

Quantum

Quantum Corporation

Annual Report

1985



Corporate Profile

Quantum Corporation develops, manufactures and markets rigid disk drives for computer systems.

Quantum's products include 8-inch and 5¼-inch Winchester-type disk drives and a new half-high 5¼-inch high-capacity series. All are sold to Original Equipment Manufacturers (OEMs). These drives are used in professional and engineering workstations; multi-user, microprocessor-based business computer systems; and emerging applications such as computer graphics and local area networks.

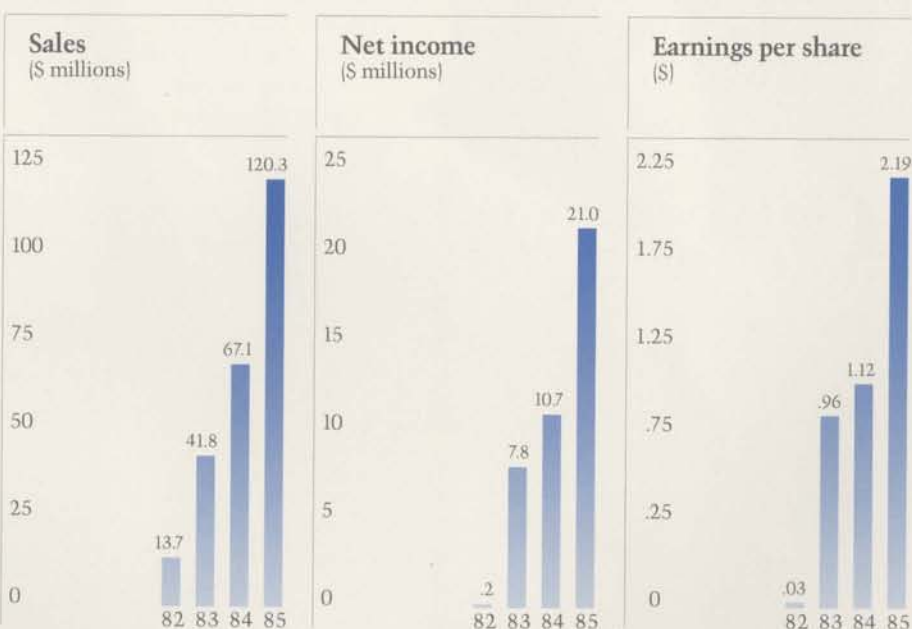
Quantum's subsidiary, Plus Development Corporation, has developed the first hard disk drive on a plug-in card designed to be added into personal computers. This product, called "Hardcard," plugs into any available expansion slot. The product will be distributed through retail computer dealers and value-added resellers (VARs).

Established in 1980, Quantum employs more than 700 people. Headquarters are located in Milpitas, California, with manufacturing facilities in Milpitas and in Ponce, Puerto Rico. Plus was incorporated in 1983 and maintains headquarters in Milpitas.

Financial Highlights

For the fiscal years ended March 31

(Thousands except per share and employee amounts)	1985	1984	1983	1982
Sales	\$120,349	\$67,069	\$41,779	\$13,656
Net income	20,973	10,673	7,838	186
Income per share:				
Income before extraordinary credit	2.19	1.12	.86	.03
Net income	2.19	1.12	.96	.03
Number of employees	771	628	291	262
Working capital	71,599	32,697	25,599	1,785
Total assets	99,526	74,816	56,630	12,121
Shareholders' equity	82,481	60,311	48,489	4,167



“Our view of the future of microcomputers led us to develop two exciting new products which will again distinguish Quantum from our competition.”



Steve Berkley, President, Plus Development Corporation Jim Patterson, President, Quantum Corporation

To Our Shareholders

Fiscal 1985 was an exciting year for Quantum. We had a record growth rate in revenues, our gross profit margin improved significantly and we developed a major new product for the Original Equipment Manufacturer (OEM) market. Our subsidiary, which we incorporated at the end of fiscal 1984, went into operation to develop a unique new product with a very different market focus.

Revenue grew 79%, from \$67,069,000 in 1984 to \$120,349,000 in 1985. Net income increased from \$10,673,000 to \$20,973,000, with earnings per share rising from \$1.12 in 1984 to \$2.19 this year.

This sound performance was due to a combination of factors. Early in the year, we began to feel the positive effects of the formation of Quantum Caribe, Inc. and the rapid production ramp of Q2000 Series® 8-inch products in Puerto Rico. As a result of tax benefits derived from manufacturing in Puerto Rico, our overall tax rate declined from 45% to 32%, contributing to a significant increase in net income. We increased production and shipments of the Q500 Series® 5¼-inch line without increasing our expense levels

and made significant progress in the efficiency of our manufacturing process, resulting in higher yields and improved margins.

One of Quantum's most exciting activities was our development of the Q200 Series.™ We designed a new disk drive product and a new manufacturing process, both based on the goal of manufacturing with 100% yields and at the same time expanding our traditional market. With its half-high size, high capacity and integrated controller, the Q200 family opens the door for Quantum to enter the large, multi-user systems market, as well as new markets for such applications as graphics, professional and engineering workstations and local area networks.

Just as exciting for all of us was the development of Hardcard™—the first product from Quantum's subsidiary, Plus Development Corporation. Hardcard is the first hard disk drive on a plug-in card. It simply plugs into the IBM PC® or other IBM-compatible personal computers. We incorporated our subsidiary at the end of fiscal 1984 under the temporary name Qew and recently changed it to Plus Development Corporation. Plus is a new venture in keeping with Quantum's entrepreneurial spirit. We built an entire new management team at Plus, tapping key Quantum managers as its genesis. By the end of the year, they in turn had created

their own team totally separate from Quantum. Unlike Quantum, Plus addresses the end-user and retail markets. This requires a well-developed, consumer-oriented marketing organization and was a key factor in opting to establish Plus as a separate corporation.

The continued strong demand for the Q2000 now has peaked and we are in the process of ramping down production at Quantum Caribe to prepare to manufacture the Q500 there. This is in keeping with our long-range manufacturing plans. New product lines are initially manufactured at our Milpitas facility; when a production process is mature, we move it offshore. Today, the Q500 has matured. Most major OEMs have selected their supplier of this class of product. Our production capability was increased to meet this demand and future growth in Q500 shipments will be closely tied to the sales growth rates of our current customers.

1985 brought significant changes to Quantum as we again distinguished ourselves from our competition. From the standpoint of technology, most disk drive manufacturers have been projecting that future disk drives will be just like those created in the past. At Quantum, we don't agree. Our view of the future led us to begin development of two compelling new products during the past fiscal year.

We believe in the continued world-wide growth of micro-computers and with it the continuing maturation of our industry. Disk drives are moving away from markets where creative engineering is the only thing that counts. We are in a transition from being engineering-driven to market-driven. As a result, the whole scale of the business is changing and our products are moving into the realm of appliances. Efficient, low-cost manufacturing processes are critical to success in this environment.

We view 1986 as being a year of implementation for Quantum

and Plus. It will be an important year because we will be finishing the transfer of the Q500 to Puerto Rico, completing the development and beginning the manufacturing ramps of the Q200 and Hardcard, and building the Plus organization. The execution of such major undertakings is something that we have proven we do well. Quantum has a well-established, solid reputation for doing what we say we are going to do.

A major priority for us is to continue the organizational development that we focused on in 1985. We have experienced a period of rapid growth. When this occurs, it is very important to have ways of communicating a company's values to all of its people. For this reason, we decided to spell out Quantum's purpose and values and to undertake a major effort to be certain they are communicated throughout our company. We have re-stated Quantum's purpose and values on the pages of this annual report.

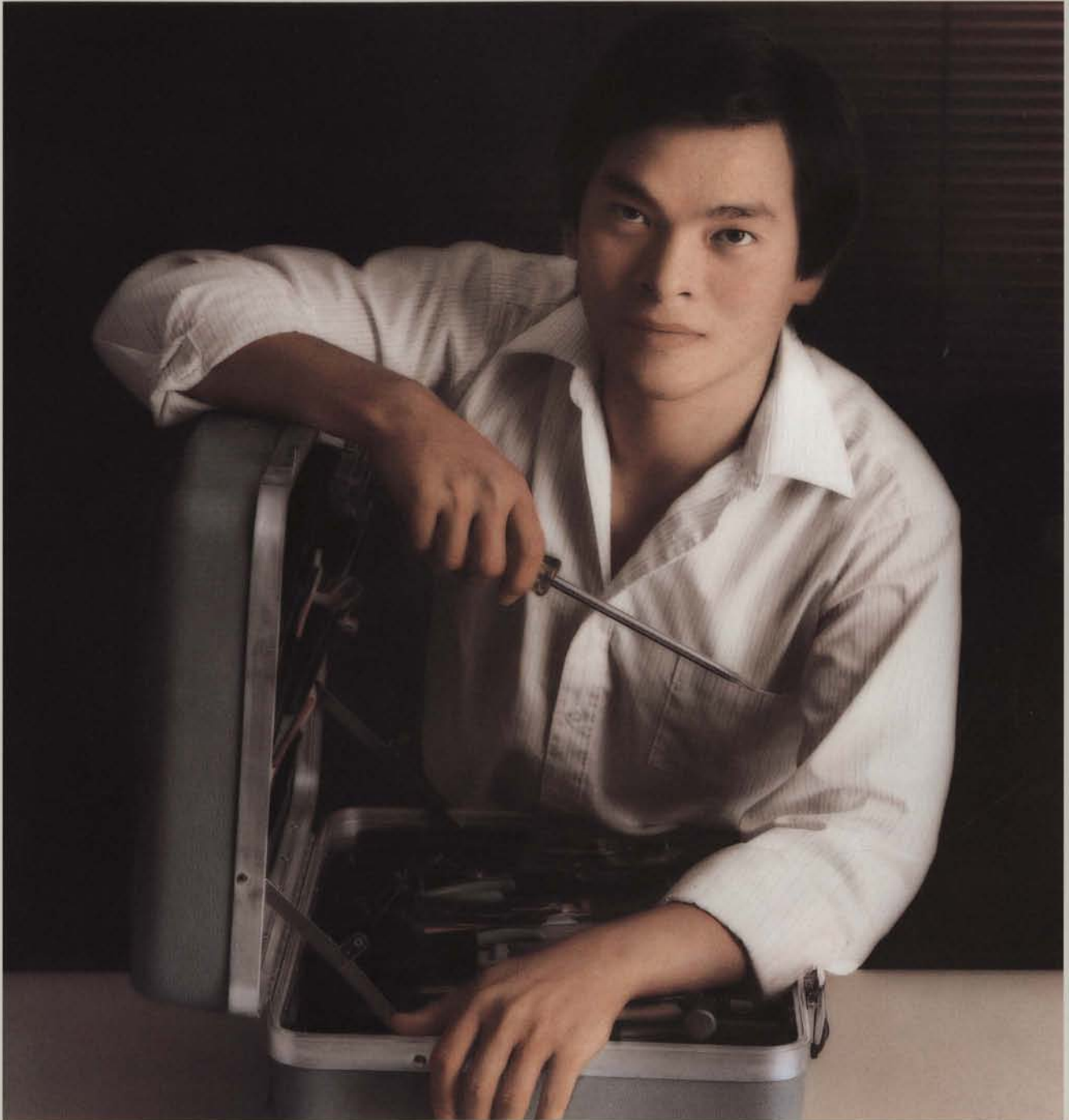
Our people are working in an environment that fosters a team spirit that led to the accomplishments of this year. It underlies the accomplishments that we anticipate for the coming years.



Fatmata Sulaiman, Manufacturing

James L. Patterson, President

“We have experienced a period of rapid growth, making it important to define and communicate Quantum’s purpose and values to all our people.”



Dat Le, Test Engineering

“Quantum’s purpose as a company is to provide our customers with products and services of value that meet their requirements. As a result of our success, we will have the opportunity to attract, retain, and benefit employees, suppliers, and shareholders.”



Tuyet Nguyen, Manufacturing Anh Tran, Manufacturing



Shirley Stough, Corporate Communications

Exhibiting Our Successful Entrepreneurial Spirit

Quantum made a major investment in developing two new disk drives during fiscal 1985 which set a new direction for our company. With these products, we will be entering a new market and we will be embarking on a new concept for our traditional market. This new direction exemplifies the successful entrepreneurial spirit on which our company was founded five years ago.

Quantum's new Q200 Series™ embodies our entrepreneurial spirit because it represents a new approach to meeting the needs of Original Equipment Manufacturers (OEMs). We set out to create a product that could be manufactured with 100 percent yields. Hardcard™, the first hard disk drive on a plug-in card for the personal computer market, was developed by Plus Development Corporation, Quantum's subsidiary. It, too, exhibits this entrepreneurial spirit because it is an innovative idea that addresses a market previously unexplored by Quantum and because we chose to create a totally separate entity as our vehicle for this new direction.

In both cases, Quantum's efforts to build our values and our company during the first five years of our history provided the foundation for our successful move in this new direction.

We had the vision to see future opportunities in our industry and to determine the most effective way to address them. We were able to move a strong management group from Quantum to form the core for Plus, and then to develop a new, stable team at both Quantum and Plus. We knew the importance of continuing to provide challenges for our people and we took care to create growth opportunities within both Quantum and Plus. And, throughout the year, we continued to meet the needs of our existing customers while steadily developing the Q200, Plus and Hardcard.

These development activities reflect the main purpose of Quantum, which is to provide our customers with products and services of real and measurable value. This philosophy has been the key to our entrepreneurial success since Quantum's beginnings. We have fulfilled this purpose through our keen understanding of our customers' needs and our consistent manufacturing of reliable products on time, economically and in quantity.

We have been able to do this because of our people. At Quantum, one of our fundamental beliefs is that our one

unique asset is our people. Fiscal 1985 was a year in which we again proved the soundness of this belief—our success demonstrates what Quantum people can accomplish.

Displaying Our Spirit: The Q200
Identifying A Need: A successful entrepreneur identifies a market with a need for a product before designing a product. At Quantum, our people made the difference. We initiated the development of our new Q200 Series after we clearly understood market trends. Continuing trends toward more automated offices, smaller systems, higher data storage capacity, lower cost, and higher system performance all are concerns we addressed in creating the Q200.

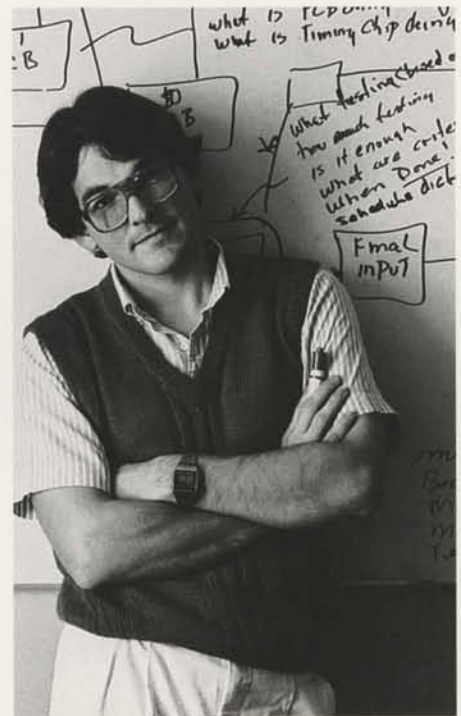
The two products in this family expand Quantum's traditional market beyond low-end microprocessor-based systems. This market currently is served by our 8-inch Q2000 Series® and our 5¼-inch Q500 Series® disk drives. With the Q200, we expanded into the high end of the OEM market for larger, multi-user systems and for specialized applications. The Q250 has a 53-megabyte (formatted) capacity, and the Q280 an 80-megabyte (formatted) capacity, an increase in capacity of up to 150 percent above previous Quantum

products. Both Q200 drives are tailored for multi-user, microprocessor-based systems; single-user professional and engineering workstations; and other emerging applications, such as local area networks and advanced graphics.

These market areas are growing rapidly, according to a major, independent, computer market research company. Shipments of multi-user, microprocessor-based systems are growing at a rate of 32 percent a year, and of professional and engineering workstation systems at a rate of 28 percent.

Applying Technology: Our entrepreneurial approach to technology and the ingenuity of our people enabled Quantum to create the Q200. We took an approach that adapts our proven, successful technology into a product family that is smaller in size and higher in performance. At the same time, our people were dedicated to a goal of designing a product that could be manufactured with 100 percent yields.

That goal led to our integrating and embedding the controller in the disk drive. This approach to technology enables us to better control our yields, to come closer to our goal of 100 percent. As a result, we can offer a disk drive with more than double the storage capacity of our earlier products and increased performance for approximately the same price.



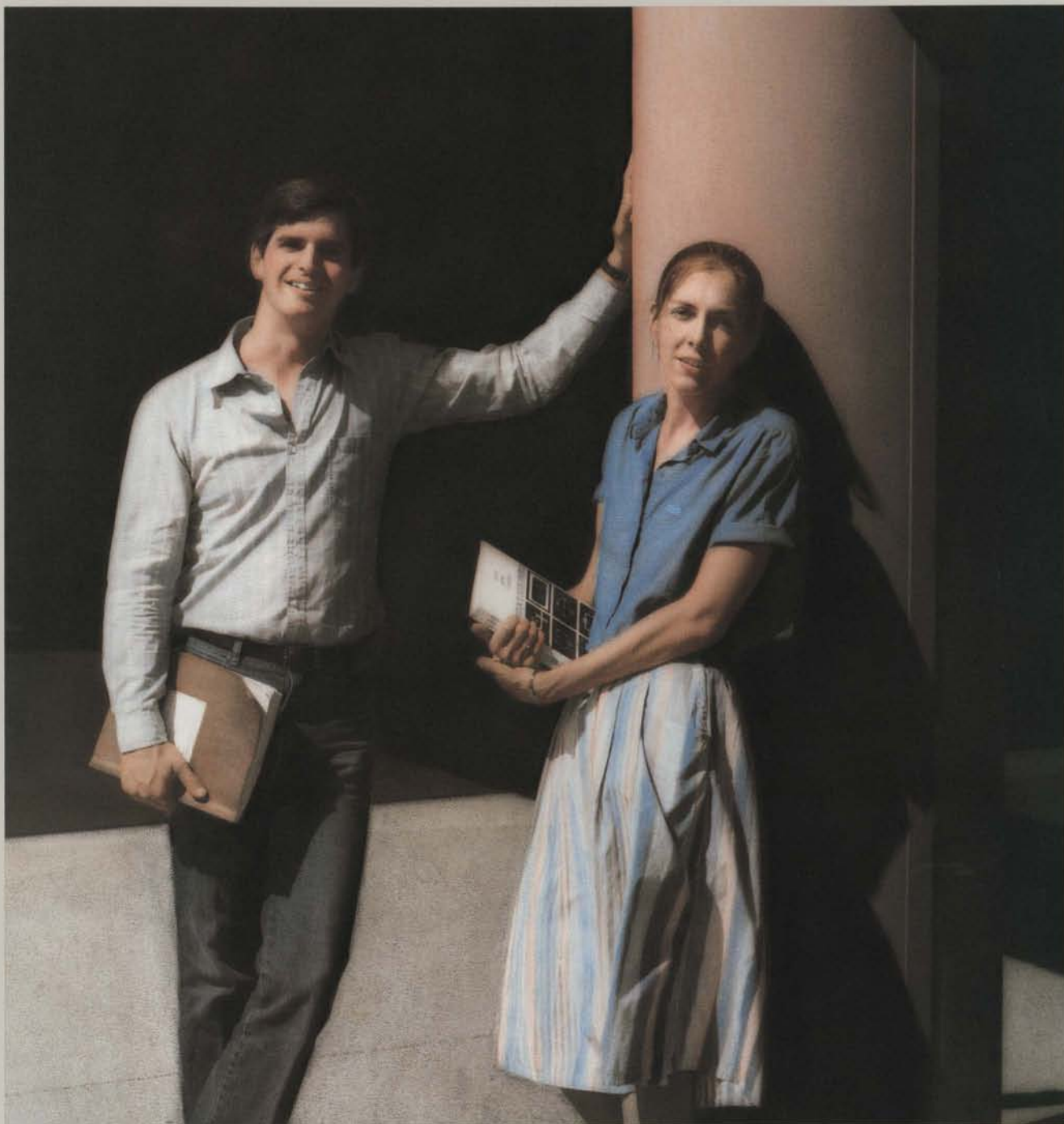
Scott Schroeder,
Business Information Systems

"We believe that effective, open, and honest communication helps us achieve our greatest potential as individuals and as a company."



Dana Kruger, Receptionist

"We believe in an environment characterized by individual freedom, cooperation between teams, and high ethical standards. This is the environment in which we and our company will flourish."



Tom Mager, Drive Engineering Collette LaChambre, Drive Engineering



Melinda Hom, Documentation

We displayed Quantum innovation in our approach to the drive actuator and the servo. In both cases, we began with the technology we knew and had proven in previous products, and then we adapted and refined it. The Q200 actuator is similar to that of the Q500, but it is smaller and, as a result, faster. We adapted our wedge servo technology into an embedded servo positioning control system for the Q200, eliminating the need for the optical encoder used in earlier drives. To meet the storage capacity requirements of this higher performance drive family, we used thin film media.

Providing Benefits: For a company to thrive, the products it creates must provide its customers with genuine benefits. Quantum has been able to accomplish this because our people never lose sight of our purpose to give value to our customers.

The Q200 sets a new standard in price and performance with the combination of high-capacity, half-high size and integrated controller all in a 5¼-inch Winchester disk drive. That means our customers save significant time and money because the need to test and integrate drives and controllers is eliminated and because they do not need to write special software for each drive. Our controller, which uses large scale integrated (LSI) circuit technology in its

design, removes these burdens from our OEM customers. The integrated controller increases reliability and performance. It also enables us to use a wide range of available media which, in turn, allows us to price our products competitively.

The interface chosen for the Q200 product family enables our OEM customers to connect other peripheral equipment to their systems without needing different interfaces for each piece. This provides our customers with additional flexibility and reduces the overall cost of configuring their systems.

Manufacturing Consistently: Designing a product that customers want is part of being an entrepreneur; achieving success as an entrepreneur requires being able to manufacture that product consistently. And as the scale of your business grows, you must do still more and you must work still harder. At Quantum, our people have proven that they thrive in this environment.

We believe hard disk drives are evolving into a new role as their usage becomes more common. Reliability, ease of use and lowest cost of ownership have become increasingly important.

To achieve a competitive

position, the scale of manufacturing must change. It is important to focus on the manufacturing operation and procurement efforts to get the most out of the economies of scale as they materialize. At Quantum, the Q200 is the vehicle with which we are attempting to do this; our priority goal is to manufacture products with 100 percent yields. We believe that if we can manufacture without waste, we will continue to provide the most cost-competitive products in our industry.

With the Q200, as with all of our disk drive families, we designed the manufacturing process at the same time that we designed the product. But before beginning even pilot production, we have focused on completely refining the entire process, from our supplier program to our testing strategy, and on refining the design to make it completely manufacturable. Once in production, we will be using an automated material transfer line to save time and reduce inventory.

**Extending Our Spirit:
Plus Development Corporation
and Hardcard.**

Success in any business endeavor requires a constant and accurate assessment of the future. In the disk drive industry, this has been especially true because of the

significant and fundamental changes that have been occurring in recent years. Hard disk drives no longer are a rarity, a technological marvel. Our products are expanding from the realm of the OEM into that of the end-user and retail customer. That means drives must be readily available from a variety of sources. They must be easy to install and service. Their manufacture must be efficient, allowing high volume and cost-effectiveness. Their marketing must take into account the completely different concerns of these customers.

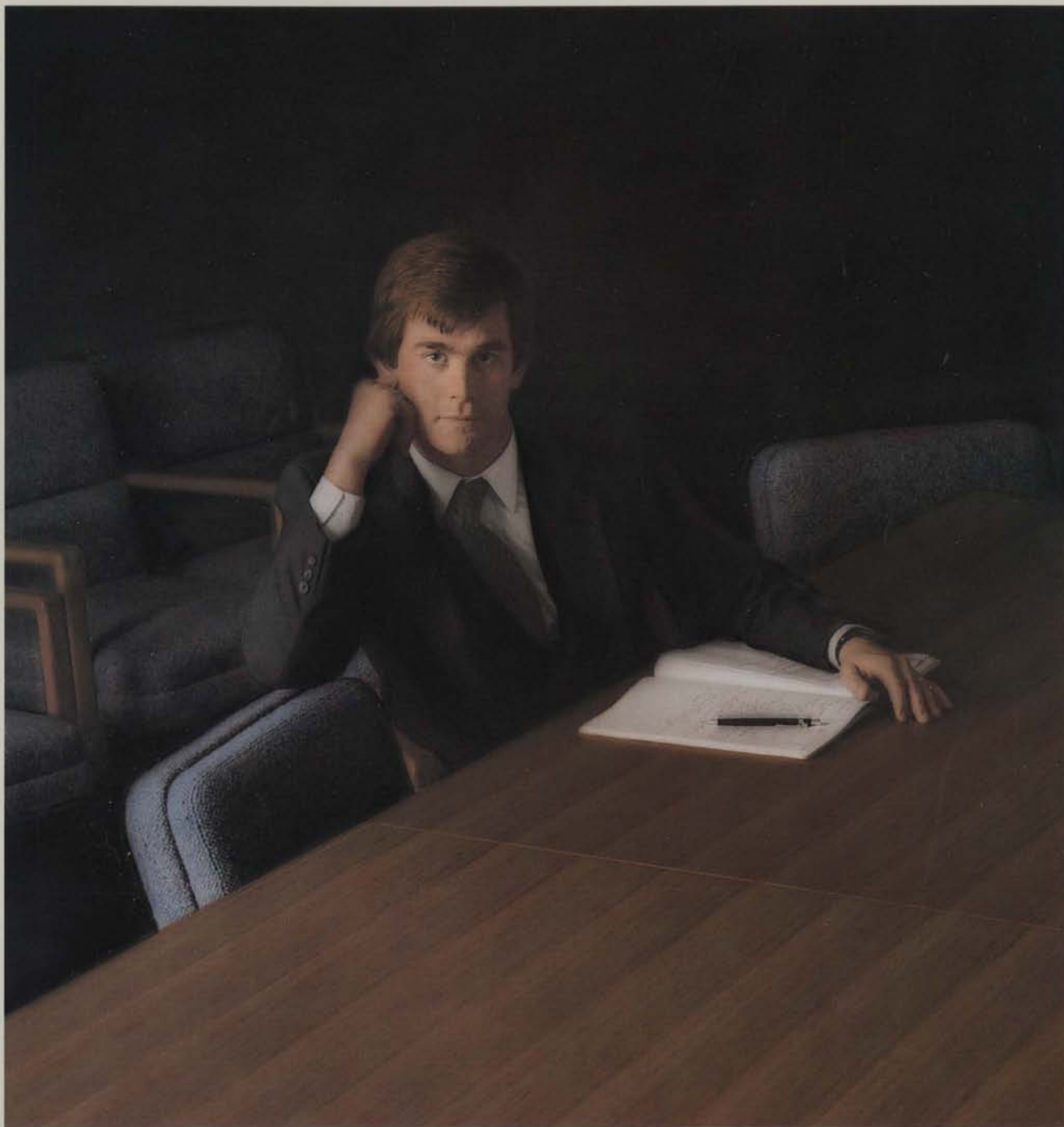
Quantum's view of the future for our industry fueled the decision to establish Plus Development Corporation. It is our intent that Plus become a world-class leader in the end-user market as Quantum has in the OEM market. We felt that separation from Quantum was key in securing the right atmosphere for embarking on such a totally new venture. Yet, the values that we hold—our team spirit, our focus, our planning—were carried over to Plus, as the basis for determining the shape for our move in this new direction. From this basis, we then came up with the most effective product, manufacturing and marketing approach to address the changing requirements of our industry.

It worked because we had the right people to start Plus and because they were given a setting



Dieter Miramontes, Shipping

"We believe that our highest priority as a company is to build mutually successful relationships with our customers, based on our understanding of their needs and a commitment to satisfying those needs."



Hank Chesbrough, Marketing, Plus Development Corporation

*"We believe that our one unique asset—
and our most valuable resource—is our people."*



David Zaia, Manufacturing



Roger Hammond, Manufacturing

where they could assume total responsibility for the project without the distractions of daily operations at Quantum. We carried our commitment to Plus even beyond this, to the financial investment, by separating the resources designated for Plus. Its success will be clearly its own.

Identifying A Need: Our vision of the future for the disk drive industry led us to take a serious look at the personal computer market.

Today, more than 2.5 million IBM PC[®]s alone are in use around the world, with approximately two-thirds of them in a corporate environment. Their users are demanding the capacity to store larger files or multiple software programs on a single disk. They want faster access and response time. They increasingly need to download files from main-frame computers for individual workstation use. And they have demonstrated that they are willing to purchase non-IBM peripherals that are easy to install and trouble-free. Basically, they want to improve the productivity of their computer without losing their initial investment.

The market for low-end, single-user, PC-like products, according to a major computer market research firm, is growing at 25 percent a year. Plus plans to address this end-user market through retail computer stores and value-added resellers (VARs).

Applying Technology: In creating Hardcard, our team at

Plus used an innovative approach to technology. Our people took the approach that a hard disk drive for a personal computer should be viewed as a standard part, as a component. Accordingly, we rejected the notion that these disk drives must continue to be designed as though they were floppy drives.

Instead, we chose to move hard disk drives into the same category as any other personal computer peripheral—a plug-in card that any user can easily purchase, install and have serviced.

To accomplish this, we created Hardcard, the first hard disk drive on a plug-in card for personal computers. It is designed to plug into any available expansion slot in the IBM PC and a range of PC-compatible computers. Though the Hardcard head/disk assembly, which stands only 1-inch high, is the smallest in the marketplace, its 10-megabyte disk provides the equivalent of 28 floppy disks of storage space.

Our underlying concept was to refine, reduce and use existing technology in a unique fashion to create a highly manufacturable and low-cost product. Hardcard represents the advanced application of Winchester disk drive technology to produce the next generation of proven technology. We used the same optical

encoder and actuator electronics as in Quantum's previous products, but put them together with an advanced head positioning system to reduce drive size. We built in the controller to increase reliability.

Providing Benefits: Plus' creation of a product that will provide personal computer users with genuine benefits is at the heart of our spirit. But then, our people never lose sight of the customer. The design is so practical that it is simple for any PC user to insert Hardcard in any available slot in the personal computer.

Once in, it allows the user to store the equivalent of 5,000 pages of double-spaced text. It enables the user to load and store multiple application programs. And it decreases access and response times. There are no external parts to take up space and create potential problems. Nor does the user have to remove any parts from the computer—including the existing floppy disk drives. Because of the crucial role that a disk drive plays in our customers' business operations, we introduced with Hardcard a reliability factor more than twice that of the industry standard for hard disk drives.

Manufacturing Consistently: As in any successful entrepreneurial venture, the market, the technology and the resulting

product together are the promise. Delivery of the promise depends on manufacturing strength. It must be consistent, on time, economical and in quantity. In high-volume products, that can require vertical integration—the in-house manufacture of component parts and the accompanying control over their quality and cost. So Plus opted to enter into a manufacturing agreement with Matsushita Kotobuki Electronic Industries, Ltd. (MKE), a Japanese manufacturer renowned for the sophistication of its manufacturing process.

The relationship will combine the strengths of both companies: MKE's manufacturing capabilities and the technological, marketing and distribution skills of Plus. Plus' people bring to the partnership an expert knowledge of the needs of the personal computer marketplace and creativity in design.

Perpetuating Our Spirit

The products that we developed in 1985 are but an expression of our excellence in building a company around people. Quantum first defined this excellence in 1980, at our inception. In 1985, Plus, too, adopted this concept as its cornerstone. Our companies will enter the coming year with the greatest of all strengths—people, our people. We have built Quantum into a leader in the OEM market for disk drives; we are prepared to do the same for Plus in the end-user market.



*Steve Campbell, Q200 Engineering
Yoshiko Earl, Manufacturing*

"We believe that success is achieved through our ability to identify critical issues, set priorities, and meet commitments. We measure our success by how well we fulfill our company's purpose."

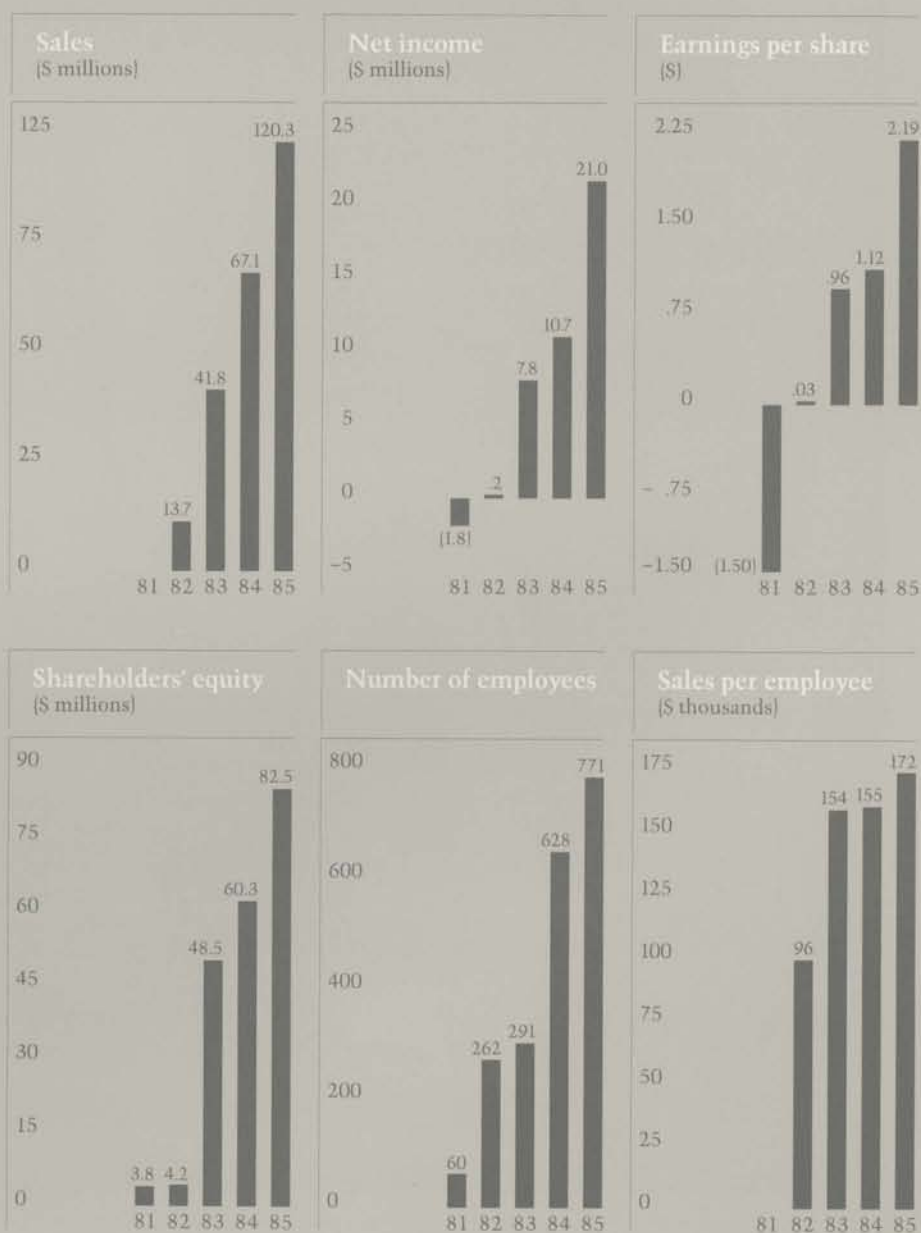


Dana Fisher, Test Equipment Manufacturing Gregg Uhlendorf, Q200 Engineering

Selected Financial Information

Five years ended March 31, 1985
(Thousands except per share amounts
and number of employees)

	1985	1984	1983	1982	1981
Net sales	\$120,349	\$67,069	\$41,779	\$13,656	\$ 0
Income (loss) before extraordinary credit	\$ 20,973	\$10,673	\$ 7,024	\$ 186	\$(1,769)
Net income (loss)	\$ 20,973	\$10,673	\$ 7,838	\$ 186	\$(1,769)
Earnings (loss) per share:					
Income before extraordinary credit	\$ 2.19	\$ 1.12	\$.86	\$.03	\$ (1.50)
Net income (loss)	\$ 2.19	\$ 1.12	\$.96	\$.03	\$ (1.50)
Common and common equivalent shares	9,589	9,516	8,172	6,595	1,175
Total assets	\$ 99,526	\$74,816	\$56,630	\$12,121	\$ 4,266
Shareholders' equity	\$ 82,481	\$60,311	\$48,489	\$ 4,167	\$ 3,788
Backlog	\$ 32,608	\$43,947	\$14,250	\$13,000	\$ 1,550
Number of employees	771	628	291	262	60
Net sales per employee	\$ 172	\$ 155	\$ 154	\$ 96	\$ 0



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

Sales for the fiscal year ended March 31, 1985 were \$120.3 million, an increase of 79.4% over the prior fiscal year sales of \$67.1 million. Sales growth was attributable to increased production and shipments of the Q500 Series 5¼-inch products. Sales of the Q500 products accounted for approximately 54% of revenue this year, compared with 17% in the prior year. Total sales of the Q2000 Series 8-inch products this year remained relatively unchanged compared with last year; however, declining demand for the product resulted in a decrease in Q2000 revenues during the second half of fiscal 1985. The Company expects this trend to continue for the 8-inch product line. Sales growth in the next fiscal year will result primarily from continued demand for the Q500 product line from existing customers, and revenues generated from new products.

In fiscal year 1985, cost of sales remained constant at 61% of sales, compared with fiscal 1984. The reduction in cost of certain components and increased productivity in the Company's Milpitas and Puerto Rico manufacturing operations countered the price declines experienced throughout the disk drive industry. The overall effect of inflation on the cost of materials, labor and other expenses was minimal.

Research and development spending during fiscal year 1985 increased substantially to support the engineering efforts for two major new products. The Q200 Series, a new generation of half-high 5¼-inch disk drives, is being developed for the Original Equipment Manufacturer marketplace. In addition, Quantum's subsidiary, Plus Development Corporation (Plus), is developing a low-cost disk drive for the personal computer marketplace.

Quantum's marketing and general and administrative costs as a percentage of sales were 8.9% in fiscal 1985, compared with 10.4% in fiscal 1984. This decrease resulted from a significant growth in revenue without a corresponding increase in these costs. However, overall spending increased as a result of marketing efforts at Plus in preparation for the product announcement, litigation expenses related to the patent infringement suit filed by the Company against Computer Memories, Inc., and the additional administrative costs associated with the operation of the Company's subsidiaries, Quantum Caribe and Plus.

Interest and the net realization on marketable investment securities decreased as a percentage of sales from 5.1% in fiscal 1984 to 1.6% in fiscal 1985. This decrease is attributable to the loss realized in fiscal 1985 on the sale of the Company's portfolio of adjustable rate preferred stock. The proceeds from the sale were invested in short-term certificates of deposit and time deposits. Interest and dividend income declined slightly from \$3.4 million in fiscal 1984 to \$3.1 million in fiscal 1985.

Quantum's effective tax rate was 32% for fiscal 1985, a 13% decrease from fiscal 1984's effective tax rate of 45%. This decrease is primarily the result of the reduced tax rate on income generated by Quantum Caribe, the Company's subsidiary in Puerto Rico.

On March 31, 1985, the Company had working capital of \$71.6 million. The increase of \$38.9 million over the prior year's balance was generated mainly by positive cash flow from operations, as well as the proceeds from the sale of the long-term marketable investment securities (adjustable rate preferred stock).

Quantum's principal source of liquidity at March 31, 1985 consisted of cash and cash equivalents of \$47.0 million, an increase of \$28.3 million over the prior year's balance of \$18.7 million. During fiscal 1985, inventories increased to \$23.0 million compared with \$17.7 million the prior year, primarily due to higher sales levels and the partial transfer of Q500 product manufacturing to our Puerto Rico subsidiary.

The Company believes that its current liquidity and anticipated cash flow from operations are sufficient to finance its planned growth.

Year ended March 31	Percentage of Net Sales			
	1985	1984	1983	1982
Sales	100.0%	100.0%	100.0%	100.0%
Costs and expenses				
Cost of sales	61.2	61.3	56.2	75.8
Research and development	6.0	4.7	5.8	3.1
Marketing	4.5	6.0	6.4	13.2
General and administrative	4.4	4.4	3.2	6.3
Total costs and expenses	76.1	76.4	71.6	98.4
Income from operations	23.9	23.6	28.4	1.6
Interest and net realization on marketable investment securities	1.6	5.1	2.4	(.2)
Income before income taxes	25.5	28.7	30.8	1.4
Provision for income taxes	8.1	12.8	14.0	
Income before extraordinary credit	17.4	15.9	16.8	1.4
Extraordinary credit			2.0	
Net income	17.4%	15.9%	18.8%	1.4%

Consolidated Statements of Operations

Year ended March 31	1985	1984	1983
Sales	\$120,349,000	\$67,069,000	\$41,779,000
Costs and expenses:			
Cost of sales	73,668,000	41,131,000	23,498,000
Research and development	7,210,000	3,156,000	2,420,000
Marketing	5,397,000	4,044,000	2,694,000
General and administrative	5,265,000	2,948,000	1,314,000
	91,540,000	51,279,000	29,926,000
Income from operations	28,809,000	15,790,000	11,853,000
Interest and dividend income (expense), net	3,098,000	3,433,000	999,000
Loss on sale of marketable securities	(1,245,000)		
Income before income taxes	30,662,000	19,223,000	12,852,000
Provision for income taxes (Note 10)	9,689,000	8,550,000	5,828,000
Income before extraordinary credit	20,973,000	10,673,000	7,024,000
Extraordinary credit-reduction of income taxes from utilization of tax loss carryforward			814,000
Net income	\$ 20,973,000	\$10,673,000	\$ 7,838,000
Income per common share (Note 1):			
Income before extraordinary credit	\$2.19	\$1.12	\$.86
Extraordinary credit			.10
Net income	\$2.19	\$1.12	\$.96
Common and common equivalents used in computing per share amounts	9,589,114	9,516,211	8,172,090

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheets

	March 31	1985	1984
Assets			
Current assets:			
Cash, including certificates of deposit and time deposits of \$45,338,000 and \$18,512,000		\$46,966,000	\$18,672,000
Accounts receivable, net of allowance for doubtful accounts of \$617,000 and \$329,000		13,407,000	9,182,000
Interest and dividends receivable		298,000	675,000
Inventories (Notes 1 and 3)		23,014,000	17,677,000
Prepaid income taxes (Note 10)		960,000	
Prepaid expenses		212,000	208,000
Other current assets		720,000	93,000
Total current assets		85,577,000	46,507,000
Property and equipment at cost less accumulated depreciation (Note 4)		13,513,000	9,184,000
Long-term marketable investment securities less valuation allowance of \$450,000 (Note 5)			18,731,000
Other assets		436,000	394,000
		\$99,526,000	\$74,816,000
Liabilities and Shareholders' Equity			
Current liabilities:			
Accounts payable		\$ 9,076,000	\$ 9,879,000
Accrued compensation		1,167,000	864,000
Income taxes payable		1,583,000	1,540,000
Deferred income taxes (Note 10)			315,000
Accrued warranty expense		1,523,000	908,000
Other accrued liabilities		629,000	304,000
Total current liabilities		13,978,000	13,810,000
Deferred income taxes (Note 10)		3,067,000	695,000
Commitments (Note 11)			
Shareholders' equity (Notes 6, 7, 8, and 9):			
Preferred stock, no par value, 4,000,000 shares authorized, none issued			
Common stock, no par value, 30,000,000 shares authorized, 9,363,985 and 9,242,608 shares outstanding		44,580,000	43,833,000
Valuation allowance for long-term marketable investment securities			(450,000)
Retained earnings		37,901,000	16,928,000
Total shareholders' equity		82,481,000	60,311,000
		\$99,526,000	\$74,816,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Financial Position

Year ended March 31	1985	1984	1983
Financial resources were provided by:			
Operations:			
Net income before extraordinary credit	\$20,973,000	\$10,673,000	\$ 7,024,000
Charges not affecting working capital—depreciation	2,433,000	1,333,000	555,000
—deferred taxes	2,372,000	366,000	329,000
—write-down of marketable investment securities	456,000	720,000	141,000
—loss on marketable investment securities	1,245,000		
Resources provided by operations	27,479,000	13,092,000	8,049,000
Extraordinary credit			814,000
Sale of convertible preferred stock, Series C			6,107,000
Proceeds from notes receivable from employees			75,000
Proceeds from sales of marketable securities	17,480,000		
Common stock transactions	747,000	424,000	31,477,000
	45,706,000	13,516,000	46,522,000
Financial resources were used for:			
Purchase of marketable investment securities			20,042,000
Acquisition of property and equipment, net of retirements	6,762,000	6,327,000	2,605,000
Other assets	42,000	91,000	61,000
	6,804,000	6,418,000	22,708,000
Increase (decrease) in working capital	\$38,902,000	\$ 7,098,000	\$23,814,000
Increase (decrease) in components of working capital:			
Cash	\$28,294,000	\$ (2,164,000)	\$20,578,000
Accounts receivable	4,225,000	3,323,000	1,215,000
Interest and dividends receivable	(377,000)	196,000	479,000
Inventories	5,337,000	11,660,000	1,321,000
Prepaid income taxes	960,000		(22,000)
Prepaid expenses	4,000	7,000	117,000
Other current assets	627,000	74,000	(16,000)
Notes payable to bank			4,385,000
Accounts payable	803,000	(7,707,000)	767,000
Accrued compensation	(303,000)	(365,000)	
Income taxes payable	(43,000)	2,273,000	(3,813,000)
Deferred income taxes	315,000	573,000	(888,000)
Accrued warranty expenses	(615,000)	(579,000)	(255,000)
Other accrued liabilities	(325,000)	(193,000)	(54,000)
Increase (decrease) in working capital	\$38,902,000	\$ 7,098,000	\$23,814,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

	Series A	
	Shares	Amount
Balance at March 31, 1982	1,013,333	\$ 3,040,000
Shares issued during April 1982 (Note 6)		
Shares repurchased under employee stock purchase agreements (Note 7)		
Conversion of all preferred stock into common stock (Note 6)	(1,013,333)	(3,040,000)
Public offering of common stock on December 10, 1982 (Note 6)		
Shares issued under employee stock option plan (Note 8)		
Valuation allowance for marketable investment securities		
Net income for year ended March 31, 1983		
Balance at March 31, 1983		
Shares repurchased under employee stock purchase agreements (Note 7)		
Shares issued under employee stock option plan (Note 8)		
Shares issued under employee stock purchase plan (Note 9)		
Shares issued as an employee stock bonus		
Reduction of valuation allowance for marketable investment securities		
Net income for year ended March 31, 1984		
Balance at March 31, 1984		
Shares repurchased from employees		
Shares issued under employee stock option plan (Note 8)		
Shares issued under employee stock purchase plan (Note 9)		
Reduction of valuation allowance for marketable investment securities		
Net income for year ended March 31, 1985		
Balance at March 31, 1985		

See accompanying notes to consolidated financial statements.

Convertible Preferred Stock				Common Stock		Valuation allowance for marketable investment securities	Retained earnings (deficit)
Series B		Series C		(Notes 6, 7, 8 and 9)			
Shares	Amount	Shares	Amount	Shares	Amount		
212,000	\$ 2,650,000			1,790,466	\$ 135,000		\$ (1,583,000)
		410,667	\$ 6,107,000				
				(49,133)	(4,000)		
(212,000)	(2,650,000)	(410,667)	(6,107,000)	5,722,666	11,797,000		
				1,673,000	31,474,000		
				14,840	7,000		
						\$ (1,175,000)	
							7,838,000
				9,151,839	\$43,409,000	\$ (1,175,000)	\$ 6,255,000
				(867)	(2,000)		
				71,904	91,000		
				17,647	299,000		
				2,085	36,000		
						725,000	
							10,673,000
				9,242,608	\$43,833,000	\$ (450,000)	\$ 16,928,000
				(1,680)	(46,000)		
				92,063	309,000		
				30,994	484,000		
						450,000	
							20,973,000
				9,363,985	\$44,580,000		\$37,901,000

Notes to Consolidated Financial Statements

Note 1—Significant accounting policies

Quantum Corporation (the Company) has adopted accounting practices which are generally accepted in the industry in which it operates. The following are the Company's significant accounting policies:

Principles of consolidation

The accompanying consolidated financial statements include the accounts of Quantum Corporation and its wholly owned and majority owned subsidiaries. All significant transactions and accounts between the Company and these subsidiaries have been eliminated in consolidation.

Revenue recognition

Revenue from sales of products is recognized upon shipment to customers.

Research and development expenses

Research and development expenditures are expensed when incurred.

Warranty expenses

The Company generally warrants its products against defect for one year. A provision for estimated future costs relating to warranty expenses is recorded when products are shipped.

Inventories

Inventories are stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or market.

Property and equipment and depreciation

Property and equipment are stated at cost. Depreciation is computed for financial reporting purposes using the straight-line method and the estimated useful lives which range from three to ten years. Amortization of leasehold improvements is computed over the shorter of the useful life of the improvement or the life of the lease. Depreciation for income tax purposes is computed using accelerated methods.

Marketable investment securities

Marketable investment securities consist of various adjustable rate preferred stocks held for investment. These securities are carried at the lower of cost or market. To the extent an excess of cost over market is considered a temporary decline in value, a valuation allowance is included in shareholders' equity. Any permanent impairment of value is charged to income. Dividends are accrued as earned. Gains and losses on securities sold are determined on the specific identification basis.

Income taxes

Investment and research and development tax credits are recognized as a reduction of income tax expense in the year the related assets are placed in service or the qualified research and development expenditures are incurred to the extent of the statutory limits applied to pre-tax accounting income.

Net income per common share

Primary net income per common and common equivalent share is computed on the weighted average number of common shares and common equivalent shares from dilutive convertible preferred stock and options outstanding during the respective periods, using the treasury stock method.

Note 2—Business segment and investment in subsidiary

The Company is engaged in a single business segment consisting of the design, manufacture and marketing of disk drives based on Winchester technology. Quantum sells its products to Original Equipment Manufacturers (OEMs) in the United States and in foreign countries through its own sales organization and through distributors. Foreign sales account for 21%, 16%, and 11% of total sales in 1985, 1984 and 1983, respectively.

Major customers (those accounting for 10% or more of sales) accounted for 16%, 14%, 11% and 10% of revenues during the year ended March 31, 1985, 15%, 10%, 10% and 10% of revenues during the year ended March 31, 1984 and 18%, 15% and 12% of revenues for the year ended March 31, 1983.

A subsidiary was formed in late fiscal 1984 to develop a low-cost mass storage subsystem for the personal computer market. Financed through the issuance of stock and borrowings from the parent company, the subsidiary incurred a pretax loss of \$6.2 million in fiscal 1985, primarily representing research and product development costs. Officers and employees of the parent company and the subsidiary hold a minority interest in the subsidiary which amounted to 14% of the voting stock of the subsidiary at March 31, 1985.

Note 3—Inventories

Inventories were composed of:

March 31	1985	1984
Materials and purchased parts	\$11,887,000	\$ 6,960,000
Work in process	5,912,000	7,469,000
Finished goods	5,215,000	3,248,000
	<u>\$23,014,000</u>	<u>\$17,677,000</u>

Note 4—Property and equipment

Property and equipment consisted of:

Machinery and equipment	\$10,629,000	\$ 6,024,000
Furniture and fixtures	1,594,000	1,300,000
Tooling	3,200,000	2,232,000
Leasehold improvements	2,287,000	1,211,000
Construction in progress	305,000	488,000
	<u>18,015,000</u>	<u>11,255,000</u>
Less-accumulated depreciation	<u>(4,502,000)</u>	<u>(2,071,000)</u>
	<u>\$13,513,000</u>	<u>\$ 9,184,000</u>

Note 5—Marketable investment securities

During fiscal 1983 the Company invested approximately \$20 million dollars in adjustable rate preferred stock purchased at a premium of \$2,784,000 above par value. The dividend rates on adjustable rate preferred stocks are revised each quarter based on changes in various money market rates. For federal income tax purposes, 85% of the dividends received on these securities are exempt from tax. During the three years ended March 31, 1985, the carrying values of these securities were reduced for the estimated permanent impairment in their market values. These securities were sold during fiscal 1985 at a loss of \$1,245,000, which represents the difference between the sales proceeds and the carrying values of the securities.

Note 6-Preferred and common stock, and initial public offering

On December 10, 1982, the Company sold 1,673,000 shares of common stock at \$20.50 per share in connection with an initial public offering. Proceeds to the Company were \$31,474,000 after deducting related costs. Coincident with the initial public offering, all outstanding preferred stock was converted to common stock.

The previously outstanding preferred stock was issued in three separate series of non-cumulative convertible stock. Series A and Series B shares were convertible into four shares of common stock and Series C shares were convertible into two shares of common stock.

Note 7-Stock purchase agreements

Under the terms of stock purchase agreements, shares were sold to employees at prices determined by the Board of Directors. Shares acquired under terms of these agreements vest on a graduated basis over five years. During this period, the employee may not sell or dispose of the unvested stock. If employment is terminated for any reason other than death or disability during this period, the Company retains the right to repurchase the unvested shares at the original purchase price. In addition, the Company has the first right to repurchase all shares acquired under the plan at a price determined by the terms set forth in the plan.

In January 1982, under a common stock purchase agreement, the Company sold 24,000 common shares to a non-employee director at \$.375 per share, in consideration for his participation on the Board. Shares issued under this agreement vest on a graduated basis during the four years following issuance. During this period the director may not sell or otherwise dispose of unvested stock. If the director should cease to serve on the Board, the Company has the right to repurchase the unvested shares at the original sales price. In addition, during this period, the Company has the first right to repurchase the shares issued to the director at a price determined in accordance with the agreement.

During the year ended March 31, 1982 and the period from February 20, 1980 (inception) through March 31, 1981, 340,000 and 1,761,000 shares of common stock, respectively, were sold to employees under the agreements. During fiscal 1985, 1984 and 1983, 0, 867, and 49,133 shares respectively, were reacquired by the Company.

Note 8-Stock option plan

In September 1981, the Company adopted the 1981 Incentive Stock Option Plan. Under this plan, 850,000 shares of common stock were reserved for issuance to eligible employees. Options under the plan are granted at prices determined by the Board of Directors, but not less than the fair market value, as determined by the Board, on the date of grant and expire five years after the date of grant. Generally, one-fifth of the grant becomes exercisable after the first year following the grant, and at one-sixtieth per month thereafter. At March 31, 1985 options with respect to 99,400 shares of common stock were available for grant.

A summary of transactions relating to outstanding stock options follows:

Year ended March 31	1985		1984	
	Shares	Option Price	Shares	Option Price
Options outstanding beginning of period	470,800	\$.19-30.25	415,000	\$.19-26.75
Options granted	224,700	17.00-20.00	139,200	16.50-30.25
Options cancelled	(32,800)	.38-30.25	(11,500)	.38-22.00
Options exercised	(92,100)	.19-22.00	(71,900)	.19- 4.00
Options outstanding end of period	570,600	\$.19-30.25	470,800	\$.19-30.25
Options exercisable end of period	41,478		39,418	

In November of 1984, the Company adopted the 1984 Incentive Stock Option Plan, and reserved 300,000 shares of common stock for issuance to eligible employees and consultants of the Company. The terms of this plan are essentially identical to those of the 1981 Incentive Stock Option Plan. No options had been granted under the plan as of March 31, 1985.

Note 9 - Employee Stock Purchase Plan

In November 1982, the Board of Directors approved the adoption of an Employee Stock Purchase Plan (the "Purchase Plan") and reserved 100,000 shares of common stock for purchase by eligible employees at the lower of 85% of the fair market value of the common stock at the beginning or at the end of each six month offering period. The Purchase Plan permits eligible employees to purchase common stock through payroll deductions, which may not exceed 10% of an employee's compensation.

During fiscal 1985 and 1984, 30,994 and 17,647 shares were issued under this plan.

Note 10 - Income taxes

The components for the provision for income taxes are presented below.

Year ended March 31	1985	1984	1983
Current - Federal	\$5,468,000	\$6,812,000	\$2,787,000
- State	3,124,000	1,945,000	990,000
Deferred - Federal	1,111,000	(125,000)	998,000
- State	(14,000)	(82,000)	239,000
Charge in lieu of Federal income taxes			814,000
Total provision for income taxes	\$9,689,000	\$8,550,000	\$5,828,000

Deferred (prepaid) income taxes represent the tax effect of transactions which are reported in different periods for financial and tax reporting purposes.

The sources of deferred (prepaid) income taxes and the income tax effect of each are as follows:

Year ended March 31	1985	1984	1983
Installment sales receivable	\$ (419,000)	\$ 116,000	\$ 879,000
Excess of tax over book depreciation	486,000	366,000	329,000
Taxable portion of DISC income not currently deductible	(63,000)	172,000	131,000
Inventory valuation allowances	(135,000)	(673,000)	
Accrued warranty expense	(191,000)	(269,000)	(148,000)
Deferred tax on income from Puerto Rico operations	1,545,000	102,000	
Other	(126,000)	(21,000)	26,000
	\$1,097,000	\$ (207,000)	\$1,217,000

As a result of the provisions of the recently enacted "Deficit Reduction Act of 1984," the Company's Domestic International Sales Corporation (DISC) terminated on December 31, 1984, and income taxes on accumulated earnings will be permanently forgiven. Since it has been the intention of the Company to reinvest indefinitely the earnings of its DISC, income taxes have not previously been provided on the accumulated DISC earnings. Accordingly, this change in the DISC rules has no effect on net earnings.

The Company's effective income tax rate for the years ended March 31, 1985, March 31, 1984 and March 31, 1983 varies from the 46% statutory federal rate for the following reasons:

Year ended March 31	1985		1984		1983	
Taxes computed at the statutory rate	\$14,105,000	46.0%	\$8,843,000	46.0%	\$5,912,000	46.0%
State income tax, net of federal benefit	1,292,000	4.2	1,005,000	5.2	664,000	5.1
Investment tax credits, net of recapture	(298,000)	(1.0)	(302,000)	(1.5)	(290,000)	(2.3)
Research and development tax credits	(590,000)	(1.9)			(310,000)	(2.4)
Dividend exclusion	(372,000)	(1.2)	(762,000)	(4.0)	(140,000)	(1.0)
Non-deductible loss on stock	572,000	1.8				
Reduced tax rate of Puerto Rican operations	(5,189,000)	(16.9)	(332,000)	(1.7)		
Other	169,000	0.6	98,000	0.5	(8,000)	(0.1)
Provision for income taxes	\$ 9,689,000	31.6%	\$8,550,000	44.5%	\$5,828,000	45.3%

Note 11-Commitments

The Company leases its present facilities and certain equipment under non-cancellable operating lease agreements that range from 5 to 10 years. Some of the leases have renewal options ranging from 5 to 10 years.

Equipment is leased through a bank for a five-year term expiring in 1986. This lease agreement requires, among other things, the Company to maintain certain financial covenants including specified minimum current ratio, working capital, tangible net worth and cash position levels and a maximum debt to tangible net worth ratio.

Rent expense charged to income is as follows:

Year ended March 31	1985	1984	1983
Rental expense	\$1,912,000	\$1,546,000	\$1,232,000
Sub-lease rental income	(282,000)	(235,000)	
Net rental expense	\$1,630,000	\$1,311,000	\$1,232,000

Future minimum lease payments under operating leases are as follows:

Year ended March 31	
1986	\$2,122,000
1987	2,047,000
1988	1,206,000
1989	889,000
1990	889,000
Thereafter	1,458,000
Total future minimum lease payments	8,611,000
Future minimum sub-lease income	(47,000)
Net future minimum lease payments	\$8,564,000

Note 12 - Unaudited quarterly consolidated financial data

1985:	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Net sales	\$25,377,000	\$30,085,000	\$31,798,000	\$33,089,000	\$120,349,000
Gross profit	9,015,000	11,268,000	12,979,000	13,419,000	46,681,000
Net income	4,271,000	4,687,000	5,949,000	6,066,000	20,973,000
Earnings per share	\$.45	\$.49	\$.62	\$.63	\$2.19
1984:					
Net sales	\$12,473,000	\$15,143,000	\$17,515,000	\$21,938,000	\$ 67,069,000
Gross profit	4,988,000	6,069,000	6,754,000	8,127,000	25,938,000
Net income	2,074,000	2,485,000	2,885,000	3,229,000	10,673,000
Earnings per share	\$.22	\$.26	\$.30	\$.34	\$1.12

The effective tax rate in the fourth quarter of 1985 is lower than in the preceding three quarters because earnings on Puerto Rico operations, which are subject to lower taxes, represented a higher percentage of total earnings than had been expected.

Report of Independent Accountants

To the Shareholders and
Board of Directors of
Quantum Corporation

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, shareholders' equity and changes in financial position present fairly the financial position of Quantum Corporation and its subsidiaries at March 31, 1985 and 1984, and the results of their operations and the changes in their financial position for each of the three years in the period ended March 31, 1985, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Price Waterhouse

San Jose, California
May 14, 1985

PRICE WATERHOUSE

Common Stock Trading Range

Quantum Corporation's common stock has been traded in the over-the-counter market under the NASDAQ symbol QNTM since the Company's initial public offering on December 10, 1982. The price per share reflected in the table represents the range of high and low closing bid prices prior to May 9, 1983 and the closing prices in the NASDAQ National Market System after such date, for the quarter indicated.

	High	Low
Fiscal 1985		
Fourth quarter ended March 31, 1985	30	20
Third quarter ended December 29, 1984	21 ³ / ₄	17 ¹ / ₄
Second quarter ended September 29, 1984	22 ³ / ₄	16 ³ / ₄
First quarter ended June 30, 1984	21 ¹ / ₄	16 ¹ / ₂
Fiscal 1984		
Fourth quarter ended March 31, 1984	20 ¹ / ₂	16
Third quarter ended December 31, 1983	23 ¹ / ₄	16 ¹ / ₂
Second quarter ended October 1, 1983	30 ¹ / ₂	18
First quarter ended July 2, 1983	34 ³ / ₄	27 ¹ / ₂

The Company has not paid cash dividends on its common stock and does not plan to pay cash dividends to its shareholders in the near future. The Company presently intends to retain its earnings to finance future growth of its business.

As of June 6, 1985 there were approximately 6,749 shareholders of the Company.

Board of Directors

Frank J. Caufield
*General Partner, Kleiner
Perkins, Caufield & Byers
(Venture capital
investments)*

Glenn M. Mueller
*General Partner,
Mayfield III and IV
(Venture capital
investments)*

James L. Patterson
*President and Chief
Executive Officer,
Quantum Corporation*

Robert E. Schroeder
*President and Chief
Executive Officer,
International Power
Technology
(Supplier of gas turbine
based co-generation systems)*

Officers

James L. Patterson
*President and
Chief Executive Officer*

Arthur P. Geffon
*Vice President,
Engineering*

Joseph Shepela
*Vice President,
Human Resources*

Joseph T. Rodgers, Jr.
*Vice President, Finance
Secretary and Treasurer*

Richard P. Taylor
*Vice President,
Manufacturing*

James G. Watson
Vice President, Marketing

Sales Offices

2 Industrial Way
Salem, NH 03079
Telephone: (603) 893-2672

125 Gaither Drive
Suite H
Mount Laurel, NJ 08054
Telephone: (609) 778-9046

1931 North Meacham Road
Suite 341
Schaumburg, IL 60195
Telephone: (312) 397-7410

4633 Old Ironsides Drive
Suite 270
Santa Clara, CA 95054
Telephone: (408) 980-8555

2659 Townsgate Road
Suite 101
Westlake Village, CA 91361
Telephone: (805) 495-7955

1000 Westlake High Drive
Suite 4B
Austin, TX 78746
Telephone: (512) 327-9322

Quantum GmbH
Hahnstrasse 70
D-6000 Frankfurt/M. 71
West Germany
Telephone 69-666-6167

**A copy of the Company's
Annual Report on
Form 10-K, as filed with the
Securities and Exchange
Commission, is available
from the Company
without charge. Please
direct your request to:**

**Joseph T. Rodgers, Jr.
Vice President, Finance
Secretary and Treasurer
Quantum Corporation
1804 McCarthy Blvd.
Milpitas, CA 95035**

**Legal Counsel
Wilson, Sonsini, Goodrich
& Rosati
Two Palo Alto Square
Palo Alto, CA 94304**

**Transfer Agent
Bank of America
555 California Street
San Francisco, CA 94104**

**The Annual Meeting of
Shareholders of Quantum
Corporation will be held
at 3:00 p.m. on August 16,
1985 in the Red Lion Inn,
2050 Gateway Place,
San Jose, CA**

*IBM and IBM PC are registered trademarks of International Business Machines Corporation.
Q2000 Series and Q500 Series are registered trademarks of Quantum Corporation.
Q200 Series is a trademark of Quantum Corporation.
Hardcard is a trademark of Plus Development Corporation.*

Designed and Produced by Torme Design
Photography by Dana Gluckstein
Written by Fenimore & Associates



Quantum Corporation
1804 McCarthy Blvd.
Milpitas, CA 95035

Jim Patterson