ADOBE SYSTEMS INC
Form 10-K
February 05, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 1, 2006

OR

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

For the transition period from   **to**

Commission file number: 0-15175

ADOBE SYSTEMS INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware	**77-0019522**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

345 Park Avenue, San Jose, California 95110-2704

(Address of principal executive offices and zip code)

(408) 536-6000

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $0.0001 par value per share	The NASDAQ Stock Market LLC (NASDAQ Global Select Market)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by checkmark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x   No o

Indicate by checkmark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o   No x

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

Indicate by checkmark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of   accelerated filer and large accelerated filer   in Rule 12b-2 of the Exchange Act. Large accelerated filer x   Accelerated filer o   Non-accelerated filer o

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

The aggregate market value of the registrant s common stock, $0.0001 par value per share, held by non-affiliates of the registrant on June 2, 2006, the last business day of the registrant s most recently completed second fiscal quarter, was $14,829,198,488 (based on the closing sales price of the registrant s common stock on that date). Shares of the registrant s common stock held by each officer and director and each person who owns 5% or more of the outstanding common stock of the registrant have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. As of December 29, 2006, 588,456,485 shares of the registrant s common stock, $0.0001 par value per share, were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2007 Annual Meeting of Stockholders (the   Proxy Statement), to be filed within 120 days of the end of the fiscal year ended December 1, 2006, are incorporated by reference in Part III hereof. Except with respect to information specifically incorporated by reference in this Form 10-K, the Proxy Statement is not deemed to be filed as part hereof.

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Forward-Looking Statements

In addition to historical information, this Annual Report on Form 10-K contains forward-looking statements, including statements regarding product plans, future growth and market opportunities, which involve risks and uncertainties that could cause actual results to differ materially. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in this section under Risk Factors. You should carefully review the risks described herein and in other documents we file from time to time with the Securities and Exchange Commission (SEC), including the Quarterly Reports on Form 10-Q to be filed in 2007. When used in this report, the words expects, could, would , may, anticipates, intends, plans, seeks, targets, estimates, looks for, looks to, and similar expressions, as well as statements regarding our focus for future, are generally intended to identify forward-looking statements. You should not place undue reliance on these forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. We undertake no obligation to publicly release any revisions to the forward-looking statements or reflect events or circumstances after the date of this document.

PART I

ITEM 1. BUSINESS

Founded in 1982, Adobe Systems Incorporated is one of the largest and most diversified software companies in the world. We offer a line of creative, business and mobile software and services used by creative professionals, designers, knowledge workers, high-end consumers, original equipment manufacturers (OEM), developers and enterprises for creating, managing, delivering and engaging with compelling content and experiences across multiple operating systems, devices and media. We distribute our products through a network of distributors and dealers, value-added resellers (VARs), systems integrators, independent software vendors (ISVs) and OEMs, direct to end users, and through our own Web site at www.adobe.com. We also license our technology to hardware manufacturers, software developers and service providers, and we offer integrated software solutions to businesses of all sizes. We have operations in the Americas; Europe, Middle East and Africa (EMEA); and Asia. Our software runs on personal computers with Microsoft Windows, Apple OS, Linux, UNIX and various non-personal computing platforms, depending on the product.

Adobe was originally incorporated in California in October 1983 and was reincorporated in Delaware in May 1997. We maintain executive offices and principal facilities at 345 Park Avenue, San Jose, California 95110-2704. Our telephone number is 408-536-6000. We maintain a Web site at www.adobe.com. Investors can obtain copies of our SEC filings from this site free of charge, as well as from the SEC Web site at www.sec.gov.

BUSINESS OVERVIEW

Since the early 1980 s, Adobe software and technologies have helped redefine how people engage with ideas and information anytime, anywhere, and through any medium. The impact of our solutions is evident across many industries and is felt by anyone who creates, views, and interacts with information.

Today, through the delivery of powerful design, imaging, and publishing software for print, Web and video production, and by delivering a ubiquitous technology platform, we help people express, share, manage and collaborate on their ideas in imaginative and meaningful new ways.

Our strategy is to address the needs of a variety of customers, which include creative professionals graphic designers, Web designers, videographers, photographers, and professional publishers; knowledge workers teams of workers who share and collaborate on high-value information. Our customers also include enterprise users IT managers, line of business managers, and executives; high-end consumers digital imaging and digital video hobbyists and enthusiasts. OEM partners such as mobile device manufacturers, printer manufacturers, Internet service providers and developers.

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We execute against this strategy by delivering products that support industry standards and can be deployed across multiple computing environments. We also leverage our technology platform, which utilizes our universal Adobe Reader and Adobe Flash Player software. Our technology platform allows users of our products and technologies to ensure reliable, secure and rich application experiences across browsers, desktops and devices.

PRODUCTS AND SERVICES OVERVIEW

At the beginning of fiscal 2006, coinciding with the completion of our acquisition of Macromedia, Inc. (Macromedia), we categorized our products and services into the following segments: Creative Solutions, Knowledge Worker Solutions, Enterprise and Developer Solutions, Mobile and Device Solutions, and Other. This overview, organized by segments, combines an explanation of our various market opportunities with a summary of our fiscal 2006 results and a discussion of our strategies to address our market opportunities in fiscal 2007 and beyond.

Creative Solutions Segment

Creative Solutions Market Opportunity

Our Creative Solutions segment focuses primarily on the needs of the creative professional customer. Creative professionals include graphic designers, production artists, Web designers, user interface designers, writers, videographers, photographers and prepress professionals who use and rely on Adobe s solutions for professional publishing, Web design, professional photography, video production, animation and motion graphic production, and printing visually rich information.

Our software tools are used by creative professionals to create much of the printed and on-line information people see and read every day, including newspapers, magazines, Web sites, catalogs, advertisements, brochures, product documentation, books, memos, reports and banners. Our tools are also used to create and enhance visually rich content, including video, animation and mobile content, that is created by multimedia, film, television, audio and video producers who work in advertising, Web design, music, entertainment, corporate and marketing communications, product design, user interface design, sales training, printing, architecture, and fine arts. Knowledge workers, hobbyists and high end consumers are also attracted to our creative products to create and deliver content that is of creative professional quality.

As technology continues to improve, the market dynamics for these creative professionals continue to evolve. Due to the ever changing ways in which people choose to receive information, creative professionals look to their software tools as a means to make their information impactful and repurpose content across a variety of media and applications. They desire greater efficiency from the software they use to streamline their publishing and content creation workflows and to effectively manage their assets. They also look for new and innovative ways to deliver their content and information to hand-held devices such as mobile handsets and consumer electronic devices.

Adobe s brand and customer loyalty in this market continues to be strong. Creative professional customers license upgrade and new units of our Creative Solutions products due to the high degree of innovative new features and significant productivity gained through their use. They also frequently license upgrade and new units of these products when they buy new computers, or migrate to new or updated operating systems.

In addition, knowledge workers at work and hobbyists at home license our Creative Solutions products. Knowledge workers desire professional-quality products to accomplish tasks such as creating visually-rich sales presentations, real estate flyers, and school year books. Hobbyists use our tools to create

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distinctive communication, photo albums, community newsletters, animations, videos and web sites for family, friends or community organizations.

The businesses of creative professionals are sensitive to the economy as they derive their revenue mainly from corporate marketing, product marketing and ad spending in corporations. In difficult economic times, corporations tend to reduce marketing spending and the businesses of creative professionals often may decline. Conversely, in an environment where the economy is stable or improving, corporations tend to increase their marketing spending, which leads to stable or improved business conditions for creative professionals. Thus, depending on economic conditions and the status of their businesses, these users adjust their spending on items such as hardware and software, and the staffing levels within their company. Due to this correlation, our Creative Solutions opportunity is closely linked to the performance of the economy in each of the countries in which we do business.

With the increasing use of the Web as a means for marketing and advertising, we believe a key driver of our Creative Solutions business will also be the growing amount of Web site and mobile device content created by our customers to deliver impactful and compelling Web-based experiences for their constituents.

Another driver of our Creative Solutions business is the growth in the use of digital devices such as digital cameras, digital video cameras, multimedia-enabled computers, DVD players, scanners, Web-capable image and video-enabled handheld devices, cellular phones, and other non-PC Internet-connected devices. In addition, Internet broadband adoption makes the Web a viable platform for the delivery of rich media, especially digital video. In turn, the growth in the use of high definition (HD) televisions and video is driving the need for HD-enhanced video tools to produce HD content for movies, and cable and commercial television.

As the use of digital photography and digital videography grows, we believe creative professionals and professional photographers throughout the world will continue to require software solutions to edit, enhance and manage their digital photographs and digital videos. In addition, we believe creative professionals and Web developers are increasing their use of digital video streams over the Web to create more compelling Web sites that leverage the adoption of broadband. We believe professional videographers are upgrading their systems to support HD video content creation, enhancement and delivery. We also believe hobbyists will use, with more frequency, digital imaging and digital video software as they purchase more affordable digital SLR cameras and digital video cameras.

Creative Solutions Business Summary

In fiscal 2006, we maintained our focus on driving adoption of our creative products, particularly our Adobe Creative Suite products, our Macromedia Studio product, and software bundles containing variations of both. Available in two options (Standard and Premium), the Adobe Creative Suite incorporates several of our technologies used by creative professionals into one product and is a complete design solution that provides efficiency through improved product integration and integrated workflow capabilities.

After achieving combined record revenue for our Adobe Creative Suite and Macromedia Studio products in the first quarter of fiscal 2006, we began to experience a decline in revenue with these products starting in our second quarter of the fiscal year. We attributed this decline to awareness by our creative professional customers of new versions of the products that are expected to ship in fiscal 2007. We also attributed customer deferral of purchase of Creative Suite products to our customers desire to have new support in Adobe applications for the Apple hardware platform which includes Intel-based processors something we publicly stated would not be available until the next release of the Creative Suite family of products.

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In fiscal 2006, we also continued to focus on driving adoption of our dynamic media and digital video-based technologies. In the first quarter of fiscal 2006, we released new versions of our digital video products, including Adobe Premiere Pro version 2.0 software for video editing, Adobe After Effects version 7.0 software for adding special effects to video, Adobe Audition version 2.0 software for audio editing and Adobe Encore version 2.0 software for DVD creation. Along with these individual digital video products, we also delivered a new suite containing these technologies called Adobe Production Studio.

In addition to various new features and ease-of-use improvements found in each of the new releases, we added enhanced support for Flash Video output to our family of digital video products to leverage the broad, increased adoption of Flash Video on the Web as a means to deliver compelling video content. These new features combined with the enhanced Flash Video support helped drive record revenue and more than 45 percent year-over-year growth for our digital video business in fiscal 2006. Adobe also won a prestigious Technical and Engineering Emmy Award from the National Academy of Television Arts and Sciences for its Flash Video technology, in recognition of the software s pivotal role in bringing television content to the Internet.

In addition to licensing our technologies as bundles or as suites during fiscal 2006, we also continued to focus on adoption of our standalone products such as Adobe After Effects Professional, Adobe InDesign, Adobe Illustrator, Adobe Photoshop, Adobe Premiere Pro, Macromedia Dreamweaver, and Macromedia Flash.

In the professional page layout market, we continued to drive market share gains during the year with our Adobe InDesign product. In addition to success with the standalone desktop version, we also saw the InDesign ecosystem grow in fiscal 2006 our software and systems integrator partners successfully deployed new innovative workflow solutions based on InDesign and InDesign Server within enterprise-class newspaper, magazine and book publishing systems. Our success in these areas contributed to a second consecutive year of record revenue in this product category.

We also maintained our focus during the year on meeting the digital imaging and video software needs of professional photographers, professional videographers, business users and hobbyists. Adobe Photoshop is an essential tool in these customers workflows, and they rely on Adobe s digital imaging and video editing solutions to create and enhance many of the pictures and video we see everyday in print, on television, in movies and on the Web.

In the first quarter of fiscal 2006, we released a new beta version of Adobe Photoshop Lightroom. Photoshop Lightroom is an all-new digital imaging solution targeted at professional photographers that delivers an efficient, powerful way to import, select, develop and showcase large volumes of digital images.

In addition, during the fourth quarter of fiscal 2006, we released version 5.0 of our Adobe Photoshop Elements software, which is our digital imaging application targeted for amateur photographers and digital imaging hobbyists. In the same quarter, we released version 3.0 of Adobe Premiere Elements software, which is our video editing software that can be used by hobbyists to enhance and share their digital video memories on DVDs. We also released a software bundle that includes the new versions of Adobe Photoshop Elements and Adobe Premiere Elements to target hobbyists who desire both applications in one affordable package. These new hobbyist product releases helped to generate record revenue in this product category during the year, and contributed year-over-year revenue growth to our overall creative business.

Creative Solutions Business Strategy

In fiscal 2007, our Creative Solutions strategy will continue to focus on driving revenue growth and increasing market share of our products through the delivery of comprehensive software platforms that meet the evolving needs of our customers. To help drive this strategy, we plan to deliver Creative

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Suite version 3, which will contain improved integration of our Creative Solutions products to enhance product functionality and to enable more efficient collaboration and workflows.

In addition, the creation and enhancement of digital video and motion graphics by creative professionals, and opportunities to improve user workflow and the delivery of this content to the Web and to mobile and other non-PC related devices, represent an emerging opportunity we intend to address as part of our Creative Solution offerings.

We believe that, while many customers have made or will make the switch to our Creative Suite products from individual applications over time, there continues to exist an opportunity of upgrading existing individual application users to newer versions of these individual applications. In addition, we will market the benefits of newer versions of the Creative Suite to existing Creative Suite and Macromedia Studio users to drive Creative Suite to Creative Suite and Studio to Creative Suite upgrades. We also will market the features of these products to new users of creative applications those who aspire to be creative professionals, or those at home or at work who wish to use the professional-level capabilities of our solutions, but are not trained creative professionals.

We intend to continue our efforts to be the recognized market leader in the professional page layout and Web layout software markets. In page layout, we intend to continue to add new features to our InDesign product, as well as continue to enhance its integration with other products print professionals utilize in their workflows. In Web layout, we strive to continue to redefine the Web experience by offering the most feature-rich, market-leading solutions for Website design and development with our Dreamweaver and Flash offerings.

We plan to continue to enhance our Photoshop product offerings to meet the evolving needs of professional photographers and creative professional customers, including graphic designers, Web designers, video producers and imaging enthusiasts to drive upgrades and new user adoption. We also plan to release version 1.0 of Adobe Photoshop Lightroom, which will improve integrated digital photography workflows for professional photographers. In addition, as we have seen during the past three fiscal years, we believe many customers will continue to license Photoshop capabilities via our Creative Suite products as opposed to licensing the standalone version.

With our set of professional digital video and motion graphic products, we strive to provide the strongest, market-leading digital video, motion graphic and animation authoring platform for our customers. To grow this business, we will continue to market the benefits of this platform to creative professionals and videographers in the film, broadcast, corporate and event videography market segments, and we are working with partners to deliver integrated video systems. With broad adoption of Adobe Flash Player and its high-quality video playback features, we will work to provide a seamless video authoring-to-playback capability for those wishing to provide a rich video experience on the Web.

In addition, as the number of imaging and video hobbyists desiring easy-to-use video editing solutions grows, we intend to enhance the video editing and DVD creation capabilities of our Adobe Premiere Elements product for the sharing of digital video memories. We also plan to continue to target the imaging and video hobbyist markets with an integrated offering of our Photoshop Elements and Premiere Elements products.

With our set of professional digital video and motion graphic products, we strive to provide the strongest, market-leading digital video, motion graphic and animation authoring platform for our customers. To grow this business, we will continue to market the benefits of this platform to creative professionals and videographers in the film, broadcast, corporate and event videography market segments, and we are working with partners to deliver integrated video systems. With broad adoption of Adobe Flash Player and its high-quality video playback features, we will work to provide a seamless video authoring-to-playback capability for those wishing to provide a rich video experience on the Web. In addition, as the

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Creative Solutions Products

Adobe After Effects professional software used to create sophisticated animation, motion graphics and visual effects found in television broadcast, film, DVD authoring and the Web; available in two versions: After Effects Standard provides basic 2D and 3D compositing, animation and visual effects tools; After Effects Professional adds advanced features such as motion tracking and stabilization, advanced keying and warping tools, more than 30 additional visual effects, and additional audio effects.

Adobe Audition a professional audio editing environment designed for demanding audio and video professionals; provides advanced audio mixing, editing and effects processing capabilities.

Adobe Creative Suite Premium Edition an integrated software solution that creative professionals can use as a platform to modify and enhance digital images, create graphics, produce professional-quality printed publications, create and maintain dynamic Web sites, author visually rich content for wireless Web devices, and share content reliably for print and screen display. The suite combines Adobe Acrobat Professional, Adobe GoLive, Adobe Illustrator, Adobe InDesign and Adobe Photoshop technologies with file management and integration technology called Version Cue and a navigational control center called Adobe Bridge.

Adobe Creative Suite Standard Edition an integrated software solution that creative professionals can use as a platform to modify and enhance digital images, create graphics, and produce professional-quality printed publications. The suite combines Adobe Illustrator, Adobe InDesign and Adobe Photoshop technologies with file management and integration technology called Version Cue and a navigational control center called Adobe Bridge.

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Adobe Encore DVD a professional DVD authoring and creation software; provides a comprehensive set of design tools and integration with other Adobe software to create a streamlined DVD creation workflow; provides ability to output projects to recordable DVD formats, ensuring a wide degree of playback compatibility.

Adobe GoLive Web design and publishing software that provides innovative tools that Web authors use to design, layout, produce and maintain content for Web sites and wireless Web devices without the need for complex multi−media programming.

Adobe Graphics Server imaging server software used to create and maintain digital graphics and images on frequently updated data-driven content, such as Web sites and printed catalogs, by automating the creation and the reuse of images; integrates with content management and e-commerce systems to automate workflows, and eliminates the tedious manual tasks of refining and reformatting images for specific purposes.

Adobe Illustrator a vector-based illustration design tool used to create compelling graphic artwork for print publications and the Web.

Adobe InCopy an editorial tool for collaboration between writers, editors and copy-fitters; Adobe InCopy is a companion to Adobe InDesign.

Adobe InDesign a page-layout application for publishing professionals; based on an open, object-oriented architecture it enables Adobe and its industry part−ners to deliver powerful publishing solutions for magazine, newspaper and other publishing applications.

Adobe InDesign Server technology for third-party systems integrators and developers to use for building design-driven, server-based publishing solutions; brings the innovative design and typography features of InDesign software to the server platform and enables Adobe partners to provide new levels of automation and efficiency in high-end editorial workflows, collateral creation, variable data publishing and Web-based design solutions.

Adobe Photoshop provides photo design, enhancement and editing capabilities for print, the Web, and multi-media; used by graphic designers, professional photographers, Web designers, professional publishers and video professionals, as well as amateur photographers and digital imaging hobbyists.

Adobe Photoshop Album offers easy-to-use interface to find, organize, share and edit digital photographs; designed for consumers to manage their collections of digital photographs, easily share photos via e-mail and the Web, create digital slide shows and photo albums, and get their photographs printed via on-line photo finishing services.

Adobe Photoshop Album Starter Edition a limited-feature version of Photoshop Album available for free; lets consumers find photos fast, fix common flaws and easily share images with others.

Adobe Photoshop Elements offers powerful yet easy-to-use photo editing functionality plus intuitive organizing, printing and sharing capabilities for amateur photographers and hobbyists who want to create professional-quality images for print and the Web.

Adobe Photoshop Lightroom a new product designed for professional photographers, it addresses their unique photography workflow needs by providing more efficient and powerful ways to import, select, develop and showcase large volumes of digital images.

Adobe Premiere Elements a powerful yet easy-to-use video-editing software for home video editing; provides tools for hobbyists to quickly edit and enhance video footage with fun effects and transitions, and create custom DVDs for sharing video with friends and family.

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Adobe Premiere Pro professional digital video-editing software used to create broadcast-quality content for video, film, DVD, multimedia and streaming over the Web.

Adobe Production Studio Premium Edition a suite of integrated application products that provides a complete digital video post-production environment and allows users to produce professional-quality video, film and DVDs; includes Adobe After Effects Professional Edition, Adobe Audition, Adobe Encore DVD, Adobe Illustrator, Adobe Photoshop and Adobe Premiere Pro, along with Creative Suite 2 features for timesaving workflow features such as Adobe Dynamic Link and Adobe Bridge.

Adobe Production Studio Standard Edition a suite of integrated application products that provides a digital video post-production environment and allows users to produce professional-quality video; includes Adobe After Effects Standard Edition, Adobe Photoshop and Adobe Premiere Pro, along with Creative Suite 2 features for timesaving workflow features such as Adobe Dynamic Link and Adobe Bridge.

Adobe Soundbooth a new application that provides video editors, designers and others who do not specialize in audio with the tools that they need to accomplish audio-based tasks in their everyday work, such as removing noise from recordings, polishing voiceovers, and customizing music to fit a video or animation production.

Adobe Stock Photos a service that allows users of Adobe Creative Suite products to purchase stock photography from leading stock photography agencies directly from within their applications.

Adobe Visual Communicator software used to create newscast-style video presentations that can be delivered via email, CD/, DVD, PowerPoint or live over the Internet.

DV Rack HD direct-to-disk recording and monitoring software which helps generate superior quality video from an SD or HD camera connected to a laptop computer.

Flash Video Streaming Service either through direct sales, or together with leading content delivery network (CDN) providers, Adobe offers hosted services for streaming on-demand Flash across high-performance networks; built with Adobe Flash Media Server, Flash Video Streaming Service provides an effective way to deliver Flash Video to large audiences without the overhead of setting up and maintaining streaming server hardware and network.

Macromedia Dreamweaver a professional software development application used by designers and developers to create a broad range of Web solutions for publishing online commerce, customer service and online educational content; includes capabilities for visually designing HTML pages, coding HTML and application logic and working with application server technologies.

Macromedia Fireworks a professional graphics design tool for building interactive Web graphics; gives professional designers and developers tools for creating images that can be deployed to Web browsers and the Adobe Flash Player; integrates with Adobe Flash and Macromedia Dreamweaver.

Macromedia Flash Basic a software development application for creating internet and rich interactive applications which integrate animations, motion graphics, sound, text and video functionality; solutions built with Macromedia Flash are deployed via the Web to browsers and to devices that run the Adobe Flash Player.

Macromedia Flash Media Server offers streaming media capabilities to deliver video on demand, video blogging and messaging, Web conferencing, and live video capabilities that can be viewed via the Flash Player; provides a flexible development environment for creating and delivering interactive media applications; utilized by many industries, including media and entertainment, telecommunications, advertising, government, and education.

Macromedia Flash Professional provides an advanced development environment for creating internet applications which integrate animations, motion graphics, sound, text and additional video

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functionality; solutions built with Macromedia Flash Professional are deployed via the Web to browsers and to devices that run Adobe Flash Player.

Macromedia Studio an advanced suite of integrated application tools for developers and experienced designers who develop internet and mobile solutions, and require additional video capabilities when developing Flash content; includes Macromedia Dreamweaver, Macromedia Flash Professional, Macromedia Fireworks, Macromedia Contribute and Adobe Flash Player.

Ovation software which allows users to enhance Microsoft PowerPoint slides into a richer visual experience to help deliver more impactful information, presentations, and messages.

Ultra software used to transform digital video and HD keying into a practical daily production tool for all types of video professionals users.

Vlog It! software which allows users to easily create dynamic video blogs containing photos, audio, video clips and narration.

Knowledge Worker Solutions Segment

Knowledge Worker Solutions Market Opportunity

Our Knowledge Worker Solutions Segment focuses on the needs of the knowledge worker customer, who we define as someone focused on creating and disseminating high-value information as part of their job on a regular basis. Knowledge workers include a wide variety of job functions such as accountants, administrative assistants, executives, architects, educators, engineers, graphic designers, insurance underwriters, software developers and stock analysts just to name a few. These jobs typically require the sharing of information, either in an information dissemination (one-way) format, or in a collaborative (multi-way) format.

Knowledge workers must create information and content from a variety of software applications, and be able to exchange this information within a reliable and ubiquitous format that ensures coworkers and constituents can reliably and securely access the information. When appropriate, this information often needs to be protected or securely managed.

Collaboration among knowledge workers can occur through face-to-face meetings, via phone calls, through e-mail or through Web conferencing technologies. Knowledge workers that participate in collaborations with their colleagues may be located in offices next door to each other, or in different parts of the world. These team members may change with every project and either be part of an organization s employee base, or be an external consultant or third party partner.

We believe there to be a significant opportunity to provide solutions which enable knowledge workers to communicate and collaborate across technical, geographical, and social boundaries, both inside and outside of their companies. We believe that with such solutions, users can collaborate and efficiently manage feedback from their colleagues in both real time and on-demand, and control how, when and by whom information is accessed.

For more than ten years, our Acrobat family of products has provided for the reliable creation and exchange of electronic documents, regardless of platform or application source type. Users can collaborate on documents with electronic comments and tailor the security of a file in order to distribute reliable Adobe PDF documents that can be viewed, printed, or interacted with utilizing the free Adobe Reader. Available in different versions which target a variety of user needs, Adobe Acrobat provides essential electronic document capabilities and services to help knowledge workers accomplish a wide range of ad hoc tasks involving digital documents ranging from simple publications to forms to mission critical engineering and architectural plans. Although Acrobat has achieved strong market adoption in document-intensive industries such as government, financial services, pharmaceutical, legal, aerospace, insurance,

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and technical publishing, we believe there are tens of millions of users who require capabilities such as those provided by Acrobat who have not yet licensed an Acrobat based solution.

In addition to sharing and collaborating on documents reliably across disparate platforms with Acrobat, we believe there is an adjacent market opportunity whereby knowledge workers will increasingly utilize Web conferencing solutions to more effectively collaborate and consult with their colleagues, partners, and customers. We also believe businesses will increasingly utilize Web conferencing to improve how they train, market, sell, and support their products and solutions to their customers.

We have recently announced and released a new product called Adobe Acrobat Connect, which was formerly known as Macromedia Breeze. Acrobat Connect provides capabilities via the Adobe Flash Player for live Web conferencing, as well as delivering on-demand rich presentations. By integrating accessibility to the functionality of Acrobat Connect from Acrobat and the free Adobe Reader, we believe we can extend adoption of Web conferencing to a broader potential market and grow the use of such technology with an easy-to-adopt business model.

Knowledge Worker Solutions Business Summary

Our Knowledge Worker business achieved solid year-over-year growth and record revenue in fiscal 2006. The largest component of our Knowledge Worker business was revenue generated by our Acrobat family of products. In fiscal 2006, success in this business was driven by continued adoption of Adobe Acrobat version 7.0 throughout the year, as well as the launch of Adobe Acrobat version 8 which began shipping in the later part of our fourth quarter and helped to achieve record quarterly revenue in the fourth quarter for this business.

The updated version 8 product family offers enhanced features that allow workgroups to manage a range of essential business activities such as assembling documents from multiple sources, controlling security and access to sensitive information, enabling the creation and filling out of intelligent electronic forms, and more effectively collaborating on documents and projects. In addition, the new Acrobat 8 family of products provides a new user interface and additional functionality to address specific customer workflow issues in vertical markets such as architecture, engineering, construction, manufacturing, education, government and financial services. These enhanced capabilities helped to continue the increase of our penetration of Acrobat desktop licenses in enterprises, thereby helping our business to grow.

To supplement our vertical market focus with Acrobat, we also shipped a new product called Adobe Acrobat 3D in our first quarter of fiscal 2006. Acrobat 3D extends document-based three dimensional (3D) design collaboration capabilities to virtually anyone in the design supply chain from engineers to manufacturers. Acrobat 3D utilizes Adobe PDF as a cross-platform standard to share complex 2D and 3D content without the need for using proprietary viewing technology for recipients receiving such content.

Over the course of fiscal 2006, we also focused on the Web conferencing market opportunity with our Macromedia Breeze product line, which is licensed by customers as server-based software, or licensed as a hosted service that we provide. This business model focuses on charging meeting organizers for the ability to host meetings, and allows for participants to join meetings for free utilizing the ubiquitous Adobe Flash player. With the release of Acrobat version 8, we re-launched Macromedia Breeze as Adobe Acrobat Connect and integrated the ability to start an online Web conference from within the new Acrobat family of products, as well as through the new version (free) of Adobe Reader.

Finally, as a supplement to our knowledge worker desktop products, we introduced a new hosted service that provides the ability to protect and secure PDF documents for a monthly fee.

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Knowledge Worker Solutions Business Strategy

In fiscal 2007, we plan to continue to market the benefits of our Knowledge Worker solutions to small and medium-sized businesses, large enterprises, and government institutions around the world. With our Acrobat family of products, we intend to continue to increase our seat penetration in these markets through the utilization of our corporate and volume licensing programs. We also intend to increase our focus on marketing and licensing Acrobat in vertical markets such as education, financial services, telecommunications, government, manufacturing, and the architecture, engineering, and construction markets.

With our Acrobat Connect product, we intend to increase awareness of our solution in targeted horizontal markets such as training and marketing, as well as targeted vertical markets such as manufacturing, financial services and telecommunications. We also intend to market the benefits of how our Acrobat and Acrobat Connect solutions can be used together to meet the synchronous and asynchronous collaboration needs in the marketplace. With the broad distribution and reach of our free Adobe Reader, we also intend to expose the capabilities of Acrobat Connect to potentially new users with a simple-to-adopt business model based on monthly or annual subscription fees.

Knowledge Worker Solutions Products

Adobe Acrobat 3D enables collaboration between extended teams of designers and engineers to more securely and reliably communicate, visualize, and document architectural and manufacturing designs using 3D data; allows users to insert and publish 3D designs from major CAD applications in Adobe PDF documents that can easily be shared with suppliers, partners, and customers using the free Adobe Reader software.

Adobe Acrobat Connect (formerly Macromedia Breeze) a rich Web-based communication system which enables organizations to reduce the costs of travel and increase the effectiveness of online training, marketing events, sales meetings and collaborative Web conferencing solutions which are instantly accessible by customers, partners and employees using Adobe Flash Player; consists of a core Connect Events Server or hosted service, and modules that provide specific application functionality, including Connect Training and Connect Events; can be deployed with either some or all of these components together; Connect Training allows organizations to build a complete online training system with Microsoft PowerPoint presentations that include surveys, analysis, course administration and content management; Connect Events allows users to provide seminar and training sessions as well as to conduct business presentations through the Web.

Adobe Acrobat Elements desktop software that enables enterprises to extend the value of their Microsoft Office investment by standardizing on Adobe PDF for reliable document distribution; provides for the easy conversion of Microsoft Office documents to Adobe PDF, preserving document integrity for reliable viewing and printing on other operating systems and hardware platforms inside and outside the enterprise s IT firewall.

Adobe Acrobat Messenger software that works with a scanner or digital copier and is designed for workgroups and departments to transform paper documents into electronic Adobe PDF files and deliver them via e-mail, Web or fax; allows users to preview their documents on-screen, crop or rotate pages, and add electronic annotations.

Adobe Acrobat Standard creates secure, reliable and compact Adobe PDF files from desktop authoring applications such as Microsoft Office software, graphics applications and more. Supports automated collaborative workflows with a rich set of commenting tools and review tracking features; includes everything needed to create and distribute rich electronic documents that can be viewed easily within leading Web browsers or on computer desktops via the free Adobe Reader.

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Adobe Acrobat Professional in addition to all the capabilities of Acrobat Standard, Acrobat Professional delivers specialized capabilities for creative professional and engineering users, such as pre-flighting, color separation and measuring tools.

Adobe Document Center a hosted service that enables businesses to secure and mange Adobe PDF files and other common business document files such as those in Microsoft Office formats.

Create Adobe PDF Online a Web-based subscription service that provides for the easy conversion of Microsoft Office documents and other application files to Adobe PDF for the secure and reliable sharing of rich electronic documents that can be viewed easily within leading Web browsers or on computer desktops via the free Adobe Reader.

Enterprise and Developer Solutions Segment

Enterprise and Developer Solutions Market Opportunity

Enterprises are under increasing pressure to save money, offer improved customer service, adhere to regulatory requirements and leverage existing investments in core systems. As a means to address these issues, a critical component of an organization s business processes is the need to interact with data stored in enterprise applications. As this need expands beyond the core users of those applications, adapting systems to accommodate a diverse group of users has become an expensive and time-consuming endeavor. The outcome is a proliferation of manual workarounds that result in process inefficiencies, delays and poor quality of information.

In addition, enterprises have built Web applications which enjoy the reach of the Web but often fail to deliver a user interface with the ease of use and richness that users expect. This impedes utilization of these applications and increases training costs, reducing the overall return on investment (ROI) that enterprises expect. Organizations are now looking to Rich Internet Applications (RIA) to boost their ROI for these Web applications by combining a rich graphical application interface with the universal reach of the Web.

We believe significant opportunities exist to help enterprises address these issues by making their business processes more efficient and their Web applications more engaging. To address these opportunities, we offer Adobe Enterprise and Developer Solutions to securely extend the reach of information, processes and services to engage with customers and constituents. Our solutions leverage our technology platform, which helps businesses and government agencies inspire commitment in their customers and constituents by engaging them anywhere, any time, and in any medium through our universal clients and application solutions.

Our technology platform utilizes our universal Adobe Reader and Adobe Flash Player software, which ensure reliable, secure and rich application experiences across browsers, desktops and devices. The technology platform provides developers with an RIA programming model to integrate and optimize workflows, and a server software framework to simplify integration and leverage existing enterprise infrastructures. We also offer services and other software components to accelerate the creation of compelling, relevant and actionable applications, either through RIAs or through intelligent electronic documents.

We believe our technology platform revolutionizes how enterprises and government agencies present, deliver, consume and interact with information and content. By providing an integrated client-server framework and toolset for developers, designers and IT organizations, we believe our Enterprise and Developer Solutions allow our customers to:

•   Engage their constituents with compelling experiences and intelligent documents providing them with the ability to act upon information or tasks presented to them for improved and effective collaboration;

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- Streamline and accelerate document-based processes so more work gets done;

- Simplify the creation and deployment of compelling, relevant and actionable applications;

- Augment existing enterprise infrastructures to deliver the next level of engagement with their stakeholders;

- Scale these solutions needs regardless of the size of their constituent populations; and

- Leverage the ubiquitous Adobe Reader and Adobe Flash Player clients to reach people inside and outside of their organizations, and across all desktops and devices.

Although our Enterprise and Developer Solutions address the needs of a diverse set of enterprise customers, we focus primarily on key vertical industries such as financial services, telecommunications, media and publishing, education, manufacturing, government and life sciences. For these customers, we offer comprehensive, scalable, secure and reliable server products and tools to develop applications tailored to their specific information and business process requirements.

Our Enterprise and Developer Solutions currently offer several families of products that we market to these customers:

- Adobe LiveCycle provides process management services to automate paper-based processes, leveraging the ubiquitous Adobe Reader for viewing, printing and interaction with information provided in Adobe PDF-based documents;

- ColdFusion MX provides a server-scripting environment and a set of features used by organizations for building database-driven applications that are accessible through Web browsers and the Adobe Flash Player; and

- Adobe Flex provides a standards-based programming framework for building and deploying enterprise-class RIAs; an Eclipse-based Integrated Development Environment (IDE); and a powerful set of server-side services for connecting with Enterprise infrastructure.

These solution sets are built on a common server architecture based on J2EE and XML, allowing for easy integration into enterprise infrastructures.

Our Adobe Flex solutions utilize the Flash file format and leverage our widely-used Flash Player technology. With Flex, developers are able to combine the rich user interface of desktop software with the reach and ease of deployment of the Web, and the processing power of desktop computers and mobile devices. This combination enables the delivery of more complex interactions than are currently supported by the Web browser model. Flex applications extend the server-based object model to client systems, improving interactivity by eliminating the constant page refreshes and context switches that users frequently experience. As a result, Flex applications enable organizations to provide users with a dramatically improved experience that supports the manipulation of data and information in ways that are impractical in a traditional browser-based environment.

Sample uses of Adobe Flex applications to build RIAs include the following:

- Guided selling Adobe Flex can aid the design and development of product-oriented applications, such as configurators, selectors, comparison engines and shopping carts. Such applications can provide customers with an integrated experience from initial inquiry to final purchase. By reducing customer search time and leading customers directly to the items they want, guided selling can increase conversion rates, drive larger sales and reduce shopping cart abandonment;

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• Data dashboards Adobe Flex can provide charting, graphing and drill-down capabilities that make it easy to consolidate data from disparate systems without slow page refreshes. Businesses can benefit from faster decision cycles and improved access to information; and

• Process and data integration With Flex, businesses can consolidate data and information, and align processes to meet the unique needs of internal and external users. Automated process and data integration can increase accuracy, improve efficiency and enhance customer service through faster response times.

To build and deliver enterprise-class RIAs, the following components are required:

• Adobe Flex Data Services Our Flex Data Services is an application that acts as the application and services intermediary between Flex applications and the existing enterprise environment. Flex Data Services easily integrates with existing enterprise application servers, and leverages existing resources and policies for functions such as deployment, session management and security;

• Industry-standard IDE Flex applications can be built and tested using Adobe Flex Builder or a third-party IDE such as Borland JBuilder, Microsoft Visual Studio and others; and

• Adobe Flash Player client The ubiquitous Adobe Flash Player client runtime application provides the user interface to Flex applications.

Our Adobe LiveCycle solutions utilize Adobe PDF documents which interact with core business applications and integrate information contained in those documents into business processes. In addition to being reliable electronic replicas, Adobe PDF documents are   intelligent   - they retain the best characteristics of paper documents, such as a familiar look, but add powerful business logic capabilities such as data validation and automated routing instructions. In addition, arbitrary data (including XML-based data) can be embedded inside of intelligent PDF documents for use or access later on in a business process. These features allow for more efficient interaction with enterprise applications while still providing the ability for people to manually access and interact with the data when necessary.

Our LiveCycle products leverage our Adobe Reader software with more than 500 million distributed copies of Adobe Reader, we have created a ubiquitous platform for accessing and interacting with intelligent electronic documents. Adobe Reader is available on the most common operating system platforms free of charge, including Microsoft Windows, Apple Macintosh, Linux, various Unix-based platforms, and portable device systems such as Palm OS, Pocket PC and the Symbian operating system for cellular phones. As a universal client, Adobe Reader enables users inside and outside the firewall to interact with intelligent PDF documents on most platforms, including desktops, laptops, PDAs, mobile phones and kiosks, regardless of the application used to author the document.

To address the specific needs of our customers, we offer   process management services.   These are services are sets of technologies that create, integrate and manage intelligent documents, and leverage the use of our Adobe Reader software for our customers   constituents to interact with data within the document. Process management services that we currently provide include:

• Process Automation products and solutions which allow organizations to automate form-based workflows deploying intelligent data capture systems and rules-based process management to automate business transactions;

• Information Assurance products and solutions to control document access and usage, enable the use of digital signatures as a replacement for paper and pen-based signatures and certify document authenticity; and

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- Document Generation products and solution which enables users to generate high-quality documents in real time and via batch processes. This can be done from desktop applications or dynamically from core systems. These products and solutions dynamically generate personalized, customer-facing documents from enterprise applications for enhanced customer communications.

Our ColdFusion products provide fast and easy ways to build and deploy powerful Internet applications. Developers can extend or integrate ColdFusion with Java or .NET applications, connect to enterprise data and applications, create and interact via Web services, or interface with SMS on mobile devices or Instant messaging clients. ColdFusion can also be used for business reporting, rich-forms generation, printable document generation, full-text search, and graphing and charting enabling customers to more fully engage their constituents with better Web experiences.

Enterprise and Developer Solutions Business Summary

Through the combination of Adobe and Macromedia technologies and execution against our go-to-market strategy in fiscal year 2006, we achieved strong year-over-year growth in our Enterprise and Developer business during the year. Our LiveCycle family of server products and technologies achieved record revenue in fiscal 2006, driven by strong adoption in targeted markets such as government and financial services. Our integration with other software vendors platforms, such as those from SAP AG, helped to further drive adoption during the year as did adoption of Adobe PDF and Adobe server technologies in markets like insurance.

With our Adobe Flex solutions, we also achieved strong revenue growth and adoption in key targeted markets during fiscal 2006. Our Macromedia ColdFusion business also continued to perform well due to revenue generated from its existing customer base that benefits from a large and active developer community. This business was also enhanced based on the delivery of an updated ColdFusion release during fiscal 2006 which added strong integration capabilities with Adobe Flex.

Enterprise and Developer Solutions Strategy

In fiscal 2007, we intend to focus on offering more complete enterprise server-based solutions targeting the document and rich internet application needs of governments and enterprises. We wish to help these customers develop and deliver self-service and assisted-service Web-based applications that blend rich user interfaces, documents and collaboration capabilities that are easy to use. We strive to provide solutions which are customer-centric and help the constituents of our customers work together on complex processes and bridge the digital and paper-based environments, and do so by providing capabilities that are accessible by anyone, anywhere, and on any Web-connected device. We intend to provide such solutions directly through our consulting services organization, as well as together with software partners such as SAP AG, and through global systems integrators we partner with that deliver comprehensive solutions to their customers.

We will focus our go-to-market efforts on markets such as financial services, government, manufacturing, and life sciences.

Enterprise and Developer Solutions Products

Adobe Acrobat Capture enables conversion of legacy paper-based documents into indexed, searchable, platform-independent electronic PDF files for archiving and distribution purposes.

Adobe Central Pro Output Server a server-based software application for document generation that allows organizations to create personalized, customer-facing documents from any data source including legacy, line-of-business, ERP, or CRM applications; merges data with an electronic document template using a powerful processing engine to dynamically generate electronic documents such as purchase orders,

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invoices, statements and checks for delivery via Adobe PDF, the Web, e-mail, fax, or print; works with Adobe Output Designer, which is a companion tool used to create sophisticated document templates.

Adobe Flex SDK The developer tools for developing RIAs with Flex. Developers use the SDK to compile and debug MXML and ActionScript files into the SWF format that executes in the Flash Player. The Flex SDK is licensed at no charge, providing a commercial grade RIA development which competes with free open source alternatives.

Adobe Flex Builder an integrated development environment tool that can be used by designers and enterprise developers for visually architecting and developing RIAs. Tightly integrated with the Flex SDK, Flex Builder provides features for quickly prototyping, coding, debugging and deploying Flash based RIAs. Flex Builder is a commercial product based on the open source Eclipse toolkit, the emerging industry standard for enterprise development tools.

Adobe Flex Data Services provides enterprise connectivity and data management capabilities for advanced Flex RIAs. Flex Data Services runs on J2EE application servers and provides messaging, high performance data connectivity, and advanced data management that integrate Flex based RIAs into enterprise infrastructure including Web services, remote Java objects and real-time data and messaging systems.

Adobe LiveCycle Assembler a server-based software application for the creation, manipulation and assembly of customized Adobe PDF documents; XML-based data can be inserted into templates to create complex, content-rich documents for more targeted and effective customer communications; integrates with leading enterprise applications as well as custom systems.

Adobe LiveCycle Designer a desktop software application which simplifies the creation and maintenance of intelligent XML form templates for deployment as Adobe PDF forms or HTML applications; provides an intuitive, graphical design tool for creating XML templates that look exactly as the author intended, and previewing them before deployment. It also simplifies adding intelligence to documents, such as calculations and validations, and binding form fields to arbitrary XML schemes for seamless integration with enterprise applications.

Adobe LiveCycle Form Manager a server-based software application which simplifies form management and increases user satisfaction by centralizing the management of all forms, regardless of file type, into a single point of access via a Web-based portal; allows administrators to manage form publication, version control and user access, as well as establish ebXML relationships with business partners and customers inside and outside the enterprise.

Adobe LiveCycle Forms offers a range of solutions for deploying intelligent forms that can be completed online or offline, across diverse platforms and devices; identifies a user s environment to deliver the richest form-filling capabilities supported and integrates with enterprise applications to pre-populate form fields, save captured data, and initiate data-driven workflows.

Adobe LiveCycle Barcoded Forms enables organizations to accurately capture user-supplied information from fill-and-print paper forms by using dynamic 2D barcodes; barcodes are initially set up through creation of the form with Adobe s Designer application; after the form is printed, signed and returned by users of the form, the barcode on the form is scanned and decoded, and form data obtained from the barcode is routed to the appropriate enterprise application through Adobe s LiveCycle server products.

Adobe LiveCycle Document Security a server-based software application that helps organizations automate the processing of electronic documents by providing batch-based capabilities to digitally sign and certify PDF files, validate digital signatures, and encrypt/decrypt PDF documents; safeguards information when it leaves a company s network and integrates with existing public key infrastructures.

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Adobe LiveCycle Policy Server a server-based software application that helps organizations manage information access securely with dynamic, persistent document control; allows for the control and monitoring of PDF, Microsoft Word, Microsoft Excel and CATIA CAD document usage inside or outside the firewall, online or offline, and across multiple document platforms; lets organizations know when a document has been viewed, printed or altered, and restricts access so that only intended recipients can open, use and forward a document; allows for previously granted document permissions and access to be revoked; leverages Adobe Acrobat and Adobe Reader and other client plug-in software to author and view protected documents.

Adobe LiveCycle Reader Extensions a server-based software application which lets enterprises easily create and share interactive PDF files with external parties who must interact with these documents without requiring recipients of the documents to acquire Acrobat software that normally would be necessary to interact with the PDF files they receive. On an individual PDF document, it unlocks features so that when such a file is opened in the free Adobe Reader, users have access to functionality that normally would not be available in Adobe Reader. Examples of document collaboration features that can be enabled in Adobe Reader by this server product include the use of digital signatures to electronically sign PDF documents, the ability to ability to fill in, submit, and save electronic documents locally, and the ability to fill-in form information.

Adobe LiveCycle PDF Generator the next-generation replacement for Acrobat Distiller Server and Acrobat Elements Server that offers server-based conversion of native PostScript, text, image formats, standard office formats, and technical drawing formats into PDF files. LiveCycle PDF Generator integrates with other LiveCycle products that apply digital rights management, document assembly, and process management to converted documents in an automated fashion. The product can generate PDF files that comply with the new PDF/A specification for long term document archives.

Adobe LiveCycle Workflow Server a server-based process management application that allows for the design, deployment and management of forms-based business processes to improve organizational agility and productivity; uses a rules-and roles-based design tool that defines business rules a process must follow, as well as the roles of each individual involved in the process.

Adobe Output Designer a design tool that allows users to create electronic document templates for use with Adobe solutions for document generation; aids in the creation of electronic documents that exactly replicate existing paper documents.

Adobe Output Pak for mySAP.com an SAP-certified server-based software application for document generation that enables organizations to optimize their investment in their SAP solution by creating personalized, professional-looking, customer-facing documents; provides an easy, fast, and cost-effective way to create and maintain documents for the SAP environment; integrates directly with an SAP system to extract information which is merged with a document template that defines the layout and formatting of the document; output can be in a variety of formats, including Adobe PDF, print, fax, e-mail and the Web.

Adobe Web Output Pak a server-based software application for document generation; creates documents in PDF and HTML for presentation on the Web, and in Wireless Markup Language (WML) for presentation to a wireless device; allows users to personalize and control the look of documents based on the data the documents contain.

Macromedia ColdFusion provides a server-scripting environment and a set of features used by organizations for building database-driven scalable applications that are accessible through Web browsers and the Adobe Flash Player; built on an open Java technology architecture and can be deployed on third-party Java application servers that support the J2EE specification.

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Mobile and Device Solutions Segment

Mobile and Device Solutions Market Opportunity

As hundreds of millions of people around the world adopt internet-connected hand-held phones and devices as a means to communicate, collaborate and entertain, as well as consumer electronic devices such as digital cameras, game consoles, music players, and electronic educational toys, we believe a significant opportunity exists to offer solutions for these devices which provide for the creation and delivery of rich content, user interfaces, and data services which allow users to engage with information more easily and effectively.

Our strategy in addressing the Mobile and Device Solutions market is to license Adobe mobile solutions, including Adobe Flash Player, Adobe Reader LE, and Macromedia FlashCast, to device manufacturers and telecommunications carriers that embed our technology on their platforms, enabling them to provide multimedia content, documents and services to their customers. As Flash Player and Adobe Reader technology penetrates digital devices and platforms, millions of developers will be able to use our content creation products to create engaging consumer content and rich mobile business applications.

To support the delivery of content and services in these millions of devices, we offer client-server solutions which leverage the broad deployment of our Flash Player and Adobe Reader technologies. FlashCast, the first of these service delivery solutions, consists of client software built upon Macromedia Flash Lite runtime technology, as well as server technology that manages the content being delivered to the mobile phone. Just as other Adobe solutions such as Acrobat Connect are built upon our technology platform, we see market opportunities to bring similar solutions to the mobile and device ecosystems.

Mobile and Device Solutions Business Summary

In fiscal 2006, despite the loss of deferred revenue due to purchase accounting adjustments made with the integration of Macromedia at the beginning of the year, we achieved solid revenue results and strong unit adoption of our client software on mobile and consumer electronic devices. As of September 30, 2006, our Flash Lite client has been installed on more than 150 million devices worldwide   on over 150 different mobile handset models and over 250 different device models. This success has been driven by key hardware OEM relationships with companies such as Nokia, Sony/Ericsson, LG Electronics, BenQ Mobile, Motorola, and Samsung.

In addition to the key OEM relationships we have established, we achieved a milestone in the United States market with the launch of Flash Lite for Qualcomm BREW on the Verizon network. This relationship signals the start of the creation of a Flash Lite ecosystem in the United States, driven initially by the ability for Verizon subscribers to view Flash-based content on their BREW enabled handsets.

We also achieved strong unit adoption of our Flash Lite client on consumer electronics devices during the fiscal year. Key customers such as Sony have licensed our Flash Lite for distribution on devices such as the Sony PlayStation Portable and the Sony PlayStation 3.

In addition to client-based revenue, we have increased traction with our server-based solution FlashCast, which provides data-based services that major wireless carriers such as NTT DoCoMo offer their subscribers. In Japan, more than 7 million DoCoMo subscribers have signed up for an Adobe FlashCast based service in its first year of availability. We also announced a relationship with Verizon to deliver Flash based services with Verizon to their millions of subscribers in North America.

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Mobile and Device Solutions Strategy

In fiscal 2007, we intend to continue our focus on client-based OEM revenue from our mobile and device hardware customers to drive revenue growth in our business. We also intend to work closely with carriers in key ecosystems to enable our authoring and content delivery solutions, and to leverage and extend our current offerings to them. Geographically, we look to expand our presence in markets such as Europe, Japan, China, and the United States. Our expansion will be driven by our own efforts, as well as those of key systems integration, distribution, and content partners that we have already signed agreements with, or those who we intend to partner with.

Mobile and Device Solutions Products

Adobe Reader LE a version of the Adobe Reader specifically developed for mobile phones that renders PDF documents on small-sized devices.

Macromedia Flash Lite a version of the Adobe Flash Player specifically developed for many devices ranging from smart phones to feature phones, and for other consumer electronic devices; designed to require fewer device resources and can therefore operate on many devices from feature phones to TVs and digital video recorders on many devices from smart phones and feature phones.

Macromedia Flash SDK a software development kit specifically developed for bringing Flash based content to consumer electronic devices; designed to require fewer device resources and can therefore operate on many devices from game devices to TVs and digital video recorders.

Macromedia FlashCast an end-to-end, client-server solution that is designed to effectively create, deliver and use rich data services which are viewed as channels of information on mobile handsets; consists of the FlashCast client software which is embedded on mobile devices such as mobile phones and is built based on the Flash Lite runtime engine, and FlashCast server software which manages subscriber accounts, aggregates and delivers FlashCast channel updates to subscribers, and generates billing transactions for fulfillment.

Other Business Segment

Our Other Business segment contains several of our products and services which address market opportunities ranging from the diverse publishing needs of technical and business publishing, to our legacy type and OEM printing businesses, to new strategic opportunities such as OEM revenue generated from our technology platform   which includes the ubiquitous Adobe Reader and Adobe Flash Player clients. These opportunities, and the products we offer to address them, are reviewed below in the following categories: Platform, OEM PostScript, and Print and Classic Publishing.

Platform Opportunities

As previously discussed, central to our long term strategy is our technology platform which enables the development of products and solutions that dramatically improves how businesses engage with their customers. While our technology platform encompasses products and technologies created across all of Adobe s segments, the Platform Business Unit focuses on the development and delivery of our technology platform client technologies, including Adobe Reader and Adobe Flash Player software. These solutions ensure reliable, secure and rich application experiences across the broadest range of browsers, operating systems and devices.

Based on how these solutions allow consumers, enterprises and government agencies to present, deliver, consume and interact with information and content, there exists an opportunity to monetize the use of our Reader and Flash Player software. While typically provided for free, the widely used nature of

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both Flash Player and Reader has created new opportunities with partners whereby we can generate revenue based on the deployment of partner technology as part of our technology platform products.

In fiscal 2007, we will continue to explore monetization opportunities for our technology platform solutions, as well as focus on the long-term strategic goal of developing a new cross-platform client (code named Apollo) based on the Flash, PDF and HTML client technologies that will enable the creation of Web-enabled desktop applications.

Platform Products

Adobe Reader software for reliable reviewing and printing of Adobe PDF files on a variety of hardware and operating system platforms; when used with certain Adobe PDF files created with Adobe LiveCycle Reader Extensions Server, Adobe Acrobat Professional, or Adobe Acrobat 3D, Adobe Reader also can be used to enable collaborative workflows through the addition of collaboration features built into the Adobe PDF file; these features include review and markup tools that normally are not present in the standard Adobe Reader product.

Adobe Flash Player the most widely distributed rich client software on PCs and consumer electronic devices, the Flash Player provides a runtime environment for text, graphics, animations, sound, video, application forms and two-way communications.

Adobe Shockwave Player a rich media player used for deploying multimedia content for use in internet solutions including education, training, games and commerce.

OEM PostScript Opportunities

Graphics professionals and professional publishers require quality, reliability and efficiency in production printing, and we believe our printing technology provides advanced functional–ity to meet the sophisticated requirements of this marketplace. As high-end printing systems evolve and transition to fully digital, composite workflows, we believe we are uniquely positioned to be a supplier of software and technology based on the Adobe PostScript and Adobe PDF standards for use by hardware manufacturers in this industry. We generate revenues by licensing our technology to OEMs that manufacture printers and other output devices.

OEM PostScript Products

Adobe PostScript a printing and imaging page description language that delivers high quality output, cross-platform compatibility and top performance for graphically-rich printing output from corporate desktop printers to high-end publishing printers; gives users the power to create and print visually rich documents with total precision; licensed to printing equipment manufacturers for integration into their printing products.

Adobe PDF Print Engine a new, next-generation printing platform that enables complete, end-to-end PDF-based workflows using common PDF technology to generate, preview, and print PDF files; allows PDF files to be rendered natively throughout a workflow, providing performance benefits such as eliminating the need to flatten transparent artwork.

Print and Classic Publishing Opportunities

In addition to the market opportunities and our businesses discussed previously, we offer a variety of products and solutions which address many different and unique publishing market needs. Our Print and Classic Publishing Business Unit focuses on these solutions, which address the diverse customer needs in markets such as: business document publishing, CD-ROM publishing, e-learning solutions, on-line help systems, technical document publishing and typography.

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Print and Classic Publishing Products

Adobe Captivate enables users to create interactive demonstrations and software simulations in the Flash file format; records users actions in any application and instantly creates Flash simulations with visible and audible mouse movements; the small file size and high resolution make Adobe Captivate simulations and demonstrations easy to publish online or burn onto a CD for use in training, sales, marketing or user support; often used in combination with Acrobat Connect, Adobe Captivate provides a robust technology solution to bring understanding and retention to the end users of rapid training and e-learning solutions.

Adobe Contribute an easy way to update, add and publish Web content; non-technical business users can make changes to intranet and internet Websites while automatically maintaining site standards for style, layout and code; as a server application, Adobe Contribute provides a Web publishing system which enables IT professionals to manage and administer users and permissions as part of the Web publishing process; also content providers and Web professionals to save time and streamline the Web-content maintenance process.

Adobe Font Folio OpenType Edition contains more than 2,200 typefaces from the Adobe Type Library in OpenType format, offering a complete type solution for print, the Web, digital video or electronic documents.

Adobe FrameMaker an application for authoring and publishing long, structured, content-rich docu−ments including books, documentation, technical manuals and reports; provides users a way to publish their content to multiple output formats, including print, Adobe PDF, HTML, XML and Microsoft Word.

Adobe PageMaker software used to create high-quality documents simply and reliably with robust page layout tools, templates and stock art.

Adobe RoboHelp an authoring tool used by developers and technical writers to create professional help systems and documentation for desktop and Web-based applications; utilizes support for XML, PDF import/export, content management, distributed workforces, team authoring capabilities, as well as JavaHelp.

Adobe Type Library includes Adobe s best-selling typefaces, plus Adobe Type Manager; makes it easy to create beautiful text for print, Web and video projects.

Adobe Type Classics for Learning a low-cost, introductory font library designed for students and educators.

Adobe Type Manager provides powerful, easy management of all PostScript Type 1, OpenType and TrueType fonts.

Adobe Type Sets various Collection packages of Adobe s best-selling typefaces; makes it easy to create beautiful text for print, Web and video projects.

Macromedia Authorware a rich media authoring tool used to develop caption based e-learning on Windows and Macintosh based platforms; use of the product ranges from creating Web-based tutorials to simulations incorporating audio and video; applications developed with Macromedia Authorware can be delivered on the Web, over corporate networks or on CD-ROM.

Macromedia Director a tool for creating professional multimedia content that combines images, text, audio and video into presentations and interactive experiences; for Websites, it provides users with the ability to deliver multimedia content that supports three dimensional images and animations for use in various markets, including education, games and commerce; also enables the creation of fixed-media content for CD titles and DVD titles in the entertainment, education and corporate training markets.

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Macromedia FreeHand MX a professional vector graphics tool designers and illustrators use to create high quality images that can be scaled; supports developing images for print, the Web and the Adobe Flash Player.

Macromedia JRun an application server based on the J2EE specification; integrates with our development tool offerings and is used to deploy applications for functions such as online banking and customer service.

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COMPETITION

The markets for our products are characterized by intense competition, evolving industry standards and business models, rapid software and hardware technology developments, and frequent new product introductions. Our future success will depend on our ability to enhance our existing products, introduce new products on a timely and cost-effective basis, meet changing customer needs, extend our core technology into new applications, and anticipate and respond to emerging standards, business models and other technological changes.

Creative Solutions

In our Creative Solutions segment, we offer the Adobe Creative Suite in two versions, which consist of combinations of several of our technologies. The Adobe Creative Suite Standard Edition combines the capabilities of Adobe InDesign, Adobe Illustrator and Adobe Photoshop, as well as file management and integration technology called Version Cue, and Adobe Bridge which provides a simple interface to easily organize, browse and locate files. The Adobe Creative Suite Premium Edition adds to this the capabilities of Adobe Acrobat Professional and Adobe GoLive. Similarly, we offer Macromedia Studio, which is a product that combines the capabilities of Macromedia Dreamweaver, Macromedia Flash Professional, Macromedia Fireworks, Macromedia Contribute and Macromedia FlashPaper. We also offer various bundles for customers who desire some of these applications in one affordable package.

Our Creative Solutions products compete with many companies, including Apple, Avid, Corel, Google, Microsoft and Quark, as they increase their presence in the creative software and solutions markets, as well as from open source initiatives.

With respect to Microsoft, it announced a new suite of products, called Expression Studio, which will compete with our Adobe Creative Suite and Macromedia Studio products and individual Creative Solutions segment products. Expected to ship in the second quarter of 2007, Expression Studio includes Microsoft Expression Design (formerly Microsoft Expression Graphic Designer) which will compete with our Adobe Illustrator, Adobe Photoshop and Macromedia Fireworks products; Microsoft Expression Blend (formerly Microsoft Expression Interactive Designer), which will compete with our Macromedia Flash product line; Microsoft Expression Web (formerly Microsoft Expression Web Designer), which will compete with our Macromedia Dreamweaver and Adobe GoLive products; and Microsoft Expression Media, which provides digital asset management, basic image editing, and video encoding/compression capabilities, and will potentially compete with some aspects of our creative and hobbyist-focused products. Microsoft s new operating system, Windows Vista, also includes new features in its Presentation Foundation that compete with Macromedia Flash.

We believe our Adobe Creative Suite products and our Macromedia Studio product compete favor–ably on the basis of features and functionality, ease of use, product reliability, price and performance characteristics. The individual technologies within the Creative Suite and Studio products also work well together, providing broader functionality and shortened product training time for the individual who uses multiple appli–cations to complete a project.

In addition to our Adobe Creative Suite and Macromedia Studio products, we offer the technologies within them as individual software applications. The competitive nature for these individual Creative Solutions products is discussed below.

Drawing and illustration products are characterized by feature-rich competition, brand awareness and price sensitivity. In addition to competition with Microsoft s Expression Design product, our Adobe Illustrator and Macromedia FreeHand products face competition from companies such as ACDsee, Autodesk, Corel, Deneba, Mediascape, Xara and the open source product called Karbon14. We believe our products compete favorably due to high awareness of their rich features, especially the drawing and

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illustration functionalities, the technical capabilities of the product, and our ability to leverage core technologies from our other established products.

The demand for Web page layout and Web content creation tools is constantly evolving and highly volatile. In addition to competition with Microsoft s Expression Blend and Web products, we believe Adobe GoLive, Macromedia Dreamweaver and Macromedia Flash face direct and indirect competition from desktop software companies such as Bare Bones Software and various proprietary and open source Web authoring tools. We also face competition from AJAX and Visual Studio products, and other integrated development environments that enable developers to create Web applications from companies such as BEA Systems, Borland and IBM. We believe our products compare favorably to these applications; however, our market share may be constrained by Microsoft s ability to target its Web software to users in markets they dominate, including users of Microsoft Office, Microsoft Windows operating system, the Microsoft Internet Explorer Web browser, and Microsoft Visual Studio.

The needs of digital imaging and video editing software users are constantly evolving due to rapid technology and hardware advancements in digital cameras, digital video cameras, printers, personal computers, cellular phones and other new devices. Our software offerings, including Adobe Photoshop, Adobe Photoshop Elements, Adobe Photoshop Lightroom, Adobe After Effects, Adobe Audition, Adobe Soundbooth, Adobe Encore DVD, Adobe Premiere Elements, and Adobe Premiere Pro, face competition from companies offering similar products. We also continue to face competition from new emerging products, including online based services and those coming from the open source movement.

Our mid-range consumer offerings, including Photoshop Elements and Adobe Premiere Elements, are subject to intense competition, price sensitivity, brand awareness and strength in OEM bundling and retail distribution. We face direct and indirect competition from a number of companies that market software which competes with ours, including ACD Systems, AI Soft (Japan), Apple, ArcSoft, Corel, i4 (Japan), Google, Kodak, Nova Development, Magix, Microsoft, Paessler GmbH (Germany), Pegasus Imaging Company, Phase One, Photodex Corporation, Sonic Pinnacle, Sony and Ulead Systems. In addition, we face competition from device, hardware and camera manufacturers such as Apple, Canon, Dell, Hewlett-Packard, Nikon, Sony and others as they try to differentiate their offerings by bundling, for free, their own digital imaging software, or those of our competitors. Similarly, we face potential competition from operating system manufacturers such as Apple and Microsoft as they integrate hobbyist-level digital imaging and image management features into their operating systems. Finally, we face potential competition from open source products, including Gimp for Linux.

We believe we compete favorably against other mid-range digital imaging, digital video and consumer-focused image management software applications with our Adobe Photoshop Elements, Adobe Premiere Elements and Adobe Photoshop Album products due to strong consumer awareness of our brand in digital imaging and digital video, our relationships with significant OEMs, positive recommendations for our products by market influencers, our increased focus on the retail software channel, and strong feature sets.

In professional digital imaging, software applications compete based on product features, brand awareness and price sensitivity. In addition to competition with Microsoft s Expression Design product, our Adobe Photoshop and Adobe Photoshop Lightroom products face direct and indirect competition from a number of companies including Apple and Corel. Our Adobe Photoshop product competes favorably due to high awareness of the Photoshop brand in digital imaging, the positive recommendations for our Photoshop product by market influencers, the features and technical capabilities of the product, and our ability to leverage core features from our other established products.

Our Adobe InDesign product, used for professional page layout, faces significant competition. The main competitor, Quark, has a competitive product, Quark XPress, which has maintained a historically strong market share in the professional page layout market. Quark also benefits from an established industry infrastructure that has been built around the use of their XPress product in print shops and

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service bureaus, and through the development of third party plug-in products. Barriers to the adoption of Adobe InDesign by Quark XPress customers include this infrastructure, as well as the cost of conversion, training and software/hardware procurement required to switch to InDesign. We have seen an increase in the adoption of InDesign software and we believe we will continue to see market share gains going forward due to a product offering that contains new innovative features, our strong brand among users, positive reviews by industry experts, adoption of InDesign by major accounts which are influencers in their industries and improved infrastructure support by the industry for our overall solution.

Applications for digital video editing, motion graphics, special effects, audio creation and DVD authoring face increasing competition as video professionals and hobbyists migrate away from analog video and audio tools towards the use of digital camcorders and digital video production on their computers and DVD systems for rich media playback. Our Adobe After Effects, Adobe Audition, Adobe Encore DVD and Adobe Premiere Pro software products, as well as the Adobe Production Studio which contains these products, face competition from companies such as Apple, Avid, Canopus, Discreet, Sonic and Sony. Our Adobe Premiere Elements software product, which is targeted for use by hobbyists, faces competition from companies such as Aist, Apple, ArcSoft, Avid, Broderbund, Cyberlink, Magix, Microsoft and Muvee.

Adobe After Effects is a leader in professional compositing and visual effects due to its strong feature set and its integration with our other products that helps create a broad video editing platform for our customers. In professional digital video editing, we are an industry leader on the Microsoft Windows platform with Adobe Premiere Pro and compete favorably due to our strong feature set, our OEM relationships and the integration with our other products to create a broad digital video publishing platform for our customers.

Knowledge Worker Solutions

With our Adobe Acrobat business, we are seeing an increase in competition from Microsoft. Microsoft has announced its new, next generation operating system, called Windows Vista, which started shipping in late 2006. Windows Vista includes a proprietary digital rights management technology and a new document format, called XML Paper Specification (XPS), which competes with Adobe PDF. In addition, Microsoft recently released the next version of its widely used Office product which offers a feature to save Microsoft Office documents as PDF files through a freely distributed plug-in. This new PDF feature in Office competes with Adobe Acrobat. Given Microsoft s market dominance, XPS, the PDF feature in Office and any other competitive Microsoft product or technology that is bundled as part of its Office product or operating system or made freely available, could harm our overall Knowledge Worker Solutions market opportunity.

Our Adobe Acrobat product family also faces competition in the PDF file creation market from many clone products marketed by companies such as AdLib, Active PDF, Ansyr Technology, Apple, Global Graphics, Nuance, Software995, Sourcenext and others. In addition, other PDF creation solutions can be found at a low cost, or for free, on the Web.

For customers that use Adobe Acrobat Standard and Adobe Acrobat Professional as part of document collaboration and document process management solutions, where electronic document delivery, exchange, collaboration, security and archival needs exist, our Acrobat product family faces compe–tition from entrenched office applications such as Microsoft Office. In the higher end of the electronic document market, Acrobat Professional provides features which compete with other creative professional PDF tool providers, such as Enfocus, Dalim, TeamPDF and Zinio. In addition, we are targeting the architecture, engineering and construction electronic document collaboration market with our Acrobat Professional product market. The capabilities of our product in this market compete with some aspects of Autodesk s solution.

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To address the threats from Microsoft and others, we are working to ensure our Adobe Acrobat applications stay at the forefront of innovation in emerging opportunities such as PDF document generation, document collaboration and document process management.

Adobe Acrobat Connect (formerly Macromedia Breeze) faces competition from many Web conferencing vendors, including WebEx and Microsoft Office Live Meeting. WebEx is a market share leader, and Microsoft has steadily increased its marketing of Microsoft Office Live Meeting. To address the threats from Microsoft and others in the Web conferencing space, we focus on providing a differentiated and enhanced user experience through our ubiquitous Adobe Flash Player.

Mobile and Device Solutions

The markets we address with our Mobile and Device solutions are influenced by evolving industry standards, rapid software and hardware technology developments, and frequent new product and technology introductions by companies or open-source initiatives targeting similar opportunities. Technologies and products which could compete with Macromedia Flash Lite include Java, Brew, SVG, WAP and Microsoft Windows Mobile, as well as solutions from the open source movement and vendors supplying clone versions of these products and technologies.

We believe our Macromedia Flash Lite solution competes favorably against these technologies and solutions due to the ubiquitous distribution of Adobe Flash Player technology on a broad set of platforms, including PCs, cellular phones, and consumer electronic devices. We also believe our robust programming model and developer tools used to create Flash content, and the large Flash developer community and ecosystem which utilize our tools, are key assets in our ability to effectively compete in this market. Further, the rich expressiveness of Flash, which provides the capability to deliver audio, video, motion graphics, vector graphics and visual effects, and results in rich user experiences and interfaces on mobile devices, is a key differentiation when compared to the capabilities of alternate solutions.

Enterprise and Developer Solutions

The markets we address with our Macromedia ColdFusion, Adobe LiveCycle and Adobe Flex products are influenced by evolving industry standards, rapid software and hardware technology developments, and new product introductions from competitors such as Microsoft and IBM.

Microsoft has already brought to market new products and technologies to address many of the emerging market needs we focus on with our Adobe LiveCycle family of products. In the Professional version of Microsoft Office 2003, it introduced a new information gathering program called InfoPath 2003. They also introduced Windows Rights Management Services in their Windows Server 2003 product, which is designed to allow corporate networks to manage and enforce restrictions built into documents.

As discussed previously, Microsoft has recently started shipping its next generation operating system, called Windows Vista. Windows Vista includes a new document format, called XPS, which competes with Adobe PDF. Windows Vista also contains a proprietary digital rights management technology which competes with Adobe LiveCycle Policy Server. In addition, Microsoft s new version of Office includes an updated version of its SharePoint product which competes with certain aspects of our Adobe LiveCycle products. Microsoft has also recently delivered technology called Windows Presentation Foundation as part of the Windows Vista release in late 2006. Windows Presentation Foundation offers an alternative to building RIA applications within the Microsoft .NET framework.

In the electronic forms solution market, in addition to competition from Microsoft Infopath based solutions, we face competition from IBM through their acquisition of an eForms solution company called PureEdge and their acquisition of FileNET s electronic form solutions. Similarly, we face competition for

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document process management solutions from workflow solution vendors such as MetaStorm, Nuance and Ultimus.

We believe that our Adobe LiveCycle server product family competes favorably against these companies and formats in terms of the combined benefits of superior functionality, cross-platform visual page fidelity/reliability, multi-platform capability, file compression, printing and security of documents expressed using Adobe PDF. We also believe that Adobe PDF and its integration with XML, combined with the broad distribution of Adobe Reader on all leading hardware platforms, provide a ubiquitous universal multi-platform solution that is more compelling than our competitors offerings.

As we broaden the scope of products and solutions offered with our Enterprise and Developer Solutions products, we face increased competition from entrenched office applications, emerging products/technologies and potentially, enterprise collaboration system providers. Additionally, current office applications and content creation/management tools that use HTML, Microsoft Word, Tagged Information File Format (TIFF) and various XML-based formats for electronic document distribution provide alternate solutions to customers, and indirectly compete with our enterprise server products and the use of Adobe PDF.

Our Adobe Flex server product provides a solution for developers and IT departments wanting to deploy enterprise class, Rich Internet Applications and leverages Adobe Flash Player technology. Beyond the competitive Microsoft threats previously discussed, vendors such as Tibco, JackBe, Backbase, and NexaWeb offer competitive solutions in the RIA market that we target with Flex. In addition, new open source technologies including AJAX techniques provide alternative methods for creating RIAs. Numerous open source groups, as well as a number of commercial software vendors are working to build tools and frameworks that make AJAX competitive with Flex.

Our Macromedia ColdFusion products face competition from major vendors including Microsoft, IBM, BEA and Sun. In addition, ColdFusion competes with several technologies available today at no cost including the PHP and PERL programming environments that are available for the Apache Web server.

Other

In technical authoring and publishing, our Adobe FrameMaker product faces competition from large-scale electronic publishing systems, XML-based publishing companies such as PTC (via their acquisition of Arbortext), as well as lower-end desktop publishing products such as Microsoft Word. Competition is based on the quality and features of products, the level of customization and integration with other publishing system components, the number of hard–ware platforms supported, service and price. We believe we can successfully compete based upon the quality and features of the Adobe FrameMaker product and our extensive application programming interface.

In desktop publishing, our Adobe PageMaker product faces competition from other software products, including Microsoft Publisher. Competition is based on the quality and features of products, ease-of-use, printer service support, and price. We believe we have a strong product and can successfully compete with these types of applications based upon the quality and features of the Adobe PageMaker product, its strong brand among users, and its widespread adoption among printer service bureaus.

In printing technologies, we believe the principal competitive factors for OEMs in selecting a page description language or a printing technology are product capabilities, market leadership, reliability, price, support and engi–neering development assistance. We believe that our competitive advantages include our technology competency, OEM customer relationships and intellectual property portfolio. Adobe PostScript faces competition from Hewlett-Packard s proprietary PCL page description language and from developers of other page description languages based on the Post–Script language standard, including Global Graphics and Xionics. In addition, as previously discussed, Microsoft has recently shipped its next

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generation operating system called Windows Vista. It includes a new document format called XPS, which competes with Adobe PDF. Certain aspects of XPS also compete with our Adobe PostScript technologies and solutions.

In e-learning content authoring, our Authorware product faces competition from vertically focused e-learning content authoring solutions. Competition is based on the quality and features of products, ease-of-use and price. We believe we have a strong product and can successfully compete based upon the quality and features of the Macromedia Authorware product and its strong brand among users, and its widespread adoption among e-learning content publishers.

In interactive simulations/e-learning, our Adobe Captivate product faces competition from general content development tools such as Microsoft PowerPoint, screen recording tools such as Techsmith s Camtasia and more advanced e-learning and software simulation solutions such as Firefly or OnDemand. Competition is based on speed of development and features of products, ease-of-use and price. We believe we have a strong product and can successfully compete based upon the quality and features of the Adobe Captivate product, its strong brand among users and its widespread adoption among training developers.

In Web content management, our Adobe Contribute product faces competition from solutions that provide for the simple creation of blogs and Wikis , as well as basic content publishing products such as Microsoft Word and Microsoft SharePoint, and, large-scale Web content management systems from companies such as Interwoven, Vignette, IBM and Oracle. Competition is based on the usability, quality and features of products, the level of customization and integration with other Web content management components, the integration with Web design tools, the number of hardware platforms supported, service, and price. We believe we can successfully compete based upon the usability and price of the Adobe Contribute product, strong brand among users and integration with other Web content management components.

In multimedia content authoring, our Director product faces competition from a variety of multimedia content authoring tools. Competition is based on the quality and features of products, ease-of-use and price. We believe we have a strong product and can successfully compete based upon the quality and features of the Macromedia Director product, its strong brand among users, and its widespread adoption among content developers and publishers.

In technical Web authoring and publishing, our Adobe RoboHelp product faces competition from large-scale Web publishing systems, XML-based Web publishing companies, as well as lower-end publishing products such as Microsoft Word. Competition is based on the quality and features of products, the level of customization and integration with other publishing system components, the number of hardware platforms supported, service, and price. We believe we can successfully compete based upon the quality and features of the Adobe RoboHelp product.

Our Macromedia JRun product competes with large Java application server vendors as well as products available at no cost including the Tomcat Java Servlet Engine provided by the Apache Foundation.

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OPERATIONS

Marketing and Sales

We market and distribute our products through sales channels, which include distributors, retailers, software developers, systems integrators, ISVs and VARs, as well as through OEM and hardware bundle customers. We also market and license our products directly using our sales force and through our own Web site at www.adobe.com.

We support our worldwide distribution network and end user customers with international offices around the world, including locations in Australia, Austria, Belgium, Brazil, Canada, China, Czech Republic, Denmark, England, Finland, France, Germany, India, Ireland, Italy, Japan, Korea, Mexico, the Netherlands, Norway, Poland, Portugal, Romania, Russia, Scotland, Singapore, Spain, Sweden, Switzerland and Taiwan.

We also license software with maintenance and support, which includes rights to upgrades, when and if available, support, updates and enhancements.

For information regarding our market and business segment revenue, geographic areas and significant customers, please refer to Note 17 of our Notes to Consolidated Financial Statements.

Order Fulfillment

The procurement of the various components of packaged products, including CDs and printed materials, and the assembly of packages for retail and other applications products is controlled by our Global Supply Chain Management operations. We outsource our order fulfillment activities to third parties in the United States, Europe and Asia.

To date, we have not experienced significant difficulties in obtaining raw materials for the manufacture of our products or in the replication of CDs, printing and assembly of components, although an interruption in production by a supplier could result in a delay in shipment of our products. The backlog of orders from customers, as of January 19, 2007 and January 20, 2006, was approximately $15.1 million and $30.9 million, respectively.

Services and Support

We provide professional services, technical support and customer service to a wide variety of customers including consumers, creative professionals and business users. Our service and support revenue consists primarily of consulting fees, software maintenance and support fees, and training fees.

Services

We have a global Adobe Consulting team dedicated to developing and implementing solutions for enterprise customers in key vertical markets and to transfer technical expertise to our solution partners. The Adobe Consulting team uses a comprehensive, customer-focused methodology to develop high quality solutions, which in turn deliver a competitive advantage to our enterprise customers. A portfolio of technical training courses is also available for desktop and server-based products to meet the needs of our enterprise customers and solution partners.

Support

A significant portion of our support revenue is composed of our extended enterprise maintenance and support offerings, which entitles customers to the right to receive product upgrades and enhancements during the term of the maintenance and support period, which is typically one year. Regional Support

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Centers are charged with providing timely, high quality technical expertise on Enterprise and Knowledge Worker Solutions products and solutions to meet the growing needs of our customers.

Our support revenue also includes support for our desktop products. We offer a range of support programs, from fee-based incidents to annual support contracts. Additionally, we provide extensive self-help and online technical support capabilities via the Web, which allows customers quick and easy access to possible solutions. We provide product support through a combination of outsourced vendors and internal support centers.

We also offer Developer Support to partners and developer organizations. The Adobe Solution Network Developer Program focuses on providing developers with high-quality tools, software development kits, information and services.

As a registered owner of the current version of an Adobe desktop product, customers are eligible to receive complimentary person-to-person support on certain matters. Support for some products and in some countries may vary.

Training

We inform customers about the use of our products through on-line informational services on our Web site (www.adobe.com) and through a growing series of how to books published by Adobe Press pursuant to a joint publishing agreement with Peachpit Press. In addition, we develop tests to certify independent trainers who teach Adobe software classes. We sponsor workshops, work with professional associations and user groups, and conduct regular beta testing programs.

Investments

We own limited partnership interests in three venture capital limited partnerships, Adobe Ventures L.P., Adobe Ventures III, L.P. and Adobe Ventures IV, L.P. (collectively Adobe Ventures), that have invested in early stage companies with innovative technologies. We also make direct investments in privately held companies. We enter into these investments with the intent of securing financial returns as well as for strategic purposes as they often increase our knowledge of emerging markets and technologies, as well as expand our opportunities to provide Adobe products and services. The partnerships are managed by Granite Ventures, an independent venture capital firm and sole general partner of Adobe Ventures.

We intend to continue direct investments in new technologies and plan to invest approximately $100 million in venture capital over the next three to five years in companies leveraging our platform technologies.

PRODUCT DEVELOPMENT

Since the personal computer and enterprise software industries are characterized by rapid technological change, a continuous high level of investment is required for the enhancement of existing products and the development of new products. We primarily develop our software internally. We occasionally acquire products developed by others by purchasing the stock or assets of the business entity that held ownership rights to the technology. In other instances, we have licensed or purchased the intellectual property ownership rights of programs developed by others with license or technology transfer agreements that may obligate us to pay royalties, typically based on a dollar amount per unit shipped or a percentage of the revenues generated by those programs.

During fiscal years ended December 1, 2006, December 2, 2005, and December 3, 2004, our research and development expenses, including costs related to contract development, were $539.7 million, $365.3 million, and $311.3 million, respectively.

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During fiscal 2006, we acquired Macromedia, Inc., a provider of software technologies that enable the development of a wide range of internet and mobile application solutions. For further information regarding this acquisition, see Note 2 of our Notes to Consolidated Financial Statements.

During fiscal 2005, we acquired OKYZ S.A., a privately held company, which provided three dimensional technology and expertise to our Intelligent Document platform.

During fiscal 2004, we acquired Q-Link Technologies, Inc, a privately-held company, which provided Java-based workflow technology that was integrated with our enterprise server products to enable customers to integrate document process management with core applications.

PRODUCT PROTECTION

We regard our software as proprietary and protect it under the laws of copyrights, patents, trademarks and trade secrets. We protect the source code of our software programs as trade secrets, and make source code available to third parties only under limited circumstances and specific security and confidentiality constraints.

Our products are generally licensed to end users on a right to use basis pursuant to a license that restricts the use of the products to a designated number of devices. We also rely on copyright laws and on shrink wrap and electronic licenses that are not physically signed by the end user. Copyright protection may be unavailable under the laws of certain countries, and the enforceability of shrink wrap and electronic licenses has not been conclusively determined in all jurisdictions. We have obtained many patents and have registered numerous copyrights, trademarks, domain names and logos in the United States and foreign countries.

Policing unauthorized use of computer software is difficult and software piracy is a persistent problem for the software industry. This problem is particularly acute in international markets. We conduct vigorous anti piracy programs directly and through certain external software associations. Although our products generally do not contain copy protection or network copy detection features, we have recently included activation technology in certain products to guard against illegal use and will continue to do so in certain future products.

EMPLOYEES

As of January 19, 2007, we employed 6,082 people. We have not experienced work stoppages and believe our employee relations are good. Competition in recruiting personnel in the software industry, especially highly skilled engineers, is intense. We believe our future success will depend in part on our continued ability to recruit and retain highly skilled technical, management and sales and marketing personnel.

AVAILABLE INFORMATION

Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed or furnished pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, are available free of charge on our Investor Relations Web site at www.adobe.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The information posted on our Web site is not incorporated into this Annual Report on Form 10-K.

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EXECUTIVE OFFICERS

Adobe s executive officers as of January 19, 2007 are as follows:

Name	Age	Positions
Bruce R. Chizen	51	Chief Executive Officer and acting Chief Financial Officer
Karen O. Cottle	57	Senior Vice President, General Counsel and Corporate Secretary
Shantanu Narayen	43	President and Chief Operating Officer
Matthew Thompson	48	Senior Vice President, Worldwide Field Operations
Richard T. Rowley	51	Vice President, Principal Accounting Officer

Mr. Chizen joined Adobe upon the closing of the acquisition of Aldus in August 1994 as Vice President and General Manager, Consumer Products Division. In December 1997, he was promoted to Senior Vice President and General Manager, Graphic Products Division and in August 1998, Mr. Chizen was promoted to Executive Vice President, Products and Marketing. In April 2000, Mr. Chizen was promoted to President of Adobe and in December 2000, he also became Adobe s Chief Executive Officer and joined the Adobe Board of Directors in December 2000. In January 2005, Mr. Chizen relinquished the title of President, but remains as Adobe s Chief Executive Officer and a member of Adobe s Board of Directors. Mr. Chizen was also appointed as Adobe s acting Chief Financial Officer in November 2006. Mr. Chizen is a member of the Board of Directors of Synopsys, Inc.

Ms. Cottle joined Adobe in February 2002 as Senior Vice President, General Counsel and Secretary. Prior to joining Adobe, Ms. Cottle served as General Counsel for Vitria Technology, Inc., a service-oriented business application software company from February 2000 to February 2002. From 1996 to 1999, Ms. Cottle served as Vice President, General Counsel and Secretary of Raychem Corporation.

Mr. Narayen joined Adobe in January 1998 as Vice President and General Manager of Adobe s engineering technology group. In January 1999, he was promoted to Senior Vice President, Worldwide Products and in March 2001 he was promoted to Executive Vice President, Worldwide Product Marketing and Development. In January 2005, Mr. Narayen was promoted to President and Chief Operating Officer of Adobe. Prior to joining Adobe, Mr. Narayen co-founded Pictra Inc., a digital photo sharing software company, in 1996. He was Director of Desktop and Collaboration products at Silicon Graphics Inc. and held various senior manager positions at Apple Inc. before founding Pictra.

Mr. Thompson joined Adobe in January 2006 as Senior Vice President, Worldwide Field Operations. Prior to joining Adobe, Mr. Thompson served as Senior Vice President of Worldwide Sales at Borland Software Corporation, a software delivery optimization solutions provider, from October 2003 to December 2006. Prior to joining Borland, Mr. Thompson was Vice President of Worldwide Sales and Field Operations for Marimba, Inc., a provider of products and services for software change and configuration management, from February 2001 to January 2003. From July 2000 to January 2001, Mr. Thompson was Vice President of Worldwide Sales for Calico Commerce, Inc., a provider of eBusiness applications. Prior to joining Calico, Mr. Thompson spent six years at Cadence Design Systems, a provider of electronics design technologies. While at Cadence, from January 1998 to June 2000, Mr. Thompson served as Senior Vice President, Worldwide Sales and Field Operations and from April 1994 to January 1998 as Vice President, Worldwide Professional Services.

Mr. Rowley joined Adobe in November 2006 as Vice President, Corporate Controller and Principal Accounting Officer. Prior to joining Adobe, Mr. Rowley served as Vice President, Corporate Controller, Treasurer and Principal Accounting Officer at Synopsys, Inc., a semiconductor design software company,

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from December 2002 to September 2005, and from 1999 to December 2002, Mr. Rowley served as Vice President, Corporate Controller and Principal Accounting Officer. From 1994 to 1999, Mr. Rowley served in several finance-related positions at Synopsys. Mr. Rowley is a certified public accountant.

ITEM 1A.   RISK FACTORS

As previously discussed, our actual results could differ materially from our forward looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed below. These and many other factors described in this report could adversely affect our operations, performance and financial condition.

Delays in development or shipment of new products or major new versions of existing products could cause a decline in our revenue.

Any delays or failures in developing and marketing our products, including upgrades of current products and the integration of Macromedia products into our product line, may have a harmful impact on our results of operations. We may have particular difficulty and delays developing products that integrate Adobe and Macromedia products, since our products are highly complex, have been designed independently and were designed without regard to such integration. Our inability to extend our core technologies into new applications and new platforms and to anticipate or respond to technological changes could affect continued market acceptance of our products and our ability to develop new products. Delays in product or upgrade introductions could cause a decline in our revenue, earnings or stock price. We cannot determine the ultimate effect these delays or the introduction of new products or upgrades will have on our revenue or results of operations.

Introduction of new products by existing and new competitors could harm our competitive position and results of operations.

The end markets for our software products are intensely and increasingly competitive, and are significantly affected by product introductions and market activities of industry competitors, including Microsoft s announced introduction of its new Vista operating system which contains a new fixed document format, XPS, which will compete with Adobe PDF, and its introduction of Office 12 which offers a feature to save Microsoft Office documents as PDF files through a freely distributed plug-in, which competes with Adobe PDF creation. If these competing products achieve widespread acceptance, our operating results could suffer. In addition, consolidation has occurred among some of the competitors in our markets. Any further consolidations among our competitors may result in stronger competitors and may therefore harm our results of operations. For additional information regarding our competition and the risks arising out of the competitive environment in which we operate, see the section entitled   Competition   contained in Item 1 of this Annual Report.

If we fail to successfully manage transitions to new business models and markets, our results of operations could be negatively impacted.

We are devoting significant resources to the development of technologies and service offerings where we have a limited operating history, including the enterprise and government markets and the mobile and device markets. In the enterprise and government markets, we intend to increase our focus on vertical markets such as education, financial services, manufacturing, and the architecture, engineering and construction markets. With our Adobe Acrobat Connect product line, we intend to increase awareness in targeted horizontal markets such as training and marketing and vertical markets such as manufacturing, financial services and telecommunications. These new offerings and markets require a considerable investment of technical, financial and sales resources, and a scaleable organization. Many of our competitors may have advantages over us due to their larger presence, larger developer network, deeper experience in the enterprise and government markets and the mobile and device markets, and greater sales

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