THE ESTĒE LAUDER COMPANIES INC. 2002 ANNUAL REPORT

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THE ESTĒE LAUDER COMPANIES INC.

The Estée Lauder Companies Inc. is one of the world's leading manufacturers and marketers of quality skin care, makeup, fragrance and hair care products. The Company's products are sold in over 130 countries and territories under well recognized brand names, including Estée Lauder, Aramis, Clinique, Prescriptives, Origins, M·A·C, La Mer, Bobbi Brown, Tommy Hilfiger, *jane,* Donna Karan, Aveda, Stila, Jo Malone, Bumble and bumble, and *kate spade beauty*.

THE AMERICAS—The Company was founded by Estée Lauder in 1946 in New York City. In fiscal 2002, the Americas region represented 61% of net sales and 49% of operating income before restructuring charges.

EUROPE, THE MIDDLE EAST & AFRICA—Our first international door opened in 1960 in London. In fiscal 2002, Europe, the Middle East & Africa represented 26% of net sales and 39% of operating income before restructuring charges. This region includes results from our travel retail business.

ASIA/PACIFIC—We established a presence in Hong Kong in 1961. In fiscal 2002, the Asia/Pacific region represented 13% of net sales and 12% of operating income before restructuring charges.

ORIGINS
A Perfect World
White tea skin guardian
Garde-peau au thé blanc
1 fl.oz./oz. liq./30 ml
Bumble and bumble.
Bb
styling
CREME
crème coiffante
8 FL OZ /OZ LIQ /250 ml
JO MALONE
LONDON
154
COLOGNE
100 ML 3.4 FL OZ
CLINIQUE
dramatically
different
moisturizing lotion

ESTĒE LAUDER
Re-Nutriv
Ultimate Lifting Creme
Crème lifting suprême
M·A·C
LIPGLASS

stila

PORTFOLIO OF BRANDS

ESTĒE LAUDER
Introduced in 1946 • Sold in more than 120 countries and territories • Select products: Intuition, Idealist Skin Refinisher, Re-Nutriv Ultimate Lifting Creme, Advanced Night Repair Eye Recovery Complex, So Ingenious Multi-Dimension Powder Makeup, Illusionist Maximum Curling Mascara, Pure Color Long Lasting Lipstick, Pure Color Nail Lacquer and Pure Color EyeShadow • Technologically advanced and innovative products with a reputation for excellence, sophistication and superior quality.

ARAMIS
Introduced in 1964 • Sold in more than 120 countries and territories • Select products: Aramis Classic, Surface by Aramis, Trifecta by Lab Series for Men, Age Rescue by Lab Series for Men and Eye Rescue by Lab Series for Men • A pioneer in the marketing of prestige men's fragrance, grooming and skin care products.

CLINIQUE
Introduced in 1968 • Sold in more than 125 countries and territories • Select products: 3-Step Skin Care System, Total Turnaround Visible Skin Renewer, Moisture Surge Extra Thirsty Skin Relief, Moisture Sheer Lipstick SPF 15, Long Pretty Lashes Mascara, Aromatics Elixir and Clinique Happy • Allergy-tested, fragrance-free products based on the research of leading dermatologists.

PRESCRIPTIVES
Introduced in 1979 • Sold in 8 countries • Select products: Traceless Skin Responsive Tint, False Eyelashes Plush Mascara, Incredible Lipcolor, Super Line Preventor and Calyx Exhilarating Fragrance • A foundation authority that celebrates women of all skins and all ages with its Color-printing system, Prescriptives is known for its Custom Beauty approach, technologically innovative skin care and makeup, and distinctive visual design.

ORIGINS
Introduced in 1990 • Sold in more than 25 countries and territories • Select products: A Perfect World White Tea Skin Guardian, Have a Nice Day Super-Charged Moisture Cream SPF 15 and Lotion SPF 15, Ginger Soufflé Whipped Body Cream and Salt Rub Smoothing Body Scrub • A feel-good alternative to traditional health and beauty, featuring multi-sensory skin care, color, bath and body, fragrance and hair care products and lifestyle accessories.

M·A·C
Majority interest acquired in 1994; acquisition completed in 1998 • Sold in more than 40 countries and territories • Select products: Studio Fix Powder Plus Foundation, M·A·C Paints, M·A·C Lipstick in 9 formulas and Lipglass • A broad line of color-oriented cosmetics, makeup tools and skin care targeting professional makeup artists and fashion-conscious consumers.

LA MER
Acquired in 1995 • Sold in more than 30 countries and territories • Select products: Crème de la Mer, The Face Serum, The Eye Balm and La Mer SkinColor • An exclusive and highly sought after treatment line combining the finest ingredients with a unique scientific process. In 1999, La Mer expanded from the original, best-selling Crème de la Mer into a complete range of facial skin care and body products.

BOBBI BROWN
Acquired in 1995 • Sold in more than 25 countries and territories • Select products: Creamy Concealer Kit, Foundation Stick, Bobbi Brown Extra, Crystal and Shimmer Lip Gloss, and Long-Wear Gel Eyeliner • A professional beauty line developed by celebrated makeup artist Bobbi Brown, encompassing color cosmetics, fragrance, skin care and professional makeup brushes and accessories.

TOMMY HILFIGER
Exclusive global licensing agreement signed in 1993 • Sold in more than 120 countries and territories • Select products: "tommy," "tommy girl," T for Him, "tommy's juiced up" tantali-zing shower gel and body lotion, "tommy" and "tommy girl" Summer Colognes • Fragrances and body products that reflect the all-American lifestyle themes of designer Tommy Hilfiger.

jane
Acquired in 1997 • Sold in the U.S. in mass merchandisers and chain drug outlets • Select products: Iced Shadow, MegaBites Glossy Gloss, MegaBites Flavorful Lipstick, Fabulizer for Lips and Fabulizer for Eyes • A color cosmetics brand targeted to teen consumers, offering a complete line of face, lip, eye and nail products.

DONNA KARAN
Exclusive global licensing agreement signed in 1997 • Sold in more than 120 countries and territories • Select products: Donna Karan Cashmere Mist, Donna Karan Formula Cleanser, Donna Karan Tinted Moisturizer, DKNY The Fragrance for Women and DKNY The Fragrance for Men • Fragrances and other cosmetics that reflect the quality, style and innovation identified with Donna Karan.

AVEDA
Acquired in 1997 • Sold in more than 20 countries and territories • Select products: Sap Moss Shampoo and Detangler, Hand Relief, Phomollient Styling Mousse, Shampure Shampoo and Conditioner, Be Curly Curl Enhancing Lotion, Rosemary Mint Body Care and Aveda Love Pure-Fume • Premium professional and consumer hair care, styling, professional hair color, skin, body and spa, aroma, makeup and lifestyle products based on the art and science of pure flower and plant essences that fulfill the brand's mission of environmental responsibility.

STILA
Acquired in 1999 • Sold in more than 15 countries • Select products: Lip Glaze, Pivotal Skin, All Over Shimmer and Eye Glaze • Stylish and pretty, makeup artist brand color cosmetics and body products known for their sense of shimmer, eco-friendly packaging and whimsical illustrations.

JO MALONE
Acquired in 1999 • Sold in 5 countries • Select products: Lime Basil & Mandarin Cologne, Grapefruit Scented Home Candle and Nutmeg & Ginger Bath Oil • Sophisticated yet simple lifestyle collection of everyday luxuries created by British fragrance and skin care authority Jo Malone.

BUMBLE AND BUMBLE
Majority interest acquired in 2000 • Sold in more than 10 countries • Select products: Surf Spray, Does It All Styling Spray, Color Support and Deeep Treatment • A New York-based hair care company and salon that markets and sells quality hair care products distributed through top-tier salons and prestige retailers.

kate spade beauty
Exclusive global licensing agreement signed in 1999 • Introduced in spring 2002 • Sold in specialty and select department stores in the United States and Canada • Select products: parfum, eau de parfum, soap trio, buttercream, body moisturizer and travel vanity • *kate spade beauty* is a collection of fragrance, bath and body products. The distinctive fragrance is feminine, timeless and unexpected—a bouquet of Kate's favorite white flowers—complex, yet beautifully tuned.

LEONARD A. LAUDER

CHAIRMAN'S MESSAGE

OUR ANNUAL REPORTS: A PORTFOLIO OF IDEAS SINCE GOING PUBLIC

1996: A Rich Heritage: Our Guiding Principles

1997: Emergence: Change, Momentum, Power, Growth

1998: Managing and Anticipating Demographic Change

1999: Retailtainment and the Revolution in Distribution Channels

2000: Entrepreneurship: New Dimensions for Our Portfolio of Brands

2001: Global Brands: Fine-tuning the Engine for Global Growth

Dear Fellow Stockholders:

World events were not for the faint-of-heart during fiscal 2002. Yet, The Estée Lauder Companies still achieved its 51st year of uninterrupted sales growth—a result all the more noteworthy and gratifying given the historic changes and turbulence in the world and, particularly, our home town of New York.

Terrorism, global economic stress, a roiling stock market, crises of faith in once-trusted institutions and an unsettling awareness that many rules of the game have changed... it is no wonder that the markets—and the people in those markets—have felt rattled. In response, many companies have been quick to announce new initiatives or reforms to bolster stockholder and consumer confidence.

At The Estée Lauder Companies, we need only point to the policies and strategies that we have established over the years to show how we are positioned to cope with these historically topsy-turvy times. Indeed, I have highlighted these strategies in my messages to you since our Company went public in 1995. They are in place both to protect your investment and to propel us for growth.

Great companies are built neither on wide swings of policy and strategy nor on a stodgy attachment to tradition. We honor our rich company heritage because it has *worked,* in tough economic times and good ones. Consistency does not preclude the ability to seize opportunities, limit losses or initiate trends. The Estée Lauder Companies' tradition does require, however, that we pursue growth in a manner consistent with—in the words of our motto—*Bringing the Best to Everyone We Touch*. Responsibly. Ethically. Persistently. Beautifully.

Consider the themes of our last six annual reports, and you will see how well positioned we are for current and future challenges on all the critical fronts:

- *We have diversified our product categories—for men and women:* We are leaders in makeup, skin care and fragrance. We took a dramatic step in hair care in 1997 when we acquired Aveda and complemented it with our acquisition in 2000 of a majority interest in Bumble and bumble, and new hair care offerings from our major brands.
- *We have anticipated demographic changes:* Our products are needed, coveted, purchased and used differently by teenagers, Generations X and Y, boomers, seniors and everyone in between. Fred Langhammer, our CEO, has characterized our brands as "rule breakers" and "rule makers". We appeal to a wider range of consumers with such "rule breaker" and niche brands as Origins, *jane*, Stila, Bobbi Brown, M·A·C, La Mer, Donna Karan and Tommy Hilfiger. Our "rule maker" brands—Estée Lauder, Clinique, Prescriptives and Aramis—have broken some rules of their own while retaining their core consumers over the years. One of our original product offerings in the 1950s, Estoderme, promised to keep youngish skin looking young. Now, our laboratories consistently develop market-leading formulas, such as Estée Lauder Advanced Night Repair Eye Recovery Complex, Clinique Total Turnaround Visible Skin Renewer, Origins A Perfect World White Tea Skin Guardian and Crème de la Mer, that help protect and repair aging skin.
- *We have diversified our distribution:* The Estée Lauder Companies can boast that it has one of the broadest portfolio of distribution options in the beauty and personal care industry, with a sophisticated logistics system that moves some 23,000 different product SKUs. Depending on the brand, its customer base and our market strategy, we can reach different consumers with the appropriate product through department stores, specialty stores, beauty salons, perfumeries, mass outlets or freestanding stores, as well as over the Internet or by direct mail.

GREAT COMPANIES ARE BUILT NEITHER ON WIDE SWINGS OF POLICY AND STRATEGY NOR ON A STODGY ATTACHMENT TO TRADITION. WE HONOR OUR RICH COMPANY HERITAGE BECAUSE IT HAS WORKED, IN TOUGH ECONOMIC TIMES AND GOOD ONES.

- *We have diversified our brands:* Our brands are conceived for diverse groups of consumers, whether they seek high glamour, natural enhancement, romantic illusion, luxurious pampering, healthy protection, outrageous fun or pure maintenance. Our 16 brands are in varying stages of development, providing balance for us in the marketplace. We will continue to look to acquire brands with unique positioning that complement our portfolio. Typically, these are rapidly growing, high-margin brands with passionate, entrepreneurial management teams and potential for long-term global growth.

- *We have diversified geographically:* We are quite excited about the potential in emerging markets, particularly Eastern Europe, Russia and China, and markets where makeup has taken on a symbolic value of freedom and self-expression. While our more developed brands are already available in over 130 countries and territories, we have many opportunities to expand further. Aveda, for example, generates around 85% of its sales domestically; the world awaits. We are able to leverage our distribution network and international expertise to expand the reach of each brand—and will do so carefully, deliberately, appropriately, when the time is right.

These growth platforms are part of a continuing process. We continue to diversify, fine-tune, balance, anticipate and innovate. Today's answer is only good until the question changes, which happens rapidly—in many languages, in many time zones, in many currencies, in many economic climates, for many skin types. What endures is the quality of our product, the quality of our trade and consumer relationships, and the quality of our corporation.

And foremost, it is the quality of our people, at all levels. They are the ones who are diversifying, fine-tuning, balancing, anticipating, innovating and realizing the portfolio of ideas that keeps us competitive.

If the greatest wealth of a company is in its people, we are a very wealthy company. Let me pay tribute to some of the people who are responsible for our success.

OUR BRANDS ARE CONCEIVED FOR DIVERSE GROUPS OF CONSUMERS, WHETHER THEY SEEK HIGH GLAMOUR, NATURAL ENHANCEMENT, ROMANTIC ILLUSION, LUXURIOUS PAMPERING, HEALTHY PROTECTION, OUTRAGEOUS FUN OR PURE MAINTENANCE.

At a time when the quality and integrity of a board of directors is more important than ever, we have assembled a most remarkable group of outside directors to protect your interests, share expertise and add perspective:

- Ambassador Charlene Barshefsky, Washington-based attorney and former U.S. Trade Representative, has been a formidable negotiator and policy maker on the international economic scene. She brings us considerable first-hand knowledge of foreign trade and regulatory issues and a special insight into Far Eastern markets.

- Lady Lynn Forester de Rothschild's concentration as an executive has been in finance and telecommunications, with a transatlantic emphasis. As an entrepreneur herself, she represents the mindset we seek in many of our most propitious acquisitions.

- Irvine O. Hockaday, Jr., retired in December 2001 as President and Chief Executive Officer of Hallmark Cards, Inc., a great family-rooted business that shares many of our beliefs in the nurturing of employees, community and culture. Irv also brings wisdom from his experience on the boards of several major public companies.

- Richard D. Parsons, the brilliant new Chief Executive Officer of AOL Time Warner and a leading citizen of New York City, provides an unparalleled global understanding and vision of the media, communications, entertainment and marketing worlds that both stimulate our business and promote our products.

- Marshall Rose, also a leading citizen of New York City, heads a privately held real estate development company. Marshall's real estate expertise is increasingly useful to us now that we have more than 375 freestanding single-brand stores around the world. We also gain valuable insights from his pivotal leadership in private/public partnerships that support culture and the humanities.

These Directors advise a senior management team that has my greatest respect and admiration. In Fred Langhammer, we have a chief executive who combines intelligence, discipline, collegiality, energy and vision. He and our group presidents—Dan Brestle, Patrick Bousquet-Chavanne, William Lauder, Philip Shearer and Ed Straw—bring collectively over 100 years of industry and company experience to their jobs. They are young "old-timers" in the best sense of the word. They have the wisdom and reflexes of professionals who know our business' culture, yet they are always receptive to new ideas.

They also share my belief that ours should be an organization with the discipline of a public company and the soul of a family business—where everyone is family. Years ago, before books were published on the "Tao" of leadership, our founder, Estée Lauder, wrote that success is based on the ability of leaders to break down barriers, share credit, bring humanity to their businesses and touch the personality in each person who works for them.

That is the work environment we cultivate, and it is the work environment that attracts and retains the best talent in the business. It is not enough, however, to be smart. We want employees who have a talent for teamwork and a commitment to the collective vision and standards of our company. As I travel around the world, I often think I can pick out our employees: They project a special sense of purpose and energy.

We work to recharge their batteries throughout their careers. Our employees regularly revitalize our business. They fuel our growth through continuous innovation in all brands and categories while we enjoy one of the highest employee retention rates in the industry.

OURS SHOULD BE AN ORGANIZATION WITH THE DISCIPLINE OF A PUBLIC COMPANY AND THE SOUL OF A FAMILY BUSINESS—WHERE EVERYONE IS FAMILY.

New product introductions like Advanced Night Repair Eye Recovery Complex, which helps repair and protect the appearance of the delicate skin around the eye, also replenish and protect our income stream. Such a product employs patented technologies, resulting from work done at our labs and elsewhere. And while our ads regularly feature exquisite faces, I would suggest that some of our most beautiful faces are those of employees from our R&D facility, pictured in this report.

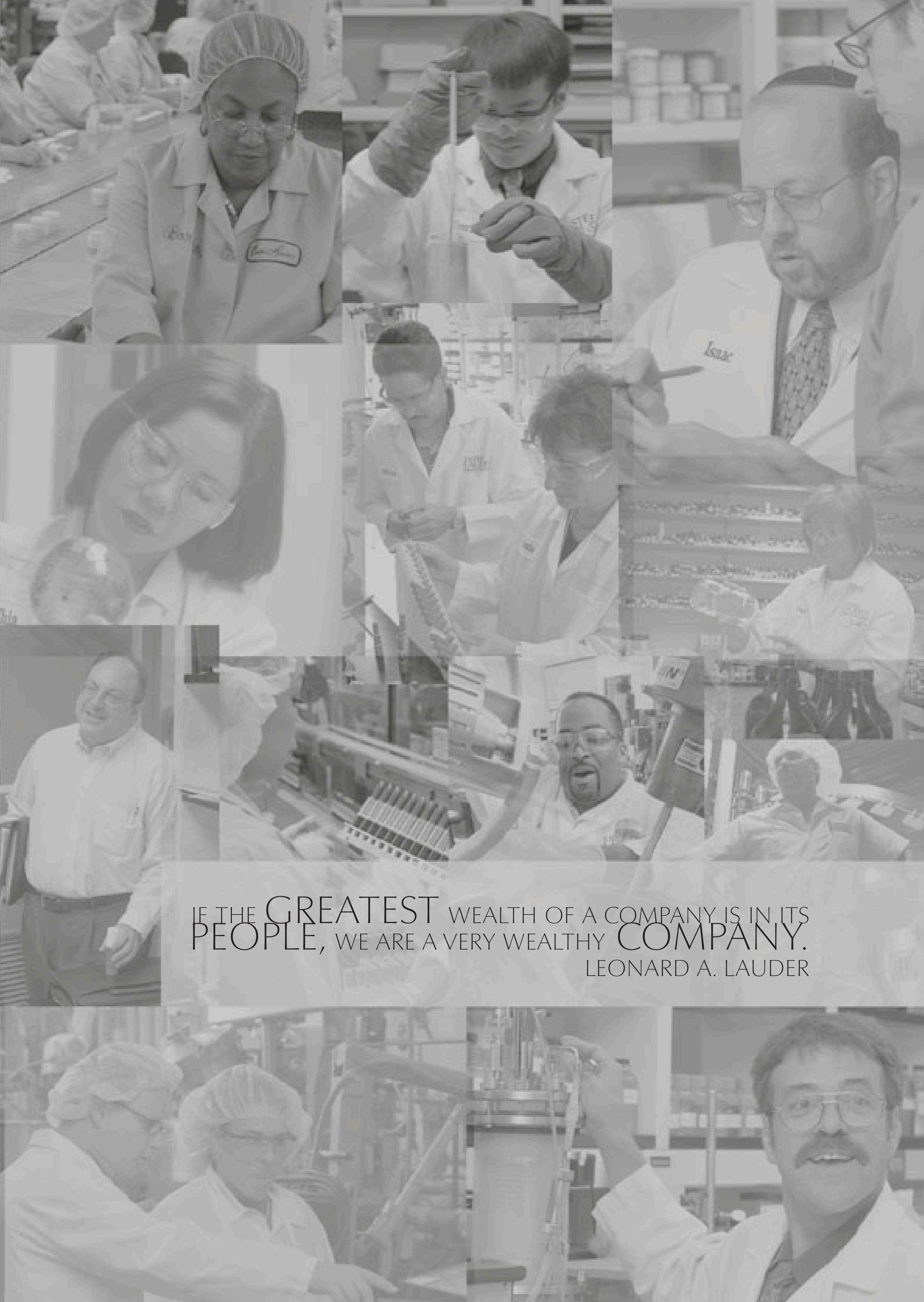
Ours is a business in which manager, employee, customer and stockholder have reason for pride and trust, in which we truly bring out the best in everyone we touch.

Pride in our accomplishments as a shared legacy is a powerful motivator when it comes to meeting and exceeding present and future goals—particularly in tough times.

We thank you for continuing to trust us with your investment. We thank you for being part of the Lauder family.

Sincerely,

Leonard A. Lauder
Chairman of the Board


IF THE GREATEST WEALTH OF A COMPANY IS IN ITS PEOPLE, WE ARE A VERY WEALTHY COMPANY.
LEONARD A. LAUDER

FRED H. LANGHAMMER

CHIEF EXECUTIVE'S REVIEW

Dear Fellow Stockholders:

This was a year of unprecedented challenges—but challenges that our Company met with commitment and determination. I am pleased to report that The Estée Lauder Companies maintained its heritage of over 50 years of uninterrupted sales growth in fiscal 2002. It was a year that demonstrated our commitment to growth even in difficult economies. It was also a year that proved once again that The Estée Lauder Companies is a company that is built on a solid foundation. While the Company is not immune to difficult worldwide challenges, we are well situated to deal with them. Once again, the diversity of our brands, geographies, categories and channels of distribution, along with our unrelenting drive for innovation, helped us to meet worldwide challenges. With 16 brands and a presence in more than 130 countries and territories, we benefit from a rich selection of highly innovative products in a balanced mix of categories that help drive consumer loyalty and sales. Our vision of ourselves as "long distance runners" as opposed to "sprinters" has proven to be a sound approach.

In fiscal 2002, many factors impeded our growth: the economic weakness in our major markets—the United States and Japan; the strength of the U.S. dollar and its effect on currency translation; the slowdown in U.S. department store and shopping mall traffic; the decline in international travel following the events of September 11th that led to a significant drop in our travel retail business and inventory contraction by U.S. retailers. This was an extraordinary convergence of events that we are factoring into our plans.

Once again, we grew our business in all regions of the world, with particular strength in Europe and some parts of Asia. For the second year, Clinique maintained its position as the second largest makeup brand in prestige distribution in Europe, and the Estée Lauder brand, which also had a strong year internationally, continued to broaden its consumer base while remaining true to its heritage.

We generated net sales in fiscal 2002 of $4.74 billion, a 2% increase over fiscal 2001. In constant currency, net sales for the year grew 3%. Our net earnings were $289.4 million compared with $347.7 million in fiscal 2001. Diluted earnings per common share were $1.10 compared with $1.34 in the prior year. These results are before the cumulative effect of a change in accounting principles and before the restructuring charges, but include $.05 per common share of goodwill amortization in fiscal 2001, as detailed in this annual report on page 43.

In Europe, the Middle East & Africa, net sales increased 3% over last year, excluding the impact of foreign currency translation. Excluding the shortfall in the Company's travel retail business, which is reported in this region, net sales in local currency increased 9%. The Company posted a 3% increase in reported net sales for the region over the prior year to $1.26 billion. On a local currency basis, Asia/Pacific net sales grew 9% versus the prior year. Net sales in the region on a reported basis rose 2% to $610.6 million. In the Americas, our largest region, which was particularly affected by external challenges, sales rose 1% to $2.88 billion.

RESULTS BY PRODUCT CATEGORY

Product innovation, one of our hallmarks, continued as a strong impetus for growth this year. Many of our brands benefited from cutting edge technologies developed by our laboratories that furthered our reputation for superior products while increasing our speed-to-market. We have introduced more than 300 new products this year that incorporate the best ideas from around the world. This is one of the key benefits of our global reorganization announced last year. Our innovation extends into our packaging and for the second year in a row, *Cosmetics and Packaging Magazine* named us Packager of the Year.

OUR VISION OF OURSELVES AS "LONG DISTANCE RUNNERS" AS OPPOSED TO "SPRINTERS" HAS PROVEN TO BE A SOUND APPROACH.

Makeup sales benefited from a surge in lip and eye products. Net sales of makeup products for the year rose 5% before the impact of foreign currency translation and increased 4% to $1.79 billion on a reported basis.

Skin care sales for the fiscal year rose 4% before foreign currency translation, while reported sales increased 3% to $1.70 billion.

Fragrance had a difficult year that resulted in a 6% decline in sales to $1.02 billion. Our fragrance category was particularly hard hit by the slowdown in the United States and the disruption in the travel retail business. These two areas account for approximately two thirds of our fragrance business. However, fragrance remains important to our Company and we will continue to support it. Collectively, The Estée Lauder Companies produces more than 70 individual fragrances and four of the top ten prestige fragrances sold at U.S. department stores during fiscal year 2002.

The **hair care** category posted the strongest sales growth, off a smaller base, with reported net sales up 19% to $215.8 million. Our focused distribution strategy has built increased awareness for our brands, resulting in higher productivity per door.

TAKING ACTION

To improve our performance, our Company continually examines all areas of our businesses. In particular, during economic slowdowns, we look to identify those areas where prospects are not apparent. This process leads to action. This year, we took a one-time, $117.4 million pre-tax charge relating to four areas—the Internet, supply chain, distribution and globalization of our organization—to position us for a return to our goal of double-digit earnings growth. These actions free resources to stimulate sales through focused investment. Our commitment to building and maintaining the equity of our brands dictates that we spend on innovation, as well as advertising and promotion. This continues to be the best recipe for growth.

This year, inventory management became more stringent as a result of slower retail sell-through and the desire of our retail customers to carry lower inventory levels. We responded quickly, adjusting procurement and manufacturing production levels. The outcome was a dramatic improvement in inventory levels that favorably affected cash flow. This accomplishment was the result of a great team effort.

Our freestanding retail stores, while not immune to overall market conditions, continue to present great opportunities for enhancing the consumer's experience with brands like Origins, M·A·C and Aveda. We now have over 375 single brand, company-owned stores around the world.

REACHING OUT TO THOSE WE CARE ABOUT

At a time when many corporations are re-examining their images, positions and codes of conduct, I believe our corporate reputation has never been stronger. We received several prestigious awards for our integrity. On June 5, 2002, the Company was honored by the Foreign Policy Association and received its award for Social Responsibility in recognition of our outstanding corporate citizenship. We at The Estée Lauder Companies strive to find new ways to be of service to our consumers, stockholders and employees, as well as to our communities.

This passion has given birth to countless initiatives in many different areas such as The Estée Lauder Breast Cancer Awareness Campaign, which supports the work done by The Breast Cancer Research Foundation; the M·A·C AIDS Fund, which has raised more than $24 million through the sales of its Viva Glam lipsticks; Aveda's support of the environment with the Earth Month Program; our contributions and our employees' contributions to the Twin Towers Fund and the American Red Cross which raised more than $1.4 million for the families who suffered the effects of September 11th, and the many other activities organized by our corporate volunteer programs.

AT A TIME WHEN MANY CORPORATIONS ARE RE-EXAMINING THEIR IMAGES, POSITIONS AND CODES OF CONDUCT, I BELIEVE OUR CORPORATE REPUTATION HAS NEVER BEEN STRONGER.

BUILDING AND BONDING FOR FUTURE GROWTH

As I continue to reflect on our growth model, two words come to mind: *building* and *bonding*. We must continue to *build* an even greater future based on the strengths and heritage of our past. And we must relentlessly forge even stronger emotional *bonds* with our customers. They are the ultimate decision-makers in buying our products. We must be relentless in meeting and exceeding their expectations and enabling them to bond with our brands, not only by selling products, but also by recognizing their needs and sharing in their concerns. In other words, bonding requires that we go beyond the products themselves and create emotional ties with consumers through the experiences we provide at every point of contact. We strive to listen carefully and translate what we

learn into the creative fulfillment of their needs. Of course, we do this every day through events, promotions and the service a customer receives every time she visits a counter. However, we also do it through our Global Consumer Communications department, which has created a substantial database of more than 300,000 customers from whom we regularly solicit feedback.

WE MUST CONTINUE TO BUILD AN EVEN GREATER FUTURE BASED ON THE STRENGTHS AND HERITAGE OF OUR PAST. AND WE MUST RELENTLESSLY FORGE EVEN STRONGER EMOTIONAL BONDS WITH OUR CUSTOMERS.

LOOKING AHEAD

As I look ahead to the coming year, I see optimism and prudence, opportunities and risks, potentials and pitfalls. First and foremost, driving brand equity is paramount. This is accomplished with exciting new products, effective advertising and promotion, and superior service. I expect continued challenges from a slower economic recovery in the U.S., but sequential improvement in our travel retail business. We will benefit from cost savings resulting from this year's restructuring and will reinvest a portion of those savings to build sales momentum. I believe the commitment to invest in sales growth sets the stage for strong performance and a return to strong earnings growth.

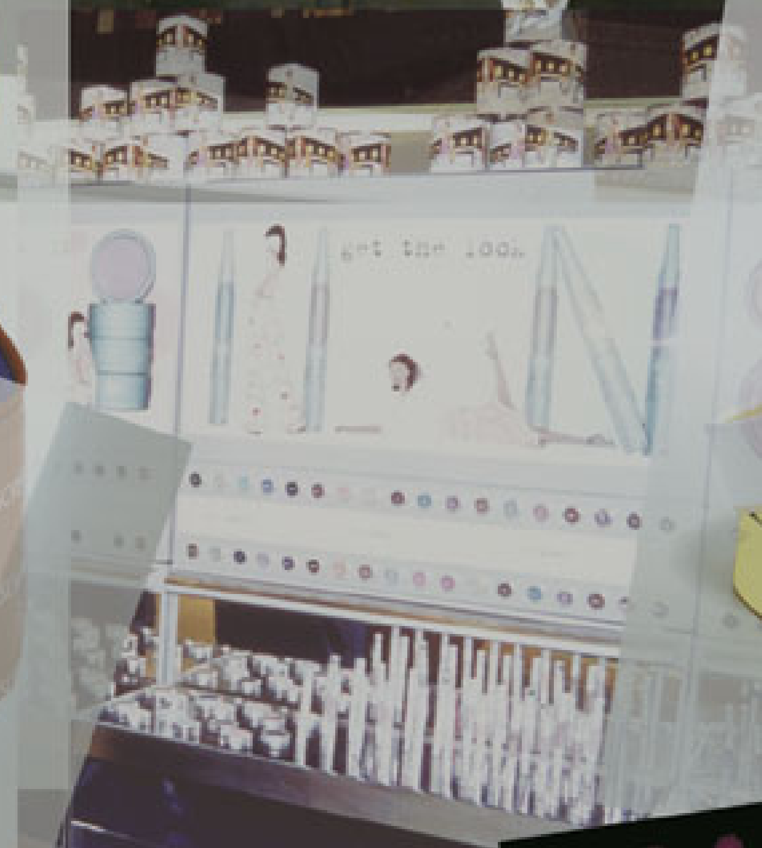
Finally, following the pressures of the year, I am more grateful than ever for the loyalty and dedication of our employees. My congratulations and gratitude to all of my colleagues. In addition, I would like to acknowledge the guidance and support of our Board of Directors during a year that demanded the highest levels of attention, and to our Chairman, Leonard Lauder, whose continued passion and inspiration are an invaluable asset to our Company. And finally, my deepest appreciation to our valued stockholders for your continued support and commitment.

Sincerely,

Fred H. Langhammer
President and Chief Executive Officer

LAUDER

PRESCRIPTIVES


get the look

WHAT'S NEW

The Estée Lauder Companies strives to bring leadership and innovation to the world of beauty—whether it's through a cutting-edge new product, an exciting packaging design, philanthropic leadership or unsurpassed training for our professionals. In fiscal 2002, our standards of excellence were recognized by more than 110 industry and magazine awards received in honor of our outstanding people and products. Following are highlights from some of the exciting 2002 brand initiatives.

Aveda opened the Aveda London Institute, with an advanced education center for beauty professionals, a retail store and a salon.

Stila launched at Bloomingdale's with a highly original vending machine display.

In 2002, Mrs. Estée Lauder was recognized as the International Business Leader of the Year by the U. S. Department of Commerce.

A new team of trend experts helped the Estée Lauder brand shape the latest global trends, while the *jane* brand collaborated with the hip, savvy teens at New York City's High School of Art and Design to develop its fresh new advertising campaign.

American patriotism was proudly showcased in the Prescriptives "Pride Bag", which was created to honor all of the American women at the Winter Games in Salt Lake City, Utah.

Estée Lauder introduced its glamorous new spokesmodel, Carolyn Murphy, in a campaign for the launch of Advanced Night Repair Eye Recovery Complex, while Intuition for Men celebrated its June launch in suitable style by ringing the closing bell at the New York Stock Exchange.

And, finally, Bobbi Brown's efforts for Dress for Success joined the long tradition of giving at The Estée Lauder Companies.

kate spade
eau de parfum

INTUITIO

tommy
summer
cologne

FRAGRANCE

After nearly 50 years and the introduction of over 70 fragrances—including White Linen, this year's Hall of Fame inductee at the Fragrance Foundation's FiFi Awards—The Estée Lauder Companies remains one of the world's pre-eminent fragrance houses. Our success is based on our ability to introduce fragrances that are both universally aspirational and timelessly appealing, then build them into true brands.

Important contributors to the category, which accounted for 21% of our net sales, included Beautiful, Clinique Happy and Estée Lauder *pleasures*, which held the top three rankings in the United States prestige distribution for the fiscal year, as well as "tommy" and the launch of T for Him. However, this category continued to be impacted by the softness of the fragrance business in the United States and the decline in our travel retail business, which depends substantially on fragrance products.

In Europe, Clinique Aromatics Elixir sold at a rate of three bottles every minute. In the U.S., the eagerly awaited debut of *kate spade beauty* in May exceeded expectations. The distinctive scent is built around honeysuckle, complemented by gardenia, jasmine, tuberose and fresh muguet. The line includes fragrance, bath and body products such as parfum, body wash and sheer body oil.

Estée Lauder's latest fragrance, Intuition, was joined by Intuition for Men, a seductive solar oriental composed of sage absolute, patchouli, cedarwood and amber. The brand also introduced new fragrance forms such as the limited-edition Estée Lauder *pleasures* Liquid Summer and Intuition Fragrance Silk.

Jo Malone added 154, named for the address of her first London store, and Red Roses, a lush floral that arrived in time for Valentine's Day.

New from Bobbi Brown is Bobbi Brown Beach, a summery fragrance combining sand jasmine, sea spray, dianthus, neroli and driftwood.

Love, an Aveda classic, returned with a new formula incorporating sandalwood sourced from sustainably managed forests in Australia, along with organic ylang ylang, jasmine and rose.

Origins expanded Peace of Mind with its Sensory Therapy Collection (five new products, including Tension Relieving Vapor Bath and Relaxing Massage Oil), which was named U.S. Bath & Body Star of the Year at the Fragrance Foundation's FiFi Awards.

Clinique introduced Clinique Happy Cooling Shimmer Gel, capitalizing on the latest trend of mixing scent with shimmer.

Cashmere Mist, the nine-year-old scent from Donna Karan, recorded its best United States performance ever. Meanwhile, DKNY Women and DKNY Men continued to be strong performers in international markets.

The Tommy Hilfiger fragrance business was driven by expanded distribution in the United States, helped by the T for Him fragrance launch, increased sales in Europe, and positive response to the "tommy" and "tommy girl" Summer Colognes in the United States.

OND DE TEINT DE LA MER™
LA MER
the fluid foundation
le fond de teint fluide

M·A·C

BOBB

stila
all over
shimmer
0.5oz. 14gm

MAKEUP

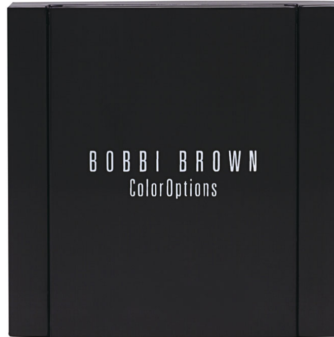
At The Estée Lauder Companies, we don't simply make makeup—we develop makeup brands with distinct identities that together appeal to a wide range of consumer tastes. This year, that diversity lifted sales of our makeup products 4%, with the category responsible for 38% of our overall net sales.

This was a particularly important year for mascara with four major launches, including Clinique's Long Pretty Lashes Mascara, which extends lashes up to 30%. Illusionist Maximum Curling Mascara from Estée Lauder launched with a special gel formula and patent-pending brush. M·A·C launched Pro-Lash Mascara, a flake-proof, smudge-proof lash lengthener/thickener. And Prescriptives created False Eyelashes Plush Mascara, which boosts volume, length, density and curl.

Clinique's highlights included Moisture Sheer Lipstick SPF 15, Gentle Light Makeup and Gentle Light Powder. In Asia, lightening/whitening technology was extended to makeup with Active White Light Reflecting Powder Makeup, Whitening Lab Formula Essence and Stay True Powder Makeup.

Unique transparent packaging created for Estée Lauder's Pure Color makeup line supported the brand's distinctive, modern and sophisticated image. And So Ingenious is a new-generation powder makeup that adjusts to shifts in light. In Japan, Estée Lauder introduced the industry's first whitening makeup, the StarWhite Brightening Collection.

M·A·C had an outstanding year. New products include Studio Tech Foundation, which creates a natural matte finish; Cheekhue, a creamy blush that dries to a powder finish, and Viva Glam IV, the fourth in a line of lipsticks benefiting the M·A·C AIDS Fund, with ads featuring Elton John, Mary J. Blige and Shirley Manson.



Prescriptives' Traceless Skin Responsive Tint, a revolutionary new sheer foundation, won Cosmetic Executive Women's Best in Beauty Award for Best New Makeup Product for Face. Traceless adjusts skin's light reflection to neutralize imperfections and even skin tone. Also new is Incredible Lip Color, 25 shades that moisturize, condition and protect.

The Bobbi Brown brand demonstrated exceptional vitality in foundations, particularly with Moisture Rich Foundation and Oil Free Even Finish Compact. Creamy Concealer Kit, Creamy Eye Pencil and Lip Liner, and Crystal Gloss gained strong acceptance.

Foundation and powder created excitement for Origins, which launched Stay Tuned Balancing Face Makeup for combination skin, and Nude and Improved Bare-face Makeup with SPF 15 sunscreen, along with Silk Screen

Refining Powder Makeup, a sheer skin perfector. Other innovations include Underwear For Lips and Underwear For Lids, primers that improve lip color and eye makeup performance.

jane delivered prestige technology to the self-select market with Iced Shadow, a reflective eye shadow in a unique sifter pot; Fabulizer for Eyes, which has a unique wand applicator, and Megabites Glossy Gloss, a lipcolor that delivers shine and condition.

Stila's packaging innovation was demonstrated by the new Lip Glaze Palette, composed of five split pans containing 10 shades. The brand expanded its Convertible Color line with Convertible Eye Color, a portable eye product that contains a shadow, liner and smudger, and launched Illuminating Liquid Foundation, a liquid version of its Illuminating Powder Foundation. Color stories, such as Winter Blues and High Tea, also attracted consumers.

CLINIQUE
sun-care
body
30
SPF sun block
5 FL.OZ./150 ml ℮

SKIN CARE

Skin care and innovation go hand in hand at The Estée Lauder Companies. This year, that potent partnership propelled four of our brands—Clinique, Estée Lauder, Origins and Prescriptives—to top-10 prestige department store skin care sales in the United States. Overseas, the Clinique and Estée Lauder brands were especially strong. In the European and Asian markets, they are among the top 10 prestige skin care brands. In all, the category, which accounts for 36% of the Company's net sales, was up 3%.

Superior technology powered blockbuster launches such as A Perfect World White Tea Skin Guardian from Origins, the first product to harness the benefits of white tea, which is approximately 100% more effective than green tea as an antioxidant. The Company's "technology bank" makes cutting-edge formulas and packaging available to individual brands. For example, Jo Malone's new skin care line contains products from this resource—products such as Juniper Skin Tonic, Protein Skin Serum and Orange & Geranium Night Cream.

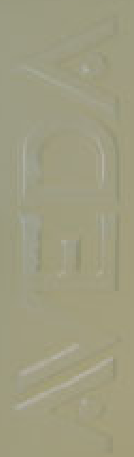
The Estée Lauder brand benefited from the global launch of Advanced Night Repair Eye Recovery Complex, which targets lines, dryness, puffiness and dark circles with a unique formula containing anti-irritant and optic technology. This outstanding product was recognized by Cosmetic Executive Women as the industry's "Best New Facial Skincare Product for Eye Treatment". Re-Nutriv Ultimate Lifting Creme entered the luxury segment with precedent-setting anti-aging technology.

Breakthrough newcomers and incumbent category leaders such as Dramatically Different Moisturizing Lotion helped Clinique remain a leader in skin care. Total Turnaround Visible Skin Renewer, a new best-seller that uses next-generation technology to improve skin's appearance, as well as Moisture Surge Extra Thirsty Skin Relief and Moisture Surge Eye Gel, drove sales worldwide, especially in Europe, where Clinique remained the second fastest-growing and fourth largest skin care line among the top ten in prestige distribution. Meanwhile, Clinique Sun Care Body Spray SPF 30 Sun Block won Cosmetic Executive Women's Best in Beauty Award for Best New Sun Product in the United States.

The latest offering from Bobbi Brown is Intensive Skin Supplement, an advanced, multi-benefit serum that refines skin's appearance while helping to prevent the visible signs of aging. This product launch, along with the Extra Skincare Collection, helped drive sales for Bobbi Brown in skin care.

Lab Series for Men by Aramis introduced Trifecta, a daily treatment that reduces shine and pore size while improving skin texture. Aramis also premiered Energizing Body Tonic, 24 Hour Performance Antiperspirant Spray and Invigorating Body Shampoo.

La Mer's momentum continued. Two launches, The SPF 18 Fluid, a lightweight sunscreen for the face, and The Lip Balm, featuring a blend of marine ingredients that help retain moisture and softness, contributed to the brand's growth.


AVEDA™
THE ART AND SCIENCE OF PURE FLOWER AND PLANT ESSENCES™
sap moss™
CONDITIONING DETANGLER
DÉMÊLANT CONDITIONNEUR
sap moss carries conditioning ingredients for dry hair
sap moss contient des ingrédients conditionneurs pour cheveux secs
AVEDA™
THE ART AND SCIENCE OF PURE FLOWER AND PLANT ESSENCES™
rosemary mint shampoo
with organic invigoration
revitalisant biologique
FOR FINE/NORMAL HAIR
POUR CHEVEUX NORMAUX OU FINS
8.5 fl oz/250ml ℮
Bb.
Bumble and bumble.
grooming
CREME
The dream creme for
ORIGINS
Ginger Up™
Aromatic conditioner
Après-shampooing aromatique
air care

HAIR CARE

Hair care remains an exciting and emerging category for us, expanding 19% and representing 5% of our overall net sales. Critical to our success is our focus on limited, prestige salon distribution for Bumble and bumble and Aveda. We find that this strategy improves the performance and quality of our existing salon customers. Finally, this was a particularly good year for our styling entries with several brands launching products that generated strong sales.

Aveda continues to grow, thanks to styling products such as Be Curly Curl Enhancing Lotion and Hang Straight Straightening Lotion. Also new this year is Control Paste, an extension of the brand's Control line of products that offers moldable texture for use on dry hair. We also launched Full Spectrum Deposit Only Color Treatment, a salon professional-use-only hair color that delivers superior color, condition and shine in a formula that is 99% naturally derived from plants and non-petroleum-based minerals. New shampoos and conditioners such as Color Conserve, as well as existing players in the Shampure and the Rosemary Mint lines, also contributed significantly to net sales, particularly in liter sizes, which are more economical and support the brand's philosophy of environmental responsibility.

Clinique's Simple Hair Care remains the category leader in United States prestige department stores. The brand added to its styling collection this year with Shaping Wax, which offers flexible, long-lasting style and texture in a non-greasy, non-sticky formula.

Bumble and bumble contributed with increased product sales. New to the line are Alojoba Shampoo and Alojoba Conditioner, moisture-rich formulas containing aloe vera, jojoba, cucumber and chamomile, and Sumotech, a paste/wax hybrid that imparts hold without stiffness. In addition to product innovation, the brand has set new marketing standards for the industry, maximizing product sales by capitalizing on the power and credibility of the stylist recommendation coupled with exciting retail presentation. These skills are taught at Bumble and bumble University, a new educational division that shares the brand's unprecedented business and technical expertise with its wholesale salon customers.

Origins' artful use of one category as a platform to launch others continued as the brand extended the ginger scent of its body products to hair care with Ginger Up Aromatic Shampoo and Conditioner. The line also benefited from the ongoing popularity of Clear Head Shampoo and Knot Free Finishing Rinse.

Cashmere Mist Shampoo, a luxurious, volume-building cleanser, and Cashmere Mist Conditioner, an intensive detangler, continued to contribute to the successful hair care business for the Donna Karan Cashmere Mist fragrance line.

The essence

NEW
FALSE EYELASHES
PLUSH MASCARA

VOLUME
VOLUPTUOUS WOW
PRESCRIPTIVES
CUSTOM BEAUTY

Take your skin to a
better place.

ORIGINS

Origins introduces
A Perfect Wo
White tea skin guardia

A Perfect World
White tea skin guardian

Soho, NorthPark Center, Century

DKNY ENERGY W
DKNY ENERGY M

T FOR HIM
THE FRAGRANCE

ADVERTISING AND PROMOTIONS

The Estée Lauder Companies builds global brands with unique personalities. Investing in the strength and growth of these brands worldwide is one of the Company's top priorities.

In fiscal 2002, advertising and promotion spending totaled $1.33 billion, an increase of 6%, driven partially by our continued desire to support the brands at retail and several successful launches, such as Clinique Total Turnaround Visible Skin Renewer, Origins' A Perfect World White Tea Skin Guardian and Estée Lauder Advanced Night Repair Eye Recovery Complex.

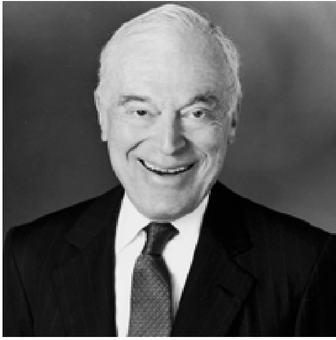
Building relationships with consumers through philanthropic activity is a key objective for brands like M·A·C. Viva Glam IV is the fourth lipstick in the line benefiting the M·A·C AIDS Fund with ads featuring Elton John, Mary J. Blige and Garbage's Shirley Manson.

Favorable coverage by the press also keeps us in the spotlight. Lifetime Television's *Intimate Portrait: Estée Lauder* was an hour-long tribute that celebrated the family's accomplishments, led by Estée, Evelyn, Aerin and Jane Lauder.

The launch of *kate spade beauty* received unparalleled attention from journalists, while La Mer's remarkable celebrity word-of-mouth added to the brand's allure. Lauder's Leading Lipstick Index made global headlines as an "economic indicator" when record sales for our holiday lipstick collections demonstrated that lipstick sales rise in a less-than-rosy economy.

Finally, nothing touches the consumer quite as directly as an in-store personal appearance. Bobbi Brown, Stila's Jeanine Lobell and Jo Malone drew an extraordinary number of customers to their counters around the world with personal appearances. Meanwhile, Clinique's global promotion, Colour Play Date—Fun with Makeup Workshops, boosted its makeup sales by double digits in the U.S. alone. Another in-store effort fueled the Tommy Hilfiger T launch with a national "T Apartment" sweepstakes, giving away $25,000 worth of furnishings, apparel and accessories.

BOARD OF DIRECTORS



LEONARD A. LAUDER[3]
Chairman
The Estée Lauder Companies Inc.

FRED H. LANGHAMMER
President
Chief Executive Officer
The Estée Lauder Companies Inc.

RONALD S. LAUDER
Chairman
Clinique Laboratories, Inc.

Private Investor

WILLIAM P. LAUDER
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The Estée Lauder Companies Inc.

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Managing Partner
The Georgetown Group

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AOL Time Warner Inc.

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ELR Holdings, Ltd.

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Wilmer, Cutler & Pickering

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Retired President & Chief Executive Officer
Hallmark Cards, Inc.

1 Member of Audit Committee
2 Member of Compensation Committee
3 Member of Nominating and Board Affairs Committee
4 Member of Stock Plan Subcommittee

OFFICERS

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Chairman

RONALD S. LAUDER
Chairman
Clinique Laboratories, Inc.

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President
Chief Executive Officer

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Group President

DANIEL J. BRESTLE
Group President

ANDREW J. CAVANAUGH
Senior Vice President
Global Human Resources

PAUL E. KONNEY
Senior Vice President
General Counsel and Secretary

RICHARD W. KUNES
Senior Vice President
Chief Financial Officer

EVELYN H. LAUDER
Senior Corporate Vice President

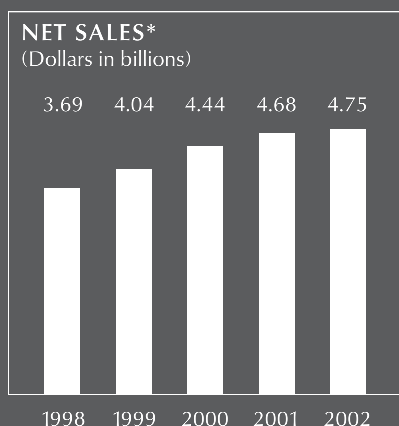
WILLIAM P. LAUDER
Group President

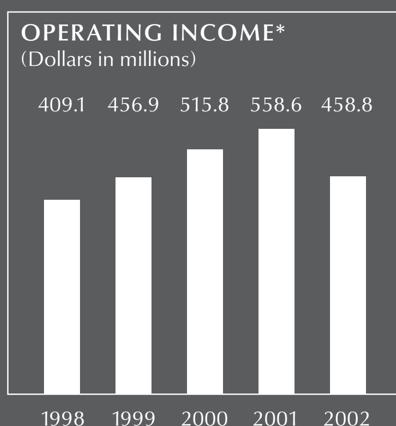
PHILIP SHEARER
Group President, International

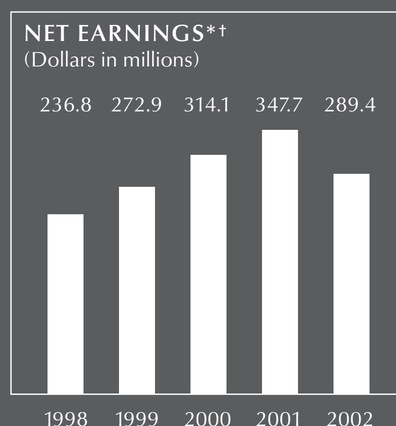
EDWARD M. STRAW
President
Global Operations

SALLY SUSMAN
Senior Vice President
Global Communications

YEAR ENDED JUNE 30	2002	2001	Percent Change
(Dollars in millions, except per share data)			
Net Sales*	**$4,749.9**	$4,675.7	2%
Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA)*	**620.6**	721.5	(14%)
Operating Income*	**458.8**	558.6	(18%)
Net Earnings (before preferred dividends)*	**289.4**	347.7	(17%)
Net Earnings Per Share—Diluted*	**1.10**	1.34	(18%)
AT JUNE 30			
Total Assets	**$3,416.5**	$3,218.8	6%
Stockholders' Equity	**1,461.9**	1,352.1	8%

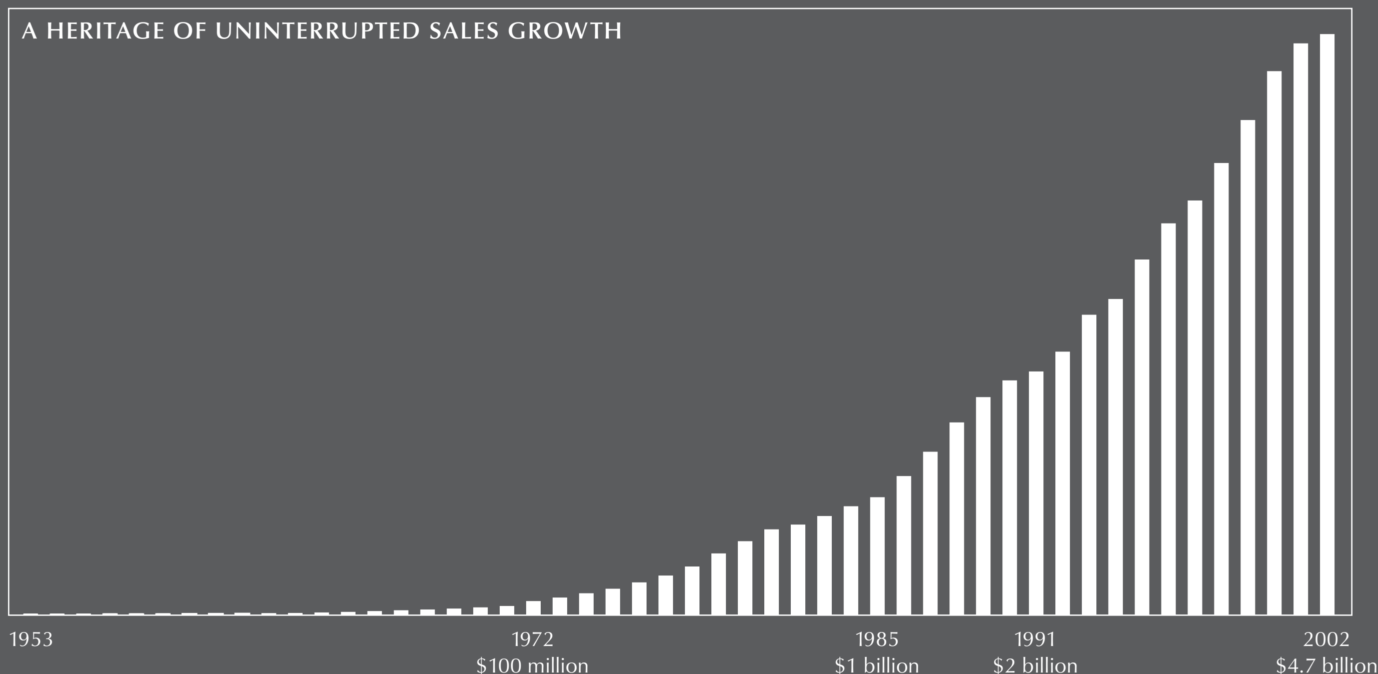






* Fiscal 2002 information is reported before considering the effect of restructuring charges of $117.4 million ($76.9 million after tax), or $.32 per common share, and before the cumulative effect of adopting a new accounting principle in the amount of $20.6 million, or $.08 per common share. Fiscal 2001 information is reported before considering the effect of restructuring and other non-recurring charges of $63.0 million ($40.3 million after tax), or $.17 per common share, before the cumulative effect of adopting a new accounting principle in the amount of $2.2 million after tax, or $.01 per common share, and includes goodwill amortization of $20.9 million ($13.4 million after tax), or $.05 per common share.

† Before preferred dividends.



The table below summarizes selected financial information. For further information, refer to the audited consolidated financial statements and the notes thereto contained elsewhere herein.

YEAR ENDED OR AT JUNE 30	**2002**	2001	2000	1999	1998
(In millions, except per share data)					
STATEMENT OF EARNINGS DATA:					
Net sales[(a)]	**$4,743.7**	$4,667.7	$4,440.3	$4,040.3	$3,688.7
Gross profit[(a)]	**3,470.3**	3,441.3	3,202.3	2,877.5	2,609.6
Operating income	**341.4**	495.6	515.8	456.9	409.1
Earnings before income taxes, minority interest and accounting change	**331.6**	483.3	498.7	440.2	402.8
Net earnings	**191.9[(b)]**	305.2[(c)]	314.1	272.9	236.8
Preferred stock dividends	**23.4**	23.4	23.4	23.4	23.4
Net earnings attributable to common stock	**168.5[(b)]**	281.8[(c)]	290.7	249.5	213.4
CASH FLOW DATA:					
Net cash flows provided by operating activities	**$ 518.0**	$ 305.4	$ 442.5	$ 352.3	$ 258.2
Net cash flows used for investing activities	**(217.0)**	(206.3)	(374.3)	(200.3)	(577.2)
Net cash flows (used for) provided by financing activities	**(121.8)**	(63.5)	(87.9)	(73.2)	345.2
PER SHARE DATA:					
Net earnings per common share[(d)]					
Basic	**$ .71[(b)]**	$ 1.18[(c)]	$ 1.22	$ 1.05	$ .90
Diluted	**$ .70[(b)]**	$ 1.16[(c)]	$ 1.20	$ 1.03	$ .89
Weighted average common shares outstanding[(d)]					
Basic	**238.2**	238.4	237.7	237.0	236.8
Diluted	**241.1**	242.2	242.5	241.2	239.5
Cash dividends declared per common share[(d)]	**$ .20**	$ .20	$ .20	$ .1775	$ .17
BALANCE SHEET DATA:					
Working capital	**$ 968.0**	$ 882.2	$ 716.7	$ 708.0	$ 617.2
Total assets	**3,416.5**	3,218.8	3,043.3	2,746.7	2,512.8
Total debt	**410.5**	416.7	425.4	429.1	436.5
Redeemable preferred stock	**360.0**	360.0	360.0	360.0	360.0
Stockholders' equity	**1,461.9**	1,352.1	1,160.3	924.5	696.4

(a) Effective January 1, 2002, we adopted Emerging Issues Task Force ("EITF") Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer". Upon adoption of this Issue, we reclassified revenues generated from our purchase with purchase activities as sales and the costs of our purchase with purchase and gift with purchase activities as cost of sales, which were previously reported net as operating expenses. Operating income has remained unchanged by this adoption. For purposes of comparability, these reclassifications have been reflected retroactively for all periods presented.

(b) Net earnings, net earnings attributable to common stock and net earnings per common share for the year ended June 30, 2002 included a restructuring charge of $76.9 million, after tax, or $.32 per common share, and a one-time charge of $20.6 million, or $.08 per common share, attributable to the cumulative effect of adopting Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets".

(c) Net earnings, net earnings attributable to common stock and net earnings per common share for the year ended June 30, 2001 included restructuring and other non-recurring charges of $40.3 million, after tax, or $.17 per common share, and a one-time charge of $2.2 million, after tax, or $.01 per common share, attributable to the cumulative effect of adopting SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities".

(d) On April 26, 1999, the Board of Directors approved a two-for-one stock split in the form of a 100% stock dividend on all of our outstanding Class A and Class B Common Stock. The stock dividend was paid on June 2, 1999 to all holders of record of shares of our Common Stock at the close of business on May 10, 1999. All share and per share data prior thereto have been restated to reflect the stock split.

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions, except per share data)			
Net Sales	**$4,743.7**	$4,667.7	$4,440.3
Cost of sales	**1,273.4**	1,226.4	1,238.0
Gross Profit	**3,470.3**	3,441.3	3,202.3
Operating expenses:			
Selling, general and administrative	**3,002.0**	2,869.2	2,653.3
Restructuring	**110.4**	37.6	—
Other non-recurring	**—**	16.3	—
Related party royalties	**16.5**	22.6	33.2
	3,128.9	2,945.7	2,686.5
Operating Income	**341.4**	495.6	515.8
Interest expense, net	**9.8**	12.3	17.1
Earnings before Income Taxes, Minority Interest and Accounting Change	**331.6**	483.3	498.7
Provision for income taxes	**114.4**	174.0	184.6
Minority interest, net of tax	**(4.7)**	(1.9)	—
Net Earnings before Accounting Change	**212.5**	307.4	314.1
Cumulative effect of a change in accounting principle, net of tax	**(20.6)**	(2.2)	—
Net Earnings	**191.9**	305.2	314.1
Preferred stock dividends	**23.4**	23.4	23.4
Net Earnings Attributable to Common Stock	**$ 168.5**	$ 281.8	$ 290.7
Basic net earnings per common share:			
Net earnings attributable to common stock before accounting change	**$ .79**	$ 1.19	$ 1.22
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**$ .71**	$ 1.18	$ 1.22
Diluted net earnings per common share:			
Net earnings attributable to common stock before accounting change	**$ .78**	$ 1.17	$ 1.20
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**$ .70**	$ 1.16	$ 1.20
Weighted average common shares outstanding:			
Basic	**238.2**	238.4	237.7
Diluted	**241.1**	242.2	242.5

See notes to consolidated financial statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in those financial statements. These judgements can be subjective and complex, and consequently actual results could differ from those estimates. Our most critical accounting policies relate to revenue recognition; concentration of credit risk; inventory; pension and other postretirement benefit costs; goodwill and other intangible assets; income taxes; and derivatives.

REVENUE RECOGNITION

Generally, revenues from merchandise sales are recorded at the time the product is shipped to the customer. We report our sales levels on a net sales basis, which is computed by deducting from gross sales the amount of actual returns received and an amount established for anticipated returns.

As is customary in the cosmetics industry, our practice is to accept returns of our products from retailers if properly requested, authorized and approved. In accepting returns, we typically provide a credit to the retailer against sales and accounts receivable from that retailer on a dollar-for-dollar basis.

Our sales return accrual is a subjective critical estimate that has a direct impact on reported net sales. This accrual is calculated based on a history of gross sales and actual returns by region and product category. In addition, as necessary, specific accruals may be established for future known or anticipated events. As a percentage of gross sales, sales returns were 4.9%, 4.9% and 4.3% in fiscal 2002, 2001 and 2000, respectively.

CONCENTRATION OF CREDIT RISK

An entity is more vulnerable to concentrations of credit risk if it is exposed to risk of loss greater than it would have had it mitigated its risk through diversification of customers. Such risks of loss manifest themselves differently, depending on the nature of the concentration, and vary in significance.

We have three major customers that owned and operated retail stores that in the aggregate accounted for approximately $1.20 billion, or 25%, of our consolidated net sales in fiscal 2002 and $177.8 million, or 28%, of our accounts receivable at June 30, 2002. These groups sell products primarily within North America. Although management believes that these customers are sound and credit worthy, a severe adverse impact on their business operations could have a corresponding material adverse effect on our net sales, cash flows, and/or financial condition.

In the ordinary course of business, we have established an allowance for doubtful accounts and customer deductions in the amount of $30.6 million and $26.8 million as of June 30, 2002 and 2001, respectively. Our allowance for doubtful accounts is a subjective critical estimate that has a direct impact on reported net earnings. This reserve is based upon the evaluation of accounts receivable aging, specific exposures and historical trends.

INVENTORY

We state our inventory at the lower of cost or fair market value, with cost being determined on the first-in, first-out (FIFO) method. We believe FIFO most closely matches the flow of our products from manufacture through sale. The reported net value of our inventory includes saleable products, promotional products, raw materials and componentry that will be sold or used in future periods. Inventory cost includes raw materials, direct labor and overhead.

We also record an inventory obsolescence reserve, which represents the difference between the cost of the inventory and its estimated market value, based on various product sales projections. This reserve is calculated using an estimated obsolescence percentage applied to the inventory based on age, historical trends and requirements to support forecasted sales. In addition, and as necessary, we may establish specific reserves for future known or anticipated events.

PENSION AND OTHER POSTRETIREMENT BENEFIT COSTS

We offer the following benefits to some or all of our employees: a noncontributory defined benefit pension plan; an unfunded, nonqualified domestic benefit pension plan to provide benefits in excess of statutory limitations; a contributory defined contribution plan; international pension plans, which vary by country, the most significant of which are defined benefit pension plans; deferred compensation; and certain other postretirement benefits.

The amounts necessary to fund future payouts under these plans are subject to numerous assumptions and variables. Certain significant variables require us to make assumptions that are within our control such as an anticipated discount rate, expected rate of return on plan assets and future compensation levels. We evaluate these

assumptions with our actuarial advisors and we believe they are within accepted industry ranges, although an increase or decrease in the assumptions or economic events outside our control could have a direct impact on reported net earnings.

For fiscal 2003, we will use a pre-retirement discount rate of 7.0% and anticipate using an expected return on plan assets of 8.75%, both of which will result in a higher calculated pension expense.

GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill is calculated as the excess of the cost of purchased businesses over the value of their underlying net assets. Other intangible assets principally consist of purchased royalty rights and trademarks. Goodwill and other intangible assets that have an indefinite life are not amortized.

On an annual basis, we test goodwill and other intangible assets for impairment. To determine the fair value of these intangible assets, there are many assumptions and estimates used that directly impact the results of the testing. We have the ability to influence the outcome and ultimate results based on the assumptions and estimates we choose. To mitigate undue influence, we use industry accepted valuation models and set criteria that are reviewed and approved by various levels of management. Additionally, we evaluated our recorded goodwill with the assistance of a third-party valuation firm.

INCOME TAXES

We have accounted for, and currently account for, income taxes in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes". This Statement establishes financial accounting and reporting standards for the effects of income taxes that result from an enterprise's activities during the current and preceding years. It requires an asset and liability approach for financial accounting and reporting of income taxes.

As of June 30, 2002, we have current net deferred tax assets of $112.4 million and non-current net deferred tax assets of $72.7 million. These net deferred tax assets assume sufficient future earnings for their realization, as well as the continued application of current tax rates. Included in net deferred tax assets is a valuation allowance of approximately $1.5 million for deferred tax assets, which relates to foreign tax loss carryforwards not utilized to date, where management believes it is more likely than not that the deferred tax assets will not be realized in the relevant jurisdiction. Based on our assessments, no additional valuation allowance is required. If we determine that a deferred tax asset will not be realizable, an adjustment to the deferred tax asset will result in a reduction of earnings at that time.

Furthermore, the Company provides tax reserves for Federal, state and international exposures relating to audit results, planning initiatives and compliance responsibilities. The development of these reserves requires judgements about tax issues, potential outcomes and timing, and is a subjective critical estimate.

DERIVATIVES

We currently account for derivative financial instruments in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. This Statement also requires the recognition of all derivative instruments as either assets or liabilities on the balance sheet and that they be measured at fair value.

We currently use derivative financial instruments to hedge certain anticipated transactions as well as receivables and payables denominated in foreign currencies. We do not utilize derivatives for trading or speculative purposes. Hedge effectiveness is documented, assessed and monitored by our employees who are qualified to make such assessments and monitor the instruments. Variables that are external to the Company such as social, political and economic risks may have an impact on our hedging program and the results thereon.

RESULTS OF OPERATIONS

We manufacture, market and sell skin care, makeup, fragrance and hair care products which are distributed in over 130 countries and territories. The following is a comparative summary of operating results for fiscal 2002, 2001 and 2000 and reflects the basis of presentation described in Note 2 to the Notes to Consolidated Financial Statements for all periods presented. Sales of products and services that do not meet our definition of skin care, makeup, fragrance and hair care have been included in the "other" category.

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions)			
NET SALES			
By Region:			
The Americas	**$2,878.2**	$2,857.8	$2,714.0
Europe, the Middle East & Africa	**1,261.1**	1,221.8	1,142.2
Asia/Pacific	**610.6**	596.1	584.1
	4,749.9	4,675.7	4,440.3
Restructuring*	**(6.2)**	(8.0)	—
	$4,743.7	$4,667.7	$4,440.3
By Product Category:			
Skin Care	**$1,703.3**	$1,660.7	$1,577.0
Makeup	**1,790.5**	1,721.6	1,603.5
Fragrance	**1,017.3**	1,085.1	1,117.2
Hair Care	**215.8**	180.7	113.9
Other	**23.0**	27.6	28.7
	4,749.9	4,675.7	4,440.3
Restructuring*	**(6.2)**	(8.0)	—
	$4,743.7	$4,667.7	$4,440.3
OPERATING INCOME			
By Region:			
The Americas	**$ 222.9**	$ 299.9	$ 287.9
Europe, the Middle East & Africa	**179.9**	201.8	168.9
Asia/Pacific	**56.0**	56.9	59.0
	458.8	558.6	515.8
Restructuring and other non-recurring expenses*	**(117.4)**	(63.0)	—
	$ 341.4	$ 495.6	$ 515.8
By Product Category:			
Skin Care	**$ 248.4**	$ 266.9	$ 240.5
Makeup	**183.2**	212.5	181.8
Fragrance	**13.4**	63.6	80.6
Hair Care	**13.7**	13.1	12.4
Other	**0.1**	2.5	0.5
	458.8	558.6	515.8
Restructuring and other non-recurring expenses*	**(117.4)**	(63.0)	—
	$ 341.4	$ 495.6	$ 515.8

*Refer to the two "Restructuring and Other Non-Recurring Expenses" sections of this Management's Discussion and Analysis of Financial Condition and Results of Operations for further information about these charges.

The following table presents certain consolidated earnings data as a percentage of net sales:

YEAR ENDED JUNE 30	**2002**	2001	2000
Net sales	**100.0%**	100.0%	100.0%
Cost of sales	**26.8**	26.3	27.9
Gross profit	**73.2**	73.7	72.1
Operating expenses:			
Selling, general and administrative	**63.3**	61.5	59.8
Restructuring	**2.3**	0.8	—
Other non-recurring	**—**	0.3	—
Related party royalties	**0.4**	0.5	0.7
	66.0	63.1	60.5
Operating income	**7.2**	10.6	11.6
Interest expense, net	**0.2**	0.2	0.4
Earnings before income taxes, minority interest and accounting change	**7.0**	10.4	11.2
Provision for income taxes	**2.4**	3.7	4.1
Minority interest, net of tax	**(0.1)**	(0.1)	—
Net earnings before accounting change	**4.5**	6.6	7.1
Cumulative effect of a change in accounting principle, net of tax	**(0.4)**	(0.1)	—
Net earnings	**4.1%**	6.5%	7.1%

FISCAL 2002 AS COMPARED WITH FISCAL 2001

NET SALES

Net sales increased 2% or $76.0 million to $4.74 billion reflecting continued growth in the makeup, skin care and hair care categories, partially offset by a decline in fragrance net sales. Excluding the impact of foreign currency translation, net sales increased 3%. The unusual events that occurred during the current fiscal year and their effect on the economy, particularly in the United States, have adversely impacted our business. In addition, the decline in worldwide travel during most of fiscal 2002 led to a 13% reduction in our travel retail sales. Sales growth from certain newer brands and recently launched products partially offset these decreases.

The following discussions of Net Sales by **Product Categories** and **Geographic Regions** exclude the impact of the restructurings in fiscal 2002 and fiscal 2001. Neither restructuring was material to our net sales, and the discussions represent the manner in which we conduct and view our business. For a discussion of the restructurings, see "Operating Expenses—Restructuring and Other Non-Recurring Expenses" in this section and under the same heading under "Fiscal 2001 as compared with Fiscal 2000".

Product Categories

Skin Care Net sales of skin care products increased 3% or $42.6 million to $1.70 billion. The net sales increase is primarily attributable to recently launched products such as Total Turnaround Visible Skin Renewer, Advanced Night Repair Eye Recovery Complex, Moisture Surge Extra and Moisture Surge Eye Gel, A Perfect World, LightSource Transforming Moisture Lotion and Cream, and Re-Nutriv Ultimate Lifting Creme. Partially offsetting these increases were lower net sales of certain existing products such as Turnaround Cream and Resilience Lift, as well as products in Clinique's 3-Step Skin Care System.

Makeup Makeup net sales increased 4% or $68.9 million to $1.79 billion. Newer brands such as M·A·C, Bobbi Brown and Stila, which are primarily makeup products, contributed through growth at existing doors and increased distribution. In addition, strong sales of the Pure Color Line of products, the worldwide launch of Gentle Light Makeup and Illusionist Mascara contributed positively to net sales growth. Partially offsetting the increase in net sales were lower sales of Two-in-One Eye Shadow, Lucidity Makeup, and Long Last Soft Shine Lipstick.

Fragrance Net sales of fragrance products decreased 6% or $67.8 million to $1.02 billion. This category continued to be impacted by the softness of the fragrance business in the United States and the decline in our travel retail business, which depends substantially on fragrance products. Lower net sales of Beautiful, Estée Lauder *pleasures,* DKNY for Women and certain existing Tommy Hilfiger licensed products were partially offset by the recent launch of T, a new fragrance in the Tommy Hilfiger line, and Intuition for Men, as well as strong sales of Donna Karan Cashmere Mist.

Hair Care Hair care net sales increased 19% or $35.1 million to $215.8 million. This increase was primarily the result of growth from Aveda, which benefited from recently launched texture lotion products and Color Conserve Shampoo and an increase in the number of Company-owned Aveda Environmental Lifestyle Stores. Sales of Bumble and bumble products increased due to an expanded product line and an increase in the number of points of sale. The results were partially offset by lower sales from Clinique's Simple Hair Care System when compared with the prior-year launch.

The introduction of new products may have some cannibalizing effect on sales of existing products, which we take into account in our business planning.

Geographic Regions

Net sales in the Americas increased 1% or $20.4 million to $2.88 billion. The increase is primarily due to the success of most newer brands, partially offset by economic weakness and uncertainty in the United States during most of the fiscal year. We expect uncertain economic conditions to persist into fiscal 2003 and we are planning accordingly. In Europe, the Middle East & Africa, net sales increased 3% or $39.3 million to $1.26 billion. This increase was primarily the result of higher net sales in the United Kingdom, Spain and Greece, where in fiscal 2002 we formed a joint venture in which we own a controlling majority interest with our former distributor. The increase was partially offset by lower net sales in our travel retail business, which has been adversely affected by a decrease in worldwide travel. Excluding the impact of our travel retail business, net sales in Europe, the Middle East & Africa increased 8% or $77.8 million. Net sales in Asia/Pacific increased 2% or $14.5 million to $610.6 million primarily due to higher net sales in Korea and Thailand, as well as in Australia where we benefited from a change in retailer arrangements. The increased sales were partially offset by lower net sales in Japan. Japan continues to remain a difficult market due to local economic conditions and increasing competition. The challenges were made more difficult by the weakness of the Japanese yen during fiscal 2002 as compared with the U.S. dollar. Excluding the impact of foreign currency translation, Asia/Pacific net sales increased 9%.

We strategically stagger our new product launches by geographic market, which may account for differences in regional sales growth.

COST OF SALES

Cost of sales as a percentage of total net sales was 26.8% as compared with 26.3% in the prior year. The lower margin can be attributed in part to production volume decreases resulting in under-absorption of overhead, as well as lower than planned raw material purchases that reduced anticipated savings from sourcing initiatives. Partially offsetting these negative factors were lower sales volumes of products with a higher cost of goods, particularly in travel retail and fragrance. Due to variations in our launch calendar and the timing of promotions, we anticipate greater fluctuations in our gross margins and operating expenses on a period-by-period basis.

OPERATING EXPENSES

Operating Expenses

Operating expenses increased to 66.0% of net sales as compared with 63.1% of net sales in the prior year. The increase in operating expenses primarily related to restructuring expenses, continued advertising and promotional spending and the cost to expand and operate our retail stores. The increase in operating expenses as a percentage of net sales reflects a slower growth rate in sales than operating expenses, primarily due to economic conditions in the United States as discussed above. As part of our long-term strategies, we continued to emphasize the building of "brand equities" through advertising and promotional spending and retail store expansion despite difficult economic times. Changes in advertising and promotional spending result from the type, timing and level of advertising and promotional activities related to product launches and rollouts, as well as the markets being emphasized. Excluding the impact of restructuring and other non-recurring expenses, operating expenses were 63.5% and 61.9% of net sales for the fiscal years ended 2002 and 2001, respectively.

Restructuring and Other Non-Recurring Expenses

During the fourth quarter of fiscal 2002, we recorded special charges for a restructuring related to repositioning certain businesses as part of our ongoing efforts to drive long-term growth and increase profitability. The restructuring focused on cost reduction opportunities related to the Internet, our supply chain, globalization of the organization and distribution channel refinements. We have committed to a defined plan of action, which resulted in an aggregate pre-tax charge of $117.4 million, of which $59.4 million is cash related. On an after-tax basis, the aggregate charge was $76.9 million, equal to $.32 per diluted share. As these initiatives are fully implemented, we expect to generate annual ongoing savings of about $46 million, of which a portion will be reinvested.

Specifically, the charge included the following:

- **Internet.** In an effort to achieve strategic objectives, reduce costs and improve profitability, we outsourced Gloss.com platform development and maintenance efforts to a third-party provider. Additionally, Gloss.com closed its San Francisco facility and consolidated its operations in New York. As a result, included in the charge was a $23.9 million provision for restructuring the Gloss.com operations, including benefits and severance packages for 36 employees as well as asset write-offs. We also took a $20.1 million charge to write-off the related Gloss.com acquisition goodwill.

- **Supply Chain.** Building on previously announced supply chain initiatives, we have restructured certain manufacturing, distribution, research and development, information systems and quality assurance operations in the United States, Canada and Europe, which included benefits and severance packages for 110 employees. A charge of $23.7 million was recorded related to this effort.

- **Globilization of Organization.** We continue to implement our previously announced transition to a global brand structure designed to streamline the decision-making process and increase innovation and speed-to-market. The next phase of this transition entailed eliminating duplicate functions and responsibilities, which resulted in charges for benefits and severance for 122 employees. We recorded a charge of $27.1 million associated with these efforts.

- **Distribution.** We evaluated areas of distribution relative to our financial targets and will focus our resources on the most productive sales channels and markets. As a result, we closed our operations in Argentina and the remaining customers will be serviced by our Chilean affiliate. We are also closing all remaining in-store "tommy's shops" and we are closing other select points of distribution. We recorded a $22.6 million provision related to these actions, which included benefits and severance for 85 employees.

Following is a summary of the charges as recorded in the consolidated statement of earnings for fiscal 2002:

	Restructuring			
	Net Sales	Cost of Sales	Operating Expenses	Total
(In millions)				
Internet	$ —	$ —	$ 44.0	$ 44.0
Supply Chain	—	—	23.7	23.7
Globalization of Organization	—	—	27.1	27.1
Distribution	6.2	0.8	15.6	22.6
Total charge	$6.2	$0.8	$110.4	117.4
Tax effect				(40.5)
Net charge				$ 76.9

The restructuring charge was recorded in other accrued liabilities or, where applicable, as a reduction of the related asset. During fiscal 2002, $9.3 million related to this restructuring was paid and approximately $5.6 million of additional payments were made through August 31, 2002. We expect to settle a majority of the remaining obligations by the end of fiscal 2003 with certain additional payments made ratably through fiscal 2006.

OPERATING RESULTS

Operating income decreased 31% or $154.2 million to $341.4 million as compared with the prior year. Operating margins were 7.2% of net sales in the current period as compared with 10.6% in the prior year. The decrease in operating margin was primarily due to restructuring expenses, lower than expected sales levels, increased support spending and new distribution channel costs. This was partially offset by the exclusion of amortization expense due to the adoption of SFAS No. 142, "Goodwill and Other Intangible Assets" in fiscal 2002 and the November 2000 expiration of amortization related to purchased royalty rights. Operating income reflected the inclusion of restructuring and other non-recurring expenses of $117.4 million and $63.0 million in fiscal 2002 and 2001, respectively. Before consideration of the restructuring and other non-recurring expenses, operating income decreased 18% to $458.8 million and operating margins were 9.7% in fiscal 2002 as compared with 11.9% in fiscal 2001.

Net earnings and net earnings per diluted share decreased approximately 37% and 39%, respectively. Net earnings declined $113.3 million to $191.9 million and net earnings per diluted share was lower by $.46 per diluted share from $1.16 to $.70. On a comparable basis, before restructuring and other non-recurring expenses, before the cumulative effect of adopting a new account-

ing principle, and excluding goodwill amortization in fiscal 2001, net earnings were $289.4 million, representing a decrease of 20% over the prior year, and diluted earnings per common share decreased 21% to $1.10 from $1.39 in the prior year.

The following discussions of Operating Income by **Product Categories** and **Geographic Regions** exclude the impact of restructuring and other non-recurring expenses and represent the manner in which we conduct and view our business.

Product Categories
Operating income decreased 79% to $13.4 million in fragrance, 14% to $183.2 million in makeup and 7% to $248.4 million in skin care, primarily due to lower than anticipated sales levels, coupled with continued advertising and promotional spending to promote new and recently launched products. Hair care operating income increased 5%, from a smaller base, to $13.7 million, primarily due to sales growth from Aveda and Bumble and bumble.

Geographic Regions
Operating income in the Americas decreased 26% or $77.0 million to $222.9 million, primarily due to lower sales attributable to weakness in the U.S. economy and continued advertising and promotional spending. In Europe, the Middle East & Africa, operating income decreased 11% or $21.9 million to $179.9 million, primarily due to the significant decrease in our travel retail business. Partially offsetting the decrease were improved operating results in Italy, the United Kingdom, Spain and Germany. We also benefited from the inclusion of operating results from our majority-owned joint venture in Greece. In Asia/Pacific, operating income decreased slightly to $56.0 million due to lower income in China and Hong Kong offset by higher results in Korea, in Australia, where we benefited from a change in retailer arrangements, and in Japan, where we were able to reduce operating expenses.

INTEREST EXPENSE, NET
Net interest expense was $9.8 million as compared with $12.3 million in the prior year. The decrease in net interest expense resulted from a lower effective interest rate compared with the prior year. This was primarily due to our interest rate risk management strategy that relied on commercial paper and variable-rate term loans. In January 2002, we took advantage of prevailing market rates and issued fixed rate long-term notes to replace our variable-rate debt. We believe this will mitigate future interest rate volatility, but we expect it will result in a higher level of interest expense in the near term.

PROVISION FOR INCOME TAXES
The Company's effective tax rate will change from year to year based on non-recurring and recurring factors including, but not limited to, the geographical mix of earnings, the timing and amount of foreign dividends, state and local taxes, tax audit settlements and interaction of various global tax strategies.

The provision for income taxes represents Federal, foreign, state and local income taxes. The effective rate for income taxes for fiscal 2002 was 34.5% compared with 36% in the prior year. These rates reflect the effect of state and local taxes, changes in tax rates in foreign jurisdictions, tax credits and certain non-deductible expenses. The decrease in the effective income tax rate was attributable to ongoing tax planning initiatives, as well as a decrease in non-deductible domestic royalty expense and the elimination of certain non-deductible goodwill amortization resulting from the implementation of SFAS No. 142, "Goodwill and Other Intangible Assets".

FISCAL 2001 AS COMPARED WITH FISCAL 2000

NET SALES
Net sales increased 5% or $227.4 million to $4.67 billion reflecting continued growth in the makeup, skin care and hair care categories, partially offset by a decline in fragrance net sales. The United States retail business demonstrated continued softness particularly in the fragrance category. Growth on a reported basis reflected the impact of a stronger U.S. dollar relative to other currencies in virtually all markets in which we do business. Net sales growth was primarily attributable to a combination of new and recently launched products, the inclusion of newer brands such as Bumble and bumble and changes in distribution, including additional retail locations. Excluding the impact of foreign currency translation, net sales increased 9%, with double-digit contributions from each of Europe, the Middle East & Africa and Asia/Pacific.

The following discussions of Net Sales by **Product Categories** and **Geographic Regions** exclude the impact of the fiscal 2001 restructuring and other non-recurring expenses, which were not material to our net sales, and represent the manner in which we conduct and view our business. For a discussion of the restructuring and other non-recurring expenses, see "Operating Expenses—Restructuring and Other Non-Recurring Expenses" in this section.

Product Categories

Skin Care Net sales of skin care products increased 5% or $83.7 million to $1.66 billion. This increase was primarily attributable to newer products such as Idealist Skin Refinisher, Anti-Gravity Firming Lift Cream, Anti-Gravity Firming Eye Lift Cream and Pro-Preferred Skincare products, the first skin care line for our M·A·C brand. By introducing new products into lines such as Re-Nutriv, the Origins Ginger Bath and Body Collection and Acne Solutions, we continued to attract consumers to the lines and maintain sales momentum. White Light Brightening System and Active White continued to be popular whitening products particularly in the Asia/Pacific region. Newly launched products such as Private Spa Collection, Origins' facial skin products and initial shipments of LightSource contributed to increased sales. Partially offsetting these increases were lower sales of certain existing products such as Fruition Extra and Diminish.

Makeup Makeup net sales increased 7% or $118.1 million to $1.72 billion. Significant contributors were recently launched products such as High Impact Eye Shadow, Moisture Surge Lipstick, Equalizer Smart Makeup, Lash Doubling Mascara, Glossware, Pure Color Lip Gloss, Luxe Makeup and Automatic Pencil Duo. In addition, established products such as Pure Color Lipstick, Quickliner For Lips, Quickliner For Eyes and Sheer Powder Blusher added to increased sales. M·A·C products also contributed to increased sales with the Eden Rocks, M·A·C Paints and Heat product lines.

Fragrance Net sales of fragrance products decreased 3% or $32.1 million to $1.09 billion, but increased 1% on a comparable currency basis. The decrease in net sales was attributable to a continued decline in sales of Tommy Hilfiger licensed products, as well as to lower sales of Estée Lauder *pleasures,* Clinique Happy and Clinique Happy for Men. The continued softness of the fragrance business in the United States in fiscal 2001 and difficult comparisons to the prior year contributed to the decline in this category. Contributing positively to the category were new products, such as Intuition, Ginger Essence and DKNY for Men, as well as the international rollout of DKNY for Women.

Hair Care Hair care net sales increased 59% or $66.8 million to $180.7 million. The increase in sales is attributable to the inclusion of Bumble and bumble, in which we acquired a controlling majority equity interest in June 2000, and the launch of Clinique's Simple Hair Care System. In addition, sales growth was generated by Aveda shampoo and conditioner products, such as the Sap Moss and Brilliant product groups, and an increase in the number of Company-owned Aveda Environmental Lifestyle Stores.

The introduction of new products may have some cannibalizing effect on sales of existing products, which we take into account in our business planning.

Geographic Regions

Sales in the Americas increased 5% or $143.8 million to $2.86 billion. This increase was driven by sales growth in the makeup, skin care, and hair care categories, particularly with the success of new and recently launched products and the growth of our newer brands. The increase was partially offset by a decline in fragrance sales due to the softness in this category in the United States. In Europe, the Middle East & Africa, net sales increased 7% or $79.6 million to $1.22 billion. The increase was primarily the result of higher net sales in the United Kingdom, Spain and France and in our distributor and travel retail businesses. This increase was partially offset by decreased sales in Germany and South Africa. Net sales in Asia/Pacific increased 2% or $12.0 million to $596.1 million primarily due to higher net sales in Korea, Hong Kong, Malaysia and Thailand, partially offset by lower sales in Japan and Australia. Excluding the impact of foreign currency translation, sales grew in each country in Europe, the Middle East & Africa and in Asia/Pacific, accounting for growth of 17% and 10%, respectively.

We strategically stagger our new product launches by geographic market, which may account for differences in regional sales growth.

COST OF SALES

Cost of sales as a percentage of total net sales improved to 26.3% from 27.9%, reflecting the impact of our manufacturing and sourcing initiatives as well as changes in distribution and product mix. Changes in distribution include the rollout of our own retail stores and the acquisition of certain distributor operations, both of which contributed to higher gross margins. In addition, the synergies achieved by incorporating recently acquired businesses into our existing manufacturing and sourcing infrastructures had a favorable impact on gross margins.

OPERATING EXPENSES

Operating Expenses

Operating expenses increased to 63.1% of net sales as compared with 60.5% of net sales in the prior year. Excluding the impact of restructuring and other non-recurring expenses, operating expenses were 61.9% of net sales. This change primarily related to the increased cost of our retail store and Internet operations, which have higher operating cost structures than our traditional

distribution channels. Additionally, depreciation and amortization charges increased compared with the prior year, reflecting increased goodwill amortization from acquisitions and depreciation related to capital investments, partially offset by the November 2000 expiration of amortization related to purchased royalty rights. Changes in advertising and promotional spending result from the type, timing and level of advertising and promotional activities related to product launches and rollouts, as well as from the markets being emphasized.

Restructuring and Other Non-Recurring Expenses
During the fourth quarter of fiscal 2001, we recorded one-time charges for restructuring and other non-recurring expenses related to repositioning certain businesses as part of our ongoing efforts to drive long-term growth and increase profitability. The restructuring and other non-recurring expenses focused on four areas: product fixtures for the *jane* brand; in-store "tommy's shops"; information systems and other assets; and global brand reorganization. We committed to a defined plan of action, which resulted in an aggregate pre-tax charge of $63.0 million, of which $35.9 million is cash related. On an after-tax basis, the aggregate charge was $40.3 million, equal to $.17 per diluted share.

Specifically, the charge included the following:

- ***jane.*** To bring product innovation rapidly to the market and drive growth, *jane* switched from its traditional wall displays to a carded program. We believed this change would lead to increased sales and improvements in profitability. The positive effects on sales and improved profitability of this initiative were offset by the reduction in the number of points of sale during fiscal 2002. The charge included a $16.1 million write-down of existing *jane* product fixtures and the return of uncarded product from virtually all of the 13,000 distribution outlets in the United States.
- **"tommy's shops."** We also restructured the in-store "tommy's shops" to focus on our most productive locations and decided to close certain shops that underperformed relative to expectations. As a result, we recorded a $6.3 million provision for the closing of 86 underperforming in-store "tommy's shops," located in the United States, and for related product returns.
- **Information systems and other assets.** In response to changing technology and our new strategic direction, the charge included a $16.2 million provision for costs associated with the reevaluation of supply chain systems that we will no longer utilize and with the elimination of unproductive assets related to the change to standard financial systems.
- **Global brand reorganization.** We recorded $20.8 million related to benefits and severance packages for 75 management employees who were affected by the reconfiguration to a global brand structure and another $3.6 million related to infrastructure costs. As of June 30, 2002, none of the 75 management employees identified in the reorganization was still an employee. We believe that the global brand structure is improving decision-making processes, thereby increasing innovation and speed to market.

Following is a summary of the charges as recorded in the consolidated statement of earnings for fiscal 2001:

	Restructuring			Other Non-Recurring	
	Net Sales	Cost of Sales	Operating Expenses	Expenses	Total
(In millions)					
jane	$ 5.7	$ 1.5	$ 4.8	$ 4.1	$ 16.1
"tommy's shops"	2.3	(0.4)	4.4	—	6.3
Information systems and other assets	—	—	4.6	11.6	16.2
Global brand reorganization	—	—	23.8	0.6	24.4
Total charge	$ 8.0	$ 1.1	$37.6	$16.3	63.0
Tax effect					(22.7)
Net charge					$ 40.3

The restructuring charge was recorded in other accrued liabilities or as a reduction of fixed assets. During fiscal 2001, $0.7 million was paid and through June 30, 2002, an additional $26.7 million was paid. As of June 30, 2002, the remaining obligation was $7.1 million, the majority of which we expect to settle by the end of fiscal 2003 with remaining payments made ratably through fiscal 2004.

OPERATING RESULTS

Operating income decreased 4% or $20.2 million to $495.6 million as compared with the prior year. Operating margins were 10.6% of net sales in fiscal 2001 as compared with 11.6% in the prior year. Operating income reflected the inclusion of restructuring and other non-recurring expenses of $46.7 million and $16.3 million, respectively. Before consideration of these one-time charges, operating income increased 8% to $558.6 million and operating margins were 11.9%. The increase in operating income was primarily due to higher net sales and an improved gross margin percentage, partially offset by increased operating expenses reflecting increased sales support spending and new distribution channel costs.

Net earnings and net earnings per diluted share decreased approximately 3%. Net earnings declined $8.9 million to $305.2 million and net earnings per diluted share was lower by $.04 per diluted share from $1.20 to $1.16. Net earnings before restructuring and other non-recurring expenses and before the cumulative effect of adopting a new accounting principle was $347.7 million, representing an increase of 11% over the prior year; diluted earnings per common share increased 12% to $1.34 from $1.20 in the prior year.

The following discussions of Operating Income by **Product Categories** and **Geographic Regions** exclude the impact of restructuring and other non-recurring expenses and represent the manner in which we conduct and view our business.

Product Categories

Operating income increased 17% to $212.5 million and 11% to $266.9 million in makeup and skin care, respectively, due primarily to the strength of recently launched products. The strong growth of our M·A·C business, which includes retail store expansion, also contributed to the increase in makeup operating income. Operating income from our fragrance business declined by $17.0 million reflecting lower sales and increased support spending versus the prior year. The nominal increase in hair care operating income was a result of the inclusion of Bumble and bumble and sales from recent launches, partially offset by costs associated with refining Aveda's salon distribution, opening new Aveda Environmental Lifestyle Stores and investing in new product introductions.

Geographic Regions

Operating income in the Americas increased 4% or $12.0 million to $299.9 million as compared with the prior year, primarily due to net sales increases related to new and recently launched products, strong growth in our M·A·C business and the inclusion of Bumble and bumble, partially offset by a decline in fragrance net sales. In Europe, the Middle East & Africa, operating income increased 19% or $32.9 million to $201.8 million primarily due to improved operating results in the United Kingdom and Spain and in the travel retail business, partially offset by lower operating income in South Africa. In Asia/Pacific, operating income decreased slightly to $56.9 million due to higher results in Korea and Hong Kong offset by lower operating income in Japan and Australia.

INTEREST EXPENSE, NET

Net interest expense was $12.3 million as compared with $17.1 million in the prior year. As a result of an increase in average available cash during the period, we had higher interest income on invested funds and lower interest expense due to reduced short-term borrowings. Additionally, we benefited from a lower effective interest rate on our long-term borrowings resulting from our interest rate risk management strategy.

PROVISION FOR INCOME TAXES

The provision for income taxes represents Federal, foreign, state and local income taxes. The effective rate for income taxes for fiscal 2001 was 36% compared with 37% in the prior year. These rates reflect the effect of state and local taxes, tax rates in foreign jurisdictions and certain non-deductible expenses. The decrease in the effective income tax rate was principally attributable to ongoing tax planning initiatives.

FINANCIAL CONDITION

LIQUIDITY AND CAPITAL RESOURCES

Our principal sources of funds historically have been cash flows from operations and borrowings under commercial paper and committed and uncommitted credit lines provided by banks in the United States and abroad. In February 2002, we repaid $200.0 million principal amount of bank borrowings with proceeds of a public offering of 6% Senior Notes due 2012 ("6% Senior Notes"). At June 30, 2002, we had cash and cash equivalents of $546.9 million compared with $346.7 million at June 30, 2001.

We have a $750.0 million commercial paper program, under which we have issued, and intend to issue, commercial paper in the United States. Our commercial paper is currently rated A-1 by Standard & Poor's and P-1 by Moody's. Our long-term credit ratings are A+ by Standard & Poor's and A1 by Moody's. At June 30, 2002, our outstanding borrowings consisted of $130.0 million of commercial paper; $248.9 million, net of $1.1 million unamortized debt discount, of 6% Senior Notes due January 2012; a 700.0 million yen loan payable (approximately $5.8 million at current exchange rates), which is due in April 2003; and a 3.0 billion yen term loan (approximately $25.0 million at current exchange rates), which is due in March 2006. Commercial paper is classified as long-term debt on our balance sheet based upon our intent and ability to refinance maturing commercial paper on a long-term basis. It is our policy to maintain backup facilities to support our commercial paper program and its classification as long-term debt. As of June 30, 2002, we had an unused $400.0 million revolving credit facility, expiring on June 28, 2006. We also have an effective shelf registration statement covering the potential issuance of up to $150.0 million in debt securities.

In January 2002, we issued and sold $250.0 million of 6% Senior Notes due 2012 in a public offering. The 6% Senior Notes were priced at 99.538% with a yield of 6.062%. Interest payments are required to be made semi-annually on January 15 and July 15 of each year. We made the first payment on July 15, 2002. The primary portion of the net proceeds of the offering was used to repay a $200.0 million term loan. The remainder was used to repay a portion of the outstanding commercial paper. We issued these fixed-rate notes in an attempt to mitigate future interest rate volatility and capitalize on the prevailing market interest rates then available for such long-term instruments. However, we do expect the refinancing to result in a higher level of interest expense in the near term.

Our business is seasonal in nature and, accordingly, our working capital needs vary. To meet these needs, we could issue up to an additional $620.0 million of commercial paper under our program, issue long-term debt securities or borrow under the revolving credit facility. As of June 30, 2002, we also had $22.9 million in unused uncommitted facilities.

Total debt as a percent of total capitalization was 18% at June 30, 2002 as compared with 20% at June 30, 2001, primarily as a result of higher total capital.

Net cash provided by operating activities was $518.0 million in fiscal 2002 as compared with $305.4 million in fiscal 2001 and $442.5 million in fiscal 2000. This improvement in net cash flows was generated primarily by a reduction of inventory. Inventory levels were unseasonably high at the end of fiscal 2001 and were lowered during the current fiscal year as part of our ongoing effort to keep inventory levels in line with forecasted sales. Operating cash flows were generally not impacted by the fiscal 2002 restructuring as lower net earnings were offset by the non-cash portion of the charge and the increase in other accrued liabilities. We expect the settlement of these accrued charges to result in a lower level of cash flow provided by operating activities in fiscal 2003. The decrease in cash provided by operating activities in fiscal 2001 as compared to fiscal 2000 reflected an increase in inventory primarily due to accelerated growth both in new distribution channels and in the rollout of new brands; a shift in the timing of Christmas production at the end of fiscal 2001 as compared with the prior year; reconfiguration of some of our distribution to improve service levels; and softer retail sales than projected in the Americas. Accounts receivable increased due to sales growth, particularly outside the United States, and the timing of shipments as compared with fiscal 2000. The decrease in other accrued liabilities in fiscal 2001 reflected the type and timing of various expenditures and the tightening of spending, particularly in the Americas, due to the difficult retail environment, partially offset by a $35.2 million accrual for restructuring and other nonrecurring expenses.

Net cash used for investing activities was $217.0 million in fiscal 2002, compared with $206.3 million in fiscal 2001 and $374.3 million in fiscal 2000. Net cash used in investing activities during fiscal 2002 is comparable to fiscal 2001 and relates primarily to capital expenditures in both periods. Investment spending in fiscal 2000 reflected capital expenditures and the acquisitions of Stila, Jo Malone, Gloss.com and Bumble and bumble, as well as certain Aveda distributors.

Capital expenditures amounted to $203.2 million, $192.2 million and $180.9 million in fiscal 2002, 2001 and 2000, respectively. Spending in all three years primarily reflected the continued upgrade of manufacturing equipment, dies and molds, new store openings, store improvements, counter construction and information technology enhancements.

Cash used for financing activities was $121.8 million, $63.5 million and $87.9 million in fiscal 2002, 2001 and 2000, respectively. Cash used for financing during fiscal 2002 and 2000 primarily relates to dividend payments and common stock repurchases. The cash used in fiscal 2001 was primarily related to dividend payments.

In September 1998, our Board of Directors authorized a share repurchase program. We have purchased, and may continue to purchase, over an unspecified period of time, a total of up to eight million shares of Class A Common Stock in the open market or in privately negotiated transactions, depending on market conditions and other factors. During fiscal 2002, we purchased 1.5 million shares for $49.7 million. As of June 30, 2002, we have purchased approximately 2.6 million shares under this program. Subsequent to year-end, we purchased an additional 4.4 million shares for $138.1 million bringing the cumulative total of acquired shares to 7.0 million.

The Board of Directors declared, and we paid, quarterly dividends on our Class A Common Stock and Class B Common Stock at the rate of $.05 per share in each quarter of fiscal 2002, 2001 and 2000. In fiscal 2002, 2001 and 2000, dividends declared on our common stock totaled $47.5 million, $47.7 million and $47.5 million, respectively. In May 2002, we announced that, after declaring the $.05 per share quarterly dividend paid on July 2, 2002, the Board of Directors determined that it would pay future cash dividends on its common stock annually rather than quarterly. We expect that the Board of Directors will declare the first annual dividend of $.20 per share in the second quarter of fiscal 2003, so it will be payable in January 2003. Accordingly, we expect total dividends paid on the Common Stock in fiscal 2003 to amount to $.25 per share. Total dividends declared, including dividends on the $6.50 Cumulative Redeemable Preferred Stock, were $70.9 million, $71.1 million and $70.9 million in fiscal 2002, 2001 and 2000, respectively.

We will be required to redeem the outstanding $6.50 Cumulative Redeemable Preferred Stock on June 30, 2005. However, in the event that Mrs. Estée Lauder were to pass away before such date, then we would have the right to redeem the shares from the current holders, and the holders of such shares would have the right to put the shares to us, at $100 per share (or an aggregate of $360.0 million). If shares of $6.50 Cumulative Redeemable Preferred Stock are put to us, we would have up to 120 days after notice to purchase such shares.

The effects of inflation have not been significant to our overall operating results in recent years. Generally, we have been able to increase selling prices sufficiently to offset cost increases, which have been moderate.

We believe that cash on hand, cash generated from operations, available credit lines and access to credit markets will be adequate to support currently planned business operations and capital expenditures on both a near-term and long-term basis.

Derivative Financial Instruments

We address certain financial exposures through a controlled program of risk management that includes the use of derivative financial instruments. We primarily enter into foreign currency forward exchange contracts and foreign currency options to reduce the effects of fluctuating foreign currency exchange rates. We categorize these instruments as entered into for purposes other than trading.

For each derivative contract we enter into, we formally document the relationship between the hedging instrument and hedged item, as well as its risk-management objective and strategy for undertaking the hedge. This process includes linking all derivatives that are designated as fair-value, cash-flow, or foreign-currency hedges to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. We also formally assess, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. If it is determined that a derivative is not highly effective, then we will be required to discontinue hedge accounting with respect to that derivative prospectively.

Foreign Exchange Risk Management

We enter into forward exchange contracts to hedge anticipated transactions as well as receivables and payables denominated in foreign currencies for periods consistent with our identified exposures. The purpose of the hedging activities is to minimize the effect of foreign exchange rate movements on our costs and on the cash flows that we receive from foreign subsidiaries. Almost all foreign currency contracts are denominated in currencies of major industrial countries and are with large financial institutions rated as strong investment grade by a major rating agency. We also enter into foreign currency options to hedge anticipated transactions where there is a high probability that anticipated exposures will materialize. The forward exchange contracts and foreign currency options have been designated as cash-flow hedges. As of June 30, 2002, these cash-flow hedges were highly effective, in all material respects.

As a matter of policy, we only enter into contracts with counterparties that have at least an "A" (or equivalent) credit rating. The counterparties to these contracts are major financial institutions. We do not have significant exposure to any one counterparty. Our exposure to credit loss in the event of nonperformance by any of the counterparties is limited to only the recognized, but not realized, gains attributable to the contracts. Management believes risk of loss under these hedging contracts is

remote and in any event would not be material to the consolidated financial results. The contracts have varying maturities through the end of July 2003. Costs associated with entering into such contracts have not been material to our consolidated financial results. We do not utilize derivative financial instruments for trading or speculative purposes. At June 30, 2002, we had foreign currency contracts in the form of forward exchange contracts in the amount of $227.2 million. The foreign currencies included in these contracts (notional value stated in U.S. dollars) are principally the Japanese yen ($70.7 million), Euro ($31.7 million), British pound ($26.2 million), Australian dollar ($16.0 million), Swiss franc ($11.8 million), Danish krone ($11.6 million) and Canadian dollar ($10.5 million).

Interest Rate Risk Management

In February 2002, we paid off our outstanding term loan, which had a floating interest rate, with the proceeds from our January 2002 public debt offering of 6% Senior Notes. As a result, we terminated the interest rate swaps and options that were previously outstanding to mitigate interest rate volatility. No material gain or loss resulted from the termination of those contracts.

Market Risk

We use a value-at-risk model to assess the market risk of our derivative financial instruments. Value-at-risk represents the potential losses for an instrument or portfolio from adverse changes in market factors for a specified time period and confidence level. We estimate value-at-risk across all of our derivative financial instruments using a model with historical volatilities and correlations calculated over the past 250 day period. The measured value-at-risk, calculated as an average, for the twelve months ended June 30, 2002, related to our foreign exchange contracts, using a variance/co-variance model with a 95 percent confidence level and assuming normal market conditions, was $10.0 million.

Our calculated value-at-risk exposure represents an estimate of reasonably possible net losses that would be recognized on our portfolio of derivative financial instruments assuming hypothetical movements in future market rates and is not necessarily indicative of actual results, which may or may not occur. It does not represent the maximum possible loss nor any expected loss that may occur, since actual future gains and losses will differ from those estimated, based upon actual fluctuations in market rates, operating exposures, and the timing thereof, and changes in the portfolio of derivative financial instruments during the year.

We believe, however, that any loss incurred would be offset by the effects of market rate movements on the respective underlying transactions for which the hedge is intended.

ACCOUNTING STANDARDS

Effective July 1, 2001, we adopted SFAS No. 141, "Business Combinations" and SFAS No. 142, "Goodwill and Other Intangible Assets". These statements established financial accounting and reporting standards for acquired goodwill and other intangible assets. Specifically, the standards address how acquired intangible assets should be accounted for both at the time of acquisition and after they have been recognized in the financial statements. The provisions of SFAS No. 141 apply to all business combinations initiated after June 30, 2001. In accordance with SFAS No. 142, intangible assets, including purchased goodwill, must be evaluated for impairment. Those intangible assets that will continue to be classified as goodwill or as other intangibles with indefinite lives are no longer amortized.

In accordance with SFAS No. 142, we completed our transitional impairment testing of intangible assets during the first quarter of fiscal 2002. That effort, and preliminary assessments of our identifiable intangible assets, indicated that little or no adjustment would be required upon adoption of this pronouncement. The impairment testing is performed in two steps: (i) we determine impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is an impairment, we measure the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. Subsequent to the first quarter of fiscal 2002, with the assistance of a third-party valuation firm, we finalized the testing of goodwill. Using conservative, but realistic assumptions to model our *jane* business, we determined that the carrying value of this unit was slightly greater than the derived fair value, indicating an impairment in the recorded goodwill. To determine fair value, we relied on three valuation models: guideline public companies, acquisition analysis and discounted cash flow. For goodwill valuation purposes only, the revised fair value of this unit was allocated to the assets and liabilities of the business unit to arrive at an implied fair value of goodwill, based upon known facts and circumstances, as if the acquisition occurred currently. This allocation resulted in a write-down of recorded goodwill in the amount of $20.6 million, which has been reported as the cumulative effect of a change in accounting principle, as of July 1, 2001, in the accompanying consolidated statements of earnings. On a product category basis, this write-down would have primarily impacted our makeup category.

The following table presents adjusted net earnings and earnings per share data restated to include the retroactive impact of the adoption of SFAS No. 142.

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions, except per share data)			
Reported Net Earnings before Accounting Change	**$212.5**	$307.4	$314.1
Cumulative effect of a change in accounting principle, net of tax	**(20.6)**	(2.2)	—
Net Earnings	**191.9**	305.2	314.1
Preferred stock dividends	**23.4**	23.4	23.4
Reported Net Earnings Attributable to Common Stock	**168.5**	281.8	290.7
Add back: Goodwill amortization, net of tax	**—**	13.4	11.1
Adjusted Net Earnings	**$168.5**	$295.2	$301.8
Basic net earnings per common share:			
Reported net earnings attributable to common stock before accounting change	**$ .79**	$ 1.19	$ 1.22
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**.71**	1.18	1.22
Goodwill amortization, net of tax	**—**	.06	.05
Adjusted net earnings attributable to common stock	**$ .71**	$ 1.24	$ 1.27
Diluted net earnings per common share:			
Reported net earnings attributable to common stock before accounting change	**$ .78**	$ 1.17	$ 1.20
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**.70**	1.16	1.20
Goodwill amortization, net of tax	**—**	.06	.04
Adjusted net earnings attributable to common stock	**$ .70**	$ 1.22	$ 1.24
Weighted average common shares outstanding:			
Basic	**238.2**	238.4	237.7
Diluted	**241.1**	242.2	242.5

Effective January 1, 2002, we adopted the Emerging Issues Task Force ("EITF") Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer", which codified and reconciled the following EITF Issues: Issue No. 00-14, "Accounting for Certain Sales Incentives", Issue No. 00-22, "Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to be Delivered in the Future", and Issue No. 00-25, "Vendor Income Statement Characterization of Consideration Paid to a Reseller of the Vendor's Products". Issue No. 00-14 addressed when sales incentives and discounts should be recognized, as well as where the related revenues and expenses should be classified in the financial statements. Upon adoption of this Issue, we reclassified revenues generated from our purchase with purchase activities as sales and the costs of our purchase with purchase and gift with purchase activities as cost of sales, which were previously reported net as operating expenses. Operating income has remained unchanged by this adoption. These reclassifications have been reported in the accompanying consolidated statements of earnings retroactively for all periods reported.

In August 2001, the Financial Accounting Standards Board issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 will be effective for financial statements relating to fiscal years beginning after December 15, 2001. We will adopt this statement for our fiscal year ending June 30, 2003 and do not anticipate that it will have a material impact on our consolidated financial results.

In June 2002, the Financial Accounting Standards Board issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". This statement covers restructuring type activities beginning with plans initiated after December 31, 2002. Should we enter into activities covered by this standard after that date, the provisions of SFAS No. 146 would be applied. As a result of this standard, there is no impact on our consolidated financial position or results of operations for the periods presented.

FORWARD-LOOKING INFORMATION

We and our representatives from time to time make written or oral forward-looking statements, including statements contained in this and other filings with the Securities and Exchange Commission, in our press releases and in our reports to stockholders. The words and phrases "will likely result," "expect," "believe," "planned," "will," "will continue," "is anticipated," "estimates," "projects" or similar expressions are intended to identify "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These statements include, without limitation, our expectations regarding sales, earnings or other future financial performance and liquidity, product introductions, entry into new geographic regions, information systems initiatives, new methods of sale and future operations or operating results. Although we believe that our expectations are based on reasonable assumptions within the bounds of our knowledge of our business and operations, actual results may differ materially from our expectations. Factors that could cause actual results to differ from expectations include, without limitation:

(i) increased competitive activity from companies in the skin care, makeup, fragrance and hair care businesses, some of which have greater resources than we do;

(ii) our ability to develop, produce and market new products on which future operating results may depend;

(iii) consolidations, restructurings, bankruptcies and reorganizations in the retail industry causing a decrease in the number of stores that sell our products, an increase in the ownership concentration within the retail industry, ownership of retailers by our competitors and ownership of competitors by our customers that are retailers;

(iv) shifts in the preferences of consumers as to where and how they shop for the types of products and services we sell;

(v) social, political and economic risks to our foreign or domestic manufacturing, distribution and retail operations, including changes in foreign investment and trade policies and regulations of the host countries and of the United States;

(vi) changes in the laws, regulations and policies, including changes in accounting standards and trade rules, and legal or regulatory proceedings, that affect, or will affect, our business;

(vii) foreign currency fluctuations affecting our results of operations and the value of our foreign assets, the relative prices at which we and our foreign competitors sell products in the same markets and our operating and manufacturing costs outside of the United States;

(viii) changes in global or local economic conditions that could affect consumer purchasing, the financial strength of our customers, the cost and availability of capital, which we may need for new equipment, facilities or acquisitions, and the assumptions underlying our critical accounting estimates;

(ix) shipment delays, depletion of inventory and increased production costs resulting from disruptions of operations at any of the facilities which, due to consolidations in our manufacturing operations, now manufacture nearly all of our supply of a particular type of product (i.e. focus factories);

(x) real estate rates and availability, which may affect our ability to increase the number of retail locations at which we sell our products;

(xi) changes in product mix to products which are less profitable;

(xii) our ability to acquire or develop e-commerce capabilities, and other new information and distribution technologies, on a timely basis and within our cost estimates;

(xiii) our ability to capitalize on opportunities for improved efficiency, such as globalization, and to integrate acquired businesses and realize value there from; and

(xiv) consequences attributable to the events that took place in New York City and Washington, D.C. on September 11, 2001, including further attacks, retaliation and the threat of further attacks or retaliation.

We assume no responsibility to update forward-looking statements made herein or otherwise.

JUNE 30	2002	2001
(In millions, except share data)		
ASSETS		
Current Assets		
Cash and cash equivalents	**$ 546.9**	$ 346.7
Accounts receivable, net	**624.8**	580.6
Inventory and promotional merchandise, net	**544.5**	630.3
Prepaid expenses and other current assets	**211.4**	181.3
Total current assets	**1,927.6**	1,738.9
Property, Plant and Equipment, net	**580.7**	528.7
Other Assets		
Investments, at cost or market value	**30.3**	41.0
Deferred income taxes	**72.7**	70.1
Goodwill, net	**675.6**	699.7
Other intangible assets, net	**18.4**	21.0
Other assets, net	**111.2**	119.4
Total other assets	**908.2**	951.2
Total assets	**$3,416.5**	$3,218.8
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Short-term debt	**$ 6.6**	$ 5.8
Accounts payable	**216.4**	239.8
Accrued income taxes	**110.0**	79.0
Other accrued liabilities	**626.6**	532.1
Total current liabilities	**959.6**	856.7
Noncurrent Liabilities		
Long-term debt	**403.9**	410.9
Other noncurrent liabilities	**231.1**	239.1
Total noncurrent liabilities	**635.0**	650.0
Commitments and Contingencies (Note 15)		
$6.50 Cumulative Redeemable Preferred Stock, at redemption value	**360.0**	360.0
Stockholders' Equity		
Common stock, $.01 par value; 650,000,000 shares Class A authorized; shares issued: 131,567,986 in 2002 and 126,053,825 in 2001; 240,000,000 shares Class B authorized; shares issued and outstanding: 108,412,533 in 2002 and 113,490,293 in 2001	**2.4**	2.4
Paid-in capital	**268.8**	258.3
Retained earnings	**1,363.7**	1,242.7
Accumulated other comprehensive income (loss)	**(92.5)**	(120.5)
	1,542.4	1,382.9
Less: Treasury stock, at cost; 2,377,860 Class A shares at June 30, 2002 and 877,860 Class A shares at June 30, 2001	**(80.5)**	(30.8)
Total stockholders' equity	**1,461.9**	1,352.1
Total liabilities and stockholders' equity	**$3,416.5**	$3,218.8

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

YEAR ENDED JUNE 30 (In millions)	**2002**	2001	2000
STOCKHOLDERS' EQUITY			
Common stock, beginning of year	**$ 2.4**	$ 2.4	$ 2.4
Common stock, end of year	**2.4**	2.4	2.4
Paid-in capital, beginning of year	**258.3**	237.1	211.6
Stock compensation programs	**10.5**	21.2	25.5
Paid-in capital, end of year	**268.8**	258.3	237.1
Retained earnings, beginning of year	**1,242.7**	1,008.6	766.2
Preferred stock dividends	**(23.4)**	(23.4)	(23.4)
Common stock dividends	**(47.5)**	(47.7)	(47.5)
Issuance of treasury stock	**—**	—	(0.8)
Net earnings for the year	**191.9**	305.2	314.1
Retained earnings, end of year	**1,363.7**	1,242.7	1,008.6
Accumulated other comprehensive income (loss), beginning of year	**(120.5)**	(57.1)	(44.3)
Other comprehensive income (loss)	**28.0**	(63.4)	(12.8)
Accumulated other comprehensive income (loss), end of year	**(92.5)**	(120.5)	(57.1)
Treasury stock, beginning of year	**(30.8)**	(30.7)	(11.4)
Acquisition of treasury stock	**(49.7)**	(0.1)	(23.6)
Issuance of treasury stock	**—**	—	4.3
Treasury stock, end of year	**(80.5)**	(30.8)	(30.7)
Total stockholders' equity	**$1,461.9**	$1,352.1	$1,160.3
COMPREHENSIVE INCOME			
Net earnings	**$ 191.9**	$ 305.2	$ 314.1
Other comprehensive income (loss):			
Net unrealized investment gains (losses)	**(3.0)**	(11.0)	7.8
Net derivative instrument losses	**(7.1)**	(2.0)	—
Net minimum pension liability adjustments	**(7.9)**	(12.4)	—
Translation adjustments	**46.0**	(38.0)	(20.6)
Other comprehensive income (loss)	**28.0**	(63.4)	(12.8)
Total comprehensive income	**$ 219.9**	$ 241.8	$ 301.3

See notes to consolidated financial statements.

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions)			
Cash Flows from Operating Activities			
Net earnings	**$ 191.9**	$ 305.2	$ 314.1
Adjustments to reconcile net earnings to net cash flows provided by operating activities:			
Depreciation and amortization	**162.0**	156.3	129.1
Amortization of purchased royalty rights	**—**	6.6	17.7
Deferred income taxes	**(22.6)**	4.7	(5.5)
Minority interest	**4.7**	1.9	—
Non-cash stock compensation	**(0.1)**	0.7	1.7
Cumulative effect of a change in accounting principle	**20.6**	2.2	—
Non-cash portion of restructuring and other non-recurring expenses	**58.0**	27.1	—
Other non-cash items	**0.9**	—	—
Changes in operating assets and liabilities:			
Increase in accounts receivable, net	**(15.4)**	(57.3)	(24.4)
Decrease (increase) in inventory and promotional merchandise, net	**102.2**	(102.1)	(31.3)
Increase in other assets	**(11.7)**	(53.6)	(39.8)
Increase (decrease) in accounts payable	**(32.6)**	14.2	12.2
Increase in accrued income taxes	**28.8**	5.9	10.9
Increase (decrease) in other accrued liabilities	**59.6**	(23.4)	35.1
Increase (decrease) in other noncurrent liabilities	**(28.3)**	17.0	22.7
Net cash flows provided by operating activities	**518.0**	305.4	442.5
Cash Flows from Investing Activities			
Capital expenditures	**(203.2)**	(192.2)	(180.9)
Acquisition of businesses, net of acquired cash	**(18.5)**	(16.0)	(180.5)
Purchases of long-term investments	**—**	—	(15.9)
Proceeds from disposition of long-term investments	**4.7**	1.9	3.0
Net cash flows used for investing activities	**(217.0)**	(206.3)	(374.3)
Cash Flows from Financing Activities			
Increase (decrease) in short-term debt, net	**0.6**	(0.1)	(0.6)
Proceeds from issuance of long-term debt, net	**247.2**	24.5	—
Repayments of long-term debt	**(256.6)**	(30.1)	(6.8)
Net proceeds from employee stock transactions	**7.7**	13.3	14.0
Payments to acquire treasury stock	**(49.7)**	(0.1)	(23.6)
Dividends paid	**(71.0)**	(71.0)	(70.9)
Net cash flows used for financing activities	**(121.8)**	(63.5)	(87.9)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	**21.0**	(9.2)	(7.5)
Net Increase (Decrease) in Cash and Cash Equivalents	**200.2**	26.4	(27.2)
Cash and Cash Equivalents at Beginning of Year	**346.7**	320.3	347.5
Cash and Cash Equivalents at End of Year	**$ 546.9**	$ 346.7	$ 320.3
Supplemental disclosures of cash flow information (see also Note 17)			
Cash paid during the year for:			
Interest	**$ 17.6**	$ 26.7	$ 29.2
Income Taxes	**$ 120.5**	$ 176.6	$ 163.8

See notes to consolidated financial statements.

NOTE 1 – DESCRIPTION OF BUSINESS

The Estée Lauder Companies Inc. manufactures, markets and sells skin care, makeup, fragrance and hair care products around the world. Products are marketed under the following brand names: Estée Lauder, Clinique, Aramis, Prescriptives, Origins, M·A·C, Bobbi Brown, La Mer, *jane,* Aveda, Stila, Jo Malone and Bumble and bumble. The Estée Lauder Companies Inc. is also the global licensee of the Tommy Hilfiger, Donna Karan and Kate Spade brands for fragrances and cosmetics.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of The Estée Lauder Companies Inc. and its subsidiaries (collectively, the "Company"). All significant intercompany balances and transactions have been eliminated.

Certain amounts in the consolidated financial statements of prior years have been reclassified to conform to current year presentation for comparative purposes.

Net Earnings Per Common Share

Net earnings per common share ("basic EPS") is computed by dividing net earnings, after deducting preferred stock dividends on the Company's $6.50 Cumulative Redeemable Preferred Stock, by the weighted average number of common shares outstanding and contingently issuable shares (which satisfy certain conditions). Net earnings per common share assuming dilution ("diluted EPS") is computed by reflecting potential dilution from the exercise of stock options.

A reconciliation between the numerators and denominators of the basic and diluted EPS computations is as follows:

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions, except per share data)			
Numerator:			
Net earnings before accounting change	**$212.5**	$307.4	$314.1
Preferred stock dividends	**(23.4)**	(23.4)	(23.4)
Net earnings attributable to common stock before accounting change	**189.1**	284.0	290.7
Cumulative effect of a change in accounting principle, net of tax	**(20.6)**	(2.2)	—
Net earnings attributable to common stock	**$168.5**	$281.8	$290.7
Denominator:			
Weighted average common shares outstanding—Basic	**238.2**	238.4	237.7
Effect of dilutive securities: Stock options	**2.9**	3.8	4.8
Weighted average common shares outstanding—Diluted	**241.1**	242.2	242.5
Basic net earnings per common share:			
Net earnings before accounting change	**$ .79**	$ 1.19	$ 1.22
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings	**$ .71**	$ 1.18	$ 1.22
Diluted net earnings per common share:			
Net earnings before accounting change	**$ .78**	$ 1.17	$ 1.20
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings	**$ .70**	$ 1.16	$ 1.20

As of June 30, 2002, 2001 and 2000, options to purchase 12.1 million, 10.5 million and 7.2 million shares, respectively, of Class A Common Stock were not included in the computation of diluted EPS because the exercise prices of those options were greater than the average market price of the common stock and their inclusion would be anti-dilutive. The options were still outstanding at the end of the applicable periods.

Cash and Cash Equivalents

Cash and cash equivalents include $426.2 million and $232.2 million of short-term time deposits at June 30, 2002 and 2001, respectively. The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents.

Accounts Receivable

Accounts receivable is stated net of the allowance for doubtful accounts and customer deductions of $30.6 million and $26.8 million as of June 30, 2002 and 2001, respectively.

Currency Translation and Transactions

All assets and liabilities of foreign subsidiaries and affiliates are translated at year-end rates of exchange, while revenue and expenses are translated at weighted average rates of exchange for the year. Unrealized translation gains or losses are reported as cumulative translation adjustments through other comprehensive income. Such adjustments amounted to $46.0 million of unrealized translation gains and $38.0 million of unrealized translation losses in fiscal 2002 and 2001, respectively.

The Company enters into forward foreign exchange contracts and foreign currency options to hedge foreign currency transactions for periods consistent with its identified exposures. Accordingly, the Company categorizes these instruments as entered into for purposes other than trading. Premiums on foreign currency options are amortized based on changes in the time-value of the options for the reporting period.

The accompanying consolidated statements of earnings include net exchange losses of $6.8 million, net exchange gains of $9.2 million and net exchange losses of $4.3 million in fiscal 2002, 2001 and 2000, respectively.

Inventory and Promotional Merchandise

Inventory and promotional merchandise only includes inventory considered saleable or usable in future periods, and is stated at the lower of cost or fair-market value, with cost being determined on the first-in, first-out method. Promotional merchandise is charged to expense at the time the merchandise is shipped to the Company's customers.

JUNE 30	**2002**	2001
(In millions)		
Inventory and promotional merchandise consists of:		
Raw materials	**$117.5**	$172.9
Work in process	**27.0**	24.4
Finished goods	**272.2**	308.0
Promotional merchandise	**127.8**	125.0
	$544.5	$630.3

Property, Plant and Equipment

Property, plant and equipment is carried at cost less accumulated depreciation and amortization. For financial statement purposes, depreciation is provided principally on the straight-line method over the estimated useful lives of the assets ranging from 3 to 40 years. Leasehold improvements are amortized on a straight-line basis over the shorter of the lives of the respective leases or the expected useful lives of those improvements.

JUNE 30	**2002**	2001
(In millions)		
Land	**$ 13.0**	$ 12.7
Buildings and improvements	**144.0**	135.7
Machinery and equipment	**611.7**	563.2
Furniture and fixtures	**86.1**	77.5
Leasehold improvements	**447.2**	311.2
	1,302.0	1,100.3
Less accumulated depreciation and amortization	**721.3**	571.6
	$ 580.7	$ 528.7

Depreciation and amortization of property, plant and equipment was $140.5 million, $112.1 million and $90.3 million in fiscal 2002, 2001 and 2000, respectively.

Goodwill and Other Intangible Assets

Effective July 1, 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations", and SFAS No. 142, "Goodwill and Other Intangible Assets". These statements established financial accounting and reporting standards for acquired goodwill and other intangible assets. Specifically, the standards address how acquired intangible assets should be accounted for both at the time of acquisition and after they have been recognized in the financial statements. The provisions of SFAS No. 141 apply to all business combinations initiated after June 30, 2001. In accordance with SFAS No. 142, intangible assets, including purchased goodwill, must be evaluated for impairment. Those intangible assets that will continue to be classified as goodwill or as other intangibles with indefinite lives are no longer amortized.

In accordance with SFAS No. 142, the Company completed its transitional impairment testing of intangible assets during the first quarter of fiscal 2002. That effort, and preliminary assessments of the Company's identifiable intangible assets, indicated that little or no adjustment would be required upon adoption of this pronouncement. The impairment testing is performed in two steps: (i) the Company determines impairment by comparing the fair value of a reporting unit with its carrying value, and (ii) if there is an impairment, the Company measures the amount of impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. Subsequent to the first quarter of fiscal 2002, with the assistance of a third-party valuation firm, the Company finalized the testing of goodwill. Using conservative, but realistic, assumptions to model the Company's *jane* business, the Company determined that the carrying value of this unit was slightly greater than the derived fair value, indicating an impairment in the recorded goodwill.

To determine fair value, the Company relied on three valuation models: guideline public companies, acquisition analysis and discounted cash flow. For goodwill valuation purposes only, the revised fair value of this unit was allocated to the assets and liabilities of the business unit to arrive at an implied fair value of goodwill, based upon known facts and circumstances, as if the acquisition occurred currently. This allocation resulted in a write-down of recorded goodwill in the amount of $20.6 million, which has been reported as the cumulative effect of a change in accounting principle, as of July 1, 2001, in the accompanying consolidated statements of earnings. On a product category basis, this write-down would have primarily impacted the Company's makeup category.

During fiscal 2002, the Company recorded a goodwill impairment charge related to its Gloss.com business as a component of its restructuring expense. See Note 5 "Restructuring and Other Non-Recurring Expenses".

The following table presents adjusted net earnings and earnings per share data restated to include the retroactive impact of the adoption of SFAS No. 142.

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions, except per share data)			
Reported Net Earnings before Accounting Change	**$212.5**	$307.4	$314.1
Cumulative effect of a change in accounting principle, net of tax	**(20.6)**	(2.2)	—
Net Earnings	**191.9**	305.2	314.1
Preferred stock dividends	**23.4**	23.4	23.4
Reported Net Earnings Attributable to Common Stock	**168.5**	281.8	290.7
Add back: Goodwill amortization, net of tax	**—**	13.4	11.1
Adjusted Net Earnings	**$168.5**	$295.2	$301.8
Basic net earnings per common share:			
Reported net earnings attributable to common stock before accounting change	**$ .79**	$ 1.19	$ 1.22
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**.71**	1.18	1.22
Goodwill amortization, net of tax	**—**	.06	.05
Adjusted net earnings attributable to common stock	**$ .71**	$ 1.24	$ 1.27
Diluted net earnings per common share:			
Reported net earnings attributable to common stock before accounting change	**$ .78**	$ 1.17	$ 1.20
Cumulative effect of a change in accounting principle, net of tax	**(.08)**	(.01)	—
Net earnings attributable to common stock	**.70**	1.16	1.20
Goodwill amortization, net of tax	**—**	.06	.04
Adjusted net earnings attributable to common stock	**$ .70**	$ 1.22	$ 1.24
Weighted average common shares outstanding:			
Basic	**238.2**	238.4	237.7
Diluted	**241.1**	242.2	242.5

Goodwill

The change in the carrying amount of goodwill is as follows:

YEAR ENDED JUNE 30, 2002	
(In millions)	
Net balance as of June 30, 2001	$699.7
Goodwill impairment loss upon adoption of new accounting principle	**(20.6)**
Restructuring write-off of Gloss.com acquisition goodwill	**(20.1)**
Goodwill acquired during the period	**16.6**
Net balance as of June 30, 2002	**$675.6**

Other Intangible Assets

Other intangible assets consist of the following:

JUNE 30, 2002	Gross Carrying Value	Accumulated Amortization	Total Net Book Value
(In millions)			
Licensing agreements	$15.0	$ 6.2	$ 8.8
Trademarks and other	15.2	6.7	8.5
Patents	1.6	0.5	1.1
Total	$31.8	$13.4	$18.4

Pursuant to the adoption of SFAS No. 142 and effective July 1, 2001, trademarks have been classified as indefinite lived assets and are no longer amortized. The cost of other intangible assets is amortized on a straight-line basis over their estimated useful lives. The aggregate

amortization expense related to amortizable intangible assets for the year ended June 30, 2002 was $1.5 million.

Long-Lived Assets

In accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets in question may not be recoverable. An impairment would be recorded in circumstances where undiscounted cash flows expected to be generated by an asset are less than the carrying value of that asset.

Accumulated Other Comprehensive Income

The components of accumulated other comprehensive income (loss) ("OCI") included in the accompanying consolidated balance sheets consist of the following:

YEAR ENDED JUNE 30	**2002**	2001	2000
(In millions)			
Net unrealized investment gains, beginning of year	**$ 2.9**	$ 13.9	$ 6.1
Unrealized investment gains (losses)	**(5.0)**	(18.3)	13.0
Provision for deferred income taxes	**2.0**	7.3	(5.2)
Net unrealized investment gains (losses), end of year	**(0.1)**	2.9	13.9
Net derivative instruments, beginning of year	**(2.0)**	—	—
Gain (loss) on derivative instruments	**(16.1)**	8.8	—
Provision for deferred income taxes on gain (loss)	**5.5**	(3.1)	—
Reclassification to earnings during the year	**5.3**	(12.0)	—
Provision for deferred income taxes on reclassification	**(1.8)**	4.3	—
Net derivative instruments, end of year	**(9.1)**	(2.0)	—
Net minimum pension liability adjustments, beginning of year	**(12.4)**	—	—
Minimum pension liability adjustments	**(11.6)**	(19.4)	—
Provision for deferred income taxes	**3.7**	7.0	—
Net minimum pension liability adjustments, end of year	**(20.3)**	(12.4)	—
Cumulative translation adjustments, beginning of year	**(109.0)**	(71.0)	(50.4)
Translation adjustments	**46.0**	(38.0)	(20.6)
Cumulative translation adjustments, end of year	**(63.0)**	(109.0)	(71.0)
Accumulated other comprehensive income (loss)	**$ (92.5)**	$(120.5)	$(57.1)

The $9.1 million, net of tax, derivative instruments loss recorded in OCI at June 30, 2002 related to forward contracts that the Company estimates will be classified to earnings as losses during the next twelve months assuming exchange rates at the time of settlement are equal to the forward rates as of June 30, 2002. The Company believes these losses would be offset by the effects of exchange rate movements on the respective underlying transactions for which the hedges are intended. With regard to interest rate contracts, upon repayment of the term loan in February 2002 and the termination of interest rate swaps and options, losses deferred in OCI were reclassified to earnings. Those losses were substantially offset by deferred gains from previously terminated interest rate swaps.

Revenue Recognition

Generally, revenues from merchandise sales are recorded at the time the product is shipped to the customer. The Company reports its sales levels on a net sales basis, which is computed by deducting from gross sales the amount of actual returns received and an amount established for anticipated returns. As a percent of gross sales, returns were 4.9% in fiscal 2002, 4.9% in fiscal 2001 and 4.3% in fiscal 2000.

Advertising and Promotion

Costs associated with advertising are expensed during the year as incurred. Global advertising expenses, which primarily include television, radio and print media, and promotional expenses, such as products used as sales incentives, were $1,326.2 million, $1,255.3 million and $1,195.8 million in fiscal 2002, 2001 and 2000, respectively. These amounts include expenses relating to purchase with purchase and gift with purchase promotions that are now reflected in net sales and cost of sales due to a change in generally accepted accounting principles. Advertising and promotional expenses included in operating expenses were $1,122.0 million, $1,060.8 million and $1,003.4 million in fiscal 2002, 2001 and 2000, respectively.

Research and Development

Research and development costs, which amounted to $61.3 million, $57.3 million and $53.8 million in fiscal 2002, 2001 and 2000, respectively, are expensed as incurred.

Related Party Royalties and Trademarks

Under agreements covering the Company's purchase of trademarks for a percentage of related sales, royalty payments totaling $16.5 million, $16.0 million and $15.5 million in fiscal 2002, 2001 and 2000, respectively, have been charged to income. Such payments were made to Mrs. Estée Lauder. During fiscal 1996, the Company purchased a stockholder's rights to receive certain U.S. royalty payments for $88.5 million, which was fully amortized in November 2000. In fiscal 2001 and 2000, $6.6 million and $17.7 million, respectively, were amortized as charges against income.

Stock Compensation

The Company observes the provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", by continuing to apply the provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees", while providing the required pro forma disclosures as if the fair value method had been applied. See Note 14 "Stock Programs".

Concentration of Credit Risk

The Company is a worldwide manufacturer, marketer and distributor of skin care, makeup, fragrance and hair care products. Domestic and international sales are made primarily to department stores, specialty retailers, perfumeries and pharmacies. The Company grants credit to all qualified customers and does not believe it is exposed significantly to any undue concentration of credit risk.

For the fiscal year ended June 30, 2002, the Company's three largest customers accounted for 25% of net sales. No customer accounted for more than 10% of the Company's net sales during 2002. One department store group accounted for 11% of the Company's net sales in fiscal years ended 2001 and 2000. In the same years, another department store group accounted for 10% of the Company's net sales.

Additionally, as of June 30, 2002, the Company's three largest customers accounted for 28% of its outstanding accounts receivable.

Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in those financial statements. Actual results could differ from those estimates and assumptions.

Derivative Financial Instruments

Effective July 1, 2000, the Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended by SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities". These statements established accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS No. 133, as amended, requires the recognition of all derivative instruments as either assets or liabilities in the statement of financial position measured at fair value.

In accordance with the provisions of SFAS No. 133, as amended, the Company recorded a non-cash charge to earnings of $2.2 million, after tax, to reflect the change in time-value from the dates of the derivative instruments' inception through the date of transition (July 1, 2000). This charge is reflected as the cumulative effect of a change in accounting principle in fiscal 2001 in the accompanying consolidated statements of earnings.

Recently Issued Accounting Standards

Effective January 1, 2002, the Company adopted the Emerging Issues Task Force ("EITF") Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer", which codified and reconciled the following EITF Issues: Issue No. 00-14, "Accounting for Certain Sales Incentives", Issue No. 00-22, "Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to be Delivered in the Future", and Issue No. 00-25, "Vendor Income Statement Characterization of Consideration Paid to a Reseller of the Vendor's Products". Issue No. 00-14 addressed when sales incentives and discounts should be recognized, as well as where the related revenues and expenses should be classified in the financial statements. Upon adoption of this Issue, the Company reclassified revenues generated from purchase with purchase activities as sales and costs of purchase with purchase and gift with purchase activities as cost of sales, which were previously reported net as operating expenses. Operating income has remained unchanged by this adoption. These reclassifications have been reported in the accompanying consolidated statements of earnings retroactively for all periods reported.

In August 2001, the Financial Accounting Standards Board issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 will be effective for financial statements of fiscal years beginning after December 15, 2001. The Company will adopt this statement for the fiscal year ending June 30, 2003 and does not anticipate that it will have a material impact on the Company's consolidated financial results.

In June 2002, the Financial Accounting Standards Board issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". This statement covers restructuring type activities beginning with plans initiated after December 31, 2002. Should the Company enter into activities covered by this standard after that date, the provisions of SFAS No. 146 would be applied. As a result of this standard, there is no impact on the Company's consolidated financial position or results of operations for the periods presented.

NOTE 3 – PUBLIC OFFERINGS

During October 2001, a member of the Lauder family sold 5,000,000 shares of Class A Common Stock in a registered public offering. The Company did not receive any proceeds from the sale of these shares.

During May and June 2000, members of the Lauder family sold 8,482,000 shares of Class A Common Stock in a registered public offering. The Company did not receive any proceeds from the sale of these shares.

NOTE 4 – ACQUISITION OF BUSINESSES

At various times during fiscal 2002, 2001 and 2000, the Company acquired businesses engaged in the wholesale distribution and retail sale of Aveda products, as well as other products, in the United States and other countries. In fiscal 2002, the Company purchased an Aveda wholesale distributor business in Korea and bought out the minority interest of its Aveda joint venture in the United Kingdom. The Company also bought out the minority interest of its joint venture in Chile.

In fiscal 2001, the Company purchased a wholesale distributor business in Israel, a majority interest of the wholesale distributor business in Chile and created a joint venture in Greece in which the Company owns a controlling majority interest.

In June 2000, the Company acquired, for cash, a controlling majority equity interest in Bumble and Bumble Products, LLC, a marketer and distributor of hair care products, and Bumble and Bumble, LLC, which operates a salon in New York City.

In April 2000, the Company acquired, for cash, the business of Gloss.com, Inc. a multi-brand Internet beauty site.

In October 1999, the Company acquired Jo Malone Limited, a London-based marketer of prestige skin care and fragrance products, for cash.

In August 1999, the Company acquired the business of Stila Cosmetics, Inc., a manufacturer and marketer of makeup products, for cash.

The aggregate purchase price for these transactions, which includes acquisition costs, was approximately $18.5 million, $16.0 million, and $186.6 million in fiscal 2002, 2001 and 2000, respectively, and each transaction was accounted for using the purchase method of accounting. Accordingly, the results of operations for each of the acquired businesses are included in the accompanying consolidated financial statements commencing with its date of original acquisition. Pro forma results of operations, as if each of such businesses had been acquired as of the beginning of the year of acquisition, have not been presented, as the impact on the Company's consolidated financial results would not have been material.

NOTE 5 – RESTRUCTURING AND OTHER NON-RECURRING EXPENSES

During the fourth quarter of fiscal 2002, the Company recorded a restructuring related to repositioning certain businesses as part of its ongoing efforts to drive long-term growth and increase profitability. The restructuring focused on cost reduction opportunities related to the Internet, supply chain, globalization of the organization and distribution channel refinements. The Company has committed to a defined plan of action, which resulted in an aggregate pre-tax charge of $117.4 million, of which $59.4 million is cash related. On an after-tax basis, the aggregate charge was $76.9 million, equal to $.32 per diluted share.

Specifically, the charge includes the following:

- **Internet.** In an effort to achieve strategic objectives, reduce costs and improve profitability, the Company outsourced Gloss.com platform development and maintenance efforts to a third-party provider. Additionally, Gloss.com closed its San Francisco facility and consolidated its operations in New York. As a result, included in the charge is a $23.9 million provision for restructuring the Gloss.com operations, including benefits and severance packages for 36 employees as well as asset write-offs. The Company also took a $20.1 million charge to write-off the related Gloss.com acquisition goodwill.

- **Supply Chain.** Building on previously announced supply chain initiatives, the Company restructured certain manufacturing, distribution, research and development, information systems and quality assurance operations in the United States, Canada and Europe which included benefits and severance packages for 110 employees. A charge of $23.7 million was recorded related to this effort.

- **Globalization of Organization.** The Company continued to implement its previously announced transition to a global brand structure designed to streamline the decision making process and increase innovation and speed-to-market. The next phase of this transition entailed eliminating duplicate functions and responsibilities, which resulted in charges for benefits and severance for 122 employees. The Company recorded a charge of $27.1 million associated with these efforts.

- **Distribution.** The Company evaluated areas of distribution relative to its financial targets and will focus its resources on the most productive sales channels and markets. As a result, the Company closed its operations in Argentina and the remaining customers will be serviced by the Company's Chilean affiliate. The Company is also closing all remaining in-store "tommy's shops" and other select points of distribution. The Company recorded a $22.6 million provision related to these actions, which included benefits and severance for 85 employees.

Following is a summary of the charges as recorded in the consolidated statement of earnings for fiscal 2002:

	Restructuring			
	Net Sales	Cost of Sales	Operating Expenses	Total
(In millions)				
Internet	$ —	$ —	$ 44.0	$ 44.0
Supply Chain	—	—	23.7	23.7
Globalization of Organization	—	—	27.1	27.1
Distribution	6.2	0.8	15.6	22.6
Total charge	$6.2	$0.8	$110.4	117.4
Tax effect				(40.5)
Net charge				$ 76.9

The restructuring charge was recorded in other accrued liabilities or, where applicable, as a reduction of related assets. During fiscal 2002, $9.3 million related to this restructuring was paid. As of June 30, 2002, the restructuring accrual balance was $54.1 million and the Company expects to settle a majority of the remaining obligations by the end of fiscal 2003 with certain additional payments made ratably through fiscal 2006.

During the fourth quarter of fiscal 2001, the Company recorded one-time charges for restructuring and other non-recurring expenses related to repositioning certain businesses as part of the Company's ongoing efforts to drive long-term growth and increase profitability. The restructuring and other non-recurring expenses focused on four areas: product fixtures for the *jane* brand; in-store "tommy's shops"; information systems and other assets; and global brand reorganization. The Company committed to a defined plan of action, which resulted in an aggregate pre-tax charge of $63.0 million, of which $35.9 million is cash related. On an after-tax basis, the aggregate charge was $40.3 million, equal to $.17 per diluted share.

Specifically, the charge included the following:

- ***jane.*** *jane* switched from its traditional wall displays to a carded program. The charge included a $16.1 million write-down of existing *jane* product fixtures and the return of uncarded product from virtually all of the 13,000 distribution outlets in the United States.

- **"tommy's shops."** The Company restructured the in-store "tommy's shops" to focus on the most productive locations and decided to close certain shops that underperformed relative to expectations. As a result, the Company recorded a $6.3 million provision for the closing of 86 under-performing in-store "tommy's shops," located in the United States, and for related product returns.

- **Information systems and other assets.** In response to changing technology and the Company's new strategic direction, the charge included a $16.2 million provision for costs associated with the reevaluation of supply chain systems that the Company no longer utilized and with the elimination of unproductive assets related to the change to standard financial systems.

- **Global brand reorganization.** The Company recorded $20.8 million related to benefits and severance packages for 75 management employees who were affected by the reconfiguration to a global brand structure and another $3.6 million related to infrastructure costs.

Following is a summary of the charges as recorded in the consolidated statement of earnings for fiscal 2001:

	Restructuring				
	Net Sales	Cost of Sales	Operating Expenses	Other Non-Recurring Expenses	Total
(In millions)					
jane	$ 5.7	$ 1.5	$ 4.8	$ 4.1	$16.1
"tommy's shops"	2.3	(0.4)	4.4	—	6.3
Information systems and other assets	—	—	4.6	11.6	16.2
Global brand reorganization	—	—	23.8	0.6	24.4
Total charge	$ 8.0	$ 1.1	$37.6	$16.3	63.0
Tax effect					(22.7)
Net charge					$40.3

The restructuring charge was recorded in other accrued liabilities or as a reduction of fixed assets. During fiscal 2001, $0.7 million was paid and through June 30, 2002 an additional $26.7 million was paid. As of June 30, 2002, the remaining obligation was $7.1 million, the majority of which the Company expects to settle through the end of fiscal 2003 with remaining payments made ratably through fiscal 2004.

NOTE 6 – INCOME TAXES

The provision for income taxes is comprised of the following:

YEAR ENDED JUNE 30	2002	2001	2000
(In millions)			
Current:			
Federal	**$ 40.7**	$ 74.0	$ 93.9
Foreign	**89.8**	87.6	82.4
State and local	**6.5**	7.7	13.8
	137.0	169.3	190.1
Deferred:			
Federal	**(13.2)**	3.7	(0.2)
Foreign	**(8.9)**	0.5	(4.1)
State and local	**(0.5)**	0.5	(1.2)
	(22.6)	4.7	(5.5)
	$114.4	$174.0	$184.6

A reconciliation between the provision for income taxes computed by applying the statutory Federal income tax rate to earnings before income taxes and minority interest and the actual provision for income taxes is as follows:

YEAR ENDED JUNE 30	2002	2001	2000
(In millions)			
Provision for income taxes at statutory rate	**$116.1**	$169.2	$174.5
Increase (decrease) due to:			
State and local income taxes, net of Federal tax benefit	**3.9**	5.3	8.2
Effect of foreign operations	**(0.9)**	(2.9)	(11.7)
Domestic royalty expense not deductible for U.S. tax purposes	**—**	1.6	4.0
Other nondeductible expenses	**3.2**	3.8	3.8
Tax credits	**(2.1)**	—	—
Other, net	**(5.8)**	(3.0)	5.8
Provision for income taxes	**$114.4**	$174.0	$184.6
Effective tax rate	**34.5%**	36.0%	37.0%

Significant components of the Company's deferred income tax assets and liabilities as of June 30, 2002 and 2001 were as follows:

	2002	2001
(In millions)		
Deferred tax assets:		
Deferred compensation and other payroll related expenses	**$ 53.3**	$ 47.7
Inventory obsolescence and other inventory related reserves	**58.5**	54.1
Pension plan reserves	**26.2**	22.5
Postretirement benefit obligations	**25.9**	21.7
Various accruals not currently deductible	**72.0**	57.6
Net operating loss carryforwards	**1.5**	3.8
Other differences between tax and financial statement values	**9.4**	5.7
	246.8	213.1
Valuation allowance for deferred tax assets	**(1.5)**	(3.8)
Total deferred tax assets	**245.3**	209.3
Deferred tax liabilities:		
Depreciation and amortization	**(60.2)**	(54.1)
Other differences between tax and financial statement values	**—**	(2.0)
Total deferred tax liabilities	**(60.2)**	(56.1)
Total net deferred tax assets	**$185.1**	$153.2

As of June 30, 2002 and 2001, the Company had current net deferred tax assets of $112.4 million and $83.1 million, respectively, which are included in prepaid expenses and other current assets in the accompanying consolidated balance sheets, and noncurrent net deferred tax assets of $72.7 million and $70.1 million, respectively.

Federal income and foreign withholding taxes have not been provided on $473.5 million, $476.4 million and $442.2 million of undistributed earnings of international subsidiaries at June 30, 2002, 2001 and 2000, respectively. The Company intends to permanently reinvest these earnings in its foreign operations, except where it is able to repatriate these earnings to the United States without any material incremental tax provision.

As of June 30, 2002 and 2001, certain international subsidiaries had tax loss carryforwards for local tax purposes of approximately $10.2 million and $21.4 million, respectively. With the exception of $3.9 million of losses with an indefinite carryforward period as of June 30, 2002, these losses expire at various dates through fiscal 2008. Deferred tax assets in the amount of $1.5 million and $3.8 million as of June 30, 2002 and 2001, respectively, have been recorded to reflect the tax benefits of the losses not utilized to date. A full valuation allowance has been provided since, in the opinion of management, it is more likely than not that the deferred tax assets will not be realized.

Earnings before income taxes and minority interest include amounts contributed by the Company's international operations of $283.4 million, $307.2 million and $281.2 million for fiscal 2002, 2001 and 2000, respectively.

NOTE 7 – OTHER ACCRUED LIABILITIES

Other accrued liabilities consist of the following:

JUNE 30	**2002**	2001
(In millions)		
Advertising and promotional accruals	**$213.5**	$157.0
Employee compensation	**169.9**	182.6
Restructuring	**61.2**	35.2
Other	**182.0**	157.3
	$626.6	$532.1

NOTE 8 – DEBT

The Company's short-term and long-term debt and available financing consist of the following:

	Debt at June 30		Available financing at June 30 – Committed		Available financing at June 30 – Uncommitted	
	2002	2001	**2002**	2001	**2002**	2001
(In millions)						
Commercial paper with an average interest rate of 1.81% and 3.96%, respectively	**$130.0**	$181.0	**$ —**	$ –	**$620.0**	$569.0
6% Senior Notes, due January 15, 2012, with an effective yield of 6.062%	**248.9**	–	**—**	–	**—**	–
Unsecured notes payable, due February 1, 2005, with an effective interest rate of 5.13%	**—**	200.0	**—**	–	**—**	–
2% Japan loan payable, due in installments through April 2003	**5.8**	11.3	**—**	–	**—**	–
1.45% Japan loan payable, due on March 28, 2006	**25.0**	24.2	**—**	–	**—**	–
Other short-term borrowings	**0.8**	0.2	**—**	–	**22.9**	30.4
Revolving credit facility	**—**	–	**400.0**	400.0	**—**	–
Shelf registration for debt securities	**—**	–	**—**	–	**150.0**	400.0
	410.5	416.7	**$400.0**	$400.0	**$792.9**	$999.4
Less current maturities	**6.6**	5.8				
	$403.9	$410.9				

In January 2002, the Company issued and sold $250.0 million of 6% Senior Notes due 2012 ("6% Senior Notes") in a public offering. The 6% Senior Notes were priced at 99.538% with a yield of 6.062%. Interest payments are required to be made semi-annually on January 15 and July 15 of each year. The first payment was made on July 15, 2002. The primary portion of the net proceeds of the offering was used to repay a $200.0 million term loan. The remainder was used to repay a portion of the outstanding commercial paper.

The Company maintains uncommitted credit facilities in various regions throughout the world. Interest rate terms for these facilities vary by region and reflect prevailing market rates for companies with strong credit ratings. During fiscal 2002 and 2001, the monthly average amount outstanding was approximately $12.9 million and $18.6 million, respectively, and the annualized monthly weighted average interest rate incurred was approximately 4.1% and 6.5%, respectively.

During fiscal 1998, the Company entered into a 2% loan payable in Japan. Principal repayments of 350.0 million yen, approximately $2.9 million at current rates, will be made semi-annually through 2003.

Effective June 28, 2001, the Company entered into a new five-year $400.0 million revolving credit facility, expiring on June 28, 2006, which includes an annual fee of .07% on the total commitment. The new facility replaced a five-year $400.0 million revolving credit facility entered into in July 1996. The 1996 facility had an annual fee of .06% on the total commitment. At June 30, 2002 and 2001, the Company was in compliance with all related financial and other restrictive covenants, including limitations on indebtedness and liens.

Commercial paper is classified as long-term debt based upon the Company's intent and ability to refinance maturing commercial paper on a long-term basis. It is the Company's policy to maintain backup facilities to support the commercial paper program and its classification as long-term debt.

NOTE 9 – FINANCIAL INSTRUMENTS

Derivative Financial Instruments

The Company addresses certain financial exposures through a controlled program of risk management that includes the use of derivative financial instruments. The Company primarily enters into foreign currency forward exchange contracts and foreign currency options to reduce the effects of fluctuating foreign currency exchange rates. The Company, if necessary, enters into interest rate swaps and options to manage the effects of interest rate movements on the Company's aggregate liability portfolio. The Company categorizes these instruments as entered into for purposes other than trading.

All derivatives are recognized on the balance sheet at their fair value. On the date the derivative contract is entered into, the Company designates the derivative as (i) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value" hedge), (ii) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge), (iii) a foreign-currency fair-value or cash-flow hedge ("foreign currency" hedge), (iv) a hedge of a net investment in a foreign operation, or (v) "held for trading" ("trading" instruments). Changes in the fair value of a derivative that is highly effective as (and that is designated and qualifies as) a fair-value hedge, along with the loss or gain on the hedged asset or liability that is attributable to the hedged risk (including losses or gains on firm commitments), are recorded in current-period earnings. Changes in the fair value of a derivative that is highly effective as (and that is designated and qualifies as) a cash-flow hedge are recorded in other comprehensive income, until earnings are affected by the variability of cash flows (e.g., when periodic settlements on a variable-rate asset or liability are recorded in earnings). Changes in the fair value of derivatives that are highly effective as (and that are designated and qualify as) foreign-currency hedges are recorded in either current-period earnings or other comprehensive income, depending on whether the hedge transaction is a fair-value hedge (e.g., a hedge of a firm commitment that is to be settled in a foreign currency) or a cash-flow hedge (e.g., a foreign-currency-denominated forecasted transaction). If, however, a derivative is used as a hedge of a net investment in a foreign operation, its changes in fair value, to the extent effective as a hedge, are recorded in accumulated other comprehensive income within equity. Furthermore, changes in the fair value of derivative trading instruments are reported in current-period earnings.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair-value, cash-flow, or foreign-currency hedges to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting

changes in fair values or cash flows of hedged items. If it is determined that a derivative is not highly effective, or that it has ceased to be a highly effective hedge, the Company will be required to discontinue hedge accounting with respect to that derivative prospectively.

Foreign Exchange Risk Management

The Company enters into forward exchange contracts to hedge anticipated transactions as well as receivables and payables denominated in foreign currencies for periods consistent with the Company's identified exposures. The purpose of the hedging activities is to minimize the effect of foreign exchange rate movements on costs and on the cash flows that the Company receives from foreign subsidiaries. Almost all foreign currency contracts are denominated in currencies of major industrial countries and are with large financial institutions rated as strong investment grade by a major rating agency. The Company also enters into foreign currency options to hedge anticipated transactions where there is a high probability that anticipated exposures will materialize. The forward exchange contracts and foreign currency options have been designated as cash-flow hedges. As of June 30, 2002, these cash-flow hedges were highly effective, in all material respects.

As a matter of policy, the Company only enters into contracts with counterparties that have at least an "A" (or equivalent) credit rating. The counterparties to these contracts are major financial institutions. The Company does not have significant exposure to any one counterparty. Exposure to credit loss in the event of nonperformance by any of the counterparties is limited to only the recognized, but not realized, gains attributable to the contracts. Management believes risk of loss under these hedging contracts is remote and in any event would not be material to the Company's consolidated financial results. The contracts have varying maturities through the end of July 2003. Costs associated with entering into such contracts have not been material to the Company's consolidated financial results. The Company does not utilize derivative financial instruments for trading or speculative purposes. At June 30, 2002, we had foreign currency contracts in the form of forward exchange contracts in the amount of $227.2 million. The foreign currencies included in these contracts (notional value stated in U.S. dollars) are principally the Japanese yen ($70.7 million), Euro ($31.7 million), British pound ($26.2 million), Australian dollar ($16.0 million), Swiss franc ($11.8 million), Danish krone ($11.6 million) and Canadian dollar ($10.5 million). At June 30, 2001, we had foreign currency contracts in the form of forward exchange contracts in the amount of $148.2 million. The foreign currencies included in these contracts (notional value stated in U.S. dollars) are principally the Japanese yen ($53.9 million), Swiss franc ($28.8 million), Korean won ($18.5 million), Taiwan dollar ($13.7 million), British pound ($13.2 million), Euro ($8.5 million) and Mexican peso ($6.8 million).

Interest Rate Risk Management

In February 2002, the Company repaid its outstanding term loan, which had a floating interest rate, with the proceeds from the January 2002 public debt offering of 6% Senior Notes. As a result, the Company terminated the interest rate swaps and options that were previously outstanding to mitigate interest rate volatility. No material gain or loss resulted from the termination of those contracts. Prior to repayment of the term loan, the Company had entered into an interest rate swap agreement to exchange floating rate for fixed rate interest payments periodically over the life of the agreement. In addition, the Company had purchased interest rate options that offer similar interest rate protection. The interest rate swap and options were designated as cash-flow hedges and were highly effective through the date of termination.

Information regarding the interest rate swap and options is presented in the following table:

YEAR ENDED OR AT JUNE 30, 2001	Notional Amounts	Weighted Average	
		Pay Rate	Receive Rate
(In millions)			
Interest rate swap	$ 67.0	6.14%	6.32%
Interest rate options	133.0	6.14	6.62

Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents:

The carrying amount approximates fair value, primarily because of the short maturity of cash equivalent instruments.

Long-term debt:

The fair value of the Company's long-term debt was estimated based on the current rates offered to the Company for debt with the same remaining maturities. Included in such amount is the fair value of the Company's commercial paper.

Cumulative redeemable preferred stock:
The fair value of the cumulative redeemable preferred stock is estimated utilizing a cash flow analysis at a discount rate equal to rates available for debt with terms similar to the preferred stock.

Foreign exchange and interest rate contracts:
The fair value of forwards, swaps and options is the estimated amount the Company would receive or pay to terminate the agreements.

The estimated fair values of the Company's financial instruments are as follows:

	JUNE 30, 2002		JUNE 30, 2001	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value
(In millions)				
Nonderivatives				
Cash and cash equivalents	**$546.9**	**$546.9**	$346.7	$346.7
Long-term debt, including current portion	**410.5**	**415.6**	416.5	418.1
Cumulative redeemable preferred stock	**360.0**	**374.9**	360.0	362.6
Derivatives				
Foreign exchange and interest rate contracts	**(14.8)**	**(14.8)**	(2.5)	(2.5)

NOTE 10 – PENSION, DEFERRED COMPENSATION AND POSTRETIREMENT BENEFIT PLANS

The Company maintains pension plans covering substantially all of its full-time employees for its U.S. operations and a majority of its international operations. Several plans provide pension benefits based primarily on years of service and employees' earnings. In certain instances, the Company adjusts benefits in connection with international employee transfers.

Retirement Growth Account Plan (U.S.)

The Retirement Growth Account Plan is a trust-based, noncontributory defined benefit pension plan. The Company's funding policy consists of an annual contribution at a rate that provides for future plan benefits and maintains appropriate funded percentages. Such contribution is not less than the minimum required by the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and subsequent pension legislation and is not more than the maximum amount deductible for income tax purposes.

Restoration Plan (U.S.)

The Company also has an unfunded, nonqualified domestic benefit Restoration Plan to provide benefits in excess of Internal Revenue Code limitations.

International Pension Plans

The Company maintains International Pension Plans, the most significant of which are defined benefit pension plans. The Company's funding policies for these plans are determined by local laws and regulations.

Postretirement Benefits

The Company maintains a domestic contributory postretirement benefit plan which provides certain medical and dental benefits to eligible employees. Employees hired after January 1, 2002 will not be eligible for retiree medical benefits when they retire. Retired employees who are receiving monthly pension benefits are eligible for participation in the plan. Contributions required and benefits received by retirees and eligible family members are dependent on the age of the retiree. It is the Company's practice to fund these benefits as incurred. The cost of the Company-sponsored programs is not significant.

Certain of the Company's international subsidiaries and affiliates have postretirement plans, although most participants are covered by government-sponsored or administered programs.

The significant components of the above mentioned plans as of and for the year ended June 30 are summarized as follows:

	Pension Plans				Other than Pension Plans	
	U.S.		International		Postretirement	
	2002	2001	**2002**	2001	**2002**	2001
(In millions)						
Change in benefit obligation:						
Benefit obligation at beginning of year	**$ 280.4**	$ 256.2	**$131.5**	$132.6	**$ 43.2**	$ 41.2
Service cost	**13.5**	12.3	**7.9**	8.0	**1.8**	1.9
Interest cost	**20.6**	19.7	**7.2**	6.7	**2.9**	3.0
Plan participant contributions	**—**	—	**0.9**	0.9	**0.1**	0.1
Actuarial loss (gain)	**10.8**	5.0	**3.6**	4.8	**(1.9)**	(1.0)
Foreign currency exchange rate impact	**—**	—	**13.8**	(14.5)	**—**	—
Benefits paid	**(14.9)**	(12.9)	**(10.2)**	(7.0)	**(1.9)**	(2.0)
Plan amendments	**(0.1)**	0.1	**—**	—	**(0.5)**	—
Other	**—**	—	**—**	—	**—**	—
Benefit obligation at end of year	**310.3**	280.4	**154.7**	131.5	**43.7**	43.2
Change in plan assets:						
Fair value of plan assets at beginning of year	**179.7**	192.1	**104.6**	117.7	**—**	—
Actual return on plan assets	**(9.5)**	(17.3)	**(0.9)**	(6.5)	**—**	—
Foreign currency exchange rate impact	**—**	—	**10.5**	(11.6)	**—**	—
Employer contributions	**46.5**	17.8	**11.4**	10.6	**1.8**	1.9
Plan participant contributions	**—**	—	**0.9**	0.9	**0.1**	0.1
Benefits paid from plan assets	**(14.9)**	(12.9)	**(10.2)**	(6.5)	**(1.9)**	(2.0)
Fair value of plan assets at end of year	**201.8**	179.7	**116.3**	104.6	**—**	—
Funded status	**(108.5)**	(100.7)	**(38.4)**	(26.9)	**(43.7)**	(43.2)
Unrecognized net actuarial loss (gain)	**104.4**	69.6	**37.2**	24.3	**(8.1)**	(6.6)
Unrecognized prior service cost	**4.0**	4.3	**2.5**	2.4	**(0.2)**	0.2
Unrecognized net transition (asset) obligation	**(1.5)**	(3.0)	**0.6**	0.8	**—**	—
Accrued benefit cost	**$ (1.6)**	$ (29.8)	**$ 1.9**	$ 0.6	**$(52.0)**	$(49.6)
Amounts recognized in the Balance Sheets consist of:						
Prepaid benefit cost	**$ 39.5**	$ 6.2	**$ 10.1**	$ 8.1	—	—
Accrued benefit liability	**(47.3)**	(46.1)	**(40.1)**	(28.0)	**$(52.0)**	$(49.6)
Intangible asset	**0.2**	3.7	**1.0**	1.1	**—**	—
Other	**6.0**	6.4	**30.9**	19.4	**—**	—
Net amount recognized	**$ (1.6)**	$ (29.8)	**$ 1.9**	$ 0.6	**$(52.0)**	$(49.6)

	Pension Plans						Other than Pension Plans		
	U.S.			International			Postretirement		
	2002	2001	2000	**2002**	2001	2000	**2002**	2001	2000
Weighted-average assumptions									
Pre-retirement discount rate	**7.00%**	7.50%	7.85%	**2.75–7.00%**	3.00–7.25%	3.00–7.50%	**7.00%**	7.50%	7.85%
Postretirement discount rate	**5.75%**	6.00%	6.25%	**—**	—	—	**—**	—	—
Expected return on assets	**9.00%**	9.00%	9.00%	**4.50–8.25%**	5.00–8.50%	5.00–8.25%	**N/A**	N/A	N/A
Rate of compensation increase	**4.50–11.00%**	5.00–11.50%	5.50–12.00%	**1.75–4.00%**	2.00–5.50%	2.00–6.50%	**N/A**	N/A	N/A
Components of net periodic benefit cost (In millions)									
Service cost, net	**$ 13.5**	$ 12.3	$ 10.8	**$ 8.0**	$ 8.0	$ 8.6	**$ 1.8**	$ 1.9	$1.9
Interest cost	**20.6**	19.7	16.9	**7.2**	6.7	6.3	**2.9**	3.0	2.8
Expected return on assets	**(17.3)**	(16.2)	(13.5)	**(8.3)**	(7.4)	(6.6)	**—**	—	—
Amortization of:									
Transition (asset) obligation	**(1.5)**	(1.4)	(1.4)	**0.2**	0.2	0.3	**—**	—	—
Prior service cost	**0.4**	0.4	0.4	**0.2**	0.2	0.3	**—**	—	—
Actuarial loss (gain)	**2.6**	1.1	1.3	**1.0**	0.9	1.2	**(0.4)**	(0.2)	—
Other	**—**	—	0.8	**—**	—	—	**—**	—	—
Net periodic benefit cost	**$ 18.3**	$ 15.9	$ 15.3	**$ 8.3**	$ 8.6	$10.1	**$ 4.3**	$ 4.7	$4.7

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates for fiscal 2002 would have had the following effects:

(In millions)	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total service and interest costs	$0.6	$(0.5)
Effect on postretirement benefit obligations	$4.8	$(4.6)

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the Company's pension plans at June 30 are as follows:

	Pension Plans					
	Retirement Growth Account		Restoration		International	
(In millions)	**2002**	2001	**2002**	2001	**2002**	2001
Projected Benefit Obligation	**$244.7**	$216.6	**$65.6**	$63.8	**$154.7**	$131.5
Accumulated Benefit Obligation	**191.5**	165.1	**47.3**	46.0	**127.9**	107.8
Fair Value of Plan Assets	**201.8**	179.7	**—**	—	**116.3**	104.6

International pension plans with accumulated benefit obligations in excess of the plans' assets had aggregate projected benefit obligations of $113.3 million and $92.9 million, aggregate accumulated benefit obligations of $97.2 million and $79.0 million and aggregate fair value of plan assets of $66.3 million and $58.0 million at June 30, 2002 and 2001, respectively.

401(k) Savings Plan (U.S.)

The Company's 401(k) Savings Plan ("Savings Plan") is a contributory defined contribution plan covering substantially all regular U.S. employees who have completed the hours and service requirements, as defined by the plan document. Effective January 1, 2002, regular full-time employees are eligible to participate in the Plan on the first day of the second month following their date of hire. The Savings Plan is subject to the applicable provisions

of ERISA. The Company matches a portion of the participant's contributions after one year of service under a predetermined formula based on the participant's contribution level and years of service. The Company's contributions were approximately $6.7 million for the fiscal years ended June 30, 2002 and 2001, and $5.8 million in fiscal 2000. Shares of the Company's Class A Common Stock are not an investment option in the Savings Plan and the Company does not use such shares to match participants' contributions.

Deferred Compensation

The Company accrues for deferred compensation and interest thereon and for the increase in the value of share units pursuant to agreements with certain key executives and outside directors. The amounts included in the accompanying consolidated balance sheets under these plans were $95.7 million and $87.3 million as of June 30, 2002 and 2001, respectively. The expense for fiscal 2002, 2001 and 2000 was $11.6 million, $11.6 million and $12.3 million, respectively.

NOTE 11 – POSTEMPLOYMENT BENEFITS OTHER THAN TO RETIREES

The Company provides certain postemployment benefits to eligible former or inactive employees and their dependents during the period subsequent to employment but prior to retirement. These benefits include health care coverage and severance benefits. Generally, the cost of providing these benefits is accrued and any incremental benefits were not material to the Company's consolidated financial results.

NOTE 12 – $6.50 CUMULATIVE REDEEMABLE PREFERRED STOCK, AT REDEMPTION VALUE

As of June 30, 2002, the Company's authorized capital stock included 23.6 million shares of preferred stock, par value $.01 per share, of which 3.6 million shares are outstanding and designated as $6.50 Cumulative Redeemable Preferred Stock. The outstanding preferred stock was issued in June 1995 in exchange for nonvoting common stock of the Company owned by The Estée Lauder 1994 Trust.

Holders of the $6.50 Cumulative Redeemable Preferred Stock are entitled to receive cumulative cash dividends at a rate of $6.50 per annum per share payable in quarterly installments. Such dividends have preference over all other dividends of stock issued by the Company. Shares are subject to mandatory redemption on June 30, 2005 at a redemption price of $100 per share. Following such date and so long as such mandatory redemption obligations have not been discharged in full, no dividends may be paid or declared upon the Class A or Class B Common Stock, or on any other capital stock ranking junior to or in parity with such $6.50 Cumulative Redeemable Preferred Stock and no shares of Class A or Class B Common Stock or such junior or parity stock may be redeemed or acquired for any consideration by the Company. Under certain circumstances, the Company may redeem the stock, in whole or in part, prior to the mandatory redemption date. Holders of such stock may put such shares to the Company at a price of $100 per share upon the occurrence of certain events.

The Company recorded the $6.50 Cumulative Redeemable Preferred Stock at its redemption value of $360.0 million and charged this amount, net of the par value of the shares of nonvoting common stock exchanged, to stockholders' equity in fiscal 1995.

NOTE 13 – COMMON STOCK

As of June 30, 2002, the Company's authorized common stock consists of 650 million shares of Class A Common Stock, par value $.01 per share, and 240 million shares of Class B Common Stock, par value $.01 per share. Class B Common Stock is convertible into Class A Common Stock, in whole or in part, at any time and from time to time at the option of the holder, on the basis of one share of Class A Common Stock for each share of Class B Common Stock converted. Holders of the Company's Class A Common Stock are entitled to one vote per share and holders of the Company's Class B Common Stock are entitled to ten votes per share.

Information about the Company's common stock outstanding is as follows:

	Class A	Class B
(Shares in thousands)		
Balance at June 30, 1999	123,481.2	113,679.3
Acquisition of treasury stock	(589.5)	–
Share grants	2.9	–
Share units converted	100.0	–
Stock option programs	1,187.1	–
Balance at June 30, 2000	124,181.7	113,679.3
Acquisition of treasury stock	(0.9)	–
Conversion of Class B to Class A	189.0	(189.0)
Stock option programs	806.2	–
Balance at June 30, 2001	125,176.0	113,490.3
Acquisition of treasury stock	**(1,500.0)**	**—**
Conversion of Class B to Class A	**5,077.8**	**(5,077.8)**
Stock option programs	**436.3**	**—**
Balance at June 30, 2002	**129,190.1**	**108,412.5**

On September 18, 1998, the Company's Board of Directors authorized a share repurchase program. The Company has purchased, and may continue to purchase, over an unspecified period of time, a total of up to eight million shares of Class A Common Stock in the open market or in privately negotiated transactions, depending on market conditions and other factors.

NOTE 14 – STOCK PROGRAMS

The Company has established the fiscal 2002 Share Incentive Plan, the Fiscal 1999 Share Incentive Plan, the Fiscal 1996 Share Incentive Plan and the Non-Employee Director Share Incentive Plan (collectively, the "Plans") and, additionally, has made available stock options and share units that were, or will be, granted pursuant to these Plans and certain employment agreements. These stock-based compensation programs are described below.

Total net compensation income attributable to the granting of share units and the related decrease in value of existing share units was $0.2 million in fiscal 2002. Total net compensation expense attributable to the granting of share units and the increase in value of existing share units was $0.7 million and $1.6 million in fiscal 2001 and 2000, respectively.

Share Incentive Plans

The Plans provide for the issuance of 30,750,000 shares to be awarded in the form of stock options, stock appreciation rights and other stock awards to key employees and stock options, stock awards and stock units to non-employee directors of the Company. As of June 30, 2002, 12,311,500 shares of Class A Common Stock were reserved and were available to be granted pursuant to the Plans. The exercise period for all stock options generally may not exceed ten years from the date of grant. Pursuant to the Plans, stock option awards in respect of 2,175,300, 2,709,500 and 6,252,300 shares were granted in fiscal 2002, 2001 and 2000, respectively, and share units in respect of 50,000 and 43,100 shares were granted in fiscal 2002 and 2001, respectively. During fiscal 2002, 40,700 share units were cancelled without the issuance of any shares, but the value of such units was transferred to a deferred compensation account. Generally, the stock option awards become exercisable at various times through January 2006, while the share units will be paid out in shares of Class A Common Stock at a time to be determined by the Company.

In addition to awards made by the Company, certain outstanding stock options were assumed as part of the October 1997 acquisition of Sassaby. Of the 221,200 originally issued options to acquire shares of the Company's Class A Common Stock, 15,104 were outstanding as of June 30, 2002, all of which were exercisable and will expire through May 2007.

Executive Employment Agreements

The executive employment agreements provide for the issuance of 11,400,000 shares to be awarded in the form of stock options and other stock awards to certain key executives. The Company has reserved 663,000 shares of its Class A Common Stock pursuant to such agreements as of June 30, 2002. In accordance with such employment agreements, stock option awards in respect of 1,650,000 shares were granted in fiscal 2000, and approximately 900 share units were granted in fiscal 2002 and 2001, and 33,700 share units were granted in fiscal 2000. The reserve is solely for dividend equivalents on units granted pursuant to one of the agreements. Most of the stock options granted pursuant to the agreements are exercisable and expire at various times from November 2005 through July 2009. The share units will be paid out in shares of Class A Common Stock at a time to be determined by the Company, but no later than 90 days subsequent to the termination of employment of the executive.

A summary of the Company's stock option programs as of June 30, 2002, 2001 and 2000, and changes during the years then ended, is presented below:

	2002		2001		2000	
	Shares	**Weighted-Average Exercise Price**	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
(Shares in thousands)						
Outstanding at beginning of year	**23,393.2**	**$34.55**	21,914.1	$33.14	15,439.1	$22.80
Granted at fair value	**2,175.3**	**39.07**	2,709.5	42.80	7,902.2	50.88
Exercised	**(435.4)**	**17.85**	(806.0)	16.50	(1,188.5)	15.28
Cancelled or Expired	**(289.6)**	**46.38**	(424.4)	48.19	(238.7)	41.06
Outstanding at end of year	**24,843.5**	**35.10**	23,393.2	34.55	21,914.1	33.14
Options exercisable at year-end	**13,149.5**	**27.59**	8,497.6	21.69	4,252.4	18.86
Weighted-average fair value of options granted during the year	**$16.02**		$17.01		$20.14	

The Company applies APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related Interpretations in accounting for stock options and share units granted under these programs. Under APB Opinion No. 25, no compensation expense is recognized if the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of the grant. Accordingly, no compensation cost has been recognized. SFAS No. 123, "Accounting for Stock-Based Compensation", requires the Company to provide pro forma information regarding net earnings and net earnings per common share as if compensation cost for the Company's stock option programs had been determined in accordance with the fair value method prescribed therein.

Had compensation cost for these programs been determined based upon the fair value at the grant dates consistent with SFAS No. 123, the Company's pro forma net earnings and net earnings per common share would have been as follows:

YEAR ENDED JUNE 30	**2002**(i)	2001(ii)	2000(ii)
(In millions, except per share data)			
Net earnings:			
As reported	**$191.9**	$305.2	$314.1
Pro forma	**189.2**	280.8	216.5
Net earnings per common share—Basic:			
As reported	**$ .71**	$ 1.18	$ 1.22
Pro forma	**.70**	1.08	.81
Net earnings per common share—Diluted:			
As reported	**$ .70**	$ 1.16	$ 1.20
Pro forma	**.68**	1.06	.79

(i) Beginning in fiscal 2002, the pro forma charge for compensation cost related to stock options granted will be recognized over the service period. The service period represents the period of time between the date of grant and the date each option becomes exercisable without consideration of acceleration provisions (e.g. retirement, change of control, etc.).

(ii) In fiscal 2001 and 2000, the Company determined the pro forma charge for compensation cost assuming all options were immediately vested upon the date of grant.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

YEAR ENDED JUNE 30	**2002**	2001	2000
Expected volatility	**31%**	31%	30%
Average expected option life	**7 years**	7 years	7 years
Average risk-free interest rate	**4.9%**	5.9%	6.1%
Dividend yield	**.50%**	.50%	.50%

Summarized information about the Company's stock options outstanding and exercisable at June 30, 2002 is as follows:

	Outstanding			Exercisable	
Exercise Price Range	Options(a)	Average Life(b)	Average Price(c)	Options(a)	Average Price(c)
$ 2.065 to $ 3.10	15.1	5.3	$ 3.08	15.1	$ 3.08
$13.00 to $20.813	3,531.6	3.4	13.06	3,531.6	13.06
$21.313 to $30.52	5,960.0	4.8	23.67	5,053.1	23.18
$31.875 to $47.625	8,788.6	7.6	39.33	2,660.1	37.63
$48.125 to $53.50	6,548.2	7.1	51.81	1,889.6	52.58
$ 2.065 to $53.50	24,843.5		35.10	13,149.5	27.59

(a) Shares in thousands.

(b) Weighted average contractual life remaining in years.

(c) Weighted average exercise price.

Subsequent to June 30, 2002, the Company granted options under the terms of the Plans described above to purchase an additional 6,410,700 of the Company's Class A Common Stock with an exercise price equal to fair market value on the date of grant. In addition, subsequent to June 30, 2002 the Company granted approximately 55,100 share units to a key executive pursuant to the terms of the Fiscal 2002 Share Incentive Plan.

NOTE 15 – COMMITMENTS AND CONTINGENCIES

Total rental expense included in the accompanying consolidated statements of earnings was $142.8 million in fiscal 2002, $120.9 million in fiscal 2001 and $100.7 million in fiscal 2000. At June 30, 2002, the future minimum rental commitments under long-term operating leases are as follows:

YEAR ENDING JUNE 30	(In millions)
2003	$ 98.7
2004	91.6
2005	79.3
2006	53.6
2007	46.9
Thereafter	173.4
	$543.5

In August 2000, an affiliate of Revlon, Inc. sued the Company and its subsidiaries in the U.S. District Court, Southern District of New York, for alleged patent infringement and related claims. Revlon alleges that five Estée Lauder products, two Origins foundations, a La Mer concealer and a *jane* foundation infringe its patent. Revlon is seeking, among other things, treble damages, punitive damages, equitable relief and attorneys' fees. The Company filed counterclaims, which, among other things, challenge the validity of the patent. Mediation directed by the Court took place in August 2001 and in January 2002, but did not result in resolution of the litigation. In January 2002, the Court indefinitely postponed the trial date (then set for February 2002) and established a schedule for pretrial motions. Both parties have filed summary judgment motions, and the Court is expected to schedule oral argument on the motions. The Company intends to defend the lawsuit vigorously. Although the final outcome cannot be predicted with certainty, based on legal analysis and the discovery proceedings in the litigation, management believes that the case will not have a material adverse effect on the Company's consolidated financial condition.

In February 2000, the Company and eight other manufacturers of cosmetics (the "Manufacturer Defendants") were added as defendants in a consolidated class action lawsuit that had been pending in the Superior Court of the State of California in Marin County. The plaintiffs purport to represent a class of all California residents who purchased prestige cosmetic products at retail for personal use from a number of department stores that sold such products in California (the "Department Store Defendants"). Plaintiffs filed their initial actions against the Department Store Defendants in May 1998. In May 2000, plaintiffs filed an amended complaint alleging that the Department Store Defendants and the Manufacturer Defendants conspired to fix and maintain retail prices and to limit the supply of prestige cosmetic products sold by the Department Store Defendants in violation of California state law. The plaintiffs are seeking, among other things, treble damages, equitable relief, attorneys' fees, interest and costs. Pre-trial proceedings and discovery have commenced. Court-directed mediation and related settlement discussions are continuing. The Company intends to defend the lawsuit vigorously. While no assurance can be given as to the ultimate outcome, based on preliminary investigation, management believes that the case will not have a material adverse effect on the Company's consolidated financial condition.

In 1998, the Office of the Attorney General of the State of New York (the "State") notified the Company and ten other entities that they are potentially responsible parties ("PRPs") with respect to the Blydenburgh landfill in Islip, New York. Each PRP may be jointly and severally liable for the costs of investigation and cleanup, which the State estimates to be $16 million. While the State has sued other PRPs in connection with the site, the State has not sued the Company. The Company and certain other PRPs are in discussions with the State regarding possible settlement of the matter. While no assurance can be given as to the ultimate outcome, management believes that the matter will not have a material adverse effect on the Company's consolidated financial condition.

In 1998, the State notified the Company and fifteen other entities that they are PRPs with respect to the Huntington/East Northport landfill. The cleanup costs are estimated at $20 million. No litigation has commenced. The Company and other PRPs are in discussions with the State regarding possible settlement of the matter. While no assurance can be given as to the ultimate outcome, management believes that the matter will not have a material adverse effect on the Company's consolidated financial condition.

The Company is involved in various routine legal proceedings incident to the ordinary course of its business. In management's opinion, the outcome of pending legal proceedings, separately and in the aggregate, will not have a material adverse effect on the Company's business or consolidated financial results.

NOTE 16 – NET UNREALIZED INVESTMENT GAINS

Under SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", available-for-sale securities are recorded at market value. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a component of stockholders' equity until realized. The Company's investments subject to the provisions of SFAS No. 115 are treated as available-for-sale and, accordingly, the applicable investments have been adjusted to market value with a corresponding adjustment, net of tax, to net unrealized investment gains in accumulated other comprehensive income. Included in accumulated other comprehensive income was an unrealized investment loss (net of deferred taxes) of $0.1 million at June 30, 2002 and an unrealized investment gain (net of deferred taxes) of $2.9 million at June 30, 2001.

NOTE 17 – STATEMENT OF CASH FLOWS

Supplemental disclosure of significant non-cash transactions

As a result of stock option exercises, the Company recorded tax benefits of $2.9 million, $7.2 million and $13.4 million during fiscal 2002, 2001 and 2000, respectively, which are included in additional paid-in capital in the accompanying consolidated financial statements.

NOTE 18 – SEGMENT DATA AND RELATED INFORMATION

Reportable operating segments, as defined by SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", include components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker (the "Chief Executive") in deciding how to allocate resources and in assessing performance. As a result of the similarities in the manufacturing, marketing and distribution processes for all of the Company's products, much of the information provided in the consolidated financial statements is similar to, or the same as, that reviewed on a regular basis by the Chief Executive. Although the Company operates in one business segment, beauty products, management also evaluates performance on a product category basis.

While the Company's results of operations are also reviewed on a consolidated basis, the Chief Executive reviews data segmented on a basis that facilitates comparison to industry statistics. Accordingly, net sales, depreciation and amortization, and operating income are available with respect to the manufacture and distribution of skin care, makeup, fragrance, hair care and other products. These product categories meet the Financial Accounting Standards Board's definition of operating segments and therefore, additional financial data are provided below. The "other" segment includes the sales and related results of ancillary products and services that do not fit the definition of skin care, makeup, fragrance and hair care.

The Company evaluates segment performance based upon operating income, which represents earnings before income taxes, minority interest and net interest income or expense. The accounting policies for each of the reportable segments are the same as those described in the summary of significant accounting policies, except for depreciation and amortization charges, which are allocated, primarily, based upon net sales. The assets and liabilities of the Company are managed centrally and are reported internally in the same manner as the consolidated financial statements, thus no additional information is produced for the Chief Executive or included herein.

YEAR ENDED OR AT JUNE 30	2002	2001	2000
(In millions)			
SEGMENT DATA			
Net Sales:			
Skin Care	**$1,703.3**	$1,660.7	$1,577.0
Makeup	**1,790.5**	1,721.6	1,603.5
Fragrance	**1,017.3**	1,085.1	1,117.2
Hair Care	**215.8**	180.7	113.9
Other	**23.0**	27.6	28.7
	4,749.9	4,675.7	4,440.3
Restructuring	**(6.2)**	(8.0)	–
	$4,743.7	$4,667.7	$4,440.3
Depreciation and Amortization:			
Skin Care	**$ 58.3**	$ 48.6	$ 39.4
Makeup	**60.0**	64.1	52.7
Fragrance	**36.0**	32.6	28.8
Hair Care	**6.5**	9.6	6.9
Other	**1.2**	1.4	1.3
	$ 162.0	$ 156.3	$ 129.1
Operating Income:			
Skin Care	**$ 248.4**	$ 266.9	$ 240.5
Makeup	**183.2**	212.5	181.8
Fragrance	**13.4**	63.6	80.6
Hair Care	**13.7**	13.1	12.4
Other	**0.1**	2.5	0.5
	458.8	558.6	515.8
Reconciliation:			
Restructuring and other non-recurring expenses	**(117.4)**	(63.0)	–
Interest expense, net	**(9.8)**	(12.3)	(17.1)
Earnings before Income Taxes, Minority Interest and Accounting Change	**$ 331.6**	$ 483.3	$ 498.7
GEOGRAPHIC DATA			
Net Sales:			
The Americas	**$2,878.2**	$2,857.8	$2,714.0
Europe, the Middle East & Africa	**1,261.1**	1,221.8	1,142.2
Asia/Pacific	**610.6**	596.1	584.1
	4,749.9	4,675.7	4,440.3
Restructuring	**(6.2)**	(8.0)	–
	$4,743.7	$4,667.7	$4,440.3
Operating Income:			
The Americas	**$ 222.9**	$ 299.9	$ 287.9
Europe, the Middle East & Africa	**179.9**	201.8	168.9
Asia/Pacific	**56.0**	56.9	59.0
	458.8	558.6	515.8
Restructuring and other non-recurring expenses	**(117.4)**	(63.0)	–
	$ 341.4	$ 495.6	$ 515.8
Total Assets:			
The Americas	**$2,467.1**	$2,379.9	$2,187.8
Europe, the Middle East & Africa	**703.3**	610.3	606.8
Asia/Pacific	**246.1**	228.6	248.7
	$3,416.5	$3,218.8	$3,043.3
Long-Lived Assets (property, plant and equipment):			
The Americas	**$ 458.4**	$ 445.2	$ 393.6
Europe, the Middle East & Africa	**99.6**	70.5	72.6
Asia/Pacific	**22.7**	13.0	14.1
	$ 580.7	$ 528.7	$ 480.3

NOTE 19 – UNAUDITED QUARTERLY FINANCIAL DATA

The following summarizes the unaudited quarterly operating results of the Company for the years ended June 30, 2002 and 2001:

	Quarter Ended				
	September 30	December 31	March 31	June 30	Total Year
(In millions, except per share data)					
Fiscal 2002					
Net sales	**$1,194.8**	**$1,298.2**	**$1,121.7**	**$1,129.0**	**$4,743.7**
Gross profit	**849.5**	**954.9**	**803.4**	**862.5**	**3,470.3**
Operating income (loss)	**152.9**	**143.5**	**81.1**	**(36.1)**	**341.4**
Net earnings (loss)	**97.1**[(a)]	**90.1**	**50.7**	**(25.4)**	**212.5**[(a)]
Basic EPS	**.30**[(a)]	**.35**	**.19**	**(.13)**	**.71**[(a)]
Diluted EPS	**.30**[(a)]	**.35**	**.19**	**(.13)**	**.70**[(a)]
Fiscal 2001					
Net sales	$1,185.0	$1,332.0	$1,103.5	$1,047.2	$4,667.7
Gross profit	835.4	993.0	805.8	807.1	3,441.3
Operating income	153.3	203.5	105.3	33.5	495.6
Net earnings	92.4[(b)]	127.3	65.1	20.4	305.2[(b)]
Basic EPS	.36[(b)]	.51	.25	.06	1.18[(b)]
Diluted EPS	.36[(b)]	.50	.24	.06	1.16[(b)]

(a) Net earnings for the Quarter ended September 30, 2001 include a one-time charge of $20.6 million or $.08 per common share, attributable to the cumulative effect of adopting SFAS No. 142, "Goodwill and Other Intangible Assets".

(b) Net earnings for the Quarter ended September 30, 2000 include a one-time charge of $2.2 million, after tax, or $.01 per common share, attributable to the cumulative effect of adopting SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities".

NOTE 20 – UNAUDITED SUBSEQUENT EVENT

Pursuant to the Company's authorized share repurchase program, subsequent to June 30, 2002, the Company purchased an additional 4.4 million shares of Class A Common Stock for $138.1 million, bringing the cumulative total of acquired shares to 7.0 million under this program.

The Board of Directors and Stockholders
The Estée Lauder Companies Inc.:

We have audited the accompanying consolidated balance sheet of The Estée Lauder Companies Inc. and subsidiaries as of June 30, 2002, and the related consolidated statements of earnings, stockholders' equity and comprehensive income and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 audit provides 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 The Estée Lauder Companies Inc. and subsidiaries as of June 30, 2002, and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2, the Company adopted Statement of Financial Accounting Standards ("Statement") No. 141, "Business Combinations", and Statement No. 142, "Goodwill and Other Intangible Assets", in the year ended June 30, 2002.

The consolidated balance sheet of The Estée Lauder Companies Inc. and subsidiaries as of June 30, 2001, and the related consolidated statements of earnings, stockholders' equity and comprehensive income, and cash flows for the years ended June 30, 2001 and 2000, were audited by other auditors who have ceased operations. As described in Note 2, these consolidated financial statements have been revised to include the transitional disclosures required by Statement No. 142, "Goodwill and Other Intangible Assets", which was adopted by the Company as of July 1, 2001. We performed the following audit procedures with respect to the disclosures in Note 2 with respect to 2001 and 2000. We (i) agreed the net income as previously reported and the adjustments to reported net income representing amortization expense (including any related tax effects) recognized in those periods related to goodwill that is no longer being amortized as a result of initially applying Statement No. 142 to the Company's underlying records obtained from management, and (ii) tested the mathematical accuracy of the reconciliation of adjusted net income to reported net income, and the related earnings per share amounts. In our opinion, the disclosures for 2001 and 2000 in Note 2 are appropriate. However, we were not engaged to audit, review, or apply any procedures to the 2001 and 2000 financial statements of the Company other than with respect to such disclosures and, accordingly, we do not express an opinion or any other form of assurance on the 2001 and 2000 consolidated financial statements taken as a whole.

KPMG LLP

New York, New York
August 9, 2002

To The Estée Lauder Companies Inc.:

We have audited the accompanying consolidated balance sheets of The Estée Lauder Companies Inc. (a Delaware corporation) and subsidiaries as of June 30, 2001 and 2000, and the related consolidated statements of earnings, stockholders' equity and comprehensive income and cash flows for each of the three years in the period ended June 30, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the 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 financial statements referred to above present fairly, in all material respects, the financial position of The Estée Lauder Companies Inc. and subsidiaries as of June 30, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2001 in conformity with accounting principles generally accepted in the United States.

New York, New York
August 10, 2001

This is a copy of the audit report previously issued by Arthur Andersen LLP in connection with the Company's filing on Form 10-K for the fiscal year ended June 30, 2001. This audit report has not been reissued by Arthur Andersen LLP.

Company Headquarters
The Estée Lauder Companies Inc.
767 Fifth Avenue, New York, New York 10153
212-572-4200

Stockholder Information
Stockholders may access Company information, including a summary of the latest financial results, 24 hours a day, by dialing our toll-free information line, 800-308-2334. News releases issued in the last 12 months are available on the World Wide Web at www.elcompanies.com.

Investor Inquiries
We welcome inquiries from investors, securities analysts and other members of the professional financial community. Please contact the Investor Relations Department in writing at the Company's headquarters or by telephone at 212-572-4384.

Form 10-K Annual Report
If you would like a copy of the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, please call the toll-free information line, 800-308-2334, or write to the Investor Relations Department at the Company's headquarters.

Common Stock Information
The Class A Common Stock of The Estée Lauder Companies Inc. is listed on the New York Stock Exchange with the symbol EL.

Quarterly Per Share Market Prices and Cash Dividends on Common Stock

Fiscal 2002	Market Price of Common Stock			Cash
Quarter Ended	High	Low	Close	Dividends
September 30	$43.55	$30.30	$33.15	$.05
December 31	34.90	29.25	32.06	.05
March 31	35.75	29.25	34.16	.05
June 30	38.80	33.50	35.20	.05

Annual Meeting
The Company's Annual Meeting of Stockholders will be held on Wednesday, October 30, 2002, at 10:00 a.m. at:
The St. Regis
Two East 55th Street
New York, New York 10022

Attendance at the Annual Meeting will require an admission ticket.

Change in Dividend Payment
Beginning in fiscal 2003, dividends on the common stock are expected to be paid annually in January, following declaration by the Board of Directors.

Stockholder Services
Mellon Investor Services is the Company's transfer agent and registrar. Please contact Mellon directly with all inquiries and requests to:

- Change the name, address or ownership of stock;
- Replace lost certificates or dividend checks;
- Obtain information about dividend reinvestment, direct stock purchase or direct deposit of dividends.

Mellon Investor Services LLC
P.O. Box 3315
South Hackensack, New Jersey 07606
888-860-6295
www.melloninvestor.com

Trademarks
The Estée Lauder Companies Inc. and its subsidiaries own numerous trademarks. Those appearing in the text of this report include: 154, 3-Step Skin Care System, A Perfect World White Tea Skin Guardian, Active White, Advanced Night Repair, Age Rescue, All Over Shimmer, Aramis, Aromatics Elixir, Aveda, Aveda Love, Be Curly, Beautiful, Bobbi Brown, Bobbi Brown Beach, Bobbi Brown Extra, Bumble and bumble, Calyx, Cheekhue, Clear Head, Clinique, Clinique Happy, Clinique Sun Care, Color Conserve, Color Support, Convertible Eye Color, Crème de la Mer, Deeep Treatment, Does It All, Dramatically Different Moisturizing Lotion, Energizing Body Tonic, Estée Lauder, Estée Lauder *pleasures*, Stila Eye Glaze, Eye Rescue, Fabulizer for Eyes, Fabulizer for Lips, False Eyelashes, Full Spectrum Deposit Only Color Treatment, Gentle Light, Ginger Souffle Whipped Body Cream, Ginger Up, Hang Straight, Have a Nice Day, Iced Shadow, Idealist, Illuminating Liquid Foundation, Illuminating Powder Foundation, Illusionist, Incredible Lipcolor, Intuition, Intuition for Men, Intuition Fragrance Silk, *jane*, Jo Malone, Juniper Skin Tonic, Knot Free, La Mer, Lab Series for Men, Stila Lip Glaze, Lipglass, Long Pretty Lashes, M·A·C, MegaBites, Moisture Sheer, Moisture Surge, Origins, Paints, Peace of Mind Sensory Therapy Collection, Pivotal Skin, Prescriptives, Pro-Lash, Pure-Fume, Re-Nutriv, Resilience Lift, Rosemary Mint Body Care, Salt Rub, Shampure, Silk Screen, So Ingenious, Stay True, Stay Tuned Balancing Face Makeup, Stila, Studio Fix, Studio Tech, Sumotech, Super Line Preventor, Surf Spray, Surface, The Face Serum, Total Turnaround, Traceless, Trifecta, Underwear for Lids, Underwear for Lips, Viva Glam IV, White Linen, Whitening Lab Formula Essence.

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THE ESTĒE LAUDER COMPANIES INC.
767 FIFTH AVENUE NEW YORK, NEW YORK 10153