

Letter to Shareholders

Corporate Profile

Altera Corporation, The Programmable Solutions Company®, is a world leader in programmable logic devices (PLDs). Altera® PLDs are standard integrated circuits that allow customers to program and personalize the application of the chip to provide market differentiation. Altera serves over 14,000 customers in four primary market segments: communications, industrial, consumer, and computer and storage.

The year 2007 was unexpectedly challenging for the programmable logic industry as weak demand from our communications customers and in parts of our industrial markets led to annual revenue declines. Even though Altera experienced a two percent decline in revenue, we gained market share, and our profitability remains the best in the programmable logic industry. Our new products, 32 percent of sales, up 65 percent from the previous year, produced faster and larger new product growth than any of our competitors. Sales in 2007 were \$1.26 billion and generated net income of \$290 million, \$0.82 per diluted share.

We focused on three inter-related core tasks during the year—growth, cost structure, and capital structure—to enable Altera to deliver increasing shareholder value in the years ahead. Our goal is for Altera to achieve 10 to 15 percent compounded top-line growth, with operating margin in the low 30 percent of sales range, and return on equity above 30 percent.

Innovative New Products to Sustain Growth

Competitively strong and innovative new products are the engine that will drive our revenue growth. During the past five years we have grown revenue at a 12 percent compound growth rate, the fastest in our industry. In the future, growing at a 10 to 15 percent compounded annual pace will most likely place us among the highest growth companies in the semiconductor industry.

The ability to drive our technology to intersect critical customer needs has been the central element in growing our revenue faster than the programmable device industry. We have nurtured a much deeper relationship with our customers over the past several years, and our insights about their needs have grown dramatically. One of the insights we gained was an understanding that reducing the power consumption of our devices would open up more growth opportunities for us.

Financial Highlights

Five years ended December 28, 2007
(In thousands, except per share amounts)

	2007	2006	2005*	2004*	2003*
Net sales	\$ 1,263,548	\$ 1,285,535	\$ 1,123,739	\$ 1,016,364	\$ 827,207
Income from operations	274,953	301,075	322,167	312,762	189,839
Net income	290,023	323,236	278,829	276,075	152,209
Diluted net income per share	0.82	0.88	0.74	0.72	0.39
Cash and investments	1,021,379	1,620,310	1,282,553	1,203,248	1,046,341
Stockholders' equity	861,450	1,608,161	1,259,588	1,274,003	1,094,227

*Excluding stock-based compensation charges

This knowledge led to a change in our products so that we could deliver solutions that help customers more easily meet ever-tighter power budgets. In 2007 we began shipping our 65-nanometer Stratix® III devices, with our unique Programmable Power Technology, offering the best performance and the highest density among high-density field-programmable gate arrays (FPGAs)—plus 50 percent lower power consumption than the previous generation. Our 65-nanometer Cyclone® III FPGAs also began shipping with an improved low-power logic fabric that strengthens our appeal across more low-cost high-volume applications. Building on the very successful MAX® II complex programmable logic device (CPLD) family, we also delivered zero-power MAX IIZ CPLDs in 2007, giving us a new way to capture more of the portable device market.

Cost Structure and Efficiency

In 2007, we took substantial steps to harness the ingenuity that has generated the industry's best growth rate and apply that tradition of innovation to reduce our cost structure. Our 2007 net income, at 23 percent of sales, and 21 percent return on equity, continues to be the best in our industry. We believe we can do better. The work underway is transforming not just our cost structure, but how we manage the company to improve our speed, efficiency, and competitiveness. We aim to maintain our 65 percent gross margin goal, but we want to drive research and development spending to 18 percent of sales and SG&A spending to 15 percent of sales, from 2007 spending of 21 percent and 22 percent respectively. As we achieve these goals, with the industry's best gross margin, the resulting operating leverage will significantly improve our profitability—moving us steadily to our 30 percent plus operating margin goal. We are already seeing progress. In 2007, we successfully reduced operating expense levels below 2006 despite increasing the research and development investments we made to keep our future revenues growing. We expect that the absolute dollar level of operating expenses in 2008 will be even lower. By the end of 2008, we should show meaningful progress against these increased efficiency goals and our drive for 30 percent plus operating income.

Effective Capital Structure

Successful new products and an efficient, quick-moving organization are essential to creating competitive strength. We recognize that when that strength is coupled with an appropriate capital structure, we have the best opportunity to optimize value generation for shareholders. In 2007, we took some significant steps to readjust Altera's capital structure. We repurchased 58.0 million shares in 2007 at a cost of \$1.2 billion as part of our plan to repurchase \$1.5 billion of our shares, which we anticipate we will complete ahead of our original mid-2008 target. These repurchases were partially supported by a new long-term credit facility that will fund approximately one-third of our plan. Even after these repurchases, our balance sheet remains strong with a \$771 million net cash position at year end. In March, we initiated the first stock dividend in the company's history as an additional way to return cash to shareholders.

Even though our asset-light business model generates healthy cash flows, we also have increased our focus on this key business metric. Beyond the cash flow improvements from operating expense efficiencies, this sharper focus is also propelling additional process improvement for cost of goods and inventory management.

Taken together, the steps we took in 2007 lead us to expect more than 30 percent return on equity in 2008, without compromising our growth aspirations.

These three themes—introducing innovative new products, developing an efficient cost structure, and creating an effective capital structure—will remain our focus in the coming years. We have made great progress this year across all these dimensions of our business. We believe this work sets the stage for more gains in the future, and creates a solid opportunity for us to create additional value for our shareholders in the years ahead.



John P. Daane
Chairman, President, and Chief Executive Officer

This letter contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are based upon information available to us at the date of this letter and include any projection of revenue, operating income, return on equity, gross margin, expense or other financial items, and our beliefs concerning expansion opportunities for our products, development of an efficient cost structure and creation of an appropriate capital structure. Readers are cautioned that all forward-looking statements in this letter involve risks and uncertainty that can cause actual results to differ from those currently anticipated, due to a number of factors, including without limitation, customer business environment, vertical market mix, market acceptance of the company's products, product introduction schedules, the rate of growth of the company's new products and changes in the mix of our business between prototyping and production-based demand, as well as changes in economic conditions and other risk factors discussed in Item 1A: Risk Factors of our Annual Report on Form 10-K as well as other documents filed by Altera with the Securities and Exchange Commission from time to time. Copies of Altera's SEC filings are posted on the company's website and are available from Altera without charge. Except as required by law, Altera does not undertake an obligation to update its forward-looking statements to reflect future events or circumstances.