements of Cash Flows Information			
Changes in operating working capital accounts:			
Accounts receivable, net	$ (837)	$ (813)	$ 190
Inventories	(130)	(53)	(21)
Accounts payable	1,595	1,283	844
Accrued and other liabilities	1,538	867	585
Other, net	(411)	(412)	(388)
	$1,755	$ 872	$1,210
Income taxes paid	$ 575	$ 699	$ 607
Interest paid	$ 31	$ 30	$ 20

NOTE 11—UNAUDITED QUARTERLY RESULTS

The following tables contain selected unaudited consolidated statements of income and stock sales price data for each quarter of fiscal 2005 and 2004:

(in millions, except per share data)	FISCAL YEAR 2005 4th Quarter[a]	3rd Quarter	2nd Quarter	1st Quarter
Net revenue	$13,457	$12,502	$11,706	$11,540
Gross margin	$ 2,495	$ 2,313	$ 2,134	$ 2,073
Net income	$ 667	$ 846	$ 799	$ 731
Earnings per common share[(b)]:				
Basic	$ 0.27	$ 0.34	$ 0.32	$ 0.29
Diluted	$ 0.26	$ 0.33	$ 0.31	$ 0.28
Weighted average shares outstanding:				
Basic	2,485	2,493	2,518	2,539
Diluted	2,553	2,546	2,574	2,593
Stock sales prices per share:				
High	$ 42.38	$ 36.66	$ 36.66	$ 36.31
Low	$ 35.06	$ 33.12	$ 34.05	$ 31.20

(in millions, except per share data)	FISCAL YEAR 2004 4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
Net revenue	$11,512	$10,622	$9,778	$9,532
Gross margin	$ 2,091	$ 1,935	$1,778	$1,748
Net income	$ 749	$ 677	$ 621	$ 598
Earnings per common share[b]:				
Basic	$ 0.29	$ 0.26	$ 0.24	$ 0.23
Diluted	$ 0.29	$ 0.26	$ 0.24	$ 0.23
Weighted average shares outstanding:				
Basic	2,557	2,563	2,567	2,572
Diluted	2,616	2,623	2,624	2,614
Stock sales prices per share:				
High	$ 36.52	$ 36.98	$34.00	$29.89
Low	$ 32.65	$ 30.94	$29.49	$22.86

[a] *During the fourth quarter of fiscal 2005. Dell recorded a tax repatriation charge of $280 million pursuant to a favorable tax incentive provided by the American Jobs Creation Act of 2004. This tax charge is related to Dell's decision to repatriate $4.1 billion in foreign earnings.*

[b] *Earnings per common share are computed independently for each of the quarters presented. Therefore, the sum of the quarterly per common share information may not equal the annual earnings per common share.*

CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures. Dell's Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of Dell's disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act) as of the end of the period covered by this report, have concluded that, based on the evaluation of these controls and procedures, Dell's disclosure controls and procedures were effective.

Management's Report on Internal Control over Financial Reporting. Dell's management, under the supervision of Dell's Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) or 15d-15(f) under the Exchange Act). Management evaluated the effectiveness of Dell's internal control over financial reporting based on the framework in *Internal Control–Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, management has concluded that Dell's internal control over financial reporting was effective as of January 28, 2005.

Management's assessment of the effectiveness of Dell's internal control over financial reporting as of January 28, 2005, has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their Report of Independent Registered Public Accounting Firm included in "Item 8–Financial Statements and Supplementary Data."

Changes in Internal Control over Financial Reporting. Dell's management, with the participation of Dell's Chief Executive Officer and Chief Financial Officer, has evaluated whether any change in Dell's internal control over financial reporting occurred

during the fourth quarter of fiscal 2005. Based on that evaluation, management concluded that there has been no change in Dell's internal control over financial reporting during the fourth quarter of fiscal 2005 that has materially affected, or is reasonably likely to materially affect, Dell's internal control over financial reporting.

DELL INC.

Valuation and Qualifying Accounts (in millions)

Fiscal Year	Description	Balance at Beginning of Period	Charged to Bad Debt Expense	Write-Offs Charged to Allowance	Balance at End of Period
2005	Allowance for doubtful accounts	$84	$31	$37	$78
2004	Allowance for doubtful accounts	$71	$48	$35	$84
2003	Allowance for doubtful accounts	$68	$39	$36	$71