

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

-----  
FORM 10-Q

(Mark One)

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended December 31, 1999.

OR

Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-8703

WESTERN DIGITAL CORPORATION  
(Exact name of Registrant as specified in its charter)

|   |   |
|---|---|
| Delaware<br>(State or other jurisdiction of<br>incorporation or organization) | 95-2647125<br>(I.R.S. Employer<br>Identification No.) |
|---|---|

|  |                     |
|--|---------------------|
| 8105 Irvine Center Drive<br>Irvine, California<br>(Address of principal executive offices) | 92618<br>(Zip Code) |
|--|---------------------|

REGISTRANT'S TELEPHONE NUMBER INCLUDING AREA CODE: (949) 932-5000  
REGISTRANT'S WEB SITE: <http://www.westerndigital.com>

N/A Former name, former address and former fiscal year if  
changed since last report.

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

Number of shares outstanding of Common Stock, as of January 29, 2000,  
is 129,078,880.

WESTERN DIGITAL CORPORATION  
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PART I. FINANCIAL INFORMATION  
 ITEM 1. FINANCIAL STATEMENTS

WESTERN DIGITAL CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
 (UNAUDITED)

|  | THREE-MONTH PERIOD ENDED |                  |
|--|--------------------------|------------------|
|  | DEC. 26,<br>1998         | DEC. 31,<br>1999 |
| Revenues, net .....                                    | \$ 738,590               | \$ 560,174       |
| Costs and expenses:                                    |                          |                  |
| Cost of revenues .....                                 | 719,423                  | 539,932          |
| Research and development .....                         | 50,363                   | 44,083           |
| Selling, general and administrative .....              | 47,819                   | 39,070           |
| Restructuring charges .....                            | --                       | 25,535           |
| Total costs and expenses .....                         | 817,605                  | 648,620          |
| Operating loss .....                                   | (79,015)                 | (88,446)         |
| Net interest expense .....                             | (3,238)                  | (3,028)          |
| Loss before extraordinary item .....                   | (82,253)                 | (91,474)         |
| Extraordinary gain from redemption of debentures ..... | --                       | 76,277           |
| Net loss .....   | \$ (82,253)              | \$ (15,197)      |
|  | =====                    | =====            |
| Basic and diluted loss per common share:               |                          |                  |
| Loss per common share before extraordinary item ....   | \$ (.93)                 | \$ (.76)         |
| Extraordinary gain .....                               | --                       | .63              |
| Loss per common share .....                            | \$ (.93)                 | \$ (.13)         |
|  | =====                    | =====            |
| Common shares used in computing per share amounts:     |                          |                  |
| Basic .....  | 88,888                   | 121,128          |
|  | =====                    | =====            |
| Diluted .....  | 88,888                   | 121,128          |
|  | =====                    | =====            |

The accompanying notes are an integral part of these condensed consolidated financial statements

WESTERN DIGITAL CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
 (UNAUDITED)

|  | SIX-MONTH PERIOD ENDED |                  |
|--|------------------------|------------------|
|  | DEC. 26,<br>1998       | DEC. 31,<br>1999 |
| Revenues, net .....                                    | \$ 1,389,448           | \$ 967,131       |
| Costs and expenses:                                    |                        |                  |
| Cost of revenues .....                                 | 1,453,033              | 1,012,232        |
| Research and development .....                         | 102,284                | 94,226           |
| Selling, general and administrative .....              | 105,151                | 82,892           |
| Restructuring charges .....                            | --                     | 57,835           |
| Total costs and expenses .....                         | 1,660,468              | 1,247,185        |
| Operating loss .....                                   | (271,020)              | (280,054)        |
| Net interest expense .....                             | (5,891)                | (8,357)          |
| Loss before extraordinary item .....                   | (276,911)              | (288,411)        |
| Extraordinary gain from redemption of debentures ..... | --                     | 166,899          |
| Net loss .....   | \$ (276,911)           | \$ (121,512)     |
|  | =====                  | =====            |
| Basic and diluted loss per common share:               |                        |                  |
| Loss per common share before extraordinary item ....   | \$ (3.12)              | \$ (2.66)        |
| Extraordinary gain .....                               | --                     | 1.54             |
| Loss per common share .....                            | \$ (3.12)              | \$ (1.12)        |
|  | =====                  | =====            |
| Common shares used in computing per share amounts:     |                        |                  |
| Basic .....  | 88,717                 | 108,523          |
|  | =====                  | =====            |
| Diluted .....  | 88,717                 | 108,523          |
|  | =====                  | =====            |

The accompanying notes are an integral part of these condensed consolidated financial statements

WESTERN DIGITAL CORPORATION  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

|   | JULY 3,<br>1999<br>----- | DEC. 31,<br>1999<br>-----<br>(UNAUDITED) |
|---|--------------------------|--|
| ASSETS  |                          |  |
| Current assets:   |                          |  |
| Cash and cash equivalents .....   | \$ 226,147               | \$ 163,675                               |
| Accounts receivable, less allowance for doubtful<br>accounts of \$18,537 at July 3, 1999 and<br>\$17,352 at December 31, 1999 .....                   | 273,435                  | 198,360                                  |
| Inventories .....   | 144,093                  | 101,728                                  |
| Prepaid expenses & other current assets .....   | 81,853                   | 95,471                                   |
| Total current assets .....  | 725,528                  | 559,234                                  |
| Property and equipment at cost, net .....   | 237,939                  | 156,891                                  |
| Intangible and other assets, net .....  | 58,935                   | 48,599                                   |
| Total assets .....  | \$ 1,022,402<br>=====    | \$ 764,724<br>=====                      |
| LIABILITIES AND SHAREHOLDERS' DEFICIENCY  |                          |  |
| Current liabilities:  |                          |  |
| Accounts payable .....  | \$ 335,907               | \$ 283,545                               |
| Accrued expenses .....  | 252,791                  | 291,195                                  |
| Current portion of long-term debt .....   | 10,000                   | --                                       |
| Total current liabilities .....   | 598,698                  | 574,740                                  |
| Long-term debt .....  | 534,144                  | 236,291                                  |
| Deferred income taxes and other .....   | 43,350                   | 41,761                                   |
| Shareholders' deficiency:   |                          |  |
| Preferred stock, \$.01 par value;<br>Authorized: 5,000 shares<br>Outstanding: None .....  | --                       | --                                       |
| Common stock, \$.01 par value;<br>Authorized: 225,000 shares<br>Outstanding: 101,908 shares at July 3, 1999<br>and 139,916 at December 31, 1999 ..... | 1,019                    | 1,399                                    |
| Additional paid-in capital .....  | 335,197                  | 492,845                                  |
| Accumulated deficit .....   | (294,841)                | (416,353)                                |
| Accumulated other comprehensive income (loss) .....   | (2,123)                  | 23,461                                   |
| Treasury stock-common stock at cost;<br>11,297 shares at July 3, 1999 and 10,884<br>shares at December 31, 1999 .....                                 | (193,042)                | (189,420)                                |
| Total shareholders' deficiency .....  | (153,790)                | (88,068)                                 |
| Total liabilities and shareholders' deficiency .....  | \$ 1,022,402<br>=====    | \$ 764,724<br>=====                      |

The accompanying notes are an integral part of these condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN THOUSANDS)  
(UNAUDITED)

|  | SIX-MONTH PERIOD ENDED |                  |
|--|------------------------|------------------|
|  | DEC. 26,<br>1998       | DEC. 31,<br>1999 |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                 |                        |                  |
| Net loss .....   | \$(276,911)            | \$(121,512)      |
| Adjustments to reconcile net loss to net cash used for operating activities: |                        |                  |
| Non-Cash Items:  |                        |                  |
| Depreciation and amortization .....  | 67,287                 | 47,223           |
| Interest accrued on convertible debentures .....                             | 12,317                 | 9,617            |
| Non-cash portion of restructuring charges .....                              | --                     | 28,804           |
| Extraordinary gain on sale of debentures .....                               | --                     | (166,899)        |
| Changes in assets and liabilities:   |                        |                  |
| Accounts receivable .....  | (2,947)                | 75,075           |
| Inventories .....  | 25,542                 | 42,365           |
| Prepaid expenses .....   | 11,788                 | 6,693            |
| Accounts payable .....   | 55,874                 | (51,754)         |
| Accrued expenses .....   | 56,322                 | 25,479           |
| Other .....  | 2,396                  | 3,670            |
|  | (48,332)               | (101,239)        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                 |                        |                  |
| Proceeds from or deposits relating to sales of property and equipment .....  | --                     | 37,019           |
| Capital expenditures, net .....  | (60,097)               | (13,843)         |
| Other investments .....  | (1,500)                | (2,200)          |
|  | (61,597)               | 20,976           |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                 |                        |                  |
| Cash used to repay bank debt (Note 5) .....                                  | (50,000)               | (33,375)         |
| Proceeds from issuance of bank debt (Note 5) .....                           | 50,000                 | --               |
| Proceeds from ESPP shares issued and stock option exercises .....            | 6,684                  | 1,627            |
| Common stock issued .....  | --                     | 49,539           |
| Costs relating to credit facility .....                                      | (2,925)                | --               |
| Net cash provided by financing activities .....                              | 3,759                  | 17,791           |
|  | (106,170)              | (62,472)         |
| Cash and cash equivalents, beginning of period .....                         | 459,830                | 226,147          |
|  | \$ 353,660             | \$ 163,675       |
|  | \$ 353,660             | \$ 163,675       |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>                    |                        |                  |
| Cash paid during the period for income taxes .....                           | \$ 3,317               | \$ 1,082         |
| Cash paid during the period for interest .....                               | 2,136                  | 937              |

The accompanying notes are an integral part of these condensed consolidated financial statements.



|                               | THREE-MONTH PERIOD ENDED |                  | SIX-MONTH PERIOD ENDED |                  |
|-------------------------------|--------------------------|------------------|------------------------|------------------|
|                               | DEC. 26,<br>1998         | DEC. 31,<br>1999 | DEC. 26,<br>1998       | DEC. 31,<br>1999 |
| Net Interest Income (Expense) |                          |                  |                        |                  |
| Interest income .....         | \$ 4,824                 | \$ 2,006         | \$ 10,115              | \$ 4,487         |
| Interest expense .....        | (8,062)                  | (5,034)          | (16,006)               | (12,844)         |
|                               | \$ (3,238)               | \$ (3,028)       | \$ (5,891)             | \$ (8,357)       |
|                               | =====                    | =====            | =====                  | =====            |

### 3. Loss per Share

As of December 26, 1998 and December 31, 1999, 17.4 and 24.0 million shares, respectively, relating to the possible exercise of outstanding stock options were not included in the computation of diluted loss per share. As of December 26, 1998 and December 31, 1999, an additional 19.4 and 8.4 million shares, respectively, issuable upon conversion of the convertible debentures were excluded from the computation of diluted loss per share. The effects of these items were not included in the computation of diluted loss per share as their effect would have been anti-dilutive.

In September 1999, the Company's Board of Directors approved a "Broad-Based" Incentive Stock Plan (the "Broad-Based Plan") under which options to purchase shares of common stock may be granted to employees of the Company and others. On October 20, 1999, the Board of Directors approved a grant to its regular, non-direct labor employees of approximately 2.4 million shares under the Broad-Based Plan and the Company's Employee Stock Option Plan, at \$3.31 per share, the fair value of the Company's common stock on the date of the grant. The options granted vest 100% one year from the date of grant.

On September 10, 1998, the Company's Board of Directors authorized and declared a dividend distribution of one Right for each share of common stock of the Company outstanding at the close of business on November 30, 1998. In addition, the Company's Board of Directors authorized the issuance of one Right for each share of common stock of the Company issued from the record date until certain dates as specified in the Company's rights agreement dated as of October 15, 1998, pursuant to which the Company's then existing shareholders rights plan was replaced by a successor ten year plan. The Rights issued become exercisable for common stock at a discount from market value upon certain events related to a change in control.

### 4. Common Stock Transactions

During the six-month period ended December 31, 1999, the Company issued approximately 362,000 shares of its common stock in connection with Employee Stock Purchase Plan ("ESPP") purchases and issued 52,000 shares of its common stock in connection with common stock option exercises, for an aggregate of \$1.6 million. During the corresponding period of the prior year, the Company issued approximately 325,000 shares of its common stock in connection with ESPP purchases and 493,000 shares of its common stock in connection with common stock option exercises, for an aggregate of \$6.7 million.

Under an existing equity facility, the Company may issue for cash, shares of common stock to institutional investors in monthly increments of \$12.5 million. The facility provides for up to \$150.0 million in cash proceeds of which \$49.5 million had been utilized as of December 31, 1999. Shares paid under the facility are at the market price of the Company's common stock less a discount ranging from 2.75% to 4.25%.

During the six-month period ended December 31, 1999, the Company issued 26.7 million shares of common stock to redeem its 5.25% zero coupon convertible subordinated debentures (the "Debentures") with a carrying value of \$284.1 million, and an aggregate principal amount at maturity of \$735.6 million. These redemptions were private, individually negotiated transactions with certain institutional investors. The redemptions resulted in extraordinary gains of \$166.9 million during the six months ended December



31, 1999. As of December 31, 1999, the carrying value of the remaining outstanding Debentures was \$219.7 million and the aggregate principal amount at maturity was \$561.6 million.

5. Credit Facility

The Company has a secured revolving credit and term loan facility ("Senior Bank Facility") which, as amended on January 15, 2000, provided the Company with up to a \$125.0 million revolving credit line (depending on the borrowing base calculation) and a \$50.0 million term loan (of which \$16.6 million was outstanding as of December 31, 1999). Borrowings under the Senior Bank Facility are secured by the Company's accounts receivable, inventory, 66% of its stock in its foreign subsidiaries and the other assets (excluding real property) of the Company and, at the option of the Company, bear interest at either LIBOR or a base rate plus a margin determined by the borrowing base, with option periods of one to three months. The Senior Bank Facility requires the Company to maintain certain amounts of net equity, prohibits the payment of cash dividends on common stock and contains a number of other covenants. This facility matures on March 31, 2000, and further borrowings through such date are not allowed. As of the date hereof, the remaining balance on the term loan has been repaid using the proceeds from the equity facility. The Company has received a proposal for a new credit facility, including a term loan. As of the date hereof, the terms and conditions of this proposal have not been finalized.

6. Sales of Real Property

On August 9, 1999, the Company sold approximately 34 acres of land in Irvine, California, upon which it had previously planned to build a new corporate headquarters, for \$26 million (the approximate cost of the land). The Company has extended the current lease of its worldwide headquarters in Irvine, California, through January 2001, and has an option to extend the lease for an additional five month period.

In December 1999, the Company agreed to sell a manufacturing facility in Tuas, Singapore for cash proceeds of \$11.0 million. In January 2000, the Company also agreed to sell its Rochester, Minnesota facility for cash proceeds of approximately \$30.0 million. These transactions are expected to close, subject to customary closing conditions, in the quarter ending March 31, 2000, each with a minimal gain or loss.

7. Restructuring Activities

During the six months ended December 31, 1999, the Company initiated a restructuring program which is intended to improve operational effectiveness and efficiency and reduce operational expenses worldwide. Charges related to the restructuring actions taken are accrued in the periods in which executive management commits to execute such actions. Committed actions for the six months ended December 31, 1999 include reorganization of operational and management responsibilities, transfer of hard drive production from Singapore to the Company's manufacturing facility in Malaysia, and closure of the Company's Singapore operations. These actions will result in a net reduction of world-wide headcount of approximately 1,000, of which approximately 100 will be management, professional and administrative personnel and the remainder will be manufacturing employees. In Asia, approximately 3,800 employees will be reduced from the Company's Singapore operation and approximately 2,900 will be added in Malaysia in connection with the transfer of production. Restructuring charges recorded in connection with these actions totaled \$57.8 million for the six-month period ended December 31, 1999 and consist of severance and outplacement costs of \$18.0 million, write-offs of manufacturing equipment and information systems assets no longer utilized as a result of the actions of \$28.8 million, and lease cancellation and other costs of \$11.0 million. Following is a summary of the charges, the amounts paid and the ending accrual balance (in thousands):

SIX-MONTH PERIOD ENDED  
DECEMBER 31, 1999  
-----

|   | Accruals<br>----- | Non-Cash<br>Charges<br>----- | Total<br>-----    |
|---|-------------------|------------------------------|-------------------|
| Equipment and information systems<br>asset write-offs | \$ --             | \$28,822                     | \$28,822          |
| Severance and outplacement                            | 18,028            | --                           | 18,028            |
| Lease cancellation and other                          | 10,985<br>-----   | --<br>-----                  | 10,985<br>-----   |
| Total charges   | 29,013            | \$28,822<br>=====            | \$57,835<br>===== |
| Cash utilized   | 7,456<br>-----    |                              |                   |
| Balance at December 31, 1999                          | \$21,557<br>===== |                              |                   |

The Company expects that remaining accruals for severance and outplacement of \$10.1 million will be paid in the third and fourth quarters of 2000. Lease cancellation and other costs are expected to be paid over the 24 months beginning October 3, 1999. The Company expects the aforementioned restructuring actions to be completed no later than June 30, 2000.

The equipment to be disposed of was determined to have minimal salvage value.

On January 19, 2000, the Company announced that it will exit the enterprise hard drive business and shift its strategic focus and resources in the enterprise storage market to Internet-related data content management systems and management software. In connection with this decision, the Company closed its Rochester, Minnesota enterprise hard drive design center, and a majority of the 420 employees in the design center have been laid off and given legally required notification and outplacement services. The exit from the enterprise business will result in nonrecurring charges against operations in the quarter ended March 31, 2000. The Company currently estimates these charges to include \$25.0 million for property and equipment write-offs, and \$11.0 million for severance (\$8.0 million relating to domestic operations). The Company is currently analyzing the effect of this decision on inventory purchase commitments and the price levels that may be needed to sell the Company's remaining enterprise products. Accordingly, additional reserves and accruals may be needed for purchase order cancellations, purchase price protection, inventory write-downs and other costs flowing from the Company's decision to exit. The Company estimates that the restructuring effort will be substantially completed by June 30, 2000.

As of December 31, 1999, the accrued expenses for the Company's 1999 restructuring efforts were substantially utilized.

8. Product Recall

On September 27, 1999, the Company announced a recall of its 6.8GB per platter series of WD Caviar(R) desktop hard drives because of a reliability problem resulting from a faulty power driver chip manufactured by a third-party supplier. Approximately 1.2 million units were manufactured with the faulty chip. Replacement of the chips involved rework of the printed circuit board assembly. Revenues of approximately \$100 million related to the products which were recalled were reversed in the three months ended October 2, 1999. In addition, the Caviar product line was shut down for approximately two weeks, eliminating approximately \$70 million of forecasted revenue during the three months ended October 2, 1999. Cost of revenues for the three months ended October 2, 1999, included charges totaling \$37.7 million for estimated costs to recall and repair the affected drives, including \$23.1 million for repair and retrieval, \$4.5 million for freight and other, and \$10.1 million for write-downs of related inventory. By the end of the three months ended December 31, 1999, the Company had completed

rework on approximately 78% of the 1.2 million units and had resolved its claims against third parties resulting from the recall.

9. Investments in Marketable Securities

The Company owns approximately 10.8 million shares of Komag common stock, which when acquired on April 8, 1999, had a fair market value of \$34.9 million. The stock is restricted as to the number of shares which can be sold in a given time period. The restrictions will lapse over a three and one-half year period. As of December 31, 1999, approximately 60% of these shares may be sold within 12 months. Because the Company has identified these shares as "available for sale" under the provisions of Statement of Financial Accounting Standards No. 115, "Investments in Certain Debt and Equity Securities" ("SFAS 115"), they have been marked to market value using published closing prices of Komag stock as of December 31, 1999. Accordingly, an incremental unrealized gain of approximately \$1.4 million was recorded during the six months ended December 31, 1999, and a total accumulated unrealized loss of \$0.7 million is included in accumulated other comprehensive income (loss). The aggregate carrying value of the shares, which approximates market value, is \$34.2 million as of December 31, 1999, of which \$20.2 million relates to "available for sale" shares and is classified as current.

The Company owns approximately 1.3 million shares of Vixel Corporation ("Vixel") common stock, all of which are restricted as to sale until March 28, 2000, pursuant to an agreement with Vixel's underwriters. The Company has identified these shares as "available for sale" under the provisions of SFAS 115. During the three months ended October 2, 1999, Vixel completed an initial public offering and the shares were marked to market value. Accordingly, an unrealized gain of \$24.2 million was recorded in accumulated other comprehensive income (loss) during the three months ended October 2, 1999. The investment in Vixel common stock is classified as current. As of December 31, 1999, the quoted market value of the Company's Vixel common stock approximated its carrying value.

10. Other Comprehensive Income (Loss)

The Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130"), beginning with the Company's fourth quarter of 1999. Prior to the fourth quarter of 1999, the Company did not possess any components of other comprehensive income as defined by SFAS 130. SFAS 130 separates comprehensive income into two components; net income and other comprehensive income (loss). Other comprehensive income (loss) refers to revenue, expenses, gains and losses that are recorded as an element of shareholders' equity but are excluded from net income. While SFAS 130 establishes new rules for the reporting and display of comprehensive income (loss), SFAS 130 has no impact on the Company's net loss or total shareholders' deficiency. The Company's other comprehensive income (loss) is comprised of unrealized gains and losses on marketable securities categorized as "available for sale" under SFAS 115. The components of total comprehensive loss for the three and six-month periods ended December 31, 1999 were as follows (in millions):

|   | Three-Month<br>Period Ended<br>Dec. 31, 1999<br>----- | Six-Month<br>Period Ended<br>Dec. 31, 1999<br>----- |
|---|---|---|
| Net loss  | \$(15.2)  | \$(121.5)   |
| Other comprehensive income:                               |   |   |
| Unrealized gain on available for<br>sale investments, net | 1.5<br>-----  | 25.6<br>-----                                       |
| Total comprehensive loss                                  | \$(13.7)<br>=====                                     | \$ (95.9)<br>=====                                  |

## 11. Legal Proceedings

The Company was sued by Amstrad PLC ("Amstrad") in December 1992 in Orange County Superior Court. The complaint alleged that hard drives supplied by the Company in calendar 1988 and 1989 were defective and caused damages to Amstrad of \$186.0 million in out-of-pocket expenses, lost profits, injury to Amstrad's reputation and loss of goodwill. The Company filed a counterclaim for \$3.0 million in actual damages in addition to exemplary damages in an unspecified amount. The first trial of this case ended in a mistrial, with the jury deadlocked on the issue of liability. The case was retried, and on June 9, 1999, the jury returned a verdict against Amstrad and in favor of Western Digital. Amstrad has filed a notice of appeal from the judgment, and the Company has filed motions seeking recovery of a portion of its legal and other costs of defense. The Company does not believe that the ultimate resolution of this matter will have a material adverse effect on the financial position, results of operations or liquidity of the Company. However, should the judgment be reversed on appeal, and if in a retrial of the case Amstrad were to prevail, the Company may be required to pay damages and other expenses, which may have a material adverse effect on the Company's financial position, results of operations and/or liquidity. In addition, the costs of defending a retrial of the case may be material, regardless of the outcome.

In 1994 Papst Licensing ("Papst") brought suit against the Company in the U.S. District Court for the Central District of California alleging infringement by the Company of five of its patents relating to disk drive motors that the Company purchases from motor vendors. Later that year Papst dismissed its case without prejudice, but it has notified the Company that it intends to reinstate the suit if the Company does not agree to enter into a license agreement with Papst. Papst has also put the Company on notice with respect to several additional patents. The Company does not believe that the ultimate resolution of this matter will have a material adverse effect on the financial position, results of operations or liquidity of the Company. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, the Company may be required to pay damages and other expenses, which may have a material adverse effect on the Company's financial position, results of operations and/or liquidity. In addition, the costs of defending such litigation may be material, regardless of the outcome.

The Company and Censtor Corporation ("Censtor") have had discussions concerning royalties, if any, that might be due Censtor under a licensing agreement. Censtor has initiated arbitration procedures under the agreement seeking payment of royalties. In response, the Company has filed a complaint in federal court seeking a determination that the patents at issue are invalid. The Federal Court action has been stayed pending completion of the arbitration procedures. The Company does not believe that the outcome of this dispute will have a material adverse effect on its financial position, results of operations and/or liquidity.

In the normal course of business, the Company receives and makes inquiry regarding possible intellectual property matters including alleged patent infringement. Where deemed advisable, the Company may seek or extend licenses or negotiate settlements. Although patent holders often offer such licenses, no assurance can be given that a license will be offered or that the terms of any license offered will be acceptable to the Company. Several such matters are currently pending. The Company does not believe that the ultimate resolution of these matters will have a material adverse effect on the financial position, results of operations or liquidity of the Company.

From time to time the Company receives claims and is a party to suits and other judicial and administrative proceedings incidental to its business. Although occasional adverse decisions (or settlements) may occur, the Company believes that the final disposition of such matters will not have a material adverse effect on the Company's financial position, results of operations or liquidity.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of federal securities laws. The statements that are not purely historical should be considered forward-looking statements. Often they can be identified by the use of forward-looking words, such as "may", "will", "could", "project", "believe", "anticipate", "expect", "estimate", "continue", "potential", "plan", "forecasts" and the like. Statements concerning current conditions may also be forward-looking if they imply a continuation of current conditions. These statements appear in a number of places in this report and include statements regarding the intentions, plans, strategies, beliefs or current expectations of the Company with respect to, among other things:

- the financial prospects of the Company
- the Company's financing plans
- litigation and other contingencies potentially affecting the Company's financial position, operating results, or liquidity
- trends affecting the Company's financial condition or operating results
- the Company's strategies for growth, operations, product development and commercialization
- conditions or trends in or factors affecting the computer, data storage, home entertainment or hard drive industry.

Forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those expressed in the forward-looking statements. Readers are urged to carefully review the disclosures made by the Company concerning risks and other factors that may affect the Company's business and operating results, including those made under the captions "Risk factors related to the hard drive industry in which we operate" and "Risk Factors relating to Western Digital particularly" in this report, as well as the Company's other reports filed with the Securities and Exchange Commission. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to publish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

RECENT DEVELOPMENTS

During the six months ended December 31, 1999, the Company initiated a restructuring program which is intended to improve operational effectiveness and efficiency and reduce operational expenses worldwide. Charges related to the restructuring actions taken are accrued in the periods in which executive management commits to execute such actions. Committed actions for the six months ended December 31, 1999 include reorganization of operational and management responsibilities, transfer of hard drive production from Singapore to the Company's manufacturing facility in Malaysia, and closure of the Company's Singapore operations. These actions will result in a net reduction of world wide headcount of approximately 1,000, of which approximately 100 will be management, professional and administrative personnel and the remainder will be manufacturing employees. In Asia, approximately 3,800 employees will be reduced from the Company's Singapore operation and approximately 2,900 will be added in Malaysia in connection with the transfer of production. Restructuring charges recorded in connection with these actions totaled \$57.8 million for the six-month period ended December 31, 1999 and consist of severance and outplacement costs of \$18.0 million, write-offs of manufacturing equipment and information systems assets no longer utilized as a result of the actions of \$28.8 million, and lease cancellation and other costs of \$11.0 million. The Company expects that remaining accruals for severance and outplacement of \$10.1 million will be paid in the third and fourth quarters of 2000. Lease cancellation and other costs are expected to be paid over the 24 months beginning October 3, 1999. The Company expects the aforementioned restructuring actions to be completed no later than June 30, 2000.

On August 9, 1999, the Company sold approximately 34 acres of land in Irvine, California, upon which it had previously planned to build a new corporate headquarters, for \$26 million (the approximate cost of the land).

The Company has extended the current lease of its worldwide headquarters in Irvine, California, through January 2001, and has an option to extend the lease for an additional five month period.

On September 27, 1999, the Company announced a recall of its 6.8GB per platter series of WD Caviar(R) desktop hard drives because of a reliability problem resulting from a faulty power driver chip manufactured by a third-party supplier. Approximately 1.2 million units were manufactured with the faulty chip. Replacement of the chips involved rework of the printed circuit board assembly. Revenues of approximately \$100 million related to the products which were recalled were reversed in the three months ended October 2, 1999. In addition, the Caviar product line was shut down for approximately two weeks, eliminating approximately \$70 million of forecasted revenue during the three months ended October 2, 1999. Cost of revenues for the three months ended October 2, 1999, included charges totaling \$37.7 million for estimated costs to recall and repair the affected drives, including \$23.1 million for repair and retrieval cost, \$4.5 million for freight and other, and \$10.1 million for write-downs of related inventory. By the end of the three months ended December 31, 1999, the Company had completed rework on approximately 78% of the 1.2 million units and had resolved its claims against third parties resulting from the recall.

In December 1999, the Company agreed to sell a manufacturing facility in Tuas, Singapore for cash proceeds of \$11.0 million. In January 2000, the Company also agreed to sell its Rochester, Minnesota facility for cash proceeds of approximately \$30.0 million. These transactions are expected to close, subject to customary closing conditions, in the quarter ending March 31, 2000, each with a minimal gain or loss.

On January 19, 2000, the Company announced that it will exit the enterprise hard drive business and shift its strategic focus and resources in the enterprise storage market to Internet-related data content management systems and management software. In connection with this decision, the Company closed its Rochester, Minnesota enterprise hard drive design center, and a majority of the 420 employees in the design center have been laid off and given legally required notification and outplacement services. The exit from the enterprise business will result in nonrecurring charges against operations in the quarter ended March 31, 2000. The Company currently estimates these charges to include \$25.0 million for property and equipment write-offs, and \$11.0 million for severance (\$8.0 million relating to domestic operations). The Company is currently analyzing the effect of this decision on inventory purchase commitments and the price levels that may be needed to sell the Company's remaining enterprise products. Accordingly, additional reserves and accruals may be needed for purchase order cancellations, purchase price protection, inventory write-downs and other costs flowing from the Company's decision to exit. The Company estimates that the restructuring effort will be substantially completed by June 30, 2000.

#### RESULTS OF OPERATIONS

Consolidated revenues were \$560.2 million for the three months ended December 31, 1999, a decrease of 24%, or \$178.4 million, from the three months ended December 26, 1998 and an increase of 38%, or \$153.2, from the immediately preceding quarter. The lower revenues during the three months ended December 31, 1999, as compared to the corresponding period of the prior year, resulted from a decline in unit shipments of approximately 2% combined with reductions in the average selling prices ("ASPs") of hard drive products due to an intensely competitive hard drive business environment. The increase in revenue for the three months ended December 31, 1999, from the immediately preceding quarter resulted primarily from higher volume (an increase in unit shipments of 56%) following the product recall in the immediately preceding quarter, as discussed above, offset by lower ASPs.

Consolidated revenues were \$967.1 million for the six months ended December 31, 1999, down 30% from the six months ended December 26, 1998. The lower revenues resulted from a decline in unit shipments of approximately 13%, which was largely due to the product recall in the three months ended October 2, 1999, combined with lower ASPs.

The gross profit for the three months ended December 31, 1999, totaled \$20.2 million, or 4% of revenue. This compares to a gross profit of \$19.2 million, or 3% of revenue, for the three months ended December 26, 1998 and a negative gross profit of \$65.3 million, or negative 16% of revenue, for the immediately preceding quarter. The negative gross profit in the immediately preceding quarter included a \$37.7 million special charge relating to the product recall. Excluding the special charge, the consolidated gross margin percentage in the immediately preceding quarter was negative 7%. The increase in gross profit over the three months ended

December 26, 1998 and the immediately preceding quarter (excluding special charges) was primarily the result of lower manufacturing costs, due to the restructuring and transfer of all desktop production to a single, highly utilized facility in Malaysia. The consolidated negative gross profit for the six months ended December 31, 1999, totaled \$7.4 million, or negative 1% of revenue (excluding the aforementioned special charges of \$37.7 million). This compares to a gross profit for the six months ended December 26, 1998 of \$13.4 million, or 1% of revenue (excluding special charges of \$77 million). The decline in the gross profit for the six-month period was the result of lower volumes due to the product recall and lower ASPs, offset by the Company's restructuring and cost-cutting efforts.

Research and development ("R&D") expense for the three months ended December 31, 1999 was \$44.1 million, a decrease of \$6.3 million from the three months ended December 26, 1998 and a decrease of \$6.1 million from the immediately preceding quarter. R&D expense for the six months ended December 31, 1999 was \$94.2 million, a decrease of \$8.1 million from the six months ended December 26, 1998. The decrease in R&D expenses was primarily due to the Company's cost-cutting efforts, particularly costs associated with HDD development, offset partially by increased spending at Connex, the Company's subsidiary, and other product line development efforts.

Selling, general and administrative ("SG&A") expense in the three months ended December 31, 1999 was \$39.1 million, a decrease of \$8.7 million from the three months ended December 26, 1998 and a decrease of \$4.8 million from the immediately preceding quarter. The decrease in SG&A expense for the three months ended December 31, 1999 compared to the three months ended December 26, 1998 and the immediately preceding quarter was primarily due to a lower revenue base and cost-cutting efforts, particularly costs associated with the Company's HDD business, offset partially by increased spending at Connex and other of the Company's developing ventures. SG&A expense was \$82.9 million for the six months ended December 31, 1999, a decrease of \$22.3 million from the six months ended December 26, 1998. The decrease was the result of cost-cutting efforts and the nonrecurrence of a \$7.5 million special charge on terminated hedging contracts recorded in SG&A expense during the six months ended December 26, 1998.

Net interest expense for the three months ended December 31, 1999 was \$3.0 million, compared to net interest expense of \$3.2 million for the three months ended December 26, 1998 and net interest expense of \$5.3 million in the immediately preceding quarter. The decrease in net interest expense for the three months ended December 31, 1999, was attributable to lower interest expense on the Company's Debentures (the average carrying value of the Company's Debentures was lower due to the Debenture redemptions which occurred during the current quarter). Net interest expense was \$8.4 million for the six months ended December 31, 1999 as compared to net interest expense of \$5.9 million for the six months ended December 26, 1998. The increase in net interest expense was the result of a decrease in interest expense on the Company's Debentures offset by a greater decrease in interest income earned on lower average cash and cash equivalents balances.

The Company initiated significant restructuring efforts during the six months ended December 31, 1999. The Company recorded restructuring charges of approximately \$32.3 million and \$25.5 million during the three months ended October 2, 1999 and the three months ended December 31, 1999, respectively. The charges related to severance and outplacement, the write-off of fixed assets, lease cancellation and other charges, as discussed above.

During the six months ended December 31, 1999, the Company issued common stock in exchange for Debentures which were retired in non-cash transactions. These redemptions were private, individually negotiated transactions with certain institutional investors. The redemptions resulted in an extraordinary gain of \$90.6 million during the three months ended October 2, 1999 and an extraordinary gain of \$76.3 million during the three months ended December 31, 1999.

The Company did not record an income tax benefit in any periods presented as no additional loss carrybacks were available and management deemed it "more likely than not" that the deferred tax benefits generated would not be realized.

## LIQUIDITY AND CAPITAL RESOURCES

At December 31, 1999, the Company had cash and cash equivalents of \$163.7 million as compared to \$226.1 million at July 3, 1999 and \$185.1 million at October 2, 1999. Net cash used in operations was \$10.2 million and \$101.2 million for the three and six months ended December 31, 1999, respectively, as compared to \$25.0 million and \$48.3 million for the comparable periods of the prior year. Net cash used in operations for the three months ended December 31, 1999 decreased by \$79.6 million as compared to the immediately preceding quarter as a result of significantly lower operating losses offset in part by lower depreciation and non-cash debenture interest and by a return to more normal inventory and accounts receivable positions following the Company's product recall.

Net cash used in operations for the six months ended December 31, 1999 increased by \$52.9 million as compared to the six months ended December 26, 1998 due to slightly higher operating losses offset by depreciation and non-cash debenture interest and by the utilization of warranty accruals established for thin-film products in the prior year.

Operating cash flows provided by changes in working capital amounted to \$39.1 million and \$101.6 million for the three and six months ended December 31, 1999 and reflect the Company's management of operating assets and liabilities during the period. For the three months ended December 31, 1999, the Company's days of sales outstanding ("DSO") was 32 days, inventory turned 21 times and days of payables outstanding was 48 days. Comparable measures for the three months ended October 2, 1999 are not meaningful due to the impact of the product recall on the Company's working capital balances at October 2, 1999. For the three months ended July 3, 1999, the Company's DSO was 38 days, inventory turned 19 times and days of payables outstanding was 48 days. The Company expects that the third quarter DSO will increase to a more normal level of between 36 and 40.

Other uses of cash during the six months ended December 31, 1999 included \$33.4 million to repay bank debt and net capital expenditures of \$13.8 million primarily to upgrade the Company's desktop production capabilities and for normal replacement of existing assets. Partially offsetting the use of cash during the period were proceeds of \$49.5 million received upon issuance of 11.2 million shares of the Company's stock under the Company's Equity Facility, and \$37 million received as proceeds and deposits relating to the sale of real property during the period.

The Company anticipates that capital expenditures for the remainder of 2000 will not be more than \$25 million and will relate to accommodating new technologies and new product lines, normal replacement of existing assets and expansion of production capabilities in Malaysia. The Company also anticipates cash expenditures of approximately \$24.2 million to be paid in the remaining six months of 2000 for severance and outplacement costs and lease cancellation and other costs of vacating leased properties related to the Company's restructuring programs. These amounts exclude any settlements with vendors on existing purchase orders related to the Company's exit of its enterprise business.

The Senior Bank Facility, as amended on January 15, 2000, provides the Company with up to a \$125.0 million revolving credit line (depending on the borrowing base calculation) and a \$50.0 million term loan (of which \$16.6 million was outstanding as of December 31, 1999). Borrowings under the Senior Bank Facility are secured by the Company's accounts receivable, inventory, 66% of its stock in its foreign subsidiaries and the other assets (excluding real property) of the Company and, at the option of the Company, bear interest at either LIBOR or a base rate plus a margin determined by the borrowing base, with option periods of one to three months. The Senior Bank Facility requires the Company to maintain certain amounts of net equity, prohibits the payment of cash dividends on common stock and contains a number of other covenants. This facility matures on March 31, 2000, and further borrowings through such date are not allowed. As of the date hereof, the remaining balance on the term loan has been repaid. The Company has received a proposal for a new credit facility, including a term loan. As of the date hereof, the terms and conditions of this proposal have not been finalized.

Under an existing equity facility, the Company may issue for cash shares of common stock to institutional investors in monthly increments of \$12.5 million. The facility provides for up to \$150.0 million in cash proceeds of which \$49.5 million had been utilized as of December 31, 1999. Shares paid under the facility are at the market price of the Company's common stock less a discount ranging from 2.75% to 4.25%. During the six months ended December 31, 1999, the Company issued 11.2 million shares of common stock under the Equity Facility for net proceeds of \$49.5 million.



During the six months ended December 31, 1999, the Company issued 26.7 million shares of common stock in exchange for Debentures with a carrying value of \$284.1 million, and an aggregate principal amount at maturity of \$735.6 million. These redemptions were private, individually negotiated transactions with certain institutional investors. The redemptions resulted in extraordinary gains of \$166.9 million during the six months ended December 31, 1999. As of December 31, 1999, the carrying value of the remaining outstanding Debentures was \$219.7 million and the aggregate principal amount at maturity was \$561.6 million.

The Company expects to continue to incur operating losses in 2000. The Company also had a working capital deficiency of \$15.5 million and a shareholders' deficiency of \$88.1 million as of December 31, 1999. However, the Company had cash balances of \$163.7 million as of December 31, 1999. In addition, the Company has restructured portions and continues to restructure other elements of its operations. In addition, the Company has other sources of liquidity available. In light of these conditions, the Company has the following plans and other options:

- The Company plans to reduce expenses and capital expenditures substantially as compared to historical levels due to:
  - Recent restructurings;
  - Reduced general and administrative spending; and
  - Reduced infrastructure resulting from the closure of its Santa Clara, California disk media operations, its disk drive manufacturing facilities in Tuas and Chai Chee, Singapore, and its enterprise hard drive design center in Rochester, Minnesota.
- The Company has the following additional sources of liquidity available to it:
  - \$150.0 million Equity Facility (\$49.5 million of which had been utilized as of December 31, 1999);
  - \$30.0 million resulting from the sale of the Rochester, Minnesota facility, subject to customary closing conditions; and
  - Other equity investments that may be disposed of during 2000, including 6.5 million shares of Komag common stock and 1.3 million shares of Vixel common stock with a combined market value of approximately \$44.4 million as of December 31, 1999.
  - The Company is also pursuing other possible external sources of equity financing in its developing subsidiaries.

Based on the above factors, the Company believes its current cash balances, its existing equity facility, and other liquidity vehicles currently available to it, will be sufficient to meet its working capital needs through the next twelve months. There can be no assurance that a new bank facility or the equity facility will continue to be available to the Company. Also, the Company's ability to sustain its working capital position is dependent upon a number of factors that are discussed below under the heading "Risk factors relating to Western Digital particularly."

#### NEW ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133 was effective for all fiscal quarters or fiscal years beginning after June 15, 1999. In August 1999, the FASB issued Statement of Financial Accounting Standards No. 137, "Accounting for Derivative Instruments and Hedging Activities -- Deferral of the Effective Date of FASB Statement No. 133, An Amendment of FASB Statement No. 133" ("SFAS 137"), which defers the effective date of SFAS 133 to all fiscal quarters for fiscal years beginning after June 15, 2000. SFAS 133 establishes accounting and reporting standards for derivative instruments embedded in other contracts and for hedging activities. Application of SFAS 133 is not expected to have a material impact on the Company's consolidated financial position, results of operations or liquidity.

YEAR 2000

On January 1, 2000, the Company incurred nominal impact on its products, equipment, computer systems and applications as a result of the Year 2000 issue. The Company attributes this to its Year 2000 readiness efforts. As of December 31, 1999, systems remediation and integration testing and development of the Company's contingency plans had been completed. Supplier management is an ongoing process, and no material impact was felt from lack of supplier readiness at January 1, 2000. Although the Company did not experience any material problems related to the Year 2000 issue, there can be no assurances that problems relating to the Year 2000 issue will not manifest themselves in the future. Expenditures related to the Year 2000 project, excluding normal replacement of existing capital assets, totaled approximately \$12.2 million .

#### RISK FACTORS RELATED TO THE HARD DRIVE INDUSTRY IN WHICH WE OPERATE

Our operating results depend on our being among the first-to-market and first-to-volume with our new products.

To achieve consistent success with computer manufacturer customers we must be an early provider of next generation hard drives featuring leading technology and high quality. If we fail to:

- consistently maintain and improve our time-to-market performance with our new products
- produce these products in sufficient volume within our rapid product cycle
- qualify these products with key customers on a timely basis by meeting our customer's performance and quality specifications, or
- achieve acceptable manufacturing yields and costs with these products

then our market share would be adversely affected, which would harm our operating results.

Short product life cycles make it difficult to recover the cost of development.

Over the past two years hard drive areal density (the gigabytes of storage per disk) has increased at a much more rapid pace than previously, and we expect this trend to continue. Higher areal densities mean that fewer heads and disks are required to achieve a given drive capacity. This has significantly shortened product life cycles, since each generation of drives is more cost effective than the previous one. Shorter product cycles make it more difficult to recover the cost of product development

Short product life cycles force us to continually qualify new products with our customers.

Due to short product life cycles, we must regularly engage in new product qualification with our customers. To be considered for qualification we must be among the leaders in time-to-market with our new products. Once a product is accepted for qualification testing, any failure or delay in the qualification process can result in our losing sales to that customer until the next generation of products is introduced. The effect of missing a product qualification opportunity is magnified by the limited number of high volume computer manufacturers most of which continue to consolidate their share of the PC market. These risks are magnified because we expect cost improvements and competitive pressures to result in declining sales and gross margins on our current generation products.

Our average selling prices and our revenue are declining.

We expect that our average selling prices for hard disk drives will continue to decline. Rapid increases in areal density mean that the average drive we sell has fewer heads and disks, and is therefore lower cost. Because of the competitiveness of the hard drive industry, lower costs generally mean lower prices. This is true even for those products that are competitive and introduced into the market in a timely manner. Our average selling prices decline even further when competitors lower prices to absorb excess capacity, liquidate excess inventories, restructure or attempt to gain market share.

Unexpected technology advances in the hard drive industry could harm our competitive position.

If one of our competitors were able to implement a significant advance in head or disk drive technology that enables a step-change increase in areal density allowing greater storage of data on a disk, it would harm our operating results.

Advances in magnetic, optical, semiconductor or other data storage technologies could result in competitive products that have better performance or lower cost per unit of capacity than our products. Some of our competitors are developing hybrid storage devices that combine magnetic and optical technologies, but we have decided not to pursue this technology at this time. If these products prove to be superior in performance or cost per unit of capacity, we could be at a competitive disadvantage to the companies offering those products.

The hard drive industry is highly competitive and characterized by rapid shifts in market share among the major competitors.

The price of hard drives has fallen over time due to increases in supply, cost reductions, technological advances and price reductions by competitors seeking to liquidate excess inventories or gain market share. In addition, rapid technological changes often reduce the volume and profitability of sales of existing products and increase the risk of inventory obsolescence. These factors, taken together, result in significant and rapid shifts in market share among the industry's major participants. For example, during 1997, we significantly increased our share of the desktop market, but these gains were lost during 1998 and 1999. If our market share erodes further, it would likely harm our operating results.

Our prices and margins are subject to declines due to unpredictable end-user demand and oversupply of hard disk drives.

Demand for our hard drives depends on the demand for computer systems manufactured by our customers and on storage upgrades to existing systems. The demand for computer systems has been volatile in the past and often has had an exaggerated effect on the demand for hard drives in any given period. As a result, the hard drive market tends to experience periods of excess capacity which typically lead to intense price competition. If intense price competition occurs, we may be forced to lower prices sooner and more than expected and transition to new products sooner than expected. For example, in the second half of 1998 and throughout 1999, as a result of excess inventory in the desktop hard drive market, aggressive pricing and corresponding margin reductions materially adversely affected our operating results. We experienced similar conditions in the high-end hard drive market during most of 1998 and 1999.

Changes in the markets for hard drives require us to develop new products.

Over the past few years the consumer market for desktop computers has shifted significantly towards lower priced systems, especially those systems priced below \$1,000. If we do not develop lower cost hard drives that can successfully compete in this market, our market share will likely fall, which could harm our operating results.

Furthermore, the PC market is fragmenting into a variety of computing devices and products. Some of these products, such as internet appliances, may not contain a hard drive. On the other hand, many industry analysts expect, as do we, that as broadcasting and communications are increasingly converted to digital technology from the older, analog technology, the technology of computers and consumer electronics and communication devices will converge, and hard drives will be found in many consumer products other than computers. While we are investing development resources in designing hard drive products for new audio-visual applications, it is too early to assess the impact of these new applications on future demand for hard drive products.

We depend on our key personnel.

Our success depends upon the continued contributions of our key employees, many of whom would be extremely difficult to replace. Worldwide competition for skilled employees in the hard drive industry is intense. We have lost a number of experienced hard drive engineers over the past year as a result of the loss of retention value of our employee stock options (because of the decrease in price of our common stock) and aggressive recruiting of our employees. If we are unable to retain our existing employees or to hire and integrate new employees, our operating results would likely be harmed.

#### RISK FACTORS RELATING TO WESTERN DIGITAL PARTICULARLY

Loss of market share with a key customer could harm our operating results.

A majority of our revenue comes from a few customers. For example, for the six month period ended December 31, 1999, sales to our top 10 customers accounted for approximately 62% of revenues. These customers have a wide variety of suppliers to choose from and therefore can make substantial demands on us. Even if we successfully qualify a product with a customer, the customer generally is not obligated to purchase any minimum volume of products from us and is able to terminate its relationship with us at any time. Our ability to maintain strong relationships with our principal customers is essential to our future performance. If we lose a key customer or if any of our key customers reduce their orders of our products or require us to reduce our prices before we are able to reduce costs, our operating results would likely be harmed. For example, this occurred early in the third quarter of 2000 in our enterprise hard drive business and is one of the factors which led to the Company's decision to exit the enterprise hard drive business and close its Rochester, Minnesota facility.

Dependence on a limited number of qualified suppliers of components could lead to delays or increased costs.

Because we do not manufacture any of the components in our hard drives, an extended shortage of required components or the failure of key suppliers to remain in business, adjust to market conditions, or to meet our quality, yield or production requirements could harm us more severely than our competitors, some of whom manufacture certain of the components for their hard drives. A number of the components used by us are available from only a single or limited number of qualified outside suppliers. If a component is in short supply, or a supplier fails to qualify or has a quality issue with a component, we may experience delays or increased costs in obtaining that component. This occurred in September 1999 when we had to shut down our Caviar product line production for approximately two weeks as a result of a faulty power driver chip which was sole-sourced from a third-party supplier.

To reduce the risk of component shortages, we attempt to provide significant lead times when buying these components. As a result, we may have to pay significant cancellation charges to suppliers if we cancel orders, as we did in 1998 when we accelerated our transition to magnetoresistive recording head technology, and as we are doing as a result of our decision to exit the enterprise hard drive business.

In April 1999, we entered into a three year volume purchase agreement with Komag under which we will buy a substantial portion of our media components from Komag. We intend that this strategic relationship will reduce our media component costs; however, it increases our dependence on Komag as a supplier. Our future operating results will depend substantially on Komag's ability to timely qualify its media components in our new development programs and to supply us with these components in sufficient volume to meet our production requirements. Any disruption in Komag's ability to manufacture and supply us with media would likely harm our operating results.

To develop new products we must maintain effective partner relationships with our strategic component suppliers.

Under our "virtual vertical integration" business model, we do not manufacture any of the parts used in our hard drives. As a result, the success of our products depends on our ability to gain access to and integrate parts that are "best in class" from reliable component suppliers. To do so we must effectively manage our relationships with our strategic component suppliers. We must also effectively integrate different products from a variety of suppliers and manage difficult scheduling and delivery problems.

We have only one manufacturing facility, which subjects us to the risk of damage or loss of the facility.

Our volume manufacturing operations currently are based in one facility. A fire, flood, earthquake or other disaster or condition affecting our facility would almost certainly result in a loss of substantial sales and revenue and harm our operating results.

Manufacturing our products abroad subjects us to numerous risks.

We are subject to risks associated with our foreign manufacturing operations, including:

- obtaining requisite United States and foreign governmental permits and approvals
- currency exchange rate fluctuations or restrictions
- political instability and civil unrest
- transportation delays or higher freight rates
- labor problems
- trade restrictions or higher tariffs
- exchange, currency and tax controls and reallocations
- loss or non-renewal of favorable tax treatment under agreements or treaties with foreign tax authorities.

We attempt to manage the impact of foreign currency exchange rate changes by, among other things, entering into short-term, forward exchange contracts. However, those contracts do not cover our full exposure and can be canceled by the issuer if currency controls are put in place, as occurred in Malaysia during the first quarter of 1999.

Our plan to broaden our business in data and content management, storage and communication takes us into new markets.

We have recently entered the storage subsystem market through our Connex subsidiary. In this market we will be facing the challenges of building volume and market share in a market which is new to us but which has several established and well-funded competitors. There is already significant competition for skilled engineers, both in the hardware and software areas, in this market. Our success will depend on Connex's ability to develop, introduce and achieve market acceptance of new products, applications and product enhancements, and to attract and retain skilled engineers. Additionally, our competitors in this market have established intellectual property portfolios. Our success will also depend on our ability to license existing intellectual property or create new innovations. Moreover, our competitors' established intellectual property portfolios increase our risk of intellectual property litigation.

We are also developing hard drives for the emerging audio-visual market. We will be facing the challenge of developing products for a market that is still evolving and subject to rapid changes and shifting consumer preferences. There are several competitors which have also entered this emerging market, and there is no assurance that the market for digital storage devices for audio-visual content will materialize or support all of these competitors.

We also expect to enter the data warehouse software and services market through our SageTree subsidiary and are considering other initiatives related to data and content management, storage and communication. In any of these initiatives we will be facing the challenge of developing products and services for markets that are still evolving and which have many current and potential competitors.

Our reliance on intellectual property and other proprietary information subjects us to the risk of significant litigation.

The hard drive industry has been characterized by significant litigation. This includes litigation relating to patent and other intellectual property rights, product liability claims and other types of litigation. We are currently evaluating several notices of alleged patent infringement or notices of patents from patent holders. We also are a party to several judicial and other proceedings relating to patent and other intellectual property rights. If we conclude that a claim of infringement is valid, we may be required to obtain a license or cross-license or modify our existing technology or design a new non-infringing technology. Such licenses or design modifications can be extremely costly. We may also be liable for any past infringement. If there is an adverse ruling against us in an infringement lawsuit, an injunction could be issued barring production or sale of any infringing product. It could also result in a damage award equal to a reasonable royalty or lost profits or, if there is a finding of willful infringement, treble damages. Any of these results would likely increase our costs and harm our operating results.

Our reliance on intellectual property and other proprietary information subjects us to the risk that these key ingredients of our business could be copied by competitors.

Our success depends, in significant part, on the proprietary nature of our technology, including our non-patentable intellectual property such as our process technology. Despite safeguards, to the extent that a competitor is able to reproduce or otherwise capitalize on our technology, it may be difficult, expensive or impossible for us to obtain necessary legal protection. Also, the laws of some foreign countries may not protect our intellectual property to the same extent as do the laws of the United States. In addition to patent protection of intellectual property rights, we consider elements of our product designs and processes to be proprietary and confidential. We rely upon employee, consultant and vendor non-disclosure agreements and a system of internal safeguards to protect our proprietary information. However, we cannot insure that our registered and unregistered intellectual property rights will not be challenged or exploited by others in the industry.

Inaccurate projections of demand for our product can cause large fluctuations in our quarterly results.

If we do not forecast total quarterly demand accurately, it can have a material adverse effect on our quarterly results. We typically book and ship a high percentage of our total quarterly sales in the third month of the quarter, which makes it difficult for us to match our production plans to customer demands. In addition, our quarterly projections and results may in the future be subject to significant fluctuations as a result of a number of other factors including:

- the timing of orders from and shipment of products to major customers
- our product mix
- changes in the prices of our products
- manufacturing delays or interruptions
- acceptance by customers of competing products in lieu of our products
- variations in the cost of components for our products
- limited access to components that we obtain from a single or a limited number of suppliers, such as Komag
- competition and consolidation in the data storage industry
- seasonal and other fluctuations in demand for computers often due to technological advances.

Rapidly changing market conditions in the hard drive industry make it difficult to estimate actual results.

We have made and continue to make a number of estimates and assumptions relating to our consolidated financial reporting. The rapidly changing market conditions with which we deal means that actual results may differ significantly from our estimates and assumptions. Key estimates and assumptions for us include:

- accruals for warranty against product defects
- price protection adjustments on products sold to resellers and distributors
- inventory adjustments for write-down of inventories to fair value
- reserves for doubtful accounts
- accruals for product returns.

The market price of our common stock is volatile.

The market price of our common stock has been, and may continue to be, extremely volatile. Factors such as the following may significantly affect the market price of our common stock:

- actual or anticipated fluctuations in our operating results
- announcements of technological innovations by us or our competitors which may decrease the volume and profitability of sales of our existing products and increase the risk of inventory obsolescence
- new products introduced by us or our competitors
- periods of severe pricing pressures due to oversupply or price erosion resulting from competitive pressures
- developments with respect to patents or proprietary rights
- conditions and trends in the hard drive industry
- changes in financial estimates by securities analysts relating specifically to us or the hard drive industry in general.

In addition, the stock market in recent months has experienced extreme price and volume fluctuations that have particularly affected the stock price of many high technology companies. These fluctuations are often unrelated to the operating performance of the companies.

Securities class action lawsuits are often brought against companies after periods of volatility in the market price of their securities. A number of such suits have been filed against us in the past, and any of these litigation matters could result in substantial costs and a diversion of resources and management's attention.

We may be unable to raise future capital through debt or equity financing.

Due to our recent financial performance and the risks described in this Report, in the future we may be unable to maintain adequate financial resources for capital expenditures, working capital and research and development. Our current borrowing agreement with our banks terminates no later than March 31, 2000, and we have agreed that we will not borrow under the agreement. If we decide to increase or accelerate our capital expenditures or research and development efforts, or if results of operations do not meet our expectations, we could require additional debt or equity financing. However, we cannot insure that additional financing will be available to us or available on favorable terms. An equity financing could also be dilutive to our existing stockholders.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

## DISCLOSURE ABOUT FOREIGN CURRENCY RISK

Although the majority of the Company's transactions are in U.S. Dollars, some transactions are based in various foreign currencies. From time to time, the Company purchases short-term, forward exchange contracts to hedge the impact of foreign currency fluctuations on certain underlying assets, liabilities and commitments for operating expenses denominated in foreign currencies. The purpose of entering into these hedge transactions is to minimize the impact of foreign currency fluctuations on the results of operations. A majority of the increases or decreases in the Company's local currency operating expenses are offset by gains and losses on the hedges. The contracts have maturity dates that do not exceed twelve months. The unrealized gains and losses on these contracts are deferred and recognized in the results of operations in the period in which the hedged transaction is consummated. The Company does not purchase short-term forward exchange contracts for trading purposes.

Historically, the Company has focused on hedging its foreign currency risk related to the Singapore Dollar, the British Pound and the Malaysian Ringgit. With the establishment of currency controls and the prohibition of purchases or sales of the Malaysian Ringgit by offshore companies, the Company has discontinued hedging its Malaysian Ringgit currency risk. Future hedging of this currency will depend on currency conditions in Malaysia. The imposition of exchange controls by the Malaysian government resulted in a \$7.5 million realized loss on terminated hedging contracts in the first quarter of 1999.

As of December 31, 1999, the Company had outstanding the following purchased foreign currency forward exchange contracts (in millions, except average contract rate):

|                                     | DECEMBER 31, 1999                    |                     |       |
|-------------------------------------|--------------------------------------|---------------------|-------|
| CONTRACT<br>AMOUNT                  | WEIGHTED<br>AVERAGE<br>CONTRACT RATE | UNREALIZED<br>GAIN* |       |
| (U.S. DOLLAR EQUIVALENT AMOUNTS)    |                                      |                     |       |
| Foreign currency forward contracts: |                                      |                     |       |
| Singapore Dollar .....              | \$ 9.0                               | 1.67                | \$ .2 |
| British Pound Sterling .....        | 3.2                                  | 1.63                | --    |
|                                     | -----                                |                     | ----- |
|                                     | \$ 12.2                              |                     | \$ .2 |
|                                     | =====                                |                     | ===== |

\* The unrealized gains on these contracts are deferred and will be recognized in the results of operations in the period in which the hedged transactions are consummated, at which time the gain is offset by the increased U.S. Dollar value of the local currency operating expense.

During the three and six months ended December 31, 1999 and 1998 total realized transaction and forward exchange contract currency gains and losses (excluding the \$7.5 million realized loss on the Malaysian Ringgit realized in the first quarter of 1999), were immaterial to the consolidated financial statements. Based on historical experience, the Company does not expect that a significant change in foreign exchange rates (up to approximately 25%) would materially affect the Company's consolidated financial statements.

## DISCLOSURE ABOUT OTHER MARKET RISKS

## Fixed Interest Rate Risk

At December 31, 1999, the market value of the Company's 5.25% zero coupon convertible subordinated debentures due in 2018 was approximately \$81.4 million, compared to the related carrying value of \$219.7 million. The convertible debentures will be repurchased by the Company, at the option of the holder, as of February 18, 2003, February 18, 2008, or February 18, 2013, or if there is a Fundamental Change (as defined in the Debenture documents), at the issue price plus accrued original issue discount to the date of redemption. The payment on those dates, with the exception of a Fundamental Change, can be in cash, stock or any combination, at the Company's option.



The Company has various note receivables from other companies. All of the notes carry a fixed rate of interest. Therefore a significant change in interest rates would not impact the Company's consolidated financial statements.

#### Variable Interest Rate Risk

The Company maintains a term loan bearing interest at LIBOR or a base rate plus margin determined by the borrowing base with an approximate current interest rate of 7.9%, as part of its Senior Bank Facility. This facility will terminate no later than March 31, 2000, and the balance has been repaid. As a result, the Company currently has no variable interest rate risk, and no further borrowings will be allowed during the remaining term of its Senior Bank Facility loan.

#### Fair Value Risk

The Company owns approximately 10.8 million shares of Komag, Inc. common stock. The stock is restricted as to the percentage of total shares which can be sold in a given time period. The unrestricted portion of the total Komag shares acquired represents the shares which can be sold within one year. The Company determines, on a quarterly basis, the fair market value of the unrestricted Komag shares and records an unrealized gain or loss resulting from the difference in the fair market value of the unrestricted shares as of the previous quarter end and the fair market value of the unrestricted shares on the measurement date. As of December 31, 1999, a \$0.7 million total accumulated unrealized loss has been recorded in accumulated other comprehensive income (loss). If the Company sells all or a portion of this stock, any unrealized gain or loss on the date of sale will be recorded as a realized gain or loss in the Company's results of operations. Due to market fluctuations, a significant decline in the stock's fair market value (of approximately 30% or more) could occur, and this decline could adversely impact the Company's consolidated financial statements. As of December 31, 1999, the quoted market value of the Company's Komag common stock holdings, without regard to discounts due to sales restrictions, was \$33.7 million.

The Company owns approximately 1.3 million shares of Vixel common stock. The shares are restricted as to sale until March 28, 2000 pursuant to an agreement with Vixel's underwriters. The Company determines, on a quarterly basis, the fair market value of the Vixel shares and records an unrealized gain or loss resulting from the difference in the fair market value of the shares as of the previous quarter end and the fair market value of the shares on the measurement date. As of December 31, 1999, a \$24.2 million total accumulated unrealized gain has been recorded in accumulated other comprehensive income (loss). If the Company sells all or a portion of this common stock, any unrealized gain or loss on the date of sale will be recorded as a realized gain or loss in the Company's results of operations. Due to market fluctuations, a significant decline in the stock's fair market value as of December 31, 1999 (of approximately 40% or more) could occur, and this decline could adversely impact the Company's consolidated financial statements.

## PART II. OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

The following discussion contains forward-looking statements within the meaning of the federal securities laws. These statements relate to the Company's legal proceedings described below. Litigation is inherently uncertain and may result in adverse rulings or decisions. Additionally, the Company may enter into settlements or be subject to judgments that may, individually or in the aggregate, have a material adverse effect on the Company's financial position, results of operations and/or liquidity. Accordingly, actual results could differ materially from those projected in the forward-looking statements.

The Company was sued by Amstrad PLC ("Amstrad") in December 1992 in Orange County Superior Court. The complaint alleged that hard drives supplied by the Company in calendar 1988 and 1989 were defective and caused damages to Amstrad of \$186.0 million in out-of-pocket expenses, lost profits, injury to Amstrad's reputation and loss of goodwill. The Company filed a counterclaim for \$3.0 million in actual damages in addition to exemplary damages in an unspecified amount. The first trial of this case ended in a mistrial, with the jury deadlocked on the issue of liability. The case was retried, and on June 9, 1999, the jury returned a verdict against Amstrad and in favor of Western Digital. Amstrad has filed a notice of appeal from the judgment, and the Company has filed motions seeking recovery of a portion of its legal and other costs of defense. The Company does not believe that the ultimate resolution of this matter will have a material adverse effect on the financial position, results of operations or liquidity of the Company. However, should the judgment be reversed on appeal, and if in a retrial of the case Amstrad were to prevail, the Company may be required to pay damages and other expenses, which may have a material adverse effect on the Company's financial position, results of operations and/or liquidity. In addition, the costs of defending a retrial of the case may be material, regardless of the outcome.

In 1994 Papst Licensing ("Papst") brought suit against the Company in the U.S. District Court for the Central District of California alleging infringement by the Company of five of its patents relating to disk drive motors that the Company purchases from motor vendors. Later that year Papst dismissed its case without prejudice, but it has notified the Company that it intends to reinstate the suit if the Company does not agree to enter into a license agreement with Papst. Papst has also put the Company on notice with respect to several additional patents. The Company does not believe that the ultimate resolution of this matter will have a material adverse effect on the financial position, results of operations or liquidity of the Company. However, because of the nature and inherent uncertainties of litigation, should the outcome of this action be unfavorable, the Company may be required to pay damages and other expenses, which may have a material adverse effect on the Company's financial position, results of operations and/or liquidity. In addition, the costs of defending such litigation may be material, regardless of the outcome.

The Company and Censtor Corporation ("Censtor") have had discussions concerning royalties, if any, that might be due Censtor under a licensing agreement. Censtor has initiated arbitration procedures under the agreement seeking payment of royalties. In response, the Company has filed a complaint in federal court seeking a determination that the patents at issue are invalid. The Federal Court action has been stayed pending completion of the arbitration procedures. The Company does not believe that the outcome of this dispute will have a material adverse effect on its financial position, results of operations and/or liquidity.

In the normal course of business, the Company receives and makes inquiry regarding possible intellectual property matters including alleged patent infringement. Where deemed advisable, the Company may seek or extend licenses or negotiate settlements. Although patent holders often offer such licenses, no assurance can be given that a license will be offered or that the terms of any license offered will be acceptable to the Company. Several such matters are currently pending. The Company does not believe that the ultimate resolution of these matters will have a material adverse effect on the consolidated financial position, results of operations and/or liquidity of the Company.

From time to time the Company receives claims and is a party to suits and other judicial and administrative proceedings incidental to its business. Although occasional adverse decisions (or settlements) may occur, the Company believes that the final disposition of such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations and/or liquidity.

## ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

During the three months ended December 31, 1999, the Company engaged in transactions pursuant to which it exchanged an aggregate principal amount at maturity of \$303.5 million of the Company's Zero Coupon Convertible Subordinated Debentures due 2018, for an aggregate of 11.7 million shares of the Company's common stock. These transactions were undertaken, in reliance upon the exemption from the registration requirements of the Securities Act afforded by Section 3(a)(9) thereof, as exchanges of securities by the Company with its existing security holders. No commission or other remuneration was paid or given directly or indirectly for such exchanges. These exchanges were consummated in private, individually negotiated transactions with institutional investors.

## ITEM 4. SUBMISSION OF MATTERS TO VOTE OF SECURITY HOLDERS

The annual meeting of shareholders was held on November 18, 1999. The shareholders elected the following seven directors to hold office until the next annual meeting and until their successors are elected and qualified:

|                     | Number of Votes |           |
|---------------------|-----------------|-----------|
|                     | For             | Withheld  |
| James A. Abrahamson | 96,975,134      | 3,115,298 |
| Peter D. Behrendt   | 96,981,406      | 3,103,412 |
| I. M. Booth         | 96,954,381      | 3,155,935 |
| Charles A. Haggerty | 96,910,097      | 3,239,812 |
| Andre R. Horn       | 96,972,074      | 3,120,075 |
| Anne O. Krueger     | 96,985,045      | 3,096,268 |
| Thomas E. Pardun    | 96,984,379      | 3,097,092 |

In addition, the shareholders approved the following proposals:

|  | Number of Votes |           |             |
|--|-----------------|-----------|-------------|
|  | For             | Against   | Abstentions |
| 1. To approve the amendment to the Company's Employee Stock Purchase Plan authorizing an additional 4,000,000 shares.      | 94,857,139      | 4,770,455 | 589,654     |
| 2. To ratify the selection of KPMG LLP as independent accountants for the Company for the fiscal year ended June 30, 2000. | 98,740,089      | 1,058,010 | 419,150     |

## ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

## (a) EXHIBITS:

- 10.3 Western Digital Corporation 1993 Employee Stock Purchase Plan, as amended on November 18, 1999. \*
- 10.22.1 Second Amendment to Lease, dated January 6, 1999, by and between The Irvine Company and Western Digital Corporation.
- 10.22.2 Letter Agreement dated December 21, 1999, by and between The Irvine Company and Western Digital Corporation.
- 10.35 Fiscal Year 2000 Western Digital Management Incentive Plan.
- 10.38.5 Fifth Amendment to Revolving Credit and Term Loan Agreement, dated as of January 14, 2000, among Western Digital Corporation, BankBoston N.A., and other lending institutions named therein.
- 10.44 Agreement dated October 7, 1999, by and between the Company and Russell R. Stern.
- 10.45 Western Digital Corporation 1999 Employee Severance Plan for U.S. Employees.
- 27 Financial Data Schedule

-----

\* Incorporated by reference to Exhibit 4.3 to the Company's Registration Statement on Form S-8 (No. 333-95499) as filed with the Securities and Exchange Commission on January 27, 2000.

## (b) REPORTS ON FORM 8-K:

On October 4, 1999, the Company filed a current report on Form 8-K to announce the close of a transaction to retire in the aggregate \$100 million principal amount of convertible debentures in exchange for shares of its common stock.

On October 7, 1999, the Company filed a current report on Form 8-K to announce the close of a transaction to retire in the aggregate \$125 million principal amount of convertible debentures in exchange for shares of its common stock.

On October 21, 1999, the Company filed a current report on Form 8-K to file its press release dated October 20, 1999, announcing its first quarter results.

On November 18, 1999, the Company filed a current report on Form 8-K to announce its retirement, in aggregate, of \$303.5 million principal amount of its convertible debentures in exchange for shares of its common stock.

SIGNATURES

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

WESTERN DIGITAL CORPORATION

-----

Registrant

/s/Teresa Hopp

-----

Teresa Hopp  
Senior Vice President  
and Chief Financial Officer

Date: February 14, 2000

## Exhibit Index

| Exhibit No.<br>----- | Description<br>-----   |
|----------------------|--|
| 10.3                 | Western Digital Corporation 1993 Employee Stock Purchase Plan, as amended on November 18, 1999. *  |
| 10.22.1              | Second Amendment to Lease, dated January 6, 1999, by and between The Irvine Company and Western Digital Corporation.   |
| 10.22.2              | Letter Agreement dated December 21, 1999, by and between The Irvine Company and Western Digital Corporation.   |
| 10.35                | Fiscal Year 2000 Western Digital Management Incentive Plan.  |
| 10.38.5              | Fifth Amendment to Revolving Credit and Term Loan Agreement, dated as of January 14, 2000, among Western Digital Corporation, BankBoston N.A., and other lending institutions named therein. |
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| 27                   | Financial Data Schedule  |

-----  
\* Incorporated by reference to Exhibit 4.3 to the Company's Registration Statement on Form S-8 (No. 333-95499) as filed with the Securities and Exchange Commission on January 27, 2000.

## SECOND AMENDMENT TO LEASE

## I. PARTIES AND DATE.

This Second Amendment to Lease dated January 6, 1999, is by and between THE IRVINE COMPANY ("Landlord"), and WESTERN DIGITAL CORPORATION, a Delaware corporation ("Tenant").

## II. RECITALS.

On January 13, 1988, Landlord and Tenant entered into an office space lease for the office building located at 8105 Irvine Center Drive, Irvine, California, and related parking and landscape areas more particularly described therein, which lease was subsequently amended by a First Amendment to Lease dated May 18, 1990 (as amended, the "Lease").

Landlord and Tenant each desire to modify the Lease to extend the Lease Term, adjust the Basic Rent, and make such other modifications as are set forth in "III. MODIFICATIONS" next below.

## III. MODIFICATIONS.

A. Lease Term. Notwithstanding any contrary provision in the Lease, unless sooner terminated for default or breach of the terms, covenants or conditions of the Lease, Landlord and Tenant hereby agree to extend the Term of the Lease to expire at midnight on December 31, 2000.

B. Basic Rent. Notwithstanding any contrary provision in the Lease, Landlord and Tenant hereby agree that the Basic Rent payable by Tenant during the six (6) month period commencing July 1, 2000 shall be Six Hundred Eighty-Seven Thousand Two Hundred Twelve Dollars (\$687,212.00) per month, based on \$1.92 per rentable square foot.

C. Right to Extend the Lease Term. Section 3.1 of the Lease is hereby amended by deleting Subparagraphs (b), (c), (d), (e), and (f) therefrom. In lieu thereof, Landlord hereby agrees that provided Tenant is not in default under any provision of the Lease at the time of exercise of the extension right granted herein, and provided further that Tenant has not assigned or sublet any of its interest in the Lease, Tenant may extend the Term of the Lease for one (1) additional period of six (6) months (the "Extension Period"). Tenant shall exercise its right to extend the Term by and only by (i) delivering to Landlord prior to December 31, 1999, Tenant's written notice of its commitment to extend (the "Commitment Notice"); and (ii) returning to Landlord, within fifteen (15) days after receipt, an executed amendment to this Lease (to be prepared by Landlord upon receipt of the Commitment Notice). The Basic Rent payable under the Lease during the Extension Period shall be at the same rate set forth in Paragraph III.B above. If Tenant fails to timely comply with any of the provisions of this paragraph, Tenant's right to extend the Term shall be extinguished and the Lease shall automatically terminate as of midnight on December 31, 2000, without any extension and without any liability to Landlord. Any attempt to assign or transfer any right or interest created by this paragraph shall be void from its inception. Tenant shall have no other right to extend the Term beyond the Extension Period described in this paragraph. Unless agreed to in a writing signed by Landlord and Tenant, any extension of the Term, whether created by an amendment to the Lease or by a holdover of the Premises by Tenant, or otherwise, shall be deemed a part of, and not in addition to, any duly exercised extension period permitted by this paragraph.

D. Parking. Landlord hereby agrees that Tenant's current parking privileges shall remain unchanged during the six (6) month period commencing July 1, 2000, and if applicable, during the Extension Period. Landlord further agrees that Tenant's allotted parking spaces shall



2  
be provided to Tenant free of charge during the aforementioned twelve (12) month period. Thereafter, the stall charge payable by Tenant shall be at Landlord's scheduled parking rates from time to time.

E. Parking Rights Agreement. Landlord and Tenant hereby agree that the separate "Parking Rights" agreement between the parties dated July 6, 1998 shall remain in full force and effect during the six (6) month period commencing July 1, 2000, and if applicable, during the Extension Period.

IV. GENERAL.

A. Effect of Amendments. The Lease shall remain in full force and effect except to the extent that it is modified by this Amendment.

B. Entire Agreement. This Amendment embodies the entire understanding between Landlord and Tenant with respect to the modifications set forth in "III. MODIFICATIONS" above and can be changed only by a writing signed by Landlord and Tenant.

C. Counterparts. If this Amendment is executed in counterparts, each is hereby declared to be an original; all, however, shall constitute but one and the same amendment. In any action or proceeding, any photographic, photostatic, or other copy of this Amendment may be introduced into evidence without foundation.

D. Defined Terms. All words commencing with initial capital letters in this Amendment and defined in the Lease shall have the same meaning in this Amendment as in the Lease, unless they are otherwise defined in this Amendment.

E. Corporate and Partnership Authority. If Tenant is a corporation or partnership, or is comprised of either or both of them, each individual executing this Amendment for the corporation or partnership represents that he or she is duly authorized to execute and deliver this Amendment on behalf of the corporation or partnership and that this Amendment is binding upon the corporation or partnership in accordance with its terms.

F. Attorneys' Fees. The provisions of the Lease respecting payment of attorneys' fees shall also apply to this Amendment.

V. EXECUTION.

Landlord and Tenant executed this Amendment on the date as set forth in "I. PARTIES AND DATE," above.

LANDLORD:

TENANT:

THE IRVINE COMPANY

WESTERN DIGITAL CORPORATION

By: /s/ WILLIAM R. HALFORD

By /s/ [SIGNATURE ILLEGIBLE] 1/4/00

-----  
William R. Halford, President  
Irvine Office Company  
a division of the Irvine Company

Title CFO  
-----

By /s/ RICHARD G. SIM

By /s/ [SIGNATURE ILLEGIBLE]

-----  
Richard G. Sim,  
Executive Vice President

Title V.P. Law & Secretary  
-----

[THE IRVINE COMPANY LOGO/LETTERHEAD]

December 21, 1999

Mr. Charles A. Haggerty  
Chairman of the Board  
President & Chief Executive Officer  
Western Digital Corporation  
8105 Irvine Center Drive  
Irvine, CA 92618

Dear Chuck:

I am in receipt of your letter dated December 20, 1999 wherein you ask that we defer the date by which Western Digital must notify The Irvine Company of your desire to extend the lease term. This letter shall serve to modify our existing agreement (Second Amendment to Lease) dated January 6, 1999 as follows: (i) in that the "Commitment Notice" must be received by Landlord no later than January 28, 2000 and (ii) the Term of the lease shall be extended to expire on midnight January 31, 2001.

Chuck, to the extent that your lease status can be resolved in January, we may well be able to backfill floors 8-15 given the current level of tenant demand for space and the lack of mid-rise office space in Irvine Spectrum. For example, the former AT&T building adjacent to your headquarters is now 98% leased with prospects to go to 100% in the next sixty days. It would be our desire to stage your downsizing to occur from the lowest floor (8) first, and move up in a contiguous fashion. We believe this would enable us to lease this space faster than if we have to lease from 15 down.

To be effective, we need to receive a signed copy of this letter agreement prior to December 31, 1999.

Mr. Charles A. Haggerty  
December 21, 1999  
Page Two

Best wishes for a Happy Holiday Season

Sincerely,

/s/ Richard G. Sim  
-----

RGS:cf

cc: William R. Halford  
James Stiepan

The above Terms are agreed to by:

Western Digital Corporation

By: /s/ Charles A. Haggerty 12-22-99  
-----

It's Authorized officer

FISCAL YEAR 2000  
WESTERN DIGITAL MANAGEMENT INCENTIVE PROGRAM (MIP)

PURPOSE  
-----

The purpose of this program is to focus participants on achieving key financial and strategic objectives at the corporate and business group levels that will lead to the creation of value for the Company's shareholders and provide participants the opportunity to earn significant awards, commensurate with performance.

ELIGIBILITY  
-----

Program eligibility is extended to all employees of Western Digital and selected employees of its domestic subsidiaries (Employees of Connex and Sagetree are not eligible for this plan) who are in, or who are hired into, salary grades 68 and above (or equivalent) on or before January 31, 2000.

Eligibility may also be granted to employees who have an authorized written agreement that grants them eligibility.

Employees of Western Digital and its domestic subsidiaries who are in salary grades 67 or below (or equivalent) are eligible for awards generated by a secondary bonus pool.

DESCRIPTION OF THE PROGRAM  
-----

The 2000 Management Incentive Program will pay as cash awards to participants for the achievement of predetermined performance goals. Each participant will be assigned a pool or target bonus percentage, which when multiplied by the participant's annual base salary as of June 30, 2000, will determine the pool or target bonus payout.

Predetermined performance goals will be established and approved by the Compensation Committee of the Board of Directors.

The actual performance achieved will determine the percentage used to calculate the award at the end of the program year. The size of the actual award can vary between 0% and 200% of the pool or target award.

In addition, individual and pool awards may be adjusted upward or downward by the Chief Executive Officer from the amount generated by the formula. The Chief Executive Officer's award may be adjusted upward or downward by the Compensation Committee.

## OPERATION OF THE PROGRAM

-----

Program Year: July 1, 1999 to June 30, 2000

Award Opportunities: The award for participants will be expressed as a percentage of salary, and determined according to salary grade.

Performance Measures: Performance will be measured at the corporate and business group levels. Performance measures that will be used in the 2000 Program are as follows:

- Cash Flow
- Time to Market
- Inventory Management

2000 Goals and Weighting: Every employee of Western Digital covered by this program will be measured on the same goals and objectives

The percentage of target bonus opportunity earned (before discretionary adjustments) will vary from the target bonus opportunity based on actual performance achieved..

## ADDITIONAL PROVISIONS

-----

Award Thresholds: Corporate operating profit/loss must be at a minimum level for incentives to be paid under any aspect of the Program.

Total Award Cap: Total awards paid under this Program may not exceed a preset amount as determined by the Compensation Committee. Any award reductions attributable to the preset cap will be made by the Chief Executive Officer.

Award Adjustment: Group award levels may be adjusted upward or downward by up to 25% by the Chief Executive Officer provided that total awards do not exceed the amounts generated by formula.

After application of the group performance, individual awards may be adjusted upward or downward based on the adjustment table below. Approval from the Chief Executive Officer is required for adjustments outside of these limits. The Chief Executive Officer's award may be adjusted upward or downward by the Compensation Committee. The adjustments by salary grade level (or equivalent) are as follows:

| Salary Grade<br>(or equivalent)<br>----- | Upward<br>Adjustment<br>----- | Downward<br>Adjustment<br>----- |
|--|-------------------------------|---------------------------------|
| All Participants                         | +100%                         | -100%                           |

All awards under this program are discretionary. The amount of the award including adjustments is determined by Western Digital in its sole discretion. No employee has any contractual right to receive an award pursuant to this program due to his/her employment at Western Digital.

|                             |   |
|-----------------------------|---|
| Extraordinary               | Events: The Compensation Committee, in its discretion, may adjust the basis upon which performance is measured to reflect the effect of significant changes that include, but are not limited to, unbudgeted acquisitions/divestitures, unusual or extraordinary accounting items, or significant, unplanned changes in the economic or regulatory environment. |
| Termination:                | Participants must be employed by the Company at the end of the program year to receive an award. If a participant terminates for reason of retirement, total and permanent disability, or death, the Compensation Committee has the discretion to pay prorated awards based upon the percentage of the year worked.   |
| Partial Year Participation: | The Compensation Committee, in its discretion, may pay prorated awards to people hired or promoted into eligible positions after July 1, 1999. In general, awards will be prorated for participants who begin before January 31, 2000 while those hired after January 31, 2000 will not be eligible to participate in the program.                              |
| Deferred                    | Payout: Before the end of the calendar year, the participant may elect to defer payout of all or part of the award in accordance with Western Digital's Deferred Compensation Plan. The deferred amount will be credited with a rate as specified in the Western Digital's Deferred Compensation Plan.  |
| Payout of Award:            | Awards will be paid in cash as soon as possible following the end of the program year or according to the participant's deferral election.  |
| Secondary Pool:             | The intent of this pool is to allow for the top 10% of the remaining population to receive 5% of their salary as a bonus at target levels of performance.   |

FIFTH AMENDMENT  
TO  
REVOLVING CREDIT AND TERM LOAN AGREEMENT

Fifth Amendment dated as of January 14, 2000 to Revolving Credit and Term Loan Agreement (the "Fifth Amendment"), by and among WESTERN DIGITAL CORPORATION, a Delaware corporation (the "Borrower") and BANKBOSTON, N.A. and the other lending institutions listed on Schedule 1 to the Credit Agreement (as hereinafter defined) (the "Banks"), amending certain provisions of the Revolving Credit and Term Loan Agreement dated as of November 4, 1998 (as amended and in effect from time to time, the "Credit Agreement") by and among the Borrower, the Banks, BankBoston, N.A. as agent for the Banks (in such capacity, the "Agent") and The CIT Group/Business Credit, Inc. as co-agent for the Banks. Terms not otherwise defined herein which are defined in the Credit Agreement shall have the same respective meanings herein as therein.

WHEREAS, the Borrower and the Banks have agreed to modify certain terms and conditions of the Credit Agreement as specifically set forth in this Fifth Amendment;

NOW, THEREFORE, in consideration of the premises and the mutual agreements contained herein and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:

SECTION 1. LIMITATION ON NEW REVOLVING CREDIT LOANS AND LETTERS OF CREDIT.

(a) Notwithstanding anything to the contrary contained in the Credit Agreement and the other Loan Documents, the Borrower hereby agrees that from the Effective Date (as defined in Section 8 hereof) through and including the Revolving Credit Loan Maturity Date (the "Limitation Period"), it will not request to borrow any Revolving Credit Loans, request any Letters of Credit be issued, extended or renewed or borrow any Revolving Credit Loans or request the issuance, renewal or extension of any Letters of Credit (with the parties hereto hereby agreeing that the only Letters of Credit to be outstanding during the Limitation Period shall be the Letters of Credit which have been issued prior to the date hereof). The parties hereto hereby acknowledge and agree that during the Limitation Period the Banks and the Agent shall have no obligation to make Revolving Credit Loans or issue, extend or renew Letters of Credit.

(b) The parties hereto hereby acknowledge and agree that after the termination of the Limitation Period, the Banks shall have no obligation to make Revolving Credit Loans and the Agent shall have no obligation to issue, extend or renew Letters of Credit.

SECTION 2. AMENDMENT TO SECTION 1 OF THE CREDIT AGREEMENT. Section 1.1 of the Credit Agreement is hereby amended as follows:

(a) the definition of "Revolving Credit Loan Maturity Date" is hereby amended by deleting the date "November 2, 2001" which appears in such definition and substituting in place thereof the date "March 31, 2000";

(b) the definition of "Term Loan Maturity Date" is hereby amended by deleting the date "November 2, 2001" which appears in such definition and substituting in place thereof the

words "The earlier to occur of (a) January 31, 2000 and (b) the date on which the Borrower incurs the Vendor Indebtedness";

(c) Section 1.1 of the Credit Agreement is further amended by inserting the following definitions in the appropriate alphabetical order:

Vendor. That certain vendor of the Borrower which has been previously identified as the "Vendor" to the Banks and the Agent by the Borrower.

Vendor Indebtedness. Indebtedness of the Borrower to the Vendor incurred pursuant to the Vendor Loan Agreement in the original principal amount of not less than \$16,625,000 in the aggregate.

Vendor Loan Agreement. That certain Loan Agreement dated or to be dated on or after January 13, 2000 between the Vendor and the Borrower and in form and substance satisfactory to the Agent.

Vixel. Vixel Corporation, a Delaware corporation.

SECTION 3. AMENDMENT TO SECTION 2.3 OF THE CREDIT AGREEMENT. Section 2.3 of the Credit Agreement is hereby amended by deleting Section 2.3 in its entirety and restating it as follows:

2.3. REDUCTION OF TOTAL COMMITMENT. The Borrower shall have the right at any time and from time to time upon five (5) Business Days prior written notice to the Agent to reduce by \$5,000,000 or a whole multiple of \$500,000 in excess thereof or terminate entirely the Total Commitment, whereupon the Commitments of the Banks shall be reduced pro rata in accordance with their respective Commitment Percentages of the amount specified in such notice or, as the case may be, terminated, provided, however, notwithstanding the foregoing, from January 1, 2000 through and including the Revolving Credit Loan Maturity Date, the Borrower shall only have the right to terminate the Total Commitment in its entirety and shall not have the right to reduce the Total Commitment by any smaller amount. Promptly after receiving any notice of the Borrower delivered pursuant to this Section 2.3, the Agent will notify the Banks of the substance thereof. Upon the effective date of any such reduction or termination, the Borrower shall pay to the Agent for the respective accounts of the Banks the full amount of any commitment fee then accrued on the amount of such reduction. No reduction or termination of the Commitments may be reinstated.

SECTION 4. AMENDMENT TO SECTION 4 OF THE CREDIT AGREEMENT. Section 4.4. of the Credit Agreement is hereby amended by deleting Section 4.4 in its entirety and restating it as follows:

4.4. OPTIONAL REPAYMENT OF TERM LOAN. The Borrower shall have the right at any time to prepay the Term Notes on or before the Term Loan Maturity Date, as a whole, or in part, upon not less than five (5) Business Days prior written notice to the Agent, without premium or penalty (but subject to Section 6.9 hereof), provided, that (a) each partial prepayment shall be in the principal amount of \$5,000,000 or an integral multiple of \$1,000,000 in excess thereof, and (b) each partial prepayment shall be allocated among the Banks, in proportion, as nearly as practicable, to the respective outstanding amount of each



Bank's Term Note, with adjustments to the extent practicable to equalize any prior prepayments not exactly in proportion. Any prepayment of principal on the Term Loan shall include all interest accrued to the date of prepayment and shall be applied against the scheduled installments of principal due on the Term Loan in the inverse order of maturity. No amount repaid with respect to the Term Loan may be reborrowed.

SECTION 5. AMENDMENT TO SECTION 10 OF THE CREDIT AGREEMENT. Section 10 of the Credit Agreement is hereby amended as follows:

(a) Section 10.1(i) of the Credit Agreement is hereby amended by deleting the text of Section 10.1(f) in its entirety and restating it as follows:

(i) the (i) Indebtedness evidenced by the Subordinated Debt Documents; and (ii) Vendor Indebtedness, provided, that as to the Vendor Indebtedness, (1) the net proceeds received by the Borrower from such Vendor Indebtedness is in the original principal amount of not less than the aggregate amount of the Term Loans outstanding on such date, together with any and all interest accrued thereon; and (2) the Borrower will use the proceeds received from the Vendor Indebtedness to prepay in full the outstanding amount of the Term Loans, together with any and all interest accrued thereon.

(b) Section 10.2(xii) of the Credit Agreement is hereby amended by deleting the text of Section 10.2(xii) in its entirety and restating it as follows:

(xii) the (i) liens in favor of the Indenture Trustee to the extent expressly provided in Section 7.07 of the Subordinated Indenture; and (ii) lien solely on the Vixel Stock in favor of the Vendor to secure the Vendor Indebtedness permitted by Section 10.1(i)(ii), provided, that as to lien on the Vixel Stock to secure the Vendor Indebtedness, (1) such lien shall only be permitted to be granted after the aggregate amount of the Term Loans of all the Banks have been repaid in full in cash; and (2) such security interest covers only the Vixel Stock and no other asset of the Borrower or any Subsidiary.

(c) Section 10.5.2(a)(i) of the Credit Agreement is hereby amended by deleting the words "enter into a sale and leaseback arrangement in respect of the real property located in Rochester, Minnesota in an arms-length transaction for fair and reasonable value" and substituting in place thereof the words "enter into a sale of the real property (together with the fixtures located thereon) located in Rochester, Minnesota in an arms-length transaction for fair and reasonable value so long as immediately prior to the consummation of such sale (1) the aggregate outstanding amount of the Term Loans, including all accrued interest thereon, has been repaid in full in cash and (2) the Borrower has provided to the Agent cash collateral in an amount sufficient to cash collateralize the Maximum Drawing Amount (together with any Reimbursement Obligations and any Unpaid Reimbursement Obligations) of all issued and outstanding Letters of Credit, and the Borrower has executed and delivered to the Agent a cash collateral agreement in respect of such cash collateral in form and substance satisfactory to the Agent with appropriate instructions prohibiting the Borrower's withdrawal of such funds so long as they remain cash collateral".

SECTION 6. AMENDMENT TO SECTION 11 OF THE CREDIT AGREEMENT. Section 11.1 of the Credit Agreement is hereby amended by deleting the table contained in Section 11.1 of the Credit Agreement in its entirety and restating it as follows:

| PERIOD   | AMOUNT                          |
|--|---------------------------------|
| Closing Date - last day of Second Fiscal Quarter, 1999                 | \$416,000,000                   |
| First Day of Third Fiscal Quarter, 1999 - Fiscal Quarter, 1999         | \$423,000,000 last day of Third |
| First Day of Fourth Fiscal Quarter, 1999 - Fourth Fiscal Quarter, 1999 | \$410,000,000 last day of       |
| First Day of First Fiscal Quarter, 2000 - Fiscal Quarter, 2000         | \$238,000,000 last day of First |
| First Day of Second Fiscal Quarter, 2000 - Second Fiscal Quarter, 2000 | \$176,000,000 last day of       |
| At any time thereafter   | \$155,000,000                   |

SECTION 7. LIMITED WAIVER. The Borrower has requested that the Banks waive compliance with Section 11.1 of the Credit Agreement for the fiscal quarter ended October 2, 1999. Subject always to compliance by the Borrower with the terms and provisions of the Credit Agreement and the other Loan Documents and the terms and conditions contained herein, from and after the effectiveness of this Fifth Amendment the Banks hereby waive the provisions of Section 11.1 of the Credit Agreement for the fiscal quarter ended October 2, 1999 and solely with respect to the determination of compliance for such fiscal quarter ended October 2, 1999.

SECTION 8. CONDITIONS TO EFFECTIVENESS. This Fifth Amendment shall not become effective until the date (the "Effective Date") on which Agent receives the following:

(a) a counterpart of this Fifth Amendment, executed by the Borrower, the Guarantors and the Banks; and

(c) payment by the Borrower to the Agent for the pro rata accounts of the Banks an amendment fee of \$200,000.

SECTION 9. REPRESENTATIONS AND WARRANTIES. The Borrower hereby repeats, on and as of the date hereof, each of the representations and warranties made by it in Section 8 of the Credit Agreement, and such representations and warranties remain true as of the date hereof (except to the extent of changes resulting from transactions contemplated or permitted by the Credit Agreement and the other Loan Documents and changes occurring in the ordinary course of business that singly or in the aggregate are not materially adverse, and to the extent that such representations and warranties relate expressly to an earlier date), provided, that all references therein to the Credit Agreement shall refer to such Credit Agreement as amended hereby. In addition, the Borrower hereby represents and warrants that the execution and delivery by the Borrower and its Subsidiaries of this Fifth Amendment and the performance by the Borrower and its Subsidiaries of all of its agreements and obligations under the Credit Agreement as amended hereby and the other Loan Documents are within the corporate authority of each the Borrower and its Subsidiaries and has been duly authorized by all necessary corporate action on the part of the Borrower and its Subsidiaries.

SECTION 10. RATIFICATION, ETC. Except as expressly amended hereby, the Credit Agreement, the Security Documents and all documents, instruments and agreements related thereto are hereby ratified and confirmed in all respects and shall continue in full force and effect. The Credit Agreement and this Fifth Amendment shall be read and construed as a single agreement. All references in the Credit Agreement or any related agreement or instrument to the Credit Agreement shall hereafter refer to the Credit Agreement as amended hereby.

SECTION 11. NO WAIVER. Except as expressly set forth in Section 7 hereof, nothing contained herein shall constitute a waiver of, impair or otherwise affect any Obligations, any other obligation of the Borrower or any rights of the Bank Agents or the Banks consequent thereon.

SECTION 12. COUNTERPARTS. This Fifth Amendment may be executed in one or more counterparts, each of which shall be deemed an original but which together shall constitute one and the same instrument.

SECTION 13. GOVERNING LAW. THIS FIFTH AMENDMENT SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE COMMONWEALTH OF MASSACHUSETTS (WITHOUT REFERENCE TO CONFLICT OF LAWS).

IN WITNESS WHEREOF, the parties hereto have executed this Fifth Amendment as a document under seal as of the date first above written.

WESTERN DIGITAL CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

BANKBOSTON, N.A.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

THE CIT GROUP/BUSINESS CREDIT, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

HELLER FINANCIAL, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FLEET CAPITAL CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FINOVA CAPITAL CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

LASALLE BUSINESS CREDIT, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FINOVA CAPITAL CORPORATION,  
SUCCESSOR BY MERGER TO:  
FREMONT FINANCIAL CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FLEET BUSINESS CREDIT CORPORATION  
(F/K/A SANWA BUSINESS CREDIT CORP.)

By: \_\_\_\_\_  
Title: \_\_\_\_\_

RATIFICATION OF GUARANTY

The undersigned guarantors hereby acknowledges and consents to the foregoing Fifth Amendment as of January 14, 2000, and agrees that the Guarantee dated as of November 4, 1998 from WD UK, the Guaranty dated as of February 12, 1999 from Connex, Inc. and the Guaranty dated as of September 22, 1999 from SageTree, Inc. in favor of the Agent and each of the Banks remains in full force and effect, and each Guarantor confirms and ratifies all of its obligations thereunder.

CONNEX, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

WESTERN DIGITAL (U.K.) LIMITED

By: \_\_\_\_\_  
Title: \_\_\_\_\_

SAGETREE, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

October 7, 1999

Mr. Russell R. Stern  
25502 Nellie Gail Road  
Laguna Hills, CA 92653

Dear Russell,

This letter, when signed by you, constitutes the agreement (the "Agreement") relative to your resignation from Western Digital Corporation (the "Company"). The terms of this Agreement are as follows:

1. RESIGNATION DATE. You will resign your position as Co-Chief Operating Officer effective Friday, October 8, 1999.
2. EMPLOYMENT PERIOD. You will continue to be treated as an employee, including stock option vesting, until the earlier of September 29, 2000 or your death (the "Employment Period"). Stock options previously granted to you under the Employee Stock Option Plan will continue to vest in accordance with their terms, which during the period from October 7, 1999 through September 29, 2000 would result in the vesting of 89,000 to 96,066 additional exercisable shares. A schedule setting forth these options, their grant dates, exercise prices, and vesting schedules is attached as Attachment "A" and incorporated herein by reference.
3. PAYMENT OF COMPENSATION. You will be paid \$400,000.00 in wage continuation based on your current base salary and not including any executive retention program amounts. Vesting on your awards under the Company's executive retention programs will cease as of October 7, 1999, and no further amounts will be credited or paid thereunder. Twenty-six (26) bi-weekly payments of \$15,384.62 will begin on October 15, 1999, and conclude with a final payment on September 29, 2000. This total exceeds the standard formula of 6 months pay (130 days - \$200,000.00), which is normally available to executives at your level and length of service.
4. STOCK OPTIONS. Any exercise of stock options by you must be in accord with the provisions of your stock option agreements and with the procedures relating to exercise as may be established by the Compensation Committee of the Board of

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October 7, 1999  
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Directors from time to time. All such procedures, unless they are to your benefit, shall be of general application and will not apply specifically to you. The Company will act expeditiously and in a supportive manner in assisting you to exercise your options. You will have up to 3 months following September 29, 2000 to exercise your vested options; provided, however, that the Company may cancel any unexpired option at any time if you are in violation of any of your covenants under Paragraph 11 hereof, without regard to the time limitation provided for therein. To the extent the options are non-qualified options under the federal income tax laws, you shall recognize compensation income in connection with your exercise of those options, and you agree to satisfy all applicable withholding taxes associated with each such exercise..

5. BENEFITS. The status of your current benefits is set forth on Attachment "B" hereto and hereby made a part hereof. During the Employment Period you will continue to receive benefits accorded to employees generally, other than vacation accruals, and benefits accorded to you and other executives in comparable pay grades ("special benefits"), provided that such special benefits continue to be furnished to executives generally in comparable pay grades. These include:
- a) your flex benefit allowance of \$306.50 per pay period.
  - b) Employee Stock Purchase Plan (ESPP) will continue and deductions will be made from your wage continuation checks through the next two purchase dates.
  - c) 401(k) participation and Western Digital employer match will continue with deductions coming from your wage continuation checks.
  - d) Tax preparation assistance of up to \$5,000 per fiscal year.
  - e) Supplemental executive medical coverage of up to \$5,000 per fiscal year.
  - f) Auto allowance of \$323.08 per pay period.

If any benefits (including special benefits) are discontinued and adjustments are made to compensation or benefits of employees generally, or of executives in comparable pay grades, in lieu of the discontinued benefits, and if such discontinuances apply to you under this Agreement, then in such instances like adjustments will be made to payments or benefits accorded to you with respect to the Employment Period. No actions will be taken with respect to the moneys payable or the benefits accorded to you that are intended to affect adversely only



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you or other terminating employees, unless such actions are taken as a result of a material breach by you of any of your obligations under this Agreement. Should you take another position prior to the expiration of wage continuation as an employee of a company with health insurance coverages, Western Digital's health coverages stop at the end of the month in which you start to work for the other company. Your Western Digital benefits will cease sixty days after the September 29, 2000 month-end. See the attachment for details. You may be entitled to continued basic health insurance coverage under the Company's COBRA plan. If you so elect, this continuation will be on terms consistent with applicable federal laws and regulations. If you elect and are eligible to continue this coverage, you will be charged a monthly premium to cover the cost of providing this insurance including a small administrative fee. Our benefits administration staff will give you complete details in this regard.

6. CONFIDENTIALITY. You and the Company agree that the terms of this arrangement will be held in confidence except to the extent that disclosures may be required by government regulations or judicial process or to receive tax, legal or financial advice. References which may request information about your employment will be referred to the Vice President of Human Resources.
7. VACATION. By October 15, 1999 you will be paid all accrued, unused vacation. Although you will continue on the Company payroll through September 29, 2000, you will accrue no more vacation subsequent to October 8, 1999.
8. SAVINGS AND PROFIT SHARING PLAN. Any distributions to which you are entitled from the Savings and Profit Sharing Plan will be made to you in accordance with the terms of that plan after your termination date of September 29, 2000.
9. OUTPLACEMENT SERVICES. The Company will provide executive outplacement assistance through Lee Hecht Harrison; Challenger, Gray and Christmas; or another firm of your choosing to assist you in finding another position. These services may begin anytime prior to September 29, 2000. Contact the Vice President of Human Resources or Pam Burdi, Director Employee Relations (949) 932-5516 for assistance with these arrangements.
10. INDEMNIFICATION AND ASSISTANCE.

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October 7, 1999  
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- (a) If you are subjected to any claim or demand involving any action or inaction allegedly taken by you during the course of your employment or directorship with the Company, you will be entitled to all rights of indemnification which may then be available to other executive officers or directors of the Company, including, without limitation, insurance protection under any director and/or officer liability insurance coverage maintained by the Company or any subsidiary and any rights to indemnification provided by applicable law or the By-laws of the Company or any subsidiary, and the Company will, and shall cause any subsidiary to, cooperate fully with you in responding to or defending against any such claim or demand.
- (b) You agree to make yourself available to respond to inquiries by the Company regarding management, regulatory, and legal activities of which you acquired knowledge while employed by the Company. You agree to make yourself available, without the requirement of being subpoenaed, to confer with counsel at reasonable times and locations and upon reasonable notice concerning any knowledge you have or may have with respect to actual and/or potential disputes arising out of the activities of the Company during your period of employment. You further agree to submit to deposition and/or testimony in accordance with the laws of the forum involved concerning any knowledge you have or may have with respect to actual and/or potential disputes arising out of the activities of the Company during your period of employment.

11. YOUR COVENANTS. As a condition to, and as consideration for, the severance and other benefits you are to receive herein, you agree that you will not, at any time during the Employment Period:

- (a) directly or indirectly, whether for your own account or as an employee, director, consultant or advisor, provide services to any business or engage in any business which at the time of commencement of such services is competitive with the Company's or any of its subsidiaries' product lines or business activities, unless you obtain the prior written consent of the Company's Chief Executive Officer;
- (b) directly or indirectly solicit any individuals to leave the Company's (or any of its subsidiaries') employ for any reason or interfere in any other manner

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with the employment relationships at the time existing between the Company (or any of its subsidiaries) and its current or prospective employees;

- (c) induce or attempt to induce any customer, supplier, distributor, licensor, licensee or other business relation of the Company (or any of its subsidiaries) to cease doing business with the Company (or any of its subsidiaries) or in any way interfere with the existing business relationship between any such customer, supplier, distributor, licensor, licensee or other business relation and the Company (or any of its subsidiaries); or
- (d) disparage, defame or slander the Company (or any of its subsidiaries) or any of their officers or directors or any of its products or services, to any one, including but not limited to any past, present or prospective customers. The foregoing sentence is not applicable to comments you may make to your immediate family. During the Employment Period the Company's Board of Directors and its officers shall refrain from any disparagement, defamation or slander of you.

12. CONFIDENTIAL INFORMATION. When you joined the Company you signed an agreement setting forth your obligations to the Company during and after your employment. A copy of your agreement is attached hereto as Attachment "C" and incorporated herein by reference. You understand and agree that in the course of your employment with the Company, you have acquired confidential information and trade secrets concerning the Company's operations, its future plans and its methods of doing business. You understand and agree it would be extremely damaging to the Company if you disclosed such information to a competitor or made it available to any other person or company. You understand and agree that such information has been divulged to you in confidence, and you understand and agree that you will keep such information secret and confidential unless disclosure is required by court order or otherwise by compulsion of law. In view of the nature of your employment and the information and trade secrets which you have received during the course of your employment, you also agree that the Company would be irreparably harmed by any violation, or threatened violation of the agreements in this Paragraph and that, therefore, the Company shall be entitled to an injunction prohibiting you from any violation or threatened violation of such agreements.

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13. RELEASE OF CLAIMS. You agree that the consideration provided for in this Agreement represents payment in full of all outstanding obligations owed to you by the Company or any subsidiary of the Company. You, on behalf of yourself and your heirs, agents, representatives, immediate family members, executors, successors, and assigns, hereby fully and forever release the Company and its agents, directors, employees, attorneys, investors, shareholders, administrators, affiliates, divisions, subsidiaries, parents, predecessor and successor corporations, and assigns from, and agree not to sue or otherwise institute or cause to be instituted any legal or administrative proceedings concerning, any claim, duty, obligation or cause of action relating to any matters of any kind, whether presently known or unknown, suspected or unsuspected, that you may possess against the Company arising from any omissions, acts or facts that have occurred up until and including the Effective Date including, without limitation,
- (a) any and all claims relating to or arising from your relationship with the Company or any subsidiary of the Company and the termination of that relationship;
  - (b) any and all claims relating to, or arising from, your right to purchase, or actual purchase of shares of stock of the Company or any subsidiary of the Company, including, without limitation, any claims for fraud, misrepresentation, breach of fiduciary duty, breach of duty under applicable state corporate law, and securities fraud under any state or federal law;
  - (c) any and all claims for wrongful discharge of employment; termination in violation of public policy; discrimination; breach of contract, both express and implied; breach of a covenant of good faith and fair dealing, both express and implied; promissory estoppel; negligent or intentional infliction of emotional distress; negligent or intentional misrepresentation; negligent or intentional interference with contract or prospective economic advantage; unfair business practices; defamation; libel; slander; negligence; personal injury; invasion of privacy; false imprisonment; and conversion;
  - (d) any and all claims for violation of any federal, state or municipal statute, including, but not limited to, Title VII of the Civil Rights Act of 1964, the Civil Rights Act of 1991, the Age Discrimination in Employment Act of

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1967, the Americans with Disabilities Act of 1990, the Fair Labor Standards Act, the Employee Retirement Income Security Act of 1974, The Worker Adjustment and Retraining Notification Act, the Older Workers Benefit Protection Act; the California Fair Employment and Housing Act, and the California Labor Code;

- (e) any and all claims for violation of the federal or any state constitution;
- (f) any and all claims arising out of any other laws and regulations relating to employment or employment discrimination; and
- (g) any and all claims for attorneys' fees and costs.

You and the Company agree that the release set forth in this Paragraph shall be and remain in effect in all respects as a complete general release as to the matters released. This release does not extend to any obligations incurred under this Agreement.

14. ACKNOWLEDGMENT OF WAIVER OF CLAIMS UNDER ADEA. You acknowledge that you are waiving and releasing any rights you may have under the Age Discrimination in Employment Act of 1967 ("ADEA") and that this waiver and release is knowing and voluntary. You and the Company agree that this waiver and release does not apply to any rights or claims that may arise under the ADEA after the Effective Date of this Agreement. You acknowledge that the consideration given for this waiver and release Agreement is in addition to anything of value to which you were already entitled. You further acknowledge that you have been advised by this writing that (a) you should consult with an attorney prior to executing this Agreement; (b) you have at least twenty-one (21) days within which to consider this Agreement; (c) you have seven (7) days following the execution of this Agreement by you to revoke the Agreement; and (d) this Agreement shall not be effective until the revocation period has expired. Any revocation should be in writing and delivered in accordance with the notice provisions of Paragraph 21 hereof by close of business on the seventh day from the date that you sign this Agreement.
15. CIVIL CODE SECTION 1542. You represent that you are not aware of any claim other than the claims that are released by this Agreement. You acknowledge that

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you have been advised by legal counsel and are familiar with the provisions of California Civil Code Section 1542, which provides as follows:

A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF KNOWN BY HIM MUST HAVE MATERIALLY AFFECTED HIS SETTLEMENT WITH THE DEBTOR.

You, being aware of said code section, agree to expressly waive any rights you may have thereunder, as well as under any other federal or state statute or common law principles of similar effect.

16. REMEDIES IN EVENT OF FUTURE DISPUTE.

(a) Except as provided in subparagraph (b) below, in the event of any future dispute, controversy or claim between you and the Company arising from or relating to this Agreement, its breach, any matter addressed by this Agreement, and/or your employment with the Company through the Termination Date, you and the Company will first attempt to resolve the dispute through confidential non-binding mediation to be conducted in Orange County, California by JAMS-Endispute or such other mediator as you and the Company shall mutually agree upon. If the dispute is not resolved through mediation, you and the Company will submit it to final and binding confidential arbitration to be conducted in Orange County, California by JAMS/Endispute in accordance with the then existing JAMS/Endispute Arbitration Rules and Procedures for Employment Disputes. In the event of such an arbitration proceeding, you and the Company shall select a mutually acceptable neutral arbitrator from among the JAMS/Endispute panel of arbitrators. If you and the Company cannot agree on an arbitrator, the Administrator of JAMS/Endispute shall appoint an arbitrator. None of you, the Company or the arbitrator shall disclose the existence, content, or results of any arbitration hereunder without the prior written consent of both of you and the Company, except as may be compelled by court order. Except as provided herein, the Federal Arbitration Act shall govern the interpretation and enforcement of such arbitration and all proceedings. The arbitrator shall apply the substantive law (and the law of remedies, if applicable) of the State of California, or

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Federal law, or both, as applicable and the arbitrator is without jurisdiction to apply any different substantive law. The arbitrator shall have the authority to entertain a motion to dismiss and/or a motion for summary judgment by either you or the Company and shall apply the standards governing such motions under the Federal Rules of Civil Procedure. The arbitrator shall render an award and a written, reasoned opinion in support thereof. Judgment upon the award may be entered in any court having jurisdiction thereof. You and the Company intend this arbitration provision to be valid, enforceable, irrevocable and construed as broadly as possible. Pending the resolution of any dispute between you and the Company, the Company may make any remaining unpaid payments due to you pursuant to paragraphs 3 and 5 hereof into a third party escrow account pending further agreement of the parties or the award of an arbitrator pursuant to the arbitration provisions of this Paragraph. The arbitrator shall be authorized to determine whether the remaining payment obligations under paragraphs 3 and 5 of this Agreement shall continue notwithstanding any alleged breach of this Agreement or are terminated as a result of the alleged breach. In the event an arbitrator determines that you have violated the terms of this Agreement, then the arbitrator shall be authorized to direct payment of the money (including any accrued interest) from the escrow account to the Company, order that the Company is not required to make any further payments to you under paragraphs 3 and 5, and award the Company any other appropriate remedies, including but not limited to reimbursement by you to the Company of the amounts paid to you pursuant to Paragraphs 3 and 5 of this Agreement.

- (b) In the event that a dispute arises concerning compliance with this Agreement, either you or the Company will be entitled to obtain from a court with jurisdiction over you and the Company preliminary and permanent injunctive relief to enjoin or restrict the other party from such breach or to enjoin or restrict a third party from inducing any such breach, and other appropriate relief, including money damages. In seeking any such relief, however, the moving party will retain the right to have any remaining portion of the controversy resolved by binding confidential arbitration in accordance with subparagraph (a) above.





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October 7, 1999  
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Irvine, CA 92618  
Attention: Vice President, Human Resources

Mr. Russell R. Stern  
October 7, 1999  
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To Mr. Stern:           25502 Nellie Gail Road  
                                  Laguna Hills, CA 92653

or in each case to such other address as you or the Company shall notify the other. Notice given by mail shall be deemed given five (5) days following the date of mailing.

22.     ENTIRE AGREEMENT. This Agreement, including its Attachments, represents the entire agreement and understanding between you and the Company concerning the subject matter herein, and supersedes and replaces any and all prior agreements and understandings.
23.     NO ORAL MODIFICATION. This Agreement may only be amended by a writing signed by you and the Chief Executive Officer of the Company or the Chief Legal Officer of the Company.
24.     GOVERNING LAW. This Agreement shall be governed by the internal substantive laws, but not the choice of law rules, of the State of California.
25.     EFFECTIVE DATE. This Agreement is effective eight days after it has been signed by both you and the Company (the "Effective Date").
26.     COUNTERPARTS. This Agreement may be executed in counterparts, and each counterpart shall have the same force and effect as an original and shall constitute an effective, binding agreement on the part of you and the Company.
27.     VOLUNTARY EXECUTION OF AGREEMENT. This Agreement is executed by you voluntarily and without any duress or undue influence on the part or behalf of the Company, with the full intent of releasing all claims. You acknowledge that:
  - (a)     you have read this Agreement;
  - (b)     you have been represented in the preparation, negotiation, and execution of this Agreement by legal counsel of your own choice or that you have voluntarily declined to seek such counsel;
  - (c)     you understand the terms and consequences of this Agreement and of the releases it contains; and



## ATTACHMENT "B"

SEPTEMBER 2000 - STATUS OF BENEFITS UPON  
TERMINATION OF EMPLOYMENT - RUSSELL R. STERN

The following information is to help you understand the status of your benefits if you are affected by a reduction in work force.

## MEDICAL INSURANCE

Medical coverage continues until November 30, 2000

## DENTAL INSURANCE

Dental coverage continues until November 30, 2000

## VISION INSURANCE

Vision coverage continues until November 30, 2000

## COBRA CONTINUATION COVERAGE

Continuation privileges may be available through COBRA for the medical, dental, vision, and health care reimbursement plans you are enrolled in at the time of termination. COBRA information and election forms will be mailed to you by the COBRA administrator for Western Digital (COBRAPRO) within two weeks from your last date of coverage.

## LIFE INSURANCE

Life insurance coverage continues until November 30, 2000. Conversion privileges to an individual policy are available after your coverage terminates. You must apply with the insurance carrier within 31 days. Conversion forms are available at the Benefits Department.

## ACCIDENTAL DEATH AND DISMEMBERMENT INSURANCE (AD&amp;D)

Accidental death and dismemberment insurance coverage continues until November 30, 2000. Conversion privileges to an individual policy are available after your coverage terminates. You must apply with the insurance carrier within 31 days. Conversion forms are available at the Benefits Department.

## DEPENDENT LIFE INSURANCE

Dependent life insurance coverage continues until November 30, 2000. Conversion privileges to an individual policy are available after your coverage terminates. You must apply with the insurance carrier within 31 days. Conversion forms are available at the Benefits Department.

**BUSINESS TRAVEL ACCIDENT COVERAGE**

Business travel accident coverage will end on your last day actively at work for Western Digital. Under the terms of the contract, no conversion privileges are available.

**LONG-TERM DISABILITY**

Long-term disability coverage will end on your last day actively at work for Western Digital. Conversion privileges to an individual policy are available by completing an application and submitting the first quarterly premium within 31 days of our termination of group coverage. To qualify for conversion, you must have been covered under the current group plan for 12 consecutive months. Conversion forms are available at the Benefits Department.

**SHORT-TERM DISABILITY**

Short-term disability coverage will end on your last day actively at work for Western Digital. Under the terms of the contract, no conversion privileges are available.

**REIMBURSEMENT ACCOUNTS**

If contributions continue to be deducted from scheduled payments, Health Care and Dependent Care Account claims may be reimbursed for ELIGIBLE EXPENSES INCURRED UP TO THE LAST DAY OF YOUR BENEFITS COVERAGE. Money left over in the account(s) at the end of the plan year (June 30) is forfeited. You will have a 90 day grace period (through January, 2001) to file a claim for reimbursement. Send the claims to FlexPro, P. O. Box 5545, Orange, CA 92613. Telephone (949) 835-6752, Fax (949) 953-9404.

**MANAGED HEALTH NETWORK (MHN)**

The MHN program will continue for you and your dependents until November 30, 2000. The toll free number is 800-327-8399. However, if you elect COBRA continuation, you may still be eligible to continue MHN benefits.

**RETIREMENT SAVINGS (401(k) & PROFIT SHARING PLAN**

As a participant in this plan, you will continue to participate in the plan until September 29, 2000. The company match is effective until September 29, 2000. After that date, you will receive 100% of your employee account, plus 100% of the profit sharing account, and the vested portion of the employer match account.

For information regarding rollover or distribution of your account, call T. Rowe Price at 800-922-9945. If you wish to withdraw your account from the plan, simply return the termination package that will be sent to you from T. Rowe Price. You may defer the withdrawal of your account until a future point in time.

**CONTRIBUTIONS CONTINUE:** Contributions will continue to be deducted from wage continuation payments unless you call T. Rowe Price at 800-922-9945 to suspend your contributions.

SAVINGS 401(k) PLAN LOANS: Bi-weekly loan payments will continue to be deducted from wage continuation payments. You will choose one of the following options to be effective after your last wage continuation payment: 1) continue making loan payments, 2) repay the entire outstanding loan balance, or 3) elect final distribution upon which any outstanding loan balance will be treated as a taxable distribution. You must complete a Loan Repayment form indicating your selection that will be provided in the T. Rowe Price termination package.

#### EMPLOYEE STOCK PURCHASE PLAN

You will continue to participate in ESPP through the next purchase dates in January and August, 2000. Deductions for ESPP will be made from your wage continuation checks. If you have previously purchased shares, then you can keep or sell them as you wish.

#### STOCK OPTIONS

If you have received stock options, they will vest through your date of termination from Western Digital in accordance with the plan provisions. Contact Stasia Shirley at 949-932-5645 for more information.

#### VACATION

All earned but unused vacation will be paid by the first wage continuation payment following your last day of active employment with Western Digital.

Vacation Buy: The cost of the extra hours you have taken but not paid for will be subtracted from your final paycheck.

Vacation Sell: The remaining amount and any accrued vacation that you haven't taken is paid to you. Exception: If you term with a negative vacation balance, the value of those hours will be subtracted from your final paycheck.

#### SICK LEAVE

All unused sick leave will be forfeited in accordance with the policy of Western Digital.

#### EDUCATIONAL REIMBURSEMENT

If you have received prior educational approval for classes that have started, but which you will not complete before your termination date, you are eligible for reimbursement for the classes you are currently attending. Reimbursement will be made following the company's receipt of proof that the class was successfully completed based on the policy guidelines.

#### CREDIT UNION

Membership is lifetime and is not based on continuing employment with Western Digital.

CALIFORNIA STATE UNEMPLOYMENT BENEFITS

You can file an application for unemployment benefits immediately, however your eligibility for benefits (as determined by the EDD- Employment Development Department) will be delayed until after your last Wage Continuation payment September 29, 2000.

If you have any questions, need to request forms, or need life conversion forms, contact:

WESTERN DIGITAL  
BENEFITS DEPARTMENT  
8105 IRVINE CENTER DRIVE  
IRVINE, CA 92618  
949-932-5700

WESTERN DIGITAL CORPORATION  
1999 EMPLOYEE SEVERANCE PLAN FOR U.S. EMPLOYEES

1. PURPOSE

The purpose of this Plan is to provide severance benefits to certain Eligible Employees (as defined herein) of Western Digital Corporation (the "Company") whose employment with the Company is terminated by reason of Job Discontinuance as described more fully herein. This instrument shall serve as both a plan document and summary plan description for purposes of Title I of ERISA.

2. EFFECTIVE DATE

All of the Company's policies and practices regarding severance benefits or similar payments upon employment termination with respect to Eligible Employees in the U.S., other than written employment or separation agreements with the Company that provide severance benefits, are hereby superseded by this Plan which shall be known as the Western Digital Corporation 1999 Employee Severance Plan For U.S. Employees, effective as of December 1, 1999.

3. AMOUNT AND PAYMENT OF SEVERANCE BENEFITS

3.1 Severance Benefits. An Eligible Employee who meets the departure conditions described in Section 3.2 shall become a Participant and the following shall apply:

(a) The Participant shall receive a severance payment based on Service Date and the Participant's Base Pay as follows:

Less than 5 years of service = 2 weeks Base Pay

5 years to less than 10 years = 3 weeks Base Pay

Over 10 years of service = 4 weeks Base Pay

(i) The severance payment shall be paid in one lump-sum cash payment within fifteen (15) days of the Participant's compliance with all provisions of Section 3.2.

(ii) A Participant may not be employed by Western Digital Corporation, its parent or subsidiaries, or any of its affiliates in any capacity including, but not limited to, consultant or temporary worker, during the period of time represented by the severance payment.

(b) The Participant shall be eligible for outplacement services provided by a vendor and in an amount (with no cash value) to be chosen by the Company, at the Company's sole discretion, as follows:



(i) Manager II, Grades 26, 35-36, 44-45, 69-72, and 85-86 shall receive up to a maximum of \$5,000 in outplacement services;

(ii) Manager I, Grades 34, 68, and 84 shall receive up to a maximum of \$3,000 in outplacement services;

(iii) Professional II, Exempt and Non-Exempt, Grades 20-24, 31-33, 41-43, 50-67, and 81-83 shall receive up to a maximum of \$2,000 in outplacement services;

(iv) Professional I, Hourly Non-Exempt shall receive up to a maximum of \$1,500 in outplacement services; and

(v) To the extent that a Participant is a Grade 73 or higher, the Committee shall determine, in its sole and exclusive judgment and discretion, the level of outplacement services, if any, to which such Participant shall be entitled.

(c) If the Participant elects COBRA continuation coverage within the applicable election period, the Company shall make the applicable COBRA premium payments for a period of two months beyond the expiration of the Participant's Company-provided medical, dental, and/or vision coverage existing as of the Participant's termination date. Notwithstanding anything in this Plan to the contrary, there shall be no obligation to make such COBRA premium payments on behalf of any Participant if the Participant otherwise becomes eligible for equivalent coverage under another employer's plan.

3.2 Departure and Entitlement Procedure. As a condition to becoming a Participant and receiving the severance benefits described in Section 3.1, the Eligible Employee must return and deliver to the Director of Human Resources or his or her designee all Company property within seven (7) days of the Eligible Employee's termination date.

3.3 Voluntary Resignation/Termination For Cause. Notwithstanding the foregoing, in no event shall an employee receive any payment hereunder if he or she quits voluntarily or is terminated for Cause.

3.4 Offsets. All severance payments under this Plan shall be subject to legal deductions, and the Company reserves the right to offset the benefits payable under this Plan by any advanced monies the Participant owes the Company. The benefits and amounts payable under this Plan shall be reduced (but not below zero) by any severance pay or benefits to which a Participant is or becomes entitled under any other severance pay plan, policy, agreement or arrangement. Notwithstanding any provision of this Plan to the contrary, to the extent that any Participant is entitled to any period of paid notice under Federal or state law including, but not limited to, the Worker Adjustment Retraining Notification Act, 29 U.S.C. Sections 2101 et seq., the benefits and amounts payable under this Plan shall be reduced (but not below zero) by the Base Pay received by the Participant during the period of such paid notice.

3.5 Loss and Reduction of Benefits. If an Eligible Employee resigns prior to his/her scheduled termination date, then he/she shall not be entitled to any severance payments or any

other severance benefits provided herein. If, during the period represented by the severance payment, an Eligible Employee accepts a position with Western Digital Corporation, its parent or subsidiaries, or any of its affiliates, he or she will not receive any further severance payments or benefits, and must repay the portion of any lump sum representing the unexpired severance benefit. If, prior to the payment of the lump-sum severance payment referenced in Section 3.1(a) herein, it is discovered that an otherwise Eligible Employee has improperly used the funds and assets of the Company, or has violated Company policies, practices or procedures at any time during his or her employment with the Company, then such employee shall not be entitled to any severance payment or any other severance benefits provided herein and all applicable benefits shall cease immediately.

3.6 Limitation On Employee Rights. This Plan shall not give any employee the right to be retained in the service of the Company or to interfere with or restrict the right of the Company to discharge any employee at any time, with or without cause.

#### 4. ADMINISTRATION

4.1 The Company shall be the administrator of the Plan for purposes of Section 3(16) of ERISA and shall have responsibility for complying with any reporting and disclosure rules applicable to the Plan under ERISA. In all other respects, except as provided herein, the Plan shall be administered and operated by the Committee. The Committee is empowered to construe and interpret the provisions of the Plan and to decide all questions of eligibility for benefits under this Plan and shall make such determinations in its sole and absolute discretion. The Committee may at any time delegate to any other named person or body, or reassume therefrom, any of its fiduciary responsibilities or administrative duties with respect to this Plan.

4.2 The members of the Committee shall be the named fiduciaries with respect to this Plan for purposes of Section 402 of ERISA.

4.3 The Committee may contract with one or more persons to render advice with regard to any responsibility it has under this Plan.

4.4 Subject to the limitations of this Plan, the Committee shall from time to time establish such rules for the administration of this Plan as it may deem desirable.

4.5 The Company shall, to the extent permitted by law, by the purchase of insurance or otherwise, indemnify and hold harmless the members of the Committee and each other fiduciary with respect to this Plan for liabilities or expenses they and each of them incur in carrying out their respective duties under the Plan, other than for any liabilities or expenses arising out of such fiduciary's gross negligence or willful misconduct. A fiduciary shall not be responsible for any breach of responsibility of any other fiduciary except to the extent provided in Section 405 of ERISA.

4.6 If a Participant or any other individual (collectively "Claimant") believes that benefits under this Plan are being wrongfully denied, that the Plan is not being operated properly, that fiduciaries of the Plan have breached their duties, or that the Claimant's legal rights are being violated with respect to the Plan, the Claimant must file a formal claim with the Committee.

Any such claim for benefits must be filed in writing within 90 days of the date upon which the Participant first knew or should have known the facts upon which the claim is based.

4.7 If any claim for benefits under this Plan is denied, in whole or in part, the claimant shall be so notified by the Committee, or its delegate, within thirty (30) calendar days of the date such person's claim is delivered to the Committee (or such person designated in writing by it). At the same time, the Committee shall notify the claimant of his or her right to a review by the Committee and shall set forth, in a manner calculated to be understood by the claimant, specific reasons for such decision, specific references to pertinent Plan provisions on which the decision is based, a description of any additional material or information necessary for the claimant to perfect his or her request for review, an explanation of why such material or information is necessary, and an explanation of the Plan's review procedure.

4.8 Any claimant or duly authorized representative may appeal from such decision by submitting to the Committee within sixty (60) calendar days after the date of such notice of its decision a written statement:

(a) Requesting a review of the claim for benefits by the Committee;

(b) Setting forth all of the grounds upon which the request for review is based and any facts in support thereof; and

(c) Setting forth any issues or comments which the claimant deems relevant to the claim. The Committee shall act upon such appeal within sixty (60) calendar days after the latter of receipt of the claimant's request for review by it or receipt of all additional materials reasonably requested by it from such claimant.

4.9 The Committee shall make a full and fair review of an appeal and all written materials submitted by the claimant in connection therewith and may require the claimant to submit, within ten (10) calendar days of written notice by the Committee, such additional facts, documents or other evidence as the Committee, in its sole discretion, deem necessary or advisable in making such a review. On the basis of its review, the Committee shall make an independent determination of the claimant's eligibility for an allowance and the amount of such allowance, if any, under this Plan. The decision of the Committee on any appeal shall be final and conclusive upon all persons if supported by substantial evidence in the record.

4.10 If the Committee denies a claim in whole or in part, it shall give written notice of its decision to the claimant setting forth, in a manner calculated to be understood by the claimant, the specific reasons for such denial and specific references to the pertinent Plan provisions on which its decision was based.

4.11 If any Claimant believes that the Committee's determination on appeal is incorrect, the Claimant or duly authorized representative may file suit related to such determination but must do so within one year from the date of the notification of the Committee's determination on appeal or the date which marks the end of the otherwise applicable limitations period under ERISA, whichever occurs first.

## 5. GENERAL

5.1 Payments to and benefits under this Plan are not assignable since they are primarily for the support and maintenance of the Participants.

5.2 The benefits and costs of this Plan shall be paid by the Company out of its general assets. The status of a claim against the Company with respect to the benefits provided hereunder shall be same as the status of a claim against the Company by any general or unsecured creditor.

5.3 This Plan is intended to be an employee welfare benefit plan, as defined in Section 3(1), Subtitle A of Title 1 of ERISA. The Plan will be interpreted to effectuate this intent.

5.4 The masculine pronoun shall include the feminine pronoun and the feminine pronoun shall include the masculine pronoun and the singular pronoun shall include the plural pronoun and the plural pronoun shall include the singular pronoun, unless the context clearly indicates otherwise.

5.5 The Plan shall be construed according to the laws of the State of California, except to the extent such laws are preempted by federal law.

5.6 ERISA Rights. An employee of the Company eligible to participate in the Plan has certain rights and protections under ERISA which entitle him or her to:

(a) examine, without charge, at the Plan administrator's office, all Plan documents and copies of all documents filed by the Plan with the U.S. Department of Labor, such as detailed annual reports and Plan descriptions.

(b) Obtain copies of all Plan documents and other Plan information upon written request to the Plan administrator. The Plan administrator may make a reasonable charge for copies.

(c) Receive a summary of the Plan's annual financial report. The Plan administrator is required by law to furnish each Participant with a copy of this summary financial report.

In addition to creating rights for Plan participants, ERISA imposes duties upon the people who are responsible for the operation of the Plan. The people who operate the Plan, called "fiduciaries" of the Plan, have a duty to do so prudently and in the interest of Eligible Employees and beneficiaries.

No one, including the Company, or any other person, may fire any person or otherwise discriminate against him or her in any way to prevent him or her from obtaining a benefit or exercising rights under ERISA.

If a claim for a benefit is denied in whole or in part, the claimant must receive a written explanation of the reason for denial. A claimant has the right to have the claim reviewed as

outlined above. Under ERISA, there are steps an employee can take to enforce the above rights. For instance, if an employee requests materials from the Plan and does not receive them within thirty (30) days, he or she may file suit in a federal court. In such a case, the court may require the Plan administrator to provide the materials and pay up to \$100 a day until he or she receives the materials, unless the materials were not sent because of reasons beyond the control of the Plan administrator.

If any employee has a claim for benefits which is denied or ignored, in whole or in part, he or she may file suit in a state or federal court. If it should happen that Plan fiduciaries misuse the Plan's money, or if an employee is discriminated against for asserting ERISA rights, he or she may seek assistance from the U.S. Department of Labor, or file suit in a federal court. The court will decide who should pay court costs and legal fees. If he or she is successful, the court may order the person sued to pay these costs and fees. If he or she loses, the court may order such person to pay these costs and fees. If such person loses, the court may order him or her to pay these costs and fees, for example, if it finds the claim is frivolous.

If an employee has any questions about the Plan, he or she should contact the Committee at the address shown below in Section 5.7. An employee with any questions about this statement or about rights under ERISA should contact the nearest Area Office of the U.S. Labor-Management Service Administration, Department of Labor.

5.7 The Plan sponsor, Plan administrator, and agent for the service of legal process is:

Plan Sponsor and Administrator:  
Western Digital Corporation  
8105 Irvine Center Drive  
Irvine, California 92718

Agent for Service of Process:  
Director of Human Resources  
Western Digital Corporation  
8105 Irvine Center Drive  
Irvine, California 92718

The Company's Employer Identification Number is 95-2647125. The Plan Number is 504.

## 6 AMENDMENT AND TERMINATION

The Company reserves the right to amend and/or terminate this Plan at any time in its sole discretion. No amendment or termination shall diminish benefits to which a participant is currently entitled under this Plan. Any termination, modification, or other amendment of the Plan shall be in writing, signed by the Chief Executive Officer or the Vice President of Human Resources.

## 7. DEFINITIONS

7.1 "Base Pay" means the employee's wages earned on a weekly basis determined as of the employment termination date, excluding bonuses and commissions, and, if paid hourly, is based on the number of regularly scheduled hours worked per week.

7.2 "Cause" means:

(a) fraud, misappropriation, embezzlement or other act of misconduct against the Company;

(b) conviction of a felony;

(c) violation of any rules or regulations of any governmental or regulatory body which has an adverse effect on the Company;

(d) a material breach of the terms of the employee's employment, or a breach of the employee's duty not to engage in any transaction that represents, directly or indirectly, self-dealing with the Company or any of the Company's affiliates, which has not been approved by the Company;

(e) unsatisfactory performance;

(f) violation of company policy;

(g) violation of state or federal law in connection with the employee's performance of his/her job;

(h) a leave of absence exceeding the period allowed by contract, policy or applicable law; or

(i) circumstances beyond the Company's control including, but not limited to, fire, flood, explosion, bombing, earthquake, and civil unrest.

Review of any determination that a termination is for Cause shall be by the Committee, in their sole and exclusive judgment and discretion, in accordance with the provisions of Section 4 herein.

7.3 "Committee" means the Severance Committee the members of which shall consist of the members of the Company's Retirement Plan Committee, unless otherwise determined by the Board of Directors of the Company.

7.4 "Eligible Employee" means any non-temporary, full-time or part-time, salaried or hourly employee (specifically excluding any individual who is not treated by the Company as a common law employee, such as an independent contractor or an individual working through a third-party provider, such as Kelly Services, without regard to the characterization or recharacterization of such individual's status by any court or governmental agency), who is paid from the Company's United States payroll, who is not a party to a written employment or separation agreement with the Company that provides severance benefits, and who is notified by

the Company that he or she has been selected for Job Discontinuance for reasons other than Cause.

7.5 "ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

7.6 "Job Discontinuance" means the termination of the employment of an Eligible Employee for reasons other than for Cause. Job Discontinuance does not apply, however, in circumstances including, but not limited to, voluntary resignation and/or voluntary retirement.

7.7 "Participant" means an Eligible Employee who is entitled, based on the provisions of Section 3.2 hereof, to the severance payment.

7.8 "Plan" means the Western Digital, Corporation 1999 Employee Severance Plan For U.S. Employees, as set forth in this instrument as it may be amended from time to time.

7.9 "Service Date" means the first date of employment or adjusted date of employment if rehired with the Company.

IN WITNESS WHEREOF, this instrument, evidencing the terms of the Western Digital Corporation 1999 Employee Severance Plan for U.S. Employees, is executed as of December 5, 1999.

WESTERN DIGITAL CORPORATION

By: /s/ Raymond M. Bukaty

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Raymond M. Bukaty  
Vice President, Corporate Law

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS AND BALANCE SHEET OF WESTERN DIGITAL CORPORATION AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH QUARTERLY REPORT ON FORM 10Q FOR THE SIX MONTH PERIOD ENDED DECEMBER 31, 1999.

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|-----------|-------------|-----------|
| 6-MOS     |             |           |
|           | JUN-30-2000 |           |
|           | JUL-04-1999 |           |
|           | DEC-31-1999 |           |
|           |             | 163,675   |
|           |             | 0         |
|           |             | 215,712   |
|           |             | 17,352    |
|           |             | 101,728   |
|           | 559,234     |           |
|           |             | 504,435   |
|           |             | 347,544   |
|           |             | 764,724   |
| 574,740   |             |           |
|           |             | 236,291   |
| 0         |             | 0         |
|           |             | 1,290     |
|           |             | (89,358)  |
| 764,724   |             |           |
|           |             | 967,131   |
|           | 967,131     |           |
|           |             | 1,012,232 |
|           |             | 1,012,232 |
|           |             | 234,953   |
|           |             | 1,000     |
|           |             | 8,357     |
|           |             | (288,411) |
|           |             | 0         |
| (288,411) |             |           |
|           |             | 0         |
|           |             | 166,899   |
|           |             | 0         |
|           |             | (121,512) |
|           |             | (1.12)    |
|           |             | (1.12)    |