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

FORM 8-K/A

CURRENT REPORT
Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): September 5, 2007

WESTERN DIGITAL CORPORATION
(Exact Name of Registrant as Specified in its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**001-08703** (Commission File Number)	**33-0956711** (I.R.S. Employer Identification No.)

20511 Lake Forest Drive **Lake Forest, California** (Address of Principal Executive Offices)	**92630** (Zip Code)

(949) 672-7000
(Registrant’s Telephone Number, Including Area Code)

Not applicable
(Former name or former address, if changed since last report.)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 240.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

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On September 5, 2007 Western Digital Corporation ("Parent") filed a Current Report on Form 8-K stating, among other things, that it had completed its acquisition of Komag, Incorporated and that the financial statements and pro forma financial information required under Item 9.01 would be filed not later than 71 calendar days after the date the Form 8-K was required to be filed. This amendment restates in its entirety Item 9.01 of the Current Report on Form 8-K to include the required financial statements and pro forma financial information.

Item 9.01. Financial Statements and Exhibits.

(a) *Financial Statements of Business Acquired*

The report of KPMG LLP, Komag, Incorporated's Independent Registered Public Accounting Firm, which was filed with Komag, Incorporated's annual report on Form 10-K for the year ended December 31, 2006, is filed as Exhibit 99.2 to this amendment and incorporated herein by reference.

The audited consolidated balance sheet of Komag, Incorporated as of December 31, 2006 and the related consolidated statements of income, stockholders' equity and comprehensive income and cash flows for the year ended December 31, 2006, and the notes related thereto, which were filed in Komag, Incorporated's annual report on Form 10-K for the year ended December 31, 2006, are filed as Exhibit 99.3 to this amendment and incorporated herein by reference.

The unaudited consolidated condensed balance sheet of Komag, Incorporated as of July 1, 2007 and the unaudited consolidated condensed statements of operations and cash flows for the three and six month periods ended July 1, 2007, and the notes related thereto, which were filed in Komag, Incorporated's quarterly report on Form 10-Q for the quarter ended July 1, 2007, are filed as Exhibit 99.4 to this amendment and incorporated herein by reference.

(b) *Pro Forma Financial Information*

The following information is filed as Exhibit 99.5 to this amendment and incorporated herein by reference:

(i) Unaudited Pro Forma Condensed Combined Balance Sheet as of June 29, 2007, and the unaudited Pro Forma Condensed Combined Statement of Operations for the year ended June 29, 2007.

(ii) Notes to the Unaudited Pro Forma Condensed Combined Balance Sheet as of June 29, 2007 and Unaudited Pro Forma Condensed Combined Statement of Operations for the year ended June 29, 2007.

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(d) Exhibits

Exhibit No.	
23.1	Consent of KPMG LLP, Independent Registered Public Accounting Firm
99.1	Press Release, dated September 5, 2007 (incorporated by reference to Western Digital Corporation's Current Report on Form 8-K filed on September 5, 2007)
99.2	Reports of Independent Registered Public Accounting Firm
99.3	The audited consolidated balance sheets of Komag, Incorporated as of December 31, 2006 and the consolidated statements of income, stockholders' equity and comprehensive income and cash flows of Komag, Incorporated for the year ended December 31, 2006, and the notes related thereto
99.4	The unaudited consolidated condensed balance sheet of Komag, Incorporated as of July 1, 2007 and the unaudited consolidated condensed statements of operations and cash flows for the three and six month periods ended July 1, 2007, and the notes related thereto
99.5	Unaudited Pro Forma Condensed Combined Financial Statements as of and for the year ended June 29, 2007

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SIGNATURE

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 hereunto duly authorized.

WESTERN DIGITAL CORPORATION
(Registrant)

Date: November 19, 2007

By: /s/ Raymond M. Bukaty
Raymond M. Bukaty
Senior Vice President, Administration, General Counsel and Secretary

EXHIBIT INDEX

Exhibit No.	Description
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99.4	The unaudited consolidated condensed balance sheet of Komag, Incorporated as of July 1, 2007 and the unaudited consolidated condensed statements of operations and cash flows for the three and six month periods ended July 1, 2007, and the notes related thereto
99.5	Unaudited Pro Forma Condensed Combined Financial Statements as of and for the year ended June 29, 2007

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We consent to the inclusion in the accompanying Exhibit 99.2 and incorporation by reference in the current report on Form 8-K of Western Digital Corporation, of our report dated February 21, 2007, with respect to the consolidated balance sheets of Komag, Incorporated and subsidiaries (“the Company”) as of December 31, 2006 and January 1, 2006 and the related consolidated statements of income, stockholders’ equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2006 and the related financial statement schedule, and our report dated February 21, 2007, with respect to management’s assessment of the effectiveness of internal control over financial reporting as of December 31, 2006, and the effectiveness of internal control over financial reporting as of December 31, 2006, which reports appear in the accompanying Exhibit 99.2 and in the December 31, 2006 annual report on Form 10-K of Komag, Incorporated, incorporated herein by reference.

As discussed in Note 11 to the consolidated financial statements, the Company changed its method of accounting for stock-based compensation in 2006 upon adoption of Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment*.

/s/ KPMG LLP
Mountain View, California
November 14, 2007

Exhibit 99.2

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Komag, Incorporated:

We have audited the accompanying consolidated balance sheets of Komag, Incorporated and subsidiaries (the Company) as of December 31, 2006 and January 1, 2006 and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2006. In connection with our audits of the consolidated financial statements, we also have audited financial statement Schedule II. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Komag, Incorporated and subsidiaries as of December 31, 2006 and January 1, 2006, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 11 to the consolidated financial statements, the Company changed its method of accounting for stock-based compensation in 2006 upon adoption of Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment.*

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 21, 2007 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG LLP

Mountain View, California
February 21, 2007

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Komag, Incorporated:

We have audited management's assessment, included in the accompanying *Management's Report on Internal Control over Financial Reporting* in Item 9A, Controls and Procedures, that Komag, Incorporated and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in *Internal Control — Integrated Framework* issued by COSO. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control — Integrated Framework* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Komag, Incorporated and subsidiaries as of December 31, 2006 and January 1, 2006, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2006. In connection with our audits of the consolidated financial statements, we also have audited financial statement Schedule II. Our report dated February 21, 2007 expressed an unqualified opinion on those consolidated financial statements and financial statement schedule.

/s/ KPMG LLP

Mountain View, California
February 21, 2007

Exhibit 99.3

KOMAG, INCORPORATED

CONSOLIDATED STATEMENTS OF INCOME

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
	(In thousands, except per share amounts)		
Net sales	$ 937,676	$ 685,946	$ 458,377
Cost of sales	689,994	497,213	346,260
Gross profit	247,682	188,733	112,117
Operating expenses:			
Research, development, and engineering	64,185	48,873	40,783
Selling, general, and administrative	34,409	23,622	17,980
Gain on disposal of assets	(364)	(1,694)	(1,028)
	98,230	70,801	57,735
Operating income	149,452	117,932	54,382
Other income (expense):			
Interest income	7,007	5,327	1,371
Interest expense	(1,764)	(1,765)	(3,176)
Other expense, net	(426)	(415)	(151)
	4,817	3,147	(1,956)
Income before income taxes	154,269	121,079	52,426
Provision for (benefit from) income taxes	(3,264)	5,442	1,071
Net income	$ 157,533	$ 115,637	$ 51,355
Basic net income per share	$ 5.27	$ 3.99	$ 1.88
Diluted net income per share	$ 4.75	$ 3.55	$ 1.71
Number of shares used in basic per share computations	29,919	29,003	27,384
Number of shares used in diluted per share computations	33,566	33,042	31,017

See accompanying notes to consolidated financial statements.

KOMAG, INCORPORATED

CONSOLIDATED BALANCE SHEETS

	December 31, 2006	January 1, 2006
	(In thousands)	
ASSETS		
Current assets		
Cash and cash equivalents	$ 129,632	$ 99,984
Short-term investments	41,500	105,050
Accounts receivable (less allowances of $2,326 and $2,866, respectively)	140,230	116,217
Inventories	104,181	54,000
Prepaid expenses and other current assets	2,119	1,846
Total current assets	417,662	377,097
Property, plant, and equipment, net	542,585	351,046
Deferred income taxes	7,346	—
Other assets	10,094	3,308
	$ 977,687	$ 731,451
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Trade accounts payable	$ 139,477	$ 97,901
Customer advances	127,181	102,898
Accrued expenses and other liabilities	25,412	28,585
Total current liabilities	292,070	229,384
Long-term debt	80,500	80,500
Deferred rent	3,091	2,562
Total liabilities	375,661	312,446
Stockholders' equity		
Common stock, $0.01 par value per share:		
Authorized — 120,000 shares		
Issued and outstanding — 31,178 and 30,092 shares, respectively	312	301
Additional paid-in capital	283,679	267,920
Deferred stock-based compensation	—	(9,695)
Accumulated other comprehensive loss	(611)	(634)
Retained earnings	318,646	161,113
Total stockholders' equity	602,026	419,005
	$ 977,687	$ 731,451

See accompanying notes to consolidated financial statements.

KOMAG, INCORPORATED

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31, 2006	Year Ended January 1, 2006	Year Ended January 2, 2005
	(In thousands)		
Operating Activities			
Net income	$ 157,533	$ 115,637	$ 51,355
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization of property, plant, and equipment	79,488	44,519	37,086
Deferred income tax benefit	(6,978)	—	—
Tax provision charged to additional paid-in capital	2,971	5,194	—
Amortization and adjustments of intangible assets	231	1,072	3,023
Stock-based compensation	18,086	3,308	555
Deferred rent	529	2,562	—
Non-cash interest charges	154	154	436
Gain on disposal of assets	(364)	(1,694)	(1,028)
Foreign exchange loss	1,309	—	—
Changes in operating assets and liabilities:			
Accounts receivable, net	(23,939)	(37,004)	(18,585)
Inventories	(50,181)	(18,185)	(10,314)
Prepaid expenses and other current assets	181	(31)	221
Trade accounts payable	51,728	18,741	3,338
Customer advances	24,283	102,898	—
Accrued expenses and other liabilities	(3,591)	8,353	(4,820)
Other non-current assets	(7,066)	—	—
Net cash provided by operating activities	244,374	245,524	61,267
Investing Activities			
Acquisition of property, plant, and equipment	(286,082)	(155,613)	(59,202)
Purchases of short-term investments	(157,755)	(282,450)	(157,000)
Proceeds from short-term investments	221,305	255,100	122,150
Proceeds from disposal of property, plant, and equipment	456	3,173	2,038
Other	(42)	(34)	(257)
Net cash used in investing activities	(222,118)	(179,824)	(92,271)
Financing Activities			
Payment of debt	—	—	(116,341)
Proceeds from the issuance of long-term debt	—	—	77,419
Proceeds from sale of common stock, net of issuance costs	5,630	7,874	69,128
Repurchase of common stock	(2,044)	—	—
Net cash provided by financing activities	3,586	7,874	30,206
Effect of exchange rate changes on cash and cash equivalents	3,806	—	—
Increase (decrease) in cash and cash equivalents	29,648	73,574	(798)
Cash and cash equivalents at beginning of year	99,984	26,410	27,208
Cash and cash equivalents at end of year	$ 129,632	$ 99,984	$ 26,410
Supplemental disclosure of cash flow information			
Cash paid for interest	$ 1,610	$ 1,611	$ 2,739
Cash paid for income taxes	$ 908	$ 541	$ 331

See accompanying notes to consolidated financial statements.

KOMAG, INCORPORATED

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

	Common Stock		Additional Paid-in Capital	Deferred Stock-Based Compensation	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total
	Shares	Amount					
	(In thousands)						
Balance at December 28, 2003	23,753	$ 238	$172,457	$ (228)	$ (5,879)	$ —	$166,588
Net income	—	—	—	—	51,355	—	51,355
Issuance of common stock, net of issuance costs	3,525	35	66,356	—	—	—	66,391
Deferred stock-based compensation	—	—	252	(252)	—	—	—
Stock-based compensation	—	—	166	389	—	—	555
Exercise of warrants	90	1	1	—	—	—	2
Common stock issued under stock plans	697	7	2,728	—	—	—	2,735
Balance at January 2, 2005	28,065	281	241,960	(91)	45,476	—	287,626
Net income	—	—	—	—	115,637	—	115,637
Unrealized loss on cash flow hedging arrangements	—	—	—	—	—	(634)	(634)
Comprehensive income							115,003
Deferred stock-based compensation	—	—	12,769	(12,769)	—	—	—
Stock-based compensation	—	—	143	3,165	—	—	3,308
Income tax adjustments	—	—	5,194	—	—	—	5,194
Exercise of warrants	604	6	2,103	—	—	—	2,109
Common stock issued under stock plans	1,423	14	5,751	—	—	—	5,765
Balance at January 1, 2006	30,092	301	267,920	(9,695)	161,113	(634)	419,005
Net income	—	—	—	—	157,533	—	157,533
Net change to unrealized gain or loss under cash flow hedging arrangements	—	—	—	—	—	23	23
Comprehensive income							157,556
Reversal of deferred stock-based compensation	—	—	(9,695)	9,695	—	—	—
Stock-based compensation	—	—	18,086	—	—	—	18,086
Income tax adjustments	—	—	3,793	—	—	—	3,793
Common stock issued under stock plans	1,139	11	5,619	—	—	—	5,630
Repurchase of common stock	(53)	—	(2,044)	—	—	—	(2,044)
Balance at December 31, 2006	31,178	$ 312	$283,679	$ —	$ 318,646	$ (611)	$602,026

See accompanying notes to consolidated financial statements.

Note 1. Basis of Presentation and Significant Accounting Policies

Company Business: The Company is a leading independent supplier of thin-film disks, the primary high-capacity storage medium for digital data in computers and consumer electronic appliances. Since it was founded in 1983, the Company has been an industry leader in production volume and technology for thin-film disks.

Consolidation: The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Fiscal Year: The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. The Company’s 2006 and 2005 fiscal years were 52-week years. The Company’s 2004 fiscal year was a 53-week year; accordingly, the additional week in 2004 was included in the Company’s first quarter of 2004.

Use of Estimates in the Preparation of Financial Statements: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S.) requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Foreign Currency Translation: The Company’s functional currency for its Malaysian operations is the U.S. dollar. Remeasurement gains and losses resulting from the process of remeasuring these foreign currency financial statements into U.S. dollars are included in operations.

Cash and Cash Equivalents: The Company considers as a cash equivalent any bank deposit, money market investments and any highly-liquid investment that has an original maturity date of three months or less at the date of purchase.

Short-Term Investments: The Company invests its excess cash in high-quality, short-term debt instruments and auction rate preferred securities. The Company’s investments are considered “available-for-sale” under SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (SFAS 115). The costs of the Company’s investments approximate fair value; accordingly, there were no unrealized gains or losses as of December 31, 2006 and January 1, 2006. Interest and dividends on the investments are included in interest income. The information in the following table (in thousands) reflects a summary of the Company’s investments by major security type at amortized cost, which approximates fair value:

	December 31, 2006	January 1, 2006
Municipal auction rate preferred securities	$ 41,500	$ 105,050
Corporate debt securities	76,529	73,168
Mortgage-backed securities	10,672	13,527
	$ 128,701	$ 191,745
Amounts included in cash and cash equivalents	$ 87,201	$ 86,695
Amounts included in short-term investments	41,500	105,050
	$ 128,701	$ 191,745

Inventories: Inventories are stated at the lower of cost (first-in, first-out method) or market, and consist of the following (in thousands):

	December 31, 2006	January 1, 2006
Raw materials	$ 78,701	$ 39,230
Work in process	15,900	6,489
Finished goods	9,580	8,281
	$ 104,181	$ 54,000

Property, Plant, and Equipment: Property, plant, and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is recognized using the straight-line method over the estimated useful lives of the assets. The estimated useful lives of the Company's buildings in Penang and Sarawak, Malaysia is 30 years, and 22 years for the Company's building in Johor, Malaysia. Furniture and equipment are generally depreciated over five years, and leasehold improvements are amortized over the shorter of the lease term or their estimated useful life.

Property, plant, and equipment consists of the following (in thousands):

	December 31, 2006	January 1, 2006
Land	$ 8,206	$ 8,206
Buildings	221,571	153,433
Leasehold improvements	5,499	3,974
Furniture	3,959	1,968
Equipment	522,738	324,123
	761,973	491,704
Less accumulated depreciation and amortization	(219,388)	(140,658)
	$ 542,585	$ 351,046

Impairment of Long-lived Assets: Long-lived assets are evaluated for impairment whenever events or changes in circumstances indicate that such assets may be impaired or the estimated useful lives are no longer appropriate. The Company reviews its long-lived assets for impairment based on estimated future undiscounted cash flows attributable to the assets. In the event that such cash flows are not expected to be sufficient to recover the recorded value of the assets, the assets are written down to their estimated fair values utilizing discounted estimates of future cash flows.

Revenue Recognition: In recognizing revenue, the Company applies the provisions of the Securities and Exchange Commission (SEC) Staff Accounting Bulletin 104, *Revenue Recognition*. The Company recognizes revenue from the sale of its products when persuasive evidence of an arrangement exists, the product has been delivered, the price is fixed or determinable, and collection of the resulting receivable is reasonably assured. Amounts billed to customers for shipping and handling costs associated with products sold are classified as revenue.

The Company generally uses a purchase order as evidence of an arrangement. In certain cases its products are sold with terms signifying that delivery occurs at the destination point. The Company defers revenue associated with these transactions until the delivery has occurred to the customers' premises and it has evidence of such delivery.

The Company provides an allowance for estimated returns of defective products based on historical data, as well as current knowledge of product quality.

Cost of Sales: Cost of sales includes direct and indirect manufacturing costs, inbound, outbound, and internal freight costs, purchasing and receiving costs, quality inspection costs, and warehousing costs.

Research and Development: Research and development costs are expensed as incurred.

Leases: The Company leases one facility in the U.S. The Company accounts for this lease as an operating lease under the provisions of SFAS No. 13, *Accounting for Leases* (SFAS 13), and subsequent amendments. SFAS 13 requires leases to be evaluated and classified as operating or capitalized leases for financial reporting purposes. In addition, the Company records the total rent payable during the operating lease term as an expense on a straight-line basis over the term of the lease, and records the difference between the rent paid and the straight-line rent expense as a deferred rent liability.

Stock-Based Compensation: Effective January 2, 2006, the Company adopted SFAS No. 123R, *Share-Based Payment* (SFAS 123R), using the modified prospective method, in which compensation cost is recognized based on the requirements of SFAS 123R for (a) all share-based payments granted or modified after the effective date and (b) for all awards granted to employees prior to the effective date of SFAS 123R that remain unvested on the effective date. The Company elected to amortize stock-based compensation for awards outstanding and unvested on its adoption of SFAS 123R as well as for awards granted on or after its adoption of SFAS 123R on a straight line basis over the requisite service (vesting) period for the entire award. The vesting period for stock options has generally been four years and the vesting for stock purchase rights generally has been three years.

Prior to January 2, 2006 and as permitted under SFAS No. 123, *Accounting for Stock-Based Compensation* (SFAS 123), the Company elected to follow APB 25, and related interpretations in accounting for stock-based awards to employees. Accordingly, compensation cost for stock options and stock purchase rights was measured as the excess, if any, of the market price of the Company's common stock at the date of grant over the exercise price. In accordance with SFAS 123 and SFAS No. 148, *Accounting for Stock-Based Compensation — Transition and Disclosure — an Amendment of SFAS 123*, prior to fiscal 2006, the Company provided pro forma disclosure of the effect on net income and earnings per share had the fair value method been used, as prescribed by SFAS 123.

Income Taxes: The Company accounts for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and for operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using the enacted tax laws expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Realization of deferred tax assets is dependent upon future earnings in specific tax jurisdictions, the timing and amount of which are uncertain. Accordingly, the Company evaluates all significant available positive and negative evidence, including the existence of losses in recent years and the forecast of future taxable income, in assessing the need for a valuation allowance. The Company records a valuation allowance to reduce its deferred tax assets to the amount that is believed more likely than not to be realized.

Comprehensive Income: Comprehensive income is defined as the change in equity during a period for non-owner transactions, and is composed of net income and other comprehensive income (loss). Other comprehensive income (loss) includes revenues, expenses, gains, and losses that are excluded from earnings under current accounting standards. The Company's other comprehensive loss included the unrealized losses, net of income taxes, related to the Company's foreign currency forward contracts that are designated as cash flow hedges.

Computation of Net Income Per Share: The Company determines net income per share in accordance with SFAS No. 128, Earnings per Share. Basic net income per common share is computed by dividing income available to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted net income per share is computed by dividing income available to common stockholders by the weighted-average number of shares and dilutive potential shares of common stock outstanding during the period. The dilutive effect of outstanding options and stock purchase rights is reflected in diluted net income per share by application of the treasury stock method. The dilutive effect of outstanding contingently convertible debt is reflected in diluted net income per share by application of the if-converted method. Interest expense related to the contingently convertible debt is an adjustment to income available to common stockholders for the diluted net income per share calculations.

The following table sets forth the computation of net income per share. The table is in thousands, except per share amounts.

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Numerator for basic net income per share:			
Net income as reported	$ 157,533	$ 115,637	$ 51,355
Numerator for diluted net income per share:			
Net income as reported	$ 157,533	$ 115,637	$ 51,355
Interest adjustment related to contingently convertible debt	1,764	1,765	1,642
	$ 159,297	$ 117,402	$ 52,997
Denominator for basic net income per share:			
Weighted average shares	29,919	29,003	27,384
Denominator for diluted net income per share:			
Weighted average shares	29,919	29,003	27,384
Effect of dilutive securities:			
Contingently convertible shares under convertible debt	3,049	3,049	2,803
Stock options	343	572	468
Warrants	—	220	362
Stock purchase rights	255	198	—
	33,566	33,042	31,017
Basic net income per share	$ 5.27	$ 3.99	$ 1.88
Diluted net income per share	$ 4.75	$ 3.55	$ 1.71

Outstanding common stock options that were not included in the diluted net income per share computation because the effect would have been anti-dilutive were approximately 42,000 in 2006, zero in 2005, and approximately 264,000 in 2004.

In January 2004, the Company issued $80.5 million of 2.0% Convertible Subordinated Notes (the Notes). The Notes are convertible, under certain circumstances, into shares of the Company’s common stock at an initial conversion price of $26.40, or approximately 3,049,000 shares. These shares have been included in the Company’s diluted earnings per share calculations for fiscal 2006, 2005 and 2004.

Recent Accounting Pronouncements: In December 2004, the FASB issued SFAS No. 151, Inventory Costs (SFAS 151). SFAS 151 clarifies the accounting for inventory when there are abnormal amounts of idle facility expense, freight, handling costs, and wasted materials. Under existing generally accepted accounting principles, items such as idle facility expense, excessive spoilage, double freight, and re-handling costs may be “so abnormal” as to require treatment as current period charges rather than recorded as adjustments to the value of the inventory. SFAS 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of “so abnormal.” In addition, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The provisions of this Statement are effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The Company adopted this pronouncement at the beginning of fiscal year 2006. The adoption of SFAS 151 had no material impact on the Company's financial position or results of operations.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections* (SFAS 154). SFAS 154 replaces APB No. 20 and FASB Statement No. 3. SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application as the required method for reporting a change in accounting principle. SFAS 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. The reporting of a correction of an error by restating previously issued financial statements is also addressed by SFAS 154. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company adopted SFAS 154 in fiscal 2006. The adoption of this standard had no material impact on the Company's financial position or results of operations.

In June 2006, the FASB issued FIN No. 48, *Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 provides guidance on recognition and measurement of uncertainties in income taxes and is applicable for fiscal years beginning after December 15, 2006. The Company does not expect the adoption of this Interpretation to have a material impact on its financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements and is applicable for fiscal years beginning after November 15, 2007. The Company has not yet completed the evaluation or determined the impact of adopting SFAS 157.

In September 2006, the SEC released Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108), which addresses how uncorrected errors in previous years should be considered when quantifying errors in current-year financial statements. SAB 108 requires companies to consider the effect of all carry over and reversing effects of prior-year misstatements when quantifying errors in current-year financial statements. SAB 108 allows companies to record the effects of adopting the guidance as a cumulative-effect adjustment to retained earnings. The Company adopted SAB 108 in the fourth quarter of 2006 and there was no financial impact on its financial statements.

Note 2. Segment and Geographic Information

The Company operates in one business segment, which is the development, production, and marketing of high-performance thin-film media (disks) for use in hard disk drives. The Company primarily sells to original equipment manufacturers in the rigid disk drive market. The Company's operations are treated as one operating segment, as the Company reports profit and loss information on an aggregate basis to the chief operating decision-maker of the Company.

Summary information for the Company's operations by geographic location is as follows (in thousands):

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Net sales:			
To customers from U.S. parent	$ 29,912	$ 37,021	$ 21,520
To customers from Malaysian subsidiary	907,764	648,925	436,857
Intercompany from Malaysian subsidiary	19,584	24,284	20,868
Intercompany from U.S. parent	986	808	170
	958,246	711,038	479,415
Intercompany eliminations	(20,570)	(25,092)	(21,038)
Total net sales	$ 937,676	$ 685,946	$ 458,377
Operating income (loss):			
U.S. parent	$ (14,520)	$ 1,604	$ (5,823)
Malaysian subsidiary	163,972	116,328	60,205
Total operating income	$ 149,452	$ 117,932	$ 54,382
Long-lived assets:			
U.S. parent	$ 36,357	$ 31,475	
Malaysian subsidiary	506,228	319,571	
Total long-lived assets	$ 542,585	$ 351,046	

External sales by geographic location, which is determined by the customers' sold-to address, are as follows (in thousands):

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Thailand	$ 559,770	$ 272,392	$ 111,904
Malaysia	157,340	78,047	42,704
Singapore	93,073	201,007	201,686
China	71,626	65,341	1,792
Taiwan	33,932	32,855	25,940
United States	19,992	33,735	53,535
Europe	1,563	1,574	37
Japan	380	995	20,779
Total net sales	$ 937,676	$ 685,946	$ 458,377

Note 3. Concentration of Customer and Supplier Risk

Most of the Company's sales are derived from a relatively small number of customers, which results in a concentration of credit risk regarding trade receivables. The Company performs ongoing credit evaluations of its customers, and generally requires no collateral for sales to these customers. Based on management's evaluation of potential credit losses and the relative strength of the disk drive industry, the Company believes that an allowance for doubtful accounts as of December 31, 2006 is not required.

Seagate accounted for $57.9 million of the Company's accounts receivable at December 31, 2006, and 36% of its net sales for 2006 (Seagate acquired Maxtor in May of 2006 and therefore we have reflected sales to Maxtor in the Seagate numbers for all of 2006). Western Digital accounted for $46.1 million of the Company's accounts receivable at December 31, 2006, and 37% of its net sales for 2006. Hitachi Global Storage Technologies (HGST) accounted for $28.5 million of the Company's accounts receivable at December 31, 2006, and 23% of its net sales for 2006.

The Company's customers are concentrated in the disk drive industry. Accordingly, the Company's future success depends on the buying patterns of these customers and the continued demand by these customers for the Company's products. Additionally, the disk drive market is characterized by rapidly changing technology, evolving industry standards, changes in end user requirements, and frequent new product introductions and enhancements. The Company's continued success will depend upon its ability to enhance existing products and to develop and introduce, on a timely basis, new products and features that keep pace with technological developments and emerging industry standards. Furthermore, as a result of its international sales, the Company's operations are subject to risks of doing business abroad, including but not limited to, fluctuations in the value of currency, longer payment cycles, and greater difficulty in collecting accounts receivable.

Because of the Company's small customer base, the loss of any one significant customer would have a material impact on the Company's business operations. During the second quarter of 2006, Seagate acquired Maxtor Corporation (Maxtor). Sales to Seagate for all of 2006 include sales to Maxtor. The Company expects to continue to derive a substantial portion of our sales from these customers, and from a small number of other customers. We entered into supply agreements, including certain amendments to these agreements, with Western Digital, Maxtor and Seagate in 2005, and with HGST in the first quarter of 2006. The supply agreement with Maxtor was assigned to Seagate as a result of Seagate's acquisition of Maxtor in May 2006. Under the supply agreements, the Company supplies certain media volumes subject to the terms and conditions of the agreements. The customers are required to pay certain advances to the Company covering future purchases of media from the Company. The customer advances, which totaled $127.2 million and $102.9 million as of December 31, 2006 and January 1, 2006, respectively, are to be repaid to the customers via a credit of a specified dollar amount per disk on future sales.

Significant customers accounted for the following percentages of net sales in 2006, 2005, and 2004:

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Western Digital Corporation	37%	24%	14%
Seagate Technology(1)	36%	16%	4%
Hitachi Global Storage Technologies(2)	23%	21%	29%
Maxtor Corporation	—	32%	47%

(1) Seagate Technology acquired Maxtor Corporation in the second quarter of 2006. Sales to Maxtor for all of 2006 have been presented on a combined basis with Seagate Technology.

(2) Sales to HGST include sales made to its contract manufacturer.

The Company relies on a limited number of suppliers for some of the materials and equipment used in its manufacturing processes, including aluminum blanks, aluminum substrates, nickel plating solutions, polishing and texturing supplies, and sputtering target materials. Kobe Steel, Ltd. is the Company's primary supplier of aluminum blanks, which is a fundamental component in producing disks. The Company also relies on Heraeus Incorporated and Williams Advanced Materials, Incorporated for its sputtering target requirements, and on OMG Fidelity, Incorporated for supplies of nickel plating solutions.

Note 4. Employee Savings and Deferred Profit Sharing Plan

The Company maintains a savings and deferred profit sharing plan. Employees in the United States who meet certain criteria are eligible to participate. In addition to voluntary employee contributions to the plan, the Company matches a portion of each employee's contributions to the plan, up to a maximum amount. The Company contributed a total of $1.4 million to the plan in 2006, $2.2 million in 2005, and $0.8 million in 2004. Plan expenses are included in selling, general, and administrative expenses.

Note 5. Income Taxes

The Company's income (loss) before the provision for income taxes consisted of the following (in thousands):

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Domestic	$ (1,368)	$ 9,311	$ (3,977)
Foreign	155,637	111,768	56,403
	$ 154,269	$121,079	$ 52,426

The Company's provision for (benefit from) income taxes consisted of the following (in thousands):

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
U.S. Federal:			
Current	$ 2,646	$ 4,747	$ —
Deferred	(6,280)	—	—
	(3,634)	4,747	—
U.S. State:			
Current	226	525	1
Deferred	(698)	—	—
	(472)	525	1
Foreign:			
Current	842	170	1,070
Deferred	—	—	—
	842	170	1,070
Total Current	3,714	5,442	1,071
Total Deferred	(6,978)	—	—
Provision for (benefit from) income taxes	$ (3,264)	$ 5,442	$ 1,071

A reconciliation of the actual income tax provision to the expected income tax provision (as measured by the U.S. statutory corporate income tax rate of 35% to pretax earnings) is as follows (in thousands):

	Year Ended		
	December 31, 2006	January 1, 2006	January 2, 2005
Income tax expense at federal statutory rate	$ 53,994	$ 42,378	$ 18,349
State income taxes, net of federal benefit	(472)	525	1
Foreign withholding taxes (refund)	49	—	(182)
Foreign rate differential	(53,685)	(38,431)	(18,489)
Change in valuation allowance	(4,566)	1,176	1,392
Other	1,416	(206)	—
	$ (3,264)	$ 5,442	$ 1,071

Deferred income taxes reflect the tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The significant components of the Company's deferred tax assets and liabilities are as follows (in thousands):

	December 31, 2006	January 1, 2006
Deferred tax assets		
Property, plant and equipment	$ 13,702	$ 16,469
Accrued compensation and benefits	5,144	2,547
Other	4,550	3,772
Tax benefit of net operating loss carryforwards	72,510	75,340
Tax benefit of credit carryforwards	36,090	33,810
Gross deferred tax assets	131,996	131,938
Valuation allowance	(124,196)	(131,938)
Total net deferred tax assets	$ 7,800	$ —

	December 31, 2006	January 1, 2006
Current:		
Gross deferred tax assets	$ 7,326	$ 4,005
Valuation allowance	(6,872)	(4,005)
Net deferred tax assets — current	454	—
Long-term:		
Gross deferred tax assets	124,670	127,933
Valuation allowance	(117,324)	(127,933)
Net deferred tax assets — long-term	7,346	—
Total net deferred tax assets	$ 7,800	$ —

Prior to 2006, the Company had established a full valuation allowance against its deferred tax assets due to the uncertainty regarding its ability to generate sufficient future taxable income. In the fourth quarter of 2006, the Company reassessed the valuation allowance previously established and determined that it was more likely than not that a portion of the deferred tax assets would be realized in 2007. As a result, the Company released a portion of the allowance resulting in an income tax benefit of $7.0 million and a credit to equity of $0.8 million in 2006. The Company will continue to assess the potential realization of the remaining deferred tax assets, and will adjust the valuation allowance in future periods, as appropriate. The recorded valuation allowance against deferred tax assets decreased by $7.7 million in 2006, increased by $4.9 million in 2005, and increased by $3.4 million in 2004. Approximately $7.3 million of the valuation allowance as of December 31, 2006 was attributable to the federal and state income tax benefits of stock compensation deductions, the benefit of which will be credited to additional paid in capital when, and if, realized.

Pursuant to Statement SFAS No. 123R, excess tax benefits associated with the stock awards are not recognized until the associated tax deduction reduces cash taxes payable. As such, the Company has been tracking the deductions attributable to these excess benefits separately. The additional tax benefits of net operating loss and tax credit carryforwards related to the stock awards was $5.5 million in 2006. These excess benefits will not be recognized as a credit to additional paid in capital until such deduction reduces tax payable.

At December 31, 2006, the Company has unrecognized deferred tax assets generated prior to the Company's reorganization in 2002 of approximately $94.5 million. Upon realization of those deferred tax assets, the Company first reduces intangible assets associated with the reorganization to zero and then credits additional paid-in capital. In 2006, the Company utilized $2.9 million of pre-emergence deferred tax assets to reduce taxes payable. In 2005 and 2004, the Company utilized $4.9 million and $1.0 million pre-emergence deferred tax assets to reduce taxes payable, respectively. These deferred tax assets were previously fully reserved by a valuation allowance. The benefit of realizing these deferred tax assets was credited to additional paid-in capital in 2006, 2005 and 2004.

At December 31, 2006, the Company had federal and state net operating loss carryforwards of approximately $208.5 million and $78.5 million, which are available to offset future federal and state taxable income through 2026 and 2016, respectively. In addition, the Company had various federal and state tax credit carryforwards of approximately $46.0 million**,** of which $13.9 million are available to offset future taxable income through 2026, and the remaining $32.1 million are available indefinitely.

The utilization of the Company's net operating loss and tax credit carryforwards are subject to certain annual limitations due to the ownership change, as defined by the Internal Revenue Code of 1986. The annual limitation on these NOL's and credits are $8.4 million and $2.9 million, respectively, for losses and credits generated before June 30, 2002.

The Company's Malaysian manufacturing facilities operate under various tax holidays. The net impact of these tax holidays increased the Company's net income by $47.7 million ($1.59 per basic share and $1.42 per diluted share) in 2006, $41.1 million ($1.42 per basic share and $1.24 per diluted share) in 2005, and $25.1 million ($0.92 per basic share and $0.81 per diluted share) in 2004. In July 2005, the Malaysian government agreed to reset the expiration dates of the existing tax holidays to December 2006 and approved a new, 10-year tax holiday covering all of the Company's Malaysian operations. The new tax holiday commences in January 2007 and expires in December 2016.

A substantial majority of the Company's income is generated by its foreign subsidiaries covered by tax holidays. No federal and state income taxes have been provided on the net undistributed earnings from foreign subsidiaries, which, as of December 31, 2006, amounted to $291.3 million. The net undistributed earnings are intended to finance local operating requirements and to satisfy the intercompany payables to the parent company and are therefore considered permanently reinvested.

Note 6. Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, short-term investments, accounts receivable, and accounts payable approximate their fair values as of December 31, 2006 and January 1, 2006, due to the relatively short period to maturity of these instruments.

As of December 31, 2006 and January 1, 2006, the fair value of the Company's Convertible Subordinated Notes was $115.9 million and $109.9 million, respectively. These values were based on the quoted price of the Notes (which are traded in the open market) as of the last business day of the Company's 2006 and 2005 fiscal years.

Note 7. Accrued Expenses and Other Liabilities

The following table (in thousands) summarizes accrued expenses and other liabilities for fiscal 2006 and fiscal 2005:

	December 31, 2006	January 1, 2006
Accrued compensation and benefits	$ 22,481	$ 24,986
Other liabilities	2,931	3,599
	$ 25,412	$ 28,585

Note 8. Customer Advances

The Company entered into supply agreements, including certain amendments to these agreements, with three major customers in 2005, and another major customer in the first quarter of 2006. Under the supply agreements, the Company supplies certain media volumes subject to the terms and conditions of the agreements. The customers are required to pay certain advances covering future purchases of media from the Company. The customer advances, which totaled $127.2 million and $102.9 million as of December 31, 2006 and January 1, 2006, respectively, are to be repaid to the customers via a credit of a specified dollar amount per disk on future sales. During 2006 and 2005, customer advance credits applied to purchases of media were $119.5 million and $1.4 million, respectively, and additional customer advance payments were $143.8 million and $104.3 million, respectively. The agreements generally provide for repayment at the end of the term of the agreement if not fully paid by credits applied to purchases. The terms of the current arrangements expire on various dates through December 2009.

Note 9. Debt and Bank Guarantee

In January 2004, the Company completed an offering of $80.5 million of 2.0% Convertible Subordinated Notes (the Notes). The Notes mature on February 1, 2024, bear interest at 2.0%, and require semiannual interest payments beginning on August 1, 2004. The Notes will be convertible, under certain circumstances, into shares of the Company's common stock based on an initial effective conversion price of $26.40. Holders of the Notes may convert the Notes into shares of the Company's common stock prior to maturity if: 1) the sale price of the Company's common stock equals or exceeds $31.68 for at least 20 trading days in any 30 consecutive trading day period within any fiscal quarter of the Company; 2) the trading price of the Notes falls below a specified threshold prior to February 19, 2019; 3) the Notes have been called for redemption; or 4) specified corporate transactions (as described in the offering prospectus for the Notes) occur. The conditions for conversion have been met, and the debt is currently convertible. The Company may redeem the Notes on or after February 6, 2007, at specified declining redemption premiums. Holders of the Notes may require the Company to purchase the Notes on February 1, 2011, 2014, or 2019, or upon the occurrence of a fundamental change, at a purchase price equal to 100% of the principal amount of the Notes, plus accrued and unpaid interest.

There are no financial covenants, guarantees, or collateral associated with the Notes. In connection with the issuance of the Notes, the Company incurred $3.1 million of loan fees. The loan fees, which are included in other assets on the condensed consolidated balance sheet, are being amortized on a straight-line basis over the 20-year life of the Notes. On December 31, 2006, unamortized loan fees were $2.6 million.

The Company has arranged bank guarantees of Malaysian ringgit 29.5 million (approximately $8.4 million) which are required by Malaysian utility companies and other Malaysian vendors. There is no expiration date on the bank guarantees. No interest will be charged on the bank guarantees, but there is a commission charge ranging between 0.05% and 0.10% on the amount of bank guarantee utilized. As of December 31, 2006, there were no liabilities outstanding related to the bank guarantees.

Note 10. Derivative Financial Instruments

The Company accounts for its derivative and hedging activities under SFAS 133. The assets or liabilities associated with its derivative instruments and hedging activities are recorded at fair value in prepaid expenses and other current assets or other current liabilities, respectively, in the consolidated balance sheets. As discussed below, the accounting for gains and losses resulting from changes in fair value depends on the use of the derivative and whether it is designated and qualifies for hedge accounting.

As of December 31, 2006, the Company had a foreign exchange forward contract to purchase approximately $0.7 million of Japanese Yen for cash flow payments denominated in Japanese Yen for future equipment purchases. The contract has been designated as a cash flow hedge in accordance with SFAS 133. The fair value of the Company's forward contract was recorded as a $23 thousand other current liability as of December 31, 2006. Fair value is determined by a dealer quote. The effectiveness of the contracts that qualify as cash flow hedges is assessed quarterly through an evaluation of critical terms and other criteria required by SFAS 133. The effective portion of gains or losses resulting from changes in fair value is initially reported as a component of accumulated other comprehensive income or (loss), net of any tax effects, in stockholders' equity and subsequently reclassified into depreciation expense over the useful life of the purchased equipment. In 2006, the hedges were perfectly effective and no ineffectiveness in hedges occurred.

The Company's foreign exchange forward contracts have maturities of less than 12 months. The Company does not use foreign exchange forward contracts for speculative or trading purposes. As of December 31, 2006, forward contracts used for purchases of raw materials are not accounted for at fair value under the normal purchases exception provided in SFAS 133.

Note 11. Stockholders' Equity

Common Stock

As of December 31, 2006, the Company is authorized to issue 120.0 million shares of common stock. The following shares of common stock are reserved for future issuance (in thousands):

Convertible Subordinated Notes	3,049
2002 Qualified Stock Plan	5,390
	8,439

Amended and Restated 2002 Qualified Stock Plan

The 2002 Qualified Stock Plan (the 2002 Stock Plan) provides for the grant of incentive stock options to the Company's employees, and for the grant of non-statutory stock options, stock purchase rights, stock appreciation rights, performance shares and performance units to the Company's employees, directors, and consultants. The term for stock options granted may not exceed 10 years. In May 2005, shareholders voted to terminate the Employee Stock Purchase Plan (ESPP) and transfer the remaining 317,054 unissued shares that were previously reserved under the ESPP to the 2002 Stock Plan. In May 2006, the Company increased the number of shares reserved for issuance by 5,000,000 shares from 4,242,054 shares to 9,242,054 shares.

As of December 31, 2006, the Company had authorized a total of 9,242,054 shares of its common stock for issuance under the 2002 Stock Plan. As of December 31, 2006, the Company had a net balance of 5,390,492 shares of the Company's common stock reserved for issuance under the 2002 Stock Plan. Of the 5,390,492 shares reserved for future issuance under the 2002 Stock Plan, 12,500 are for stock purchase rights deferred under the Deferred

Compensation Plan, 485,262 are for the exercise of outstanding stock options, and 4,892,730 are for future grants of stock options and stock purchase rights.

Stock-Based Compensation

Effective January 2, 2006, the Company adopted SFAS No. 123R using the modified prospective method, in which compensation cost is recognized based on the requirements of SFAS 123R for (a) all share-based payments granted or modified after the effective date and (b) for all awards granted to employees prior to the effective date of SFAS 123R that remain unvested on the effective date. The Company elected to amortize stock-based compensation for awards outstanding and unvested on its adoption of SFAS 123R as well as for awards granted on or after its adoption of SFAS 123R on a straight line basis over the requisite service (vesting) period for the entire award. The vesting period for stock options has generally been four years and the vesting period for stock purchase rights generally has been three years.

Stock-based compensation expense related to outstanding stock options and stock purchase rights amounted to $3.1 million and zero for 2006 and 2005, respectively, and $15.0 million and $3.2 million for 2006 and 2005, respectively. As a result of adopting SFAS 123R on January 2, 2006, the Company's income before income taxes and net income for 2006 were approximately $3.4 million and $3.3 million lower, than if it had continued to account for stock-based compensation under APB 25. Basic and diluted net income per share for 2006 were approximately $0.10 and $0.08 lower, respectively, due to the adoption of SFAS 123R.

As of December 31, 2006, there was approximately $27.2 million of total unrecognized compensation cost related to stock-based compensation arrangements. The cost is expected to be recognized on a straight line basis over the remaining vesting period of the stock-based awards through the third quarter of 2010. The weighted average remaining vesting period is approximately two years.

Summary of Assumptions and Activity

In 2006 and 2005, the Company recorded $3.1 million and zero, respectively, of stock-based compensation expense related to stock options. The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton option pricing model. The following assumptions were used to estimate the fair value of option grants in 2006: risk-free interest rate of 4.80%; expected volatility of the market price of the Company's common stock of 54.3%; no dividend yield, and a weighted-average expected life of 4.0 years. The fair value of options granted in 2006, 2005 and 2004 was $18.10, $11.57 and $7.02 per share, respectively. Options to purchase 100,000 shares of the Company's common stock were granted in 2006.

Compensation expense related to stock options is amortized on a straight line basis over the vesting period of 48 months. As of December 31, 2006, the unamortized fair value of unvested stock options was $3.0 million and will be amortized on a straight line basis over a remaining weighted average vesting period of approximately 2.3 years.

A summary of stock option transactions is as follows:

	Shares	Weighted-Average Exercise Price (Per share)	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at December 28, 2003	1,220,085	$ 8.68		
Granted	422,880	$ 17.19		
Exercised	(237,912)	$ 5.78		
Cancelled	(37,669)	$ 12.50		
Outstanding at January 2, 2005	1,367,384	$ 11.72		
Granted	53,436	$ 20.34		
Exercised	(489,716)	$ 10.13		
Cancelled	(62,251)	$ 13.80		
Outstanding at January 1, 2006	868,853	$ 12.99		
Granted	100,000	$ 38.65		
Exercised	(479,209)	$ 11.73		
Cancelled	(4,382)	$ 14.55		
Outstanding at December 31, 2006(1)	485,262	$ 19.51	7.53	$ 8,990,193
Exercisable at December 31, 2006	244,341	$ 12.99	6.75	$ 6,082,026

(1) Also represents vested and expected to vest.

The total intrinsic value of options exercised during 2006, 2005 and 2004 was $14.7 million, $8.8 million and $3.0 million, respectively. In 2006, 2005 and 2004 the cash received from exercise of options was $5.6 million, $5.0 million and $1.4 million, respectively. Upon the exercise of options, the Company issues new common stock from its authorized shares.

The following table sets forth a summary of the Company's stock purchase rights for 2006:

	Shares	Weighted-Average Grant Date Fair Value (Per share)
Outstanding at January 1, 2006	573,201	$ 22.34
Granted	659,809	$ 44.25
Vested	(240,719)	$ 24.03
Cancelled	(17,823)	$ 34.87
Outstanding at December 31, 2006	974,468	$ 36.53

In 2006, 2005 and 2004, the Company recorded $15.0 million, $3.2 million and $0.4 million, respectively, of stock-based compensation expense related to stock purchase rights. The cumulative effect of adopting SFAS 123R related to applying an estimated forfeiture rate to unvested stock purchase rights outstanding on the date of adoption was a $0.2 million credit, which was credited to operating costs and expenses. The Company determines the fair value of stock purchase rights based on the Nasdaq closing stock price on the date of grant. Compensation expense related to stock purchase rights is amortized on a straight line basis over the vesting period of 36 months (one-third vests annually upon the anniversary date of the grant date). As of December 31, 2006, the unamortized fair value of unvested restricted stock awards was $24.1 million and will be amortized on a straight line basis over a remaining weighted average vesting period of approximately 1.8 years.

During the first quarter of 2006, the Company announced the anticipated retirement of its Chief Executive Officer (CEO), which became effective on October 1, 2006. Certain agreements were entered into with the CEO as a result of the anticipated retirement. These agreements were filed as exhibits to the Form 10-K filed for the year ended January 1, 2006. Under the agreements, the vesting of certain stock options and stock purchase rights were accelerated to provide additional compensation in connection with the CEO's retirement and for his assistance during a planned transition period. The Company recorded an additional $5.1 million of stock-based compensation expense related to the modification of the CEO's stock options and stock purchase rights for 2006, respectively. Effective October 1, 2006, Timothy Harris, the Company's then-Chief Operating Officer, became the Company's new CEO. The Company's then-CEO retired effective as of such date, and continued to provide transitional consulting services to the Company for three months.

Pro forma information for Periods Prior to the Adoption of SFAS 123R

Prior to January 2, 2006 and as permitted under SFAS No. 123, the Company elected to follow APB 25, and related interpretations in accounting for stock-based awards to employees. Accordingly, compensation cost for stock options and stock purchase rights was measured as the excess, if any, of the market price of the Company's common stock at the date of grant over the exercise price. In accordance with SFAS 123 and SFAS No. 148, *Accounting for Stock-Based Compensation — Transition and Disclosure — an Amendment of SFAS 123*, prior to fiscal 2006, the Company provided pro forma disclosure of the effect on net income and earnings per share had the fair value method been used, as prescribed by SFAS 123.

The following table reflects the effect on the Company's net income and income per share had the fair value method been applied to all outstanding and unvested awards in 2005 and 2004. The table is in thousands, except per share amounts.

	Year Ended	
	January 1, 2006	**January 2, 2005**
Net income, as reported	$ 115,637	$ 51,355
Add stock-based employee compensation expense included in reported net income	3,308	555
Deduct stock-based compensation expense determined under the fair value method for all awards	(5,973)	(3,571)
Pro forma net income	$ 112,972	$ 48,339
Net income per share:		
Basic — as reported	$ 3.99	$ 1.88
Diluted — as reported	$ 3.55	$ 1.71
Basic — pro forma	$ 3.90	$ 1.77
Diluted — pro forma	$ 3.49	$ 1.63

For pro forma disclosure purposes, the Company used the Black-Scholes-Merton option pricing model to estimate the fair value of each option and stock purchase right grant on the date of grant.

The following assumptions were used to estimate the fair value of option grants in fiscal 2005 and 2004:

	2005	2004
Risk-free interest rate	4.0%	2.7%
Volatility factor of the expected market price of the Company’s common stock	71.8%	81.8%
Weighted-average expected option life (in years)	4.0	4.0
Weighted-average per share fair value of options granted	$11.57	$7.02

The following assumptions were used to estimate the fair value of employee purchase rights under the Amended and Restated 2002 Employee Stock Purchase Plan in 2005, and 2004:

	2005	2004
Risk-free interest rate	1.7%	1.6%
Volatility factor of the expected market price of the Company’s common stock	50.8%	61.2%
Weighted-average expected purchase rights life (in years)	0.5	0.5
Weighted-average fair value of purchase rights granted	$3.12	$3.43

Because the Company does not pay out dividends, no dividend yield was included in the fair value calculation.

Deferred Compensation Plan

Employees at or above the director level are eligible to participate in the Company’s Deferred Compensation Plan, which provides for the deferral of stock purchase rights. Eligible employees may elect to defer any stock purchase rights they are eligible to receive during any calendar year the plan remains in effect. All deferrals must equal 100% of the shares to be awarded at the fair market value, calculated on the date of grant, of the stock purchase rights that would have otherwise been received. Distributions shall be paid in the form of shares of the Company’s common stock at such time as may be elected by each participant.

As of December 31, 2006, the issuance of 12,500 shares have been deferred in accordance with the Deferred Compensation Plan.

Warrants

In June 2002, the Company issued warrants to purchase 1,000,000 shares of the Company’s common stock. The warrants were exercisable until June 30, 2005 and had an exercise price of $9.00. In 2003 through 2005, approximately 992,000 warrants were exercised, and approximately 300,000 were surrendered in lieu of paying cash upon the exercise of certain warrants. The remaining approximate 8,000 warrants which expired as of June 30, 2005 were cancelled.

Note 12. Leases and Commitments

The Company leases a research and administrative facility under an operating lease that expires in 2014. The lease includes two renewal options of five years each.

As of December 31, 2006, the future minimum commitments for the non-cancelable operating facility lease, and non-cancelable equipment leases, are as follows (in thousands):

	Minimum Lease Payments
2007	$ 2,512
2008	2,057
2009	3,159
2010	3,150
2011	3,143
Thereafter	10,101
	$ 24,122

Rental expense for all operating leases was $3.4 million in 2006, $3.5 million in 2005, and $3.9 million in 2004.

During 2006 and 2005, the Company recorded $0.5 million and $2.6 million, respectively, of deferred rent related to the Company's renewal of its leased headquarters facility in San Jose, California. As of December 31, 2006, the deferred rent balance was $3.1 million.

Note 13. Quarterly Financial Data

(Unaudited, in thousands, except per share data)

	2006			
	1st Quarter(1)	2nd Quarter	3rd Quarter	4th Quarter
Net sales	$ 208,512	$ 233,627	$ 239,608	$ 255,929
Gross profit	59,093	64,968	61,780	61,841
Operating income	36,054	39,788	34,321	39,289
Net income	$ 36,237	$ 40,289	$ 34,498	$ 46,509
Basic net income per share	$ 1.22	$ 1.35	$ 1.15	$ 1.54
Diluted net income per share	$ 1.09	$ 1.21	$ 1.04	$ 1.39
Number of shares used in basic per share computations	29,685	29,883	29,969	30,138
Number of shares used in diluted per share computations	33,499	33,544	33,565	33,715

(1) Fourth quarter results included a release of $7.0 million, representing a portion of the Company's deferred tax valuation allowance, to recognize deferred tax assets that in the Company's judgment are more likely than not to be realized in 2007.

	2005			
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Net sales	$ 140,275	$ 172,740	$ 180,011	$ 192,920
Gross profit	35,063	48,080	50,887	54,703
Operating income	18,762	30,819	32,343	36,008
Net income	$ 18,527	$ 29,893	$ 31,982	$ 35,235
Basic net income per share	$ 0.66	$ 1.04	$ 1.09	$ 1.20
Diluted net income per share	$ 0.59	$ 0.92	$ 0.97	$ 1.07
Number of shares used in basic per share computations	28,261	28,834	29,396	29,476
Number of shares used in diluted per share computations	32,313	32,971	33,381	33,329

Note 14. Subsequent Events

Stock Purchase Rights and Stock Options

On February 15, 2007, the Company's Compensation Committee of its Board of Directors approved the grant of a total of 380,854 stock purchase rights with an exercise price of $0.01 to employees. Of this total, 313,881 was to non-officers and 66,973 was to officers. The vesting for the stock purchase rights granted is one-third at the end of each of the first three anniversaries of the date of grant, subject to the employee continuing to be a service provider. In addition, 180,819 stock options were granted to officers with an exercise price of $32.10. The vesting for the stock options granted is one-third at the end of the first anniversary of the date of grant and 1/24th each month thereafter.

KOMAG, INCORPORATED

Schedule II — VALUATION AND QUALIFYING ACCOUNTS

Column A	Column B	Column C	Column D	Column E
Description	Balance at Beginning of Year	Additions Charged to Costs and Expenses	Deductions	Balance at End of Year
	(In thousands)			
Year ended January 2, 2005				
Allowance for doubtful accounts	$ 398	$ (398)	$ —	$ —
Year ended January 1, 2006				
Allowance for doubtful accounts	$ —	$ —	$ —	$ —
Year ended December 31, 2006				
Allowance for doubtful accounts	$ —	$ —	$ —	$ —

Exhibit 99.4

PART I. FINANCIAL INFORMATION
ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

KOMAG, INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended		Six Months Ended	
	July 1, 2007	July 2, 2006	July 1, 2007	July 2, 2006
Net sales	$ 187,173	$ 233,627	$ 451,839	$ 442,139
Cost of sales	181,045	168,659	386,705	318,078
Gross profit	6,128	64,968	65,134	124,061
Operating expenses:				
Research, development, and engineering	15,406	16,081	31,905	31,156
Selling, general, and administrative	11,707	9,125	20,174	17,149
Gain on disposal of assets	(166)	(26)	(220)	(86)
	26,947	25,180	51,859	48,219
Operating income (loss)	(20,819)	39,788	13,275	75,842
Other income (expense):				
Interest income	2,300	1,867	3,759	3,938
Interest expense	(1,637)	(441)	(2,148)	(882)
Other income (expense), net	3	41	(2)	(435)
	666	1,467	1,609	2,621
Income (loss) before income taxes	(20,153)	41,255	14,884	78,463
Provision for income taxes	823	966	2,883	1,937
Net income (loss)	$ (20,976)	$ 40,289	$ 12,001	$ 76,526
Basic net income (loss) per share	$ (0.72)	$ 1.35	$ 0.41	$ 2.57
Diluted net income (loss) per share	$ (0.72)	$ 1.21	$ 0.42	$ 2.31
Number of shares used in basic per share computations	29,084	29,883	29,625	29,784
Number of shares used in diluted per share computations	29,084	33,544	33,841	33,525

See accompanying notes to condensed consolidated financial statements.

KOMAG, INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value)
(Unaudited)

	July 1, 2007	December 31, 2006
ASSETS		
Current assets		
Cash and cash equivalents	$ 99,888	$ 129,632
Short-term investments	83,150	41,500
Accounts receivable (less allowances of $1,431 and $2,326 respectively)	112,597	140,230
Inventories	191,667	104,181
Prepaid expenses and other current assets	2,126	2,119
Total current assets	489,428	417,662
Property, plant, and equipment (net of accumulated depreciation of $270,943 and $219,388, respectively)	533,330	542,585
Deferred income taxes	5,343	7,346
Other assets	12,986	10,094
	$ 1,041,087	$ 977,687
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Trade accounts payable	$ 126,796	$ 139,477
Customer advances	79,045	127,181
Accrued expenses and other current liabilities	19,825	25,412
Total current liabilities	225,666	292,070
Long-term debt	250,000	80,500
Other long term liabilities	3,810	3,091
Total liabilities	479,476	375,661
Stockholders' equity		
Common stock, $0.01 par value per share:		
Authorized - 120,000 shares		
Issued and outstanding - 30,363 and 31,178 shares, respectively	304	312
Additional paid-in capital	329,828	283,679
Accumulated other comprehensive loss	(628)	(611)
Retained earnings	232,107	318,646
Total stockholders' equity	561,611	602,026
	$ 1,041,087	$ 977,687

See accompanying notes to condensed consolidated financial statements.

KOMAG, INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended	
	July 1, 2007	July 2, 2006
Operating Activities		
Net income	$ 12,001	$ 76,526
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization of property, plant, and equipment	52,263	32,753
Deferred income taxes	2,234	—
Tax provision (benefit) charged to additional paid-in capital	(94)	1,572
Stock-based compensation	8,842	8,713
Non-cash interest charges	241	77
Other non-cash charges	184	267
Foreign exchange loss	2,041	502
Changes in operating assets and liabilities:		
Accounts receivable, net	27,661	(11,737)
Inventories	(87,486)	(21,421)
Prepaid expenses and other current assets	(238)	476
Trade accounts payable	(15,817)	40,206
Customer advances	(48,136)	37,262
Accrued expenses and other liabilities	(5,120)	(5,946)
Other non-current assets	985	—
Net cash (used in) provided by operating activities	(50,439)	159,250
Investing Activities		
Acquisition of property, plant, and equipment	(41,806)	(177,409)
Purchases of short-term investments	(122,300)	(77,850)
Proceeds from short-term investments	80,650	124,900
Proceeds from disposal of property, plant, and equipment	262	162
Other	5	(67)
Net cash used in investing activities	(83,189)	(130,264)
Financing Activities		
Proceeds from issuance of long-term debt, net of issuance costs	243,215	—
Repurchase of common stock	(140,417)	(1,080)
Proceeds from sale of common stock	1,021	3,235
Net cash provided by financing activities	103,819	2,155
Effect of exchange rate changes on cash and cash equivalents	65	1,074
Increase (decrease) in cash and cash equivalents	(29,744)	32,215
Cash and cash equivalents at beginning of period	129,632	99,984
Cash and cash equivalents at end of period	$ 99,888	$ 132,199

See accompanying notes to condensed consolidated financial statements.

Note 1. Basis of Presentation and Summary of Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements include the accounts of Komag, Incorporated (the Company), a Delaware corporation, and its wholly-owned subsidiaries. These financial statements have been prepared in accordance with United States of America (US) generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by US generally accepted accounting principles. While the financial information furnished is unaudited, in the opinion of management, all normal recurring adjustments considered necessary for a fair presentation of the condensed consolidated financial position, operating results, and cash flows for the periods presented, have been included. Operating results for the six months ended July 1, 2007, are not necessarily indicative of the results that may be expected for the year ending December 30, 2007. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2006, which are included in the Company's Annual Report on Form 10-K.

Use of Estimates in the Preparation of Financial Statements: The preparation of financial statements in conformity with accounting principles generally accepted in the US requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fiscal Year: The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. The Company's 2007 fiscal year will include 52 weeks. The three-month and six-month reporting periods included in this report include 13 weeks and 26 weeks, respectively.

Inventories: Inventories are stated at the lower of cost or market, and consist of the following (in thousands):

	July 1, 2007	December 31, 2006
Raw materials	$ 152,459	$ 78,701
Work in process	18,292	15,900
Finished goods	20,916	9,580
	$ 191,667	$ 104,181

Derivative Financial Instruments: In the second quarter of 2007, the Company commenced hedging a portion of its forecasted ringgit based expenses to help mitigate short term exposure to fluctuations of the currency by entering foreign exchange forward rate contracts. We account for our derivative and hedging activities under SFAS No. 133, *Accounting for Derivative and Hedging Activities*

(SFAS 133). The assets or liabilities associated with our derivative instruments and hedging activities are recorded at fair value in other current assets or other current liabilities, respectively, in our Condensed Consolidated Balance Sheets. As discussed below, the accounting for gains and losses resulting from changes in fair value depends on the use of the derivative and whether it is designated and qualifies for hedge accounting.

A majority of our sales, expense, and capital purchasing activities is transacted in U.S. dollars. However, a large portion of our payroll, certain manufacturing and operating expenses, and inventory and capital purchases is transacted in the Malaysian ringgit (ringgit), subjecting us to foreign currency risk. We enter foreign currency forward contracts, generally with maturities of 12 months or less, to reduce the volatility of cash flows primarily related to forecasted expenses denominated in ringgit. In addition, we utilize foreign exchange forward contracts to mitigate foreign currency exchange rate risk associated with ringgit denominated liabilities.

Cash Flow Hedging Activities: All hedging relationships are formally documented at the inception of the hedge and must be highly effective in offsetting changes to future cash flows on hedged transactions. The effectiveness of the cash flow hedge contracts, excluding time value, is assessed monthly using regression analysis. The effective portion of gains or losses resulting from changes in fair value of these hedges is initially reported as a component of accumulated other comprehensive income in stockholders' equity. The gross amount of the effective portion of gains or losses resulting from changes in fair value of these hedges is subsequently reclassified into operating expenses in the period when the forecasted transaction is recognized in the Condensed Consolidated Statements of Operations. The effective portion of gains or losses on hedges recognized in accumulated other comprehensive income at the end of each quarter will be reclassified to earnings within 12 months. The ineffective portion of gains or losses resulting from changes in fair value, if any, is reported immediately in our Condensed Consolidated Statements of Operations in cost of goods sold.

During the second quarter of 2007, the Company recorded less than $0.1 million of net unrealized losses on derivative financial instruments to accumulated other comprehensive income. There were no reclassifications to operating expenses during the second quarter of 2007. The ineffective portion of gains or losses resulting from changes in fair value was not material. The loss representing time value excluded from the assessment of hedge effectiveness was less than $0.1 million in the second quarter of 2007, which is included in cost of goods sold in the Condensed Consolidated Statement of Operations. As of July 1, 2007, we had foreign currency forward contracts to purchase approximately $87.4 million in ringgit. As of July 1, 2007, these foreign currency forward contracts outstanding had a fair value of $0.6 million, included in other current liabilities and a fair value of $0.5 million, included in other current assets.

Non-designated Hedging Activities: Some of the Company's foreign exchange forward contracts are not designated as hedging instruments under SFAS 133. Accordingly, any gains or losses resulting from changes in the fair value of these forward contracts are reported immediately in cost of goods sold. The gains and losses on these forward contracts generally offset the gains and losses associated with the underlying foreign-currency-denominated liabilities, which are also reported in cost of goods sold, in the Condensed Consolidated Statements of Operations.

Computation of Net Income (Loss) Per Share: Basic net income (loss) per common share is computed by dividing income (loss) available to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted net income (loss) per share is computed by dividing income (loss) available to common stockholders by the weighted-average number of shares and dilutive potential shares of common stock outstanding during the period. The dilutive effect of outstanding options and unvested common stock is reflected in diluted net income per share by application of the treasury stock method. The dilutive effect of outstanding contingently convertible debt is reflected in diluted net income per share by application of the if-converted method. Interest expense related to the contingently convertible debt is an adjustment to income available to common stockholders for the diluted net income per share calculation.

The computation of diluted net loss per share for the second fiscal quarter of 2007 excludes the interest adjustment related to the contingently convertible debt of $1.6M and common stock equivalents of 4.8 million shares of common stock since their inclusion would be antidilutive.

The following table sets forth the computation of net income (loss) per share. The table is in thousands, except per share amounts.

	Three Months Ended		Six Months Ended	
	July 1, 2007	July 2, 2006	July 1, 2007	July 2, 2006
Numerator for basic net income (loss) per share:				
Net income (loss) as reported	$ (20,976)	$ 40,289	$ 12,001	$ 76,526
Numerator for diluted net income (loss) per share:				
Net income (loss) as reported	$ (20,976)	$ 40,289	$ 12,001	$ 76,526
Interest adjustment related to contigently convertible debt	—	441	2,148	882
	$ (20,976)	$ 40,730	$ 14,149	$ 77,408
Denominator for basic net income per share:				
Weighted average shares outstanding	29,084	29,883	29,625	29,784
Denominator for diluted net income per share:				
Weighted average shares outstanding	29,084	29,883	29,625	29,784
Effect of dilutive securities:				
Shares under contingently convertible debt	—	3,049	3,983	3,049
Stock options	—	369	136	429
Unvested common stock	—	243	97	263
	29,084	33,544	33,841	33,525
Basic net income (loss) per share	$ (0.72)	$ 1.35	$ 0.41	$ 2.57
Diluted net income (loss) per share	$ (0.72)	$ 1.21	$ 0.42	$ 2.31

Recent Accounting Pronouncements: In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 provides guidance on recognition and measurement of uncertainties in income taxes and is applicable for fiscal years beginning after December 15, 2006. The Company adopted this pronouncement beginning in fiscal year 2007. The adoption of FIN 48 had no material effect on the Company's financial position or results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements and is applicable for fiscal years beginning after November 15, 2007. The Company has not yet completed the evaluation or determined the impact of adopting SFAS 157.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits companies to choose to measure certain financial instruments and other items at fair value. The standard requires that unrealized gains and losses be reported in earnings for items measured using the fair value option and is applicable for fiscal years beginning after November 15, 2007. The Company has not yet completed the evaluation or determined the impact of adopting SFAS 159.

Note 2. Common Stock

The Company repurchased and retired 0.5 million and 4.3 million shares of Company common stock at an average share price of $27.71 and $32.18, for a total cost of $13.8 million and $138.8 million in the three and six months ended July 1, 2007, respectively. These share repurchases are part of a March 2007 share repurchase authorization by the board of directors for an amount up to $200 million. The Company does not expect to repurchase additional shares under this authorization as the Merger Agreement prohibits such stock repurchases (see Note 8 on Proposed Acquisition). The Company immediately retired the shares repurchased, which decreased common stock by $5,000 and $43,000 for the par value of the common stock retired, additional paid-in capital by $5.4 million and $40.3 million and retained earnings by $8.4 million and $98.5 million, in the three and six months ended July 1, 2007, respectively. In addition, the Company has made periodic repurchases of common stock in connection with an employee stock plan.

Note 3. Concentration of Customer, Supplier, and Geographic Risk

The following table reflects the percentage of the Company's net sales by major customer (2):

	Three Months Ended		Six Months Ended	
	July 1, 2007	July 2, 2006	July 1, 2007	July 2, 2006
Western Digital Corporation	40%	38%	37%	37%
Seagate Technology	34%	32%	35%	36%
Hitachi Global Storage Technologies (1)	18%	26%	19%	24%

(1) Includes sales to Hitachi Global Storage Technologies' contract manufacturer.

(2) Total revenue used to calculate the customer concentration percentage excludes the sale of approximately $2.3 and $13.5 million of precious metal inventory in the three and six months ended July 1, 2007. No such sales occurred in the 2006 periods.

The Company relies on a limited number of suppliers for some of the materials and equipment used in its manufacturing processes, including aluminum blanks, aluminum substrates, nickel plating solutions, polishing and texturing supplies, and sputtering target materials. Kobe Steel, Ltd. is the Company's primary supplier of aluminum blanks, which is a fundamental component in producing disks. The Company also relies on Heraeus Incorporated and Williams Advanced Materials, Incorporated for its sputtering target requirements, and on OMG Fidelity, Incorporated for supplies of nickel plating solutions.

A majority of the Company’s long-lived assets is located at its Malaysian manufacturing facilities. These assets totaled $497.9 million as of July 1, 2007, and $506.2 million as of December 31, 2006. The majority of the Company’s sales is delivered to manufacturing facilities located in Asia.

Note 4. Accrued Expenses and Other Current Liabilities

The following table (in thousands) summarizes accrued expenses and other liabilities balances at July 1, 2007 and December 31, 2006:

	July 1, 2007	December 31, 2006
Accrued compensation and benefits	$ 10,679	$ 22,481
Other current liabilities	9,146	2,931
	$ 19,825	$ 25,412

Note 5. Customer Advances

The Company has supply agreements with each of its major customers. Under the supply agreements, the Company supplies certain media volumes subject to the terms and conditions of the agreements. The customers provided cash advances covering future purchases of media from the Company. The customer advances, which totaled $79.0 million and $127.2 million as of July 1, 2007 and December 31, 2006, respectively, are to be repaid to the customers based on a specified dollar amount per disk purchased. During the three and six months ended July 1, 2007, customer advances repaid to customers were $22.1 million and $48.3 million, respectively. The agreements generally provide for repayment at the end of the term of the agreement if not fully paid in connection with purchases. The terms of the current arrangements expire on various dates through December 2009.

Note 6. Debt

Conversion of Convertible Subordinated Notes due 2024

On March 28, 2007, the Company called for redemption on April 17, 2007, all $80.5 million of then outstanding principal amount of its 2.0% Convertible Subordinated Notes due 2024 (the Notes). All of the Notes were converted into 3.0 million shares of the Company’s common stock in April 2007. In accordance with the terms of the Notes, each $1,000 principal amount of the Notes was converted into 37.8788 shares of the Company’s common stock. As a result of the redemption, accrued interest of $0.3 million, unamortized loan issuance fees of $2.6 million and the outstanding debt balance of $80.5 million were re-classified to additional paid in capital with the exception of $30 thousand for the par value of the common stock issued, which was re-classified to common stock. The Company did not incur any gains or losses as a result of the conversion.

Convertible Subordinated Notes due 2014

On March 28, 2007, the Company completed an offering of $250 million of 2.125% Convertible Subordinated Notes (the New Notes). The New Notes mature on April 1, 2014, bear interest at a rate of 2.125% per annum, and require semiannual interest payments beginning on October 1, 2007. The New Notes may be converted, at the option of the holder, into shares of the Company’s common stock based upon a base conversion rate of 17.2414 shares of common stock per $1,000 principal amount of the notes. The conversion rate is equivalent to a base conversion price of approximately $58.00 per share and is subject to adjustment in certain dilution events. If at the time of conversion, the Company’s common stock price exceeds the base conversion price, holders will receive up to an additional 13.2836 shares of common stock per $1,000 principal amount of the notes, as determined pursuant to a specified formula.

Upon the occurrence of a fundamental change of the Company (which would generally include a change of control (including of our board of directors), liquidation or dissolution of the Company or the failure of our shares to be listed on a national securities exchange or other trading market), holders may require the Company to repurchase some or all of their notes for cash at a price equal to 100% of the principal amount of the notes being repurchased, plus accrued and unpaid interest, if any. Also, if a fundamental change occurs, the Company may be required in certain circumstances to increase the conversion rate for any notes converted in connection with such fundamental change by a specified number of shares of our common stock. On June 28, 2007, the Company entered into an Agreement and Plan of Merger with Western Digital Corporation (Western Digital) and State M Corporation, a wholly-owned subsidiary of Western Digital, pursuant to which State M Corporation commenced a cash tender offer on July 11, 2007 for all outstanding shares of our common stock. If the tender offer is successfully completed, it will constitute a fundamental change. The Company does not expect that the consummation of the current tender offer would result in an increase in the conversion rate, however, the Company cannot assure you that such an increase will not be triggered since the determination is made under the indenture for the New Notes based on the average of the closing price of the Company’s common stock over a five consecutive trading day period ending on the trading day immediately preceding the effective date of the fundamental change.

There are no financial covenants or guarantees and there is no collateral associated with the New Notes. In connection with the issuance of the New Notes, the Company incurred approximately $6.8 million of loan issuance fees. The loan issuance fees, which are included in other assets on the condensed consolidated balance sheet, are being amortized on a straight-line basis over the 7-year maturity of the New Notes. On July 1, 2007, unamortized loan fees were $6.6 million.

Note 7. Income Taxes

The Company adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48)*, on January 1, 2007. Total unrecognized income tax benefits at the date of adoption were $0.7 million and remained unchanged from the amount of the Company’s pre-implementation income tax contingency reserves. The unrecognized income tax benefits, if realized, will not affect the annual effective tax rate but will be credited to additional paid in capital.

Unrecognized tax benefits are expected to decrease by $0.2 million within the next 12 months due to the anticipated lapse of an applicable statute of limitation.

Interest and penalties related to unrecognized income tax benefits will be accrued in interest expense and selling, general and administrative expense, respectively. The Company has not accrued interest or penalties as of the date of adoption because they are not applicable.

The Company and its subsidiaries file income tax returns in the U.S., California, the Netherlands and Malaysia. The tax years 2000 to 2006 remain open to examination in each of these major taxing jurisdictions.

Note 8. Commitments and Contingencies

The Company provides indemnification to customers under customer contracts for potential intellectual property infringement claims involving the Company's products. The company has received such a claim for reimbursement of legal defense costs from its customers in connection with a claim of intellectual property infringement. The Company can not currently estimate the amount of potential liability related to such claim. As of July 1, 2007, the expense incurred by the Company under customer indemnity provisions has not been material.

Note 9. Proposed Acquisition

On June 28, 2007, the Company entered into an Agreement and Plan of Merger with Western Digital Corporation and State M Corporation, an indirect wholly-owned subsidiary of Western Digital, pursuant to which State M Corporation commenced a cash tender offer on July 11, 2007 for all outstanding shares of our common stock at a price per share of $32.25. Unless extended pursuant to the terms and conditions set forth in the Agreement and Plan of Merger, the tender offer was originally scheduled to expire on August 7, 2007, but was extended by Western Digital Corporation until September 5, 2007. In the event the tender offer is successfully completed, State M Corporation will merge with and into Komag and Komag will become an indirect wholly-owned subsidiary of Western Digital Corporation, and each share of Komag common stock not purchased in the tender offer will be converted into the right to receive $32.25 in cash. The tender offer and merger are subject to customary closing conditions, including certain regulatory approvals. We currently expect that the merger will be completed in the third quarter of 2007. The merger agreement provides for the payment by the Company of a termination fee of $38 million if the merger agreement is terminated in certain circumstances in connection with a competing third-party acquisition proposal and certain other circumstances. The boards of directors of each of the Company, Western Digital and State M Corporation have unanimously approved the tender offer and the merger, on the terms and subject to the conditions set forth in the merger agreement. Western Digital is a significant customer of the Company (see Note 3).

EXHIBIT 99.5

WESTERN DIGITAL CORPORATION

UNAUDITED PRO FORMA CONDENSED COMBINED FINANCIAL STATEMENTS

Western Digital Corporation ("WDC") acquired all of the outstanding common shares and stock purchase rights of Komag, Incorporated ("Komag") in a cash transaction announced on June 28, 2007 and consummated on September 5, 2007. The transaction was structured as a cash tender offer by State M Corporation ("State M"), an indirect wholly-owned subsidiary of WDC, for all outstanding shares of Komag's common stock, followed by a merger of State M and Komag whereby Komag became an indirect wholly-owned subsidiary of WDC and changed its name to WD Media, Inc. The following unaudited pro forma condensed combined financial statements are based on the historical financial statements of WDC and Komag after giving effect to the acquisition of Komag by WDC (the "Merger") using the purchase method of accounting and applying the assumptions and adjustments described in the accompanying notes.

The unaudited pro forma condensed combined statements of operations for the fiscal year ended June 29, 2007 are presented as if the acquisition had occurred on July 1, 2006. The unaudited pro forma condensed combined balance sheet is presented as if the acquisition had occurred on June 29, 2007. You should read this information in conjunction with the:

- accompanying notes to the Unaudited Pro Forma Condensed Combined Financial Statements;
- separate historical financial statements of WDC as of and for the fiscal year ended June 29, 2007, included in WDC's annual report on Form 10-K for the fiscal year ended June 29, 2007;
- separate unaudited historical financial statements of Komag as of and for the three and six-month periods ended July 1, 2007, included in the Komag quarterly report on Form 10-Q for the quarter ended July 1, 2007, which is incorporated by reference into this document;
- separate historical financial statements of Komag as of and for the fiscal year ended December 31, 2006, included in the Komag annual report on Form 10-K for the fiscal year ended December 31, 2006, which is incorporated by reference into this document.

The pro forma information presented is for illustrative purposes only and is not necessarily indicative of the financial position or results of operations that would have been realized if the Merger had been completed on the dates indicated, nor is it indicative of future operating results or financial position. The pro forma adjustments are based upon currently available information and certain assumptions that management believes are reasonable.

The unaudited pro forma condensed combined financial statements do not include the effects of:

- likely revenue attrition that will result in lower combined revenues during the initial quarters following the closing of the Merger;
- anticipated operating efficiencies and cost savings after the first full year of integration;
- future stock based compensation expense of approximately $12 million (see note 1 to the unaudited pro forma condensed combined financial statements).

Pursuant to the purchase method of accounting, the total estimated purchase price, calculated as described in Note 1 to these unaudited pro forma condensed combined financial statements, has been allocated to assets acquired and liabilities assumed based on their respective fair values. WDC's management has estimated the fair value of the intangible assets and tangible assets acquired and liabilities assumed. Any differences between the fair value of the consideration issued and the fair value of the assets acquired and liabilities assumed is recorded as goodwill.

WDC and Komag have different fiscal year ends which end on the Friday closest to June 30 and the Sunday closest to December 31, respectively. As such, Komag's historical results have been aligned to more closely conform to those of WDC. In addition, certain reclassifications have been made to Komag's historical financial statements to conform to the presentation used in WDC's historical financial statements. Such reclassifications had no effect on Komag's previously reported net income.

WESTERN DIGITAL CORPORATION
UNAUDITED PRO FORMA CONDENSED COMBINED STATEMENT OF OPERATIONS
For the Year Ended June 29, 2007
(in millions, except per share data)

	Year Ended June 29, 2007 Western Digital	Four Quarters Ended July 1, 2007 Komag	Pro Forma Adjustments		Pro Forma Combined
Revenue, net	$ 5,468	$ 948	$ (356)	(a)	$ 6,060
Cost of revenue	4,568	759	$ (349)	(b)	4,978
Gross margin	900	189	$ (7)		1,082
Operating expenses:					
Research and development	306	66	$ 17	(c)	389
Selling, general and administrative	179	37	$ (11)	(d)	205
Total operating expenses	485	103	$ 6		594
Operating income	415	86	$ (13)		488
Non-operating income:					
Interest income	32	8	$ —		40
Interest and other expense	4	2	$ 49	(e)	55
Total non-operating income (expense)	28	6	$ (49)		(15)
Income before income taxes	443	92	$ (62)		473
Income tax benefit	(121)	(2)	$ —		(123)
Net income	$ 564	$ 94	$ (62)		$ 596
Income per common share:					
Basic	$ 2.57				$ 2.72
Diluted	$ 2.50				$ 2.64
Weighted average shares outstanding:					
Basic	219				219
Diluted	226				226

Explanatory notes appear in Note 2 below.

WESTERN DIGITAL CORPORATION
UNAUDITED PRO FORMA CONDENSED COMBINED BALANCE SHEET
June 29, 2007
(in millions)

	June 29, 2007 Western Digital	July 1, 2007 Komag	Pro Forma Adjustments		Pro Forma Combined
ASSETS					
Current assets:					
Cash and cash equivalents	$ 700	$ 100	$ (212)	(f)	$ 588
Short-term investments	207	83	—		290
Accounts receivable, net	697	113	(58)	(g)	752
Inventories	259	192	—		451
Advances to suppliers	63	—	(14)	(g)	49
Other current assets	103	2	4	(h)	109
Total current assets	2,029	490	(280)		2,239
Property and equipment, net	741	533	132	(i)	1,406
Goodwill	—	—	71	(j)	71
Other intangible assets, net	4	—	89	(k)	93
Other non-current assets	127	18	105	(l)	250
Total assets	$ 2,901	$ 1,041	$ 117		$ 4,059
LIABILITIES AND SHAREHOLDERS' EQUITY					
Current liabilities:					
Accounts payable	$ 882	$ 126	$ (62)	(g)	$ 946
Accrued expenses and other liabilities	163	20	45	(m)	228
Accrued warranty	73	—	—		73
Customer advances	0	79	(14)	(g)	65
Current portion of long-term debt	12	—	998	(n)	1,010
Total current liabilities	1,130	225	967		2,322
Long-term debt	10	250	(250)	(o)	10
Other liabilities	45	4	11	(p)	60
Total liabilities	1,185	479	728		2,392
Shareholders' equity	1,716	562	(611)	(q)	1,667
Total liabilities and shareholders' equity	$ 2,901	$ 1,041	$ 117		$ 4,059

Explanatory notes appear in Note 2 below.

1. BASIS OF PRO FORMA PRESENTATION

On June 28, 2007, WDC and Komag entered into a definitive Merger agreement and announced the merger. The transaction was consummated on September 5, 2007 through a cash tender offer for all outstanding shares of Komag's common stock and Komag became an indirect wholly-owned subsidiary of WDC. The transaction was accounted for using the purchase method of accounting.

The unaudited pro forma condensed combined balance sheet is presented to give effect to WDC's acquisition of Komag as if the transaction had been consummated on June 29, 2007. The statement of operations is presented as if the transaction had been consummated on July 1, 2006.

Preliminary Purchase Price Allocation

The aggregate purchase price for Komag was $995 million, consisting of cash paid for outstanding shares, transaction fees, severance and other employee-related equity payments. The application of purchase accounting under SFAS No. 141, "Business Combinations" ("SFAS 141"), requires that the total purchase price be allocated to the fair value of assets acquired and liabilities assumed based on their fair values at the acquisition date, with amounts exceeding the fair values being recorded as goodwill. The allocation process requires an analysis and valuation of acquired assets, including fixed assets, deferred tax assets, technologies, customer contracts and relationships, trade names and liabilities assumed, including contractual commitments and legal contingencies. The values assigned to certain acquired assets and liabilities are preliminary, and in accordance with SFAS 141 they may be adjusted as further information becomes available during the allocation period of up to 12 months from the date of the acquisition.

Additional information that may become available subsequently and may result in changes in the values allocated to various assets and liabilities includes, but is not limited to, changes in the timing and actual number of employees terminated, unidentified claims from suppliers or other contingent obligations, the amounts required to settle them, the progress or outcomes of various litigation, and the value of deferred tax assets. Any changes in the values allocated to tangible and specifically identified intangible assets acquired and liabilities assumed during the allocation period may result in material adjustments to goodwill.

WDC identified and recorded the assets, including specifically identifiable intangible assets, and liabilities assumed from Komag at their estimated fair values at September 5, 2007, the date of the acquisition, and allocated the residual value of approximately $84 million to goodwill.

Tangible assets acquired and liabilities assumed:	
Cash and short-term investments	$ 130
Accounts receivable	114
Inventories	205
Other current assets	6
Property and equipment	667
Other non-current assets	123
Accounts payable	(130)
Accrued liabilities	(79)
Debt assumed	(248)
Other liabilities	(15)
Intangible assets	89
In-process research and development	49
Goodwill	84
Total	$ 995

Property, Equipment and Leasehold Improvements

The plant and equipment acquired as part of the acquisition continues to be utilized and was valued at current replacement cost for similar assets. Land and buildings have been estimated at fair value on September 5, 2007, the date of the acquisition. The following table summarizes the estimated fair value of the property, plant and equipment acquired from Komag and their estimated useful lives:

	Estimated Fair Value (In millions)	Estimated Weighted-Average Useful Life (In Years)
Land leases	$ 17	36.8
Buildings and improvements	224	17.8
Equipment	426	5.0
Total property, plant and equipment	$ 667	10.3

Inventories

Total inventories at September 5, 2007 included $205 million of inventory acquired through the acquisition, of which $11 million and $40 million represent finished goods and work-in-process, respectively. Finished goods and work-in-process were valued at estimated selling prices less costs of disposal, estimated reseller profit and costs to complete. In addition, total inventories at September 5, 2007 included $154 million in raw materials, primarily precious metals, acquired from Komag and is valued based on fair value at the date of the acquisition. Raw materials were valued at estimated replacement cost.

Identifiable Intangible Assets Acquired

In accordance with SFAS 141, WDC identified intangible assets apart from goodwill if one of the following criteria was met: 1) the asset arises from contractual or other legal rights; or 2) the asset is capable of being separated or divided from the acquired enterprise and sold, transferred, licensed, rented, or exchanged, either individually or in conjunction with a related contract, asset, or liability. The recorded values and estimated useful lives of the intangibles acquired from Komag were:

	Estimated Fair Value (In millions)	Weighted-Average Useful Life (In Years)
Existing technology	$ 79	9.7
Customer substrate relationships	10	5.0
Total acquired identifiable intangible assets	$ 89	9.2

Existing technology relates to Komag's media and substrate products that have reached technological feasibility as well as a combination of Komag's processes, patents, and trade secrets developed through years of experience in the design and production of their products. Existing technology was valued using the Excess Earnings Method under the Income Approach. This approach reflects the present value of projected cash flows that a market participant would expect to generate from these technologies less charges related to the contribution of other assets to those cash flows. The fair value of the existing technology is being amortized to Cost of Revenue over the weighted average useful life of 9.7 years.

The fair value of customer substrate relationships was determined using the Excess Earnings Method under the Income Approach based on the estimated revenues to be derived from Komag's customers. This approach reflects the present value of projected cash flows that a market participant would expect to generate from these customer substrate relationships less charges related to the contribution of other assets to those cash flows. The fair values of the customer substrate relationships are being amortized to Cost of Revenue over the weighted average useful life of five years.

In-Process Research and Development

Komag had an in-process research and development project associated with technology for higher recording densities on advanced perpendicular recording media. The project is expected to incorporate significant changes in the magnetic structure of the media to achieve higher recording density. As these advanced products are not ready for commercial production and have no alternative future use, the development cost did not qualify for capitalization. Accordingly, WDC recorded $49 million as a charge to research and development expense at the time of the acquisition. Costs to complete the development of this technology are expected to approximate $5 million and are expected to utilize existing engineering personnel. The technology may be necessary to remain competitive with anticipated industry advances in areal recording densities for thin-film media. The in-process research and development was valued using the Excess Earnings Method under the Income Approach. This approach reflects the present value of projected cash flows that a market participant would expect to generate from these technologies less costs related to the contribution of other assets to those cash flows.

Debt Assumed

As a result of the acquisition, WDC assumed $250 million face value of additional debt in the form of Convertible Subordinated Notes issued by Komag on March 28, 2007. The original terms of the Notes have a maturity of April 1, 2014, and currently bear interest at an annual rate of 2.625%. In addition, the terms specify that upon the occurrence of a fundamental change of Komag (including a change of control) the Notes, at the request of the Note holder, must be repurchased for a value equal to 100% of the principal amount of the Notes, plus accrued and unpaid interest through the Fundamental Change Purchase Date, which is December 5, 2007. Fair value of the debt was estimated to be $248 million, which represents the present value at current market interest rates considering the repayment date of December 5, 2007. Other terms of the debt which might otherwise impact its market value have been effectively eliminated due to the change of control provisions. There are no financial covenants or guarantees and there is no collateral associated with the Notes.

Adverse/Favorable Leasehold Interests

In accordance with the guidance in SFAS 141, WDC analyzed its contractual facility lease to determine the fair value of the leasehold interest. An adverse leasehold position exists when the present value of the contractual rental obligation is greater than the present value of the market rental obligation, and conversely for a favorable leasehold interest. WDC recorded a favorable leasehold interest aggregating $4 million and has been classified within Other Non-current Assets in the purchase price allocation table in this footnote. The $4 million will be amortized to Cost of Revenue and Operating Expenses over the remaining duration of the lease, which ends December 31, 2014.

Recognition of Liabilities in Connection with Komag Acquisition

Under EITF 95-3, “Recognition of Liabilities in Connection with a Business Combination”, WDC has accrued certain exit costs aggregating $33 million, which relate to employee severance and the cash payment for equity related liabilities due to the employment termination of Komag employees.

Stock-Based Compensation

In connection with the acquisition, each outstanding option to purchase shares of Komag’s common stock with an exercise price below $32.25 as of the date of the acquisition was converted into a right to receive $32.25 in cash less the exercise price of the option. In addition, each share of Komag restricted common stock granted on or before September 5, 2007 was converted into $32.25 per share in cash. These converted option and restricted stock awards are payable in cash according to their original vesting schedules. All shares of restricted stock and options remain subject to their original terms, including the terms and conditions of Komag’s Amended and Restated 2002 Qualified Stock Plan, the applicable restricted stock and option agreement and the Merger Agreement. As of September 5, 2007, the future expense for the converted Komag options and restricted stock awards is $12 million, which will be expensed based on individual award vesting terms between the date of acquisition and April 2010.

2. PRO FORMA ADJUSTMENTS

The following pro forma adjustments are included in the unaudited pro forma condensed combined statement of operations and the unaudited pro forma condensed combined balance sheet:

(a) To eliminate revenue associated with purchases WDC made from Komag.

(b) Adjustments to cost of revenue (in millions):

	Year Ended June 29, 2007
To reduce cost of revenue associated with purchases WDC made from Komag	$ (356)
To record the impact of an adjustment to conform the classification of the costs of new product introductions	(15)
To record the impact of an adjustment to conform the presentation of certain manufacturing plant level costs	7
To record the amortization of intangibles associated with the Merger	12
To increase depreciation expense to reflect the higher fair value over original net cost basis of depreciable fixed assets acquired	3
	$ (349)

(c) Adjustments to research and development (in millions):

	Year Ended June 29, 2007
To record the impact of an adjustment to conform the classification of costs of new product introductions	$ 15
To increase depreciation expense to reflect the higher fair value over original net cost basis of depreciable fixed assets acquired	2
	$ 17

(d) Adjustments to sales, general and administrative (in millions):

	Year Ended June 29, 2007
To record the impact of an adjustment to conform the presentation of certain manufacturing plant level costs	$ (7)
To eliminate Komag's accrued non-recurring Merger related expenses	(4)
	$ (11)

(e) Adjustments to interest and other expense (in millions):

	Year Ended June 29, 2007
To record interest expense associated with new debt related to the Merger	$ 47
To record accretion of interest expense related to the fair value of the debt acquired from Komag	2
	$ 49

(f) Adjustments to cash and cash equivalents (in millions):

To record use of cash by WDC for the Merger	$ 208
To eliminate cash Komag received from WDC included in both company's balance sheets due to differing fiscal quarter end dates	4
	$ 212

(g) To eliminate inter company balance sheet accounts between Komag and WDC.

(h) To record current deferred tax asset as a result of the Merger

(i) To record increase in property and equipment acquired from Komag to reflect fair value

(j) To record the preliminary purchase price allocation to goodwill as though the acquisition had occurred on June 29, 2007

(k) To record the preliminary purchase price allocation to intangible assets

(l) Adjustments to other non-current assets (in millions):

To record non-current deferred tax asset as a result of the Merger	$ 108
To record fair value of facility lease	4
To eliminate Komag's debt issuance costs	(7)
	$ 105

(m) Adjustments to accrued expenses and other liabilities (in millions):

To record severance and related costs and stock purchase rights assumed as part of the purchase price of the Merger	$ 33
To record accrual of Komag's direct acquisition related costs	7
To record accrual of WDC's direct acquisition related costs	5
	$ 45

(n) Adjustments to current portion of long-term debt (in millions):

To record WDC's debt related to the Merger	$ 750
Komag's convertible debt reclassified to short-term	250
To reduce Komag's convertible debt to fair value	(2)
	$ 998

(o) To reclassify Komag's convertible debt to short-term

(p) Adjustments to other liabilities (in millions):

To record long-term tax liability	$ 14
To eliminate Komag's deferred rent as part of the purchase price allocation	(3)
	$ 11

(q) Adjustments to shareholders' equity (in millions):

To eliminate Komag's shareholders' equity	$	562
To record immediate write-off of In Process Research & Development		49
	$	611

3. TAXES

Upon the combination of the two companies, WDC expects that the companies' respective U.S. entities would be taxed in the U.S. on a consolidated basis. Due to utilization of net operating losses and tax holidays on earnings in foreign jurisdictions, there would be no impact to the historical tax provisions used in the pro forma condensed combined statement of operations. As future income is expected from the combined U.S. entities, the Komag valuation allowance against deferred tax assets was released and credited to goodwill as of the acquisition date. The gross value of the deferred tax assets, net of estimated tax liabilities has been reflected on the pro forma condensed combined balance sheet and not in the pro forma condensed combined statement of operations due to the non-recurring nature of this reduction in the valuation allowances.