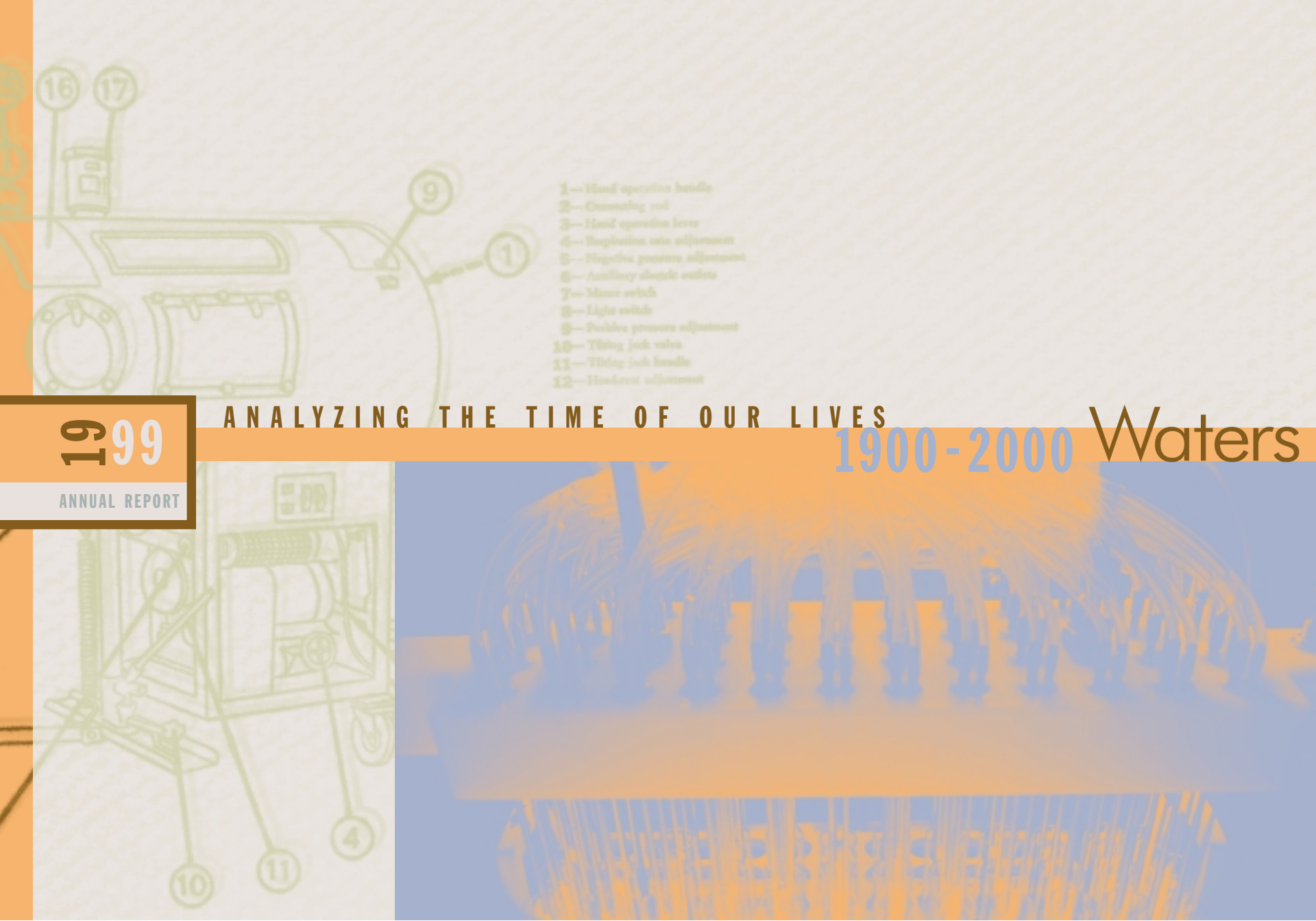

1999
ANNUAL REPORT
ANALYZING THE TIME OF OUR LIVES
1900-2000
Waters

FINANCIAL HIGHLIGHTS
ADJUSTED FINANCIAL RESULTS (A):

	1999	1998	INCREASE
($ in thousands, except per share data)			

Waters Corporation (NYSE: WAT) is the world's leading supplier of high-performance liquid chromatography (HPLC) instrumentation and consumables, as well as thermal analysis and mass spectrometry (MS) products. Around the world, Waters® products are used by pharmaceutical, life science, industrial, university and government scientists in research and development, quality assurance and in environmental testing laboratories. For these customers, we provide technology that gives them fundamental data on chemical mixtures and materials. Then, by turning these analytical data into useful information, we help scientists understand the complexities of chemistry and of life itself.

FOR THE YEAR:	NET SALES	OPERATING INCOME	PERCENTAGE OF SALES	INCOME FROM OPERATIONS BEFORE INCOME TAXES	NET INCOME AVAILABLE TO COMMON STOCKHOLDERS	NET INCOME PER BASIC COMMON SHARE	NET INCOME PER DILUTED COMMON SHARE	RETURN ON AVERAGE ASSETS	RETURN ON AVERAGE EQUITY	AT YEAR END: TOTAL ASSETS	STOCKHOLDERS' EQUITY	EMPLOYEES
	$704,400	$176,509	25.1%	$167,561	$121,876	$1.98	$1.84	21.0%	55.1%	$584,437	$292,162	2,968
	$618,813	$136,325	22.0%	$118,047	$89,936	$1.50	$1.39	15.9%	84.7%	$577,701	$150,119	2,758
	+14%	+29%		+42%	+36%	+32%	+32%					

(A) Adjusted financial results for 1998 reflect reported results of operations excluding a $16,500 nonrecurring charge related to the September 1997 acquisition of Micromass Limited for revaluation of acquired inventory which had no related tax effect. All per share amounts have been retroactively restated to reflect a two-for-one common stock split distributed in the form of a 100% stock dividend on June 10, 1999.

PHARMACEUTICAL AND BIOTECHNOLOGY CUSTOMER DEMAND HAS BEEN OUR STRONGEST SOURCE OF GROWTH.

DEMAND FROM CUSTOMERS IN THE PROTEOMICS RESEARCH SEGMENT OF THE LIFE SCIENCES MARKET GREW RAPIDLY AS 1999 PROGRESSED.

KEY TO OUR GROWTH IS A RECORD NUMBER OF NEW PRODUCTS.

1999 LETTER TO SHAREHOLDERS

The past year was a notable one. The business and market factors that have driven the Company's growth over the last several years continued to build momentum, while at the same time, several new exciting initiatives took center stage.

Pharmaceutical and biotechnology customer demand has been our strongest source of growth. These companies continue to invest heavily in technologies that increase the number of compounds being synthesized and screened for early stage drug discovery, and that accelerate promising compounds through the drug development phase. Waters products and service offerings help increase productivity at these companies, and appeal to their almost insatiable demand for increased detection sensitivity and higher throughput. The combination of our recently introduced HPLC systems — the Alliance® HT and the CapLC™ — and our market-leading Micromass® mass spectrometry systems — the Quattro Ultima,™ the LCT™ with MUX Technology™ and the Q-TOF™ — have fulfilled customer needs and generated significant revenues.

Demand from customers in the proteomics research segment of the life sciences market grew rapidly as 1999 progressed. In proteomics, scientists study the protein content of cells, typically in the search for new drug targets. In 1999, we partnered with Bio-Rad Laboratories, a well-known life science company, to introduce an integrated proteomics workstation and analysis system, anchored by our industry-leading Q-TOF mass spectrometer. We believe that the life science industry is in the early stages of investing in proteomics research, and we are in the process of bringing to market more high-value products to this important emerging area.

The key to our growth has been our rich pipeline of new products, and the year 2000 is shaping up as yet another stellar new product year. We plan major introductions and enhancements to our HPLC and HPLC-MS product lines that should continue our strong leadership positions. In the fast-moving mass spectrometry field, the number of major new product launches planned for 2000 is evidence of our innovative capacity and our ability to rapidly commercialize these innovations.

IN 1999, SALES GREW 14%, EARNINGS PER SHARE GREW 32% AND FREE CASH FLOW REACHED A RECORD $127 MILLION.

The combination of fast-growing markets, innovative products and a dedication to operational excellence has resulted in the company's industry-leading financial performance. In 1999, sales grew 14%, earnings per share grew 32% and free cash flow reached a record $127 million. Our strong financial performance gives us the flexibility to pursue growth aggressively.

I want to thank our customers and our employees across our business units — Waters, TA Instruments and Micromass — for their dedicated efforts and contributions to our success.

As we survey the field of new opportunities before us — evolving customer needs in high-throughput combinatorial chemistry for drug discovery, the impact of proteomics on understanding disease causation and the much anticipated contribution of genomics on drug development and personalized medicine — we are confident that Waters is in an extraordinary position to apply our technologies and continue to produce outstanding business performance.

Douglas Berthiaume

DOUGLAS A. BERTHIAUME
Chairman, President and Chief Executive Officer

FIRST SUCCESSFUL KIDNEY TRANSPLANT USHERS IN A NEW ERA OF HUMAN ORGAN TRANSPLANTATION.

DISCOVERING NEW WAYS TO MAKE DISEASE HISTORY.

1929

ALEXANDER FLEMING DISCOVERS THE BACTERIA-KILLING PROPERTIES OF *PENICILLIN NOTATUM*, PAVING THE WAY FOR FUTURE EXPERIMENTATION THAT LEADS TO THE INTRODUCTION OF PENICILLIN.

1938

THE U.S. FOOD, DRUG, AND COSMETIC ACT REPLACES THE 1906 FOOD AND DRUGS ACT, CREATING THE U.S. FOOD AND DRUG ADMINISTRATION (FDA).

1953

JONAS SALK REFINES THE POLIO VACCINE AND SUCCESSFULLY TESTS IT ON HUMANS FOR THE FIRST TIME.

1954

International Conference on Harmonization begins the task of "harmonizing" the technical requirements for registering pharmaceutical products among the European Union, Japan and the U.S.

1988

U.S. Surgeon General C. Everett Koop releases *The Surgeon General's Report on Nutrition and Health*, the federal government's first formal recognition of the role of diet in certain chronic diseases.

1990's

Thanks to cholesterol-lowering statin drugs, high blood pressure, heart failure, irregular heartbeats and heart attacks all become treatable conditions.

1991

today

The pharmaceutical industry has never held more promise than it does today. Every day, discoveries are made leading to the development of new lifesaving drugs. Waters products play a critical role in a broad range of processes throughout drug discovery, development and manufacturing. Our industry-leading high performance liquid chromatography (HPLC), mass spectrometry (MS) and separation chemistry products are helping researchers break substances down to their most fundamental, molecular level, and test them for safety and effectiveness more efficiently than ever before. Our chromatography software allows researchers to work more efficiently with their data, build better audit trails and keep ahead of the curve by maintaining compliance with the newest FDA regulations. As a result, our products help pharmaceutical companies close the gap between the development of lifesaving drugs for diseases like cancer and AIDS, and the availability of those drugs to the people who need them most.

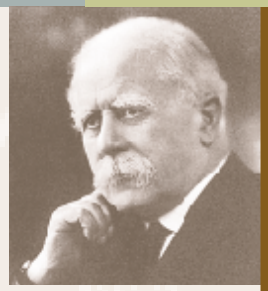
tomorrow

Over the next five years, drugs accounting for $60 billion in annual sales will come off patent. And pharmaceutical companies are racing to create new drugs to replace old ones. Our products assist drug companies in determining which of the thousands of compounds they generate using medicinal and combinatorial chemistry show the most promise of becoming a new drug. In fact, we're the leading supplier of HPLC and MS tools to the rapidly growing $335 billion pharmaceutical market. These tools are far and away the most prevalent techniques found in the pharmaceutical laboratory. In 1999, we launched several new products for pre-clinical, drug discovery purposes. These new HPLC, MS and separation chemistry products are all redefining automated high-throughput drug analysis, shattering traditional HPLC/MS boundaries. And as the demand for powerful new drugs increases – pharmaceutical research and development spending is forecasted to double by the year 2005 – the need for our products will, too.

SEARCHING FOR THE SECRET OF LIFE.

1909

Archibald Garrod first proposes that genes might be involved in creating the proteins that carry out the chemical reactions of metabolism.



1924

Microscope studies of DNA and protein show that both substances are present in chromosomes.

1953

James Watson and Francis Crick decipher the structure of DNA, the molecule that carries the genetic code.

1973

Herbert Boyer and Stanley Cohen pioneer recombinant DNA technology, ushering in the modern biotechnology era.

1982

Genentech licenses the marketing rights to the first recombinant protein – human insulin – to Eli Lilly and Co.

The International Human Genome Project is initiated in an attempt to identify the estimated 100,000 genes in human DNA.

1983

Kary Mullis conceives of the polymerase chain reaction (PCR), enabling DNA fingerprinting, genetic disease diagnosis and detection of bacteria and viruses (particularly the AIDS virus).

1990

W. French Anderson performs the first gene therapy on a human patient in an effort to repair a faulty immune system.

today

Fundamental advances are being made in understanding the relationship between human genes, the proteins they encode and their impact on disease. Key to this understanding is the use of sophisticated HPLC/MS instruments and software available exclusively through the Micromass division of Waters. Today, Waters technologies allow researchers to fully characterize biomolecules that are present in inconceivably small quantities. As a result, drugs can be developed that target the cause rather than the symptom of disease. And thanks to our global distribution network, scientists can quickly and efficiently access all of the critical instrumentation and software they require to expedite their research.

tomorrow

In 1990, a group of talented scientists initiated the International Human Genome Project, a plan to sequence the estimated 100,000 genes in human DNA. If successful, this project could identify 25,000 or more new targets for disease analysis. A subsequent mammoth undertaking will attempt to determine the relationship between the DNA sequence, the proteins they produce and what role those proteins play in human health. Known as "proteomics," this new field of scientific endeavor will call for the most advanced automated mass spectrometry systems. And Waters will be the company to deliver those technologies. Our HPLC/MS systems will be instrumental in helping scientists push the boundaries of proteomic research and will set new performance standards in the painstaking process of finding cures for gene-related diseases.

LEADING LONGER, MORE FULFILLING LIVES.

1900

Felix Hoffman formulates acetylsalicylic acid, which Bayer Corporation later markets under the name Aspirin®.

1912

Frederick Hopkins and Casimir Funk advance the vitamin hypothesis of deficiency, postulating that the absence of sufficient amounts of a vitamin may lead to certain diseases.

1945

Synthetic drugs known as antihistamines are introduced to combat common allergies.

Grand Rapids, Michigan, becomes the first city to fluoridate its drinking water to ward off dental caries.

1960

G.D. Searle and Company introduces the first oral contraceptive, Enovid®, dramatically altering the future lives of women and the family.

Pfizer Inc. introduces Viagra®, spotlighting the popularity of lifestyle drugs.

1970

Linus Pauling publishes "Vitamin C and The Common Cold," single-handedly making vitamin C the world's favorite dietary supplement.

1997

today

In 1900, life expectancy in the United States was 48 years. Today it is 76. Thanks to discoveries made in health and nutrition, researchers are empowering people to make informed dietary and lifestyle decisions that greatly improve their quality of life. Today, effective treatments for conditions like hair loss, allergies, and physical dysfunction are fueling greater demand for lifestyle drugs. And as nutraceuticals like Ginseng Root, Melatonin and St. John's Wort gain in popularity, so too, do our products. They provide both the pharmaceutical and nutraceutical companies with the tools they need to develop, test and deliver high-quality supplements.

tomorrow

In the U.S., the functional foods market is expected to multiply three times over the next ten years, from an estimated $20 billion industry to a $60 billion industry in 2010. Because natural products are highly complex, understanding their chemical nature requires sophisticated HPLC/MS tools. And as more people turn to dietary supplements, the industry invokes the scrutiny of the FDA. The companies that can prove their products are pure, contain consistent levels of active ingredients and can prove efficacy to an increasingly discerning consumer are the companies that will succeed. That means future opportunity for our analytical instrumentation within the lifestyle industry is strong. As government agencies and pharmaceutical companies keep working together to find better ways to help people lead longer, quality lives, our products will continue to push the limits of research farther.

Rachel Carson's book "Silent Spring" inaugurates the worldwide environmental movement, showing how industrial chemical contamination harms the environment.

DEVELOPING A HEALTHIER CLIMATE FOR THE NEXT GENERATION.

1916

The U.S. National Park Service is founded to protect the bio-diversity of large tracts of wilderness.

1935

The Wilderness Society is founded to develop a nationwide network of wild lands through public education, scientific analysis and advocacy.

1962

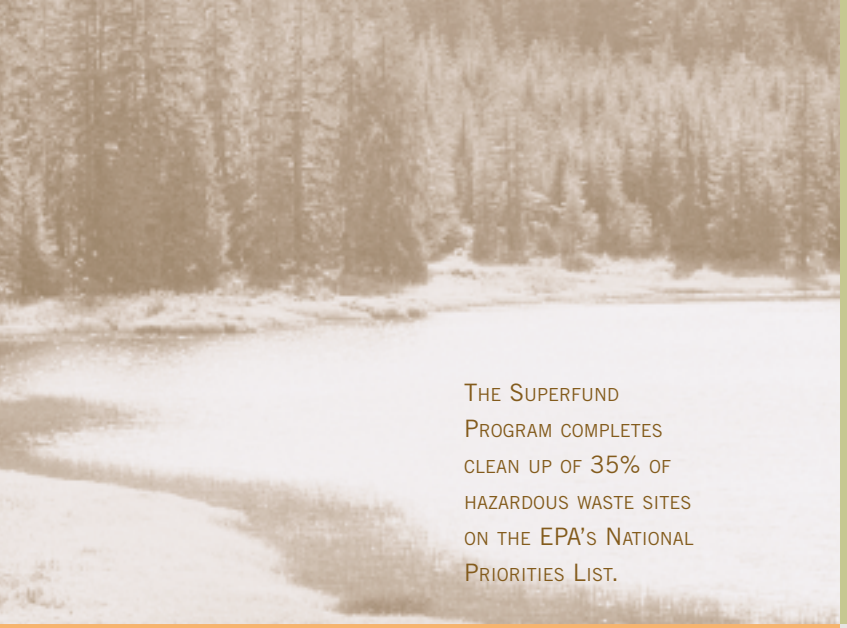
1970

Earth Day is celebrated for the first time.

The U.S. Environmental Protection Agency (EPA) is created in response to confusing and ineffective state and municipal environmental protection laws.

1980

Comprehensive Environmental Response, Compensation, and Liability Act is passed, establishing the Superfund Program to clean up contaminated sites collectively dubbed the National Priorities List.



The Superfund Program completes clean up of 35% of hazardous waste sites on the EPA's National Priorities List.

today

Waters products are helping people everywhere to breathe a little easier. Even before the worldwide environmental movement gained momentum in the early '60s, Waters maintained a dual commitment, both internally and externally, to the environment. Today, reports of dangerously high pesticide levels found in fruits, vegetables and drinking water have created a demand for stricter regulations regarding pesticide use. Our HPLC and MS products ensure that pesticide levels in water, soil and food are within safe limits. Our MS sytems are the instruments of choice for ultra low-level, trace dioxin analysis, a process that is being given special attention, especially in Japan. In addition, they are favored by numerous government agencies investigating the relationships between suspected contaminants and adverse health effects in birds, fish and mammals.

1992

Framework Convention on Climate Change in Rio De Janeiro, Brazil, commits signatories to reduce levels of greenhouse gases.

1997

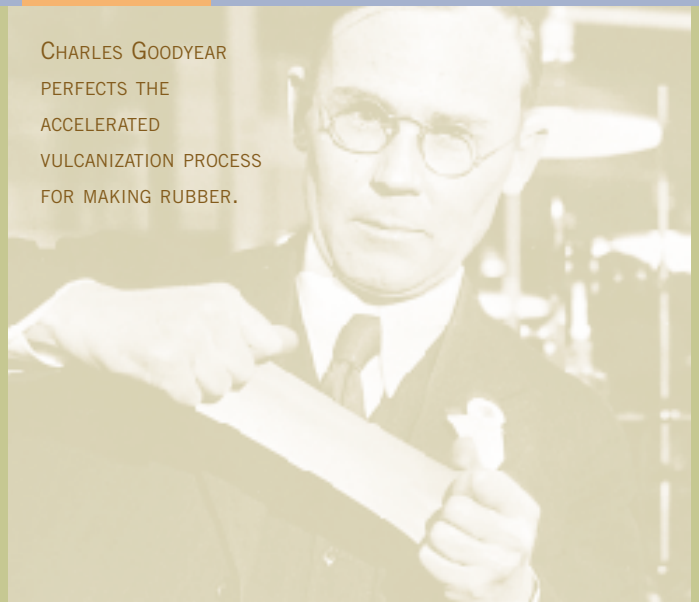
tomorrow

World economic growth brings with it challenges to control pollution in our air, water and soil. Our products are being used around the world by countries and companies that have made point-of-source monitoring, prevention, recycling and waste reduction not only a priority, but a mandate. Recently, the EPA launched the Endocrine Disruptor Research Initiative. This initiative will investigate the hypothesis that there are chemicals present in our environment causing adverse health effects by interacting with the human endocrine system. Understanding the molecular make-up of these compounds, where they exist, how they bind to cells and what happens when they do is significant. And all of our HPLC and MS products will be tools used to aid in these discovery processes.

REFINING THE NATURE OF THINGS.

1907

Charles Goodyear perfects the accelerated vulcanization process for making rubber.



1909

Leo Baekeland invents Bakelite,® the first thermosetting plastic that doesn't soften when heated.

1935

Wallace Carothers invents nylon and polyester.

1940

DuPont introduces nylon stockings, selling five million pairs in one day to a riotous public.

1979

Total volume production of plastics surpasses that of steel in the U.S.

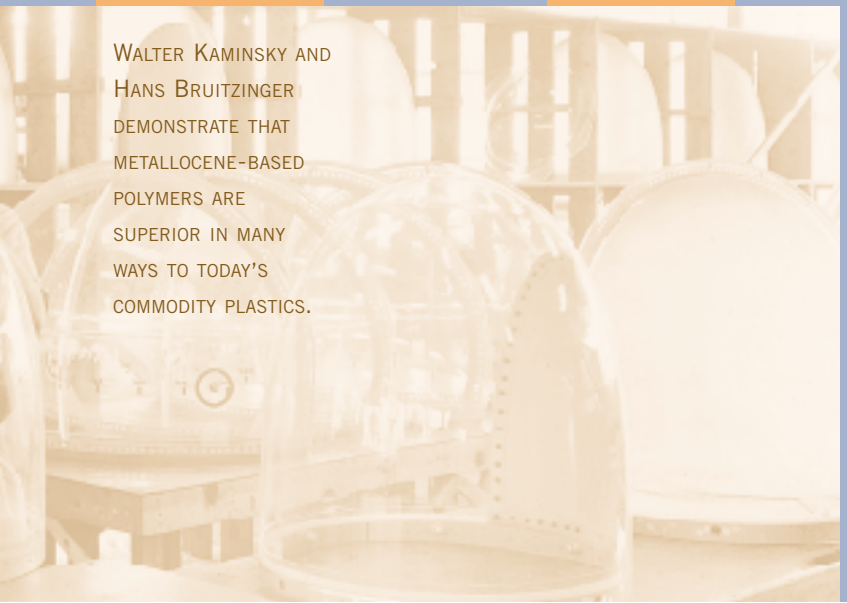
Dr. William DeVries sustains Barney Clark for 112 days with the first artificial heart made of polyurethane and Dacron® polyester fiber mesh.

today

Researchers are forever discovering new and innovative ways to expand the role polymers play in our lives. From the most mundane plastic product, to multi-layered engineered materials, researchers rely on Waters thermal analysis and gel permeation chromatography products to help them design and develop stronger and better performing materials, constituting the basis for a myriad of innovative products. And these advances will grow more frequent in the year 2000, with our launch of the most advanced gel permeation chromatography system ever created. This remarkable instrument's performance characteristics are unavailable in competitive products, providing just what polymer scientists need to develop tomorrow's advanced materials.

1980's

1982



Walter Kaminsky and Hans Bruitzinger demonstrate that metallocene-based polymers are superior in many ways to today's commodity plastics.

tomorrow

Tomorrow will be the age of micro-thermal analysis, a process combining the capabilities of thermal analysis with atomic force microscopy. As scientists and astronauts venture farther into space and surgeons venture farther into the realm of artificial organ transplants, micro-thermal analysis will analyze the polymer-based materials used in these mission-critical applications. Combinatorial synthesis techniques will become more practical as a means of combining synthetic molecules into new and useful classes of polymers, many of which will only lend themselves to high temperature analysis. And the most capable instrumentation available for next generation room-to-high temperature polymer analysis is our Alliance® GPC 2000. So you can expect to see it being used for everything from testing various space shuttle materials to artificial heart valves.

DOUGLAS A. BERTHIAUME
Chairman, President and Chief Executive Officer

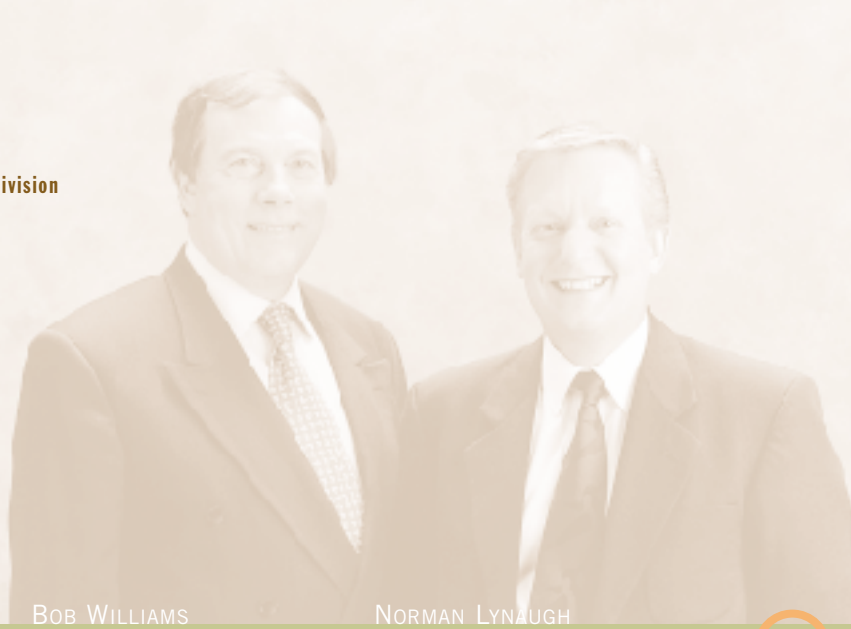
PHILIP S. TAYMOR
Senior Vice President and Chief Financial Officer

1999 COMPANY OFFICERS

JOHN ORNELL
Vice President, Operations

JOHN R. NELSON
Senior Vice President, Research, Development and Engineering

DEVETTE W. RUSSO
Vice President, Chromatography Consumables Division



BOB WILLIAMS
Chairman, Micromass, Limited

NORMAN LYNAUGH
Managing Director, Micromass, Limited

ARTHUR G. CAPUTO
Senior Vice President, Worldwide Sales and Marketing

THOMAS W. FELLER
Senior Vice President, E-Business Initiative

BRIAN K. MAZAR
Vice President, Human Resources and Investor Relations

FORWARD THINKING

Time marches on. And it's clear that, at Waters, our ingenuity does too. Today, we're looking forward to our role in the adventure called "Tomorrow," and to strengthening and solidifying our position as the leading supplier of value-added solutions to the industries we serve. And yet, that focus represents only part of our commitment to the analytical instrumentation industry as a whole. We take special pride in providing our customers with industry-leading, global service and support programs and instrumentation training. Doing so reinforces the value we bring to our customer, our industry and to you, our investors. By using our time wisely and bringing the best minds, products and services together today, we're accelerating the discovery of the best solutions for tomorrow's toughest problems.

FINANCIAL

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

Waters Corporation ("Waters" or the "Company"), an analytical instrument manufacturer, is the world's largest manufacturer and distributor of high performance liquid chromatography ("HPLC") instruments, columns and other consumables, and related service. The Company has the largest HPLC market share in the United States, Europe and non-Japan Asia and has a leading position in Japan. HPLC, the largest product segment of the analytical instrument market, is utilized in a broad range of industries to detect, identify, monitor and measure the chemical, physical and biological composition of materials, and to purify a full range of compounds. Through its Micromass Limited ("Micromass") subsidiary, the Company is a market leader in the development, manufacture and distribution of mass spectrometry ("MS") instruments, which are complementary products that can be integrated and used along with other analytical instruments, especially HPLC. Through its TA Instruments, Inc. ("TAI") subsidiary, the Company is also the world's leader in thermal analysis, a prevalent and complementary technique used in the analysis of polymers.

Sales grew by 14% in 1999 and by 33% in 1998. Sales growth in both years reflected increased customer demand for new products and in 1998 was augmented by the effect of 1997 acquisitions. Operating income for the year ended December 31, 1999 was $176.5 million, a 29% increase over the $136.3 million generated in 1998, excluding a $16.5 million nonrecurring charge in 1998 for revaluation of acquired inventory related to the purchase of Micromass. Earnings per diluted common share were $1.84 in 1999, a 32% increase over the $1.39 in 1998 excluding the nonrecurring charge.

During 1999, approximately 59% of the Company's combined net sales were derived from operations outside the United States. The Company believes that the geographic diversity of its sales reduces its dependence on any particular region. The U.S. dollar value of these revenues varies with currency exchange fluctuations, and such fluctuations can affect the Company's results from period to period.

YEAR ENDED DECEMBER 31, 1999 COMPARED TO YEAR ENDED DECEMBER 31, 1998

net sales

Net sales for 1999 were $704.4 million, compared to $618.8 million for the year ended December 31, 1998, an increase of 14%. The impact of currency on 1999 net sales compared to 1998 net sales was negligible. Demand growth was strongest for our mass spectrometry product family, in particular, time-of-flight mass spectrometry products for protein analysis and high-throughput drug discovery. Pharmaceutical customer demand was particularly strong and generally was broad based across all geographies.

gross profit

Gross profit for 1999 was $447.3 million, compared to $369.8 million for 1998, an increase of $77.5 million or 21%. Excluding the $16.5 million nonrecurring charge for revaluation of acquired inventory in 1998 related to purchase accounting for the 1997 Micromass acquisition, gross profit increased by 16% in 1999.

Gross profit as a percentage of sales excluding the inventory revaluation charge increased to 63.5% in 1999 from 62.4% in 1998, primarily as a result of increased efficiencies in the Company's manufacturing operations and lower raw material costs.

selling, general and administrative expenses

Selling, general and administrative expenses for 1999 were $226.6 million, compared to $206.2 million for 1998. As a percentage of net sales, selling, general and administrative expenses decreased to 32.2% for 1999 from 33.3% for 1998 as a result of higher sales volume and expense controls. The $20.4 million or 10% increase in total expenditures primarily resulted from increased headcount required to support increased sales levels.

research and development expenses

Research and development expenses were $36.1 million for 1999 compared to $34.4 million for 1998, a $1.7 million or 5% increase from prior year levels. The Company continued to invest significantly in the development of new and improved HPLC, thermal analysis, rheology and mass spectrometry products.

goodwill and purchased technology amortization

Goodwill and purchased technology amortization for 1999 was $8.1 million, compared to $9.4 million for 1998, a decrease of $1.3 million or 14%. Expense decreased as a portion of purchased technology reached full amortization during the year.

operating income

Operating income for 1999 was $176.5 million, an increase of $56.7 million or 47% from the prior year. Excluding the $16.5 million nonrecurring charge for revaluation of acquired inventory, operating income was $136.3 million for the year ended December 31, 1998, and 1999 results represented a $40.2 million or 29% increase over 1998. Waters improved operating income levels on the strength of sales growth, volume leverage and continued focus on cost controls in all operating areas.

interest expense, net

Net interest expense decreased by $9.3 million, or 51%, from $18.3 million in 1998 to $9.0 million in 1999. The current year decrease primarily reflected lower average debt levels as a result of repayments from the Company's cash flow.

provision for income taxes

The Company's effective income tax rate was 27% in 1999 and 23% in 1998, excluding the nonrecurring nondeductible charge related to the revaluation of acquired inventory. The 1999 tax rate increased primarily because a majority of the net operating loss carryforwards were utilized in 1998.

income from operations

Income from operations for 1999 was $122.3 million, compared to $74.4 million for 1998, an increase of $47.9 million or 64%. Excluding the nonrecurring acquisition related charge in 1998, the Company increased its $90.9 million of income in 1998 to $122.3 million in 1999. The improvement over the prior year was a result of sales growth, productivity improvement in all operating areas and a decline in interest expense, offset by the impact of an increase in the Company's effective income tax rate.

YEAR ENDED DECEMBER 31, 1998 COMPARED TO YEAR ENDED DECEMBER 31, 1997

net sales

Net sales for 1998 were $618.8 million, compared to $465.5 million for the year ended December 31, 1997, an increase of 33%. Excluding the adverse effects of a stronger U.S. dollar, net sales increased by 35% in 1998. The Company's core HPLC and thermal analysis products grew by 12%, while the impact of the Micromass acquisition resulted in the remaining 23% points of growth. HPLC growth was generally broad based across all geographies except the Pacific Rim, and particularly strong in the U.S. and Europe offsetting declines in the Pacific Rim. Japan had moderate sales growth for the year. Pharmaceutical customer demand was especially strong across all geographies. Sales of the Company's mass spectrometry products grew strongly as well with increased use of mass spectrometry as an analytical tool within the pharmaceutical industry, especially in conjunction with HPLC.

gross profit

Gross profit for 1998 was $369.8 million, compared to $275.7 million for 1997, an increase of $94.1 million or 34%. Excluding each $16.5 million nonrecurring charge in 1997 and 1998 for revaluation of acquired inventory related to purchase accounting for the Micromass acquisition, gross profit increased by 32% in 1998. Gross profit as a percentage of sales excluding the inventory revaluation charges decreased to 62.4% in 1998 from 62.8% in 1997, reflecting the inclusion of Micromass results after its September 1997 acquisition. (Micromass mass spectrometry gross margins were lower than Waters HPLC historical gross margins, but its operating expenses were commensurately lower, and its overall operating margins were comparable to those of Waters.) Excluding the impact of Micromass results, gross profit as a percentage of sales increased in 1998, primarily as a result of increased efficiencies in the Company's manufacturing operations and lower raw material costs.

selling, general and administrative expenses

Selling, general and administrative expenses for 1998 were $206.2 million, compared to $167.3 million for 1997. As a percentage of net sales, selling, general and administrative expenses decreased to 33.3% for 1998 from 35.9% for 1997 as a result of higher sales volume and expense controls. The $38.9 million or 23% increase in total expenditures primarily resulted from including the expenses of Micromass.

research and development expenses

Research and development expenses were $34.4 million for 1998 compared to $25.8 million for 1997, an $8.6 million or 33% increase from prior year levels. Spending increased in 1998 due to the inclusion of acquired company expenses. The Company continued to invest significantly in the development of new and improved HPLC, thermal analysis, rheology and mass spectrometry products.

goodwill and purchased technology amortization

Goodwill and purchased technology amortization for 1998 was $9.4 million, compared to $6.5 million for 1997, an increase of $2.9 million or 45%. This increase primarily was related to the acquisition of Micromass.

operating income

Operating income for 1998 was $119.8 million, an increase of $98.6 million from the prior year. Operating income in 1998 included a $16.5 million nonrecurring acquisition related charge while 1997 included $71.5 million of similar charges. Excluding the revaluation of acquired inventory charges in 1998 and 1997 and the expensed in-process research and development charge in 1997, all in connection with the Micromass acquisition, operating income was $136.3 million for the year ended December 31, 1998 and represented a $43.6 million or 47% increase over 1997. As in 1997, Waters continued to improve operating income levels in 1998 on the strength of sales growth, volume leverage, continued focus on cost reduction in all operating areas and the accretive impact of acquisitions.

interest expense, net

Net interest expense increased by $4.6 million, or 34%, from $13.7 million in 1997 to $18.3 million in 1998. The 1998 increase reflected higher average 1998 debt levels as a result of borrowings which financed the late 1997 acquisition of Micromass, reduced by 1998 repayments from the Company's cash flow.

provision for income taxes

The Company's effective income tax rate, excluding nonrecurring nondeductible charges related to the revaluation of acquired inventory in 1998 and revaluation of acquired inventory and expensed in-process research and development in 1997, was 23% in 1998 and 20% in 1997.

income (loss) from operations

Income from operations for 1998 was $74.4 million, compared to an $(8.3) million loss from operations for 1997. Excluding nonrecurring acquisition related charges in 1998 and 1997, the Company generated $90.9 million of income in 1998 compared to $63.2 million in 1997. The improvement over 1997 was a result of sales growth, continued focus on cost reductions in all operating areas and the accretive impact of the Micromass acquisition.

YEAR 2000

The Company engaged in a concerted effort to ready its business systems and products in anticipation of Year 2000 ("Y2K"). The Company did not experience any significant Y2K related issues at year end and believes its internal systems and related software are Y2K compliant. The Company has experienced no signs of disruption to its business and will continue to monitor its material software and systems. Corrective action, if necessary, will be taken to minimize any significant detrimental effects on operations.

While the Company believes its efforts have provided reasonable assurance that future material disruptions are not likely to occur, the potential for interruption and adverse effects still remotely exists. However, the company does not expect that any potential Y2K disruptions would have a material effect on the Company. In addition, recovery under existing insurance policies may be available depending upon the circumstances of a Y2K related event. To date, approximately $11.0 million has been spent over the past four years in connection with bringing the Company's internal systems into compliance, primarily capital expenditures for entirely new business and communications systems that replaced predecessor systems. These costs do not include any allocation for the time devoted by regular employees of the Company addressing Y2K problems, as the Company did not separately track such time.

EURO CURRENCY CONVERSION

Several countries of the European Union will adopt the euro as their legal currency effective July 1, 2002. A transition period has been established from January 1, 1999 to July 1, 2002 during which companies conducting business in these countries may use the euro or their local currency. The Company has considered the potential impact of the euro conversion on pricing competition, information technology systems, currency risk and risk management. Currently, the Company does not expect that the euro conversion will result in any material increase in costs to the Company or have a material adverse effect on its business or financial condition.

LIQUIDITY AND CAPITAL RESOURCES

During 1999, net cash provided by the Company's operating activities was $150.2 million, primarily as a result of net income for the year after adding back depreciation and amortization. In addition, the Company received $11.2 million of proceeds from the exercise of stock options and its employee stock purchase plan. Primary uses of this cash flow during the year were $127.2 million of net bank debt repayment, $24.4 million of property, plant and equipment and software capitalization investments, and a $9.5 million redemption of its preferred stock.

The Company believes that existing cash balances and current cash flow from operating activities together with borrowings available under the Bank Credit Agreement will be sufficient to fund working capital, capital spending and debt service requirements of the Company in the foreseeable future.

As a publicly held company, the Company has not paid any dividends and does not plan to pay any dividends in the foreseeable future.

ENVIRONMENTAL MATTERS

The Company's facilities are subject to federal, state and local environmental requirements, including those relating to discharges to air, water and land, the handling and disposal of solid and hazardous waste and the cleanup of properties affected by hazardous substances. The Company does not currently anticipate any material adverse effect on its operations or financial condition as a result of its efforts to comply with, or its liabilities under, such requirements. The Company does not currently anticipate any material capital expenditures for environmental control facilities. Some risk of environmental liability is inherent in the Company's business, however, and there can be no assurance that material environmental costs will not arise in the future. In particular, the Company might incur capital and other costs to comply with increasingly stringent environmental laws and enforcement policies. Although it is difficult to predict future environmental costs, the Company does not anticipate any material adverse effect on its operations, financial condition or competitive position as a result of future costs of environmental compliance. In connection with the acquisition of the predecessor HPLC business of Millipore Corporation ("Millipore") in August 1994, Millipore retained environmental liabilities resulting from pre-acquisition operations of the Company's facilities.

RECENT ACCOUNTING STANDARDS CHANGES

In June 1999, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard ("SFAS") 137, Accounting for Derivative Instruments and Hedging Activities — Deferral of the Effective Date of SFAS 133. SFAS 137 amends SFAS 133, Accounting for Derivative Instruments and Hedging Activities, which was issued in June 1998 and was to be effective previously for all fiscal quarters of fiscal years beginning after June 15, 1999. SFAS 137 defers the effective date of SFAS 133 to June 15, 2000. Earlier application is permitted. SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. While management has not determined the impact of the new standard, it is not expected to be material to the Company.

FORWARD-LOOKING INFORMATION

safe harbor statement under private securities litigation reform act of 1996

Certain statements contained herein are forward looking. Many factors could cause actual results to differ from these statements, including, but not limited to, obsolescence resulting from the introduction of technologically advanced products by other companies, pressure on prices from competitors with significantly greater financial resources, regulatory obstacles to new product introductions, reduction in capital spending of pharmaceutical customers, and market risk described below. Please refer also to the Company's Form 10-K for additional risk factors.

market risk

The Company is exposed to financial risk in several areas including changes in foreign exchange rates and interest rates. The Company attempts to minimize its exposures by using certain financial instruments, for purposes other than trading, in accordance with the Company's overall risk management guidelines. Further information regarding the Company's accounting policies for financial instruments and disclosures of financial instruments can be found in Notes 2 and 6 to the Company's consolidated financial statements.

foreign exchange

The Company has operations in various countries and currencies all over the world. As a result, the Company's financial position, results of operations and cash flows can be affected by fluctuations in foreign currency exchange rates. The Company uses debt swap agreements to mitigate partially such effects.

In February 1999, the Company closed certain outstanding debt swap agreements and entered into new debt swap agreements in European currencies, which hedged foreign exchange exposures. These new debt swap agreements also extended the time period of the agreements until February 2001. These agreements combined with other outstanding debt swap agreements that the Company maintained at December 31, 1999 effectively swapped higher U.S. dollar fixed rate borrowings for lower fixed rate borrowings denominated in the respective currencies. The effect of these debt swap agreements lowers overall annual interest cost by approximately $3.3 million over the lives of the swap agreements at interest rates in effect under the respective contracts on December 31, 1999. The Company

could incur higher or lower principal payments over the term of the swap agreements. At currency exchange rates in effect on December 31, 1999, the fair market value of those instruments was an unrealized gain of $6.1 million. Details of these swap agreements are as follows:

Geography	Notional Amount (In thousands)	Composite Interest Rate	Expiration Dates
Japan	$ 32,933	1.10%	January 2001
Europe	73,000	4.20%	February 2001
Canada	6,400	4.05%	January 2000
Total	$112,333		

Assuming a hypothetical adverse change of 10% in year-end exchange rates (a weakening of the U.S. dollar), the fair market value of those instruments would decrease by $11.2 million.

interest rates

The Company is exposed to risk of interest rate fluctuations in connection with its Bank Credit Agreement. As a result, the Company attempts to minimize its interest rate exposures by using certain financial instruments described below for purposes other than trading.

In November 1999, the Company closed an interest swap agreement with Bankers Trust Company and entered into a new agreement with decreased notional amounts. During 1999 and 1998, the Company swapped $103 million and $135 million, respectively, in notional amount of floating rate LIBOR borrowings for an equivalent notional amount of borrowings at a fixed interest rate of 6.3%. The new interest swap agreement reduces notional amounts progressively to zero over a thirteen-month period and expires on December 29, 2000. The notional amount of the interest swap exceeded the aggregate borrowings at December 31, 1999 by $21.9 million. At December 31, 1999 and 1998, the fair market value of the swap agreements was an unrealized loss of $16 thousand and $4.4 million, respectively. At December 31, 1999, a one percentage point decrease in the LIBOR rate would decrease the fair market value by approximately $.5 million.

The Company's debt swap agreements also fix the interest rate on its Bank Credit Agreement. At December 31, 1999, a one percentage point decrease in the LIBOR rate would increase the fair market value of the debt swaps by approximately $.6 million.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of Waters Corporation:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, stockholders' equity, and cash flows present fairly, in all material respects, the financial position of Waters Corporation and Subsidiaries at December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1999, in conformity with accounting principles generally accepted in the United States. 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 of these statements in accordance with auditing standards generally accepted in the United States, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

Boston, Massachusetts
January 21, 2000

CONSOLIDATED BALANCE SHEETS

December 31 (In thousands, except per share data)	1999	1998
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,803	$ 5,497
Accounts receivable, less allowances for doubtful accounts of $3,741 and $2,966 at December 31, 1999 and 1998, respectively	149,271	136,806
Inventories	80,363	80,281
Other current assets	13,893	16,448
Total current assets	247,330	239,032
Property, plant and equipment, net	91,841	89,029
Other assets	74,530	72,146
Goodwill, less accumulated amortization of $16,068 and $12,281 at December 31, 1999 and 1998, respectively	170,736	177,494
Total assets	$584,437	$577,701
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable and current portion of long-term debt	$ 14,164	$ 4,259
Accounts payable	34,771	36,510
Deferred revenue and customer advances	31,406	29,706
Accrued retirement plan contributions	5,181	5,934
Accrued income taxes	16,350	16,112
Accrued other taxes	4,026	4,225
Other current liabilities	91,943	88,827
Total current liabilities	197,841	185,573
Long-term debt	81,105	218,250
Redeemable preferred stock	—	9,058
Other liabilities	13,329	14,701
Total liabilities	292,275	427,582
Stockholders' equity:		
Common stock, par value $0.01 per share, 100,000 shares authorized, 62,259 and 60,594 shares issued and outstanding at December 31, 1999 and 1998, respectively	623	606
Additional paid-in capital	195,455	174,414
Deferred stock option compensation	(166)	(386)
Retained earnings (deficit)	100,041	(21,697)
Accumulated other comprehensive (loss)	(3,791)	(2,818)
Total stockholders' equity	292,162	150,119
Total liabilities and stockholders' equity	$584,437	$577,701

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

CONSOLIDATED STATEMENTS OF OPERATIONS

Year Ended December 31 (In thousands, except per share data)	1999	1998	1997
Net sales	$704,400	$618,813	$465,470
Cost of sales	257,136	232,497	173,275
Revaluation of acquired inventory	—	16,500	16,500
Gross profit	447,264	369,816	275,695
Selling, general and administrative expenses	226,593	206,211	167,290
Research and development expenses	36,094	34,433	25,750
Goodwill and purchased technology amortization	8,068	9,347	6,468
Expensed in-process research and development	—	—	55,000
Operating income	176,509	119,825	21,187
Interest expense, net	8,948	18,278	13,720
Income from operations before income taxes	167,561	101,547	7,467
Provision for income taxes	45,243	27,148	15,755
Net income (loss)	122,318	74,399	(8,288)
Accretion of and 6% dividend on preferred stock	(825)	(963)	(942)
Gain on redemption of preferred stock	383	—	—
Net income (loss) available to common stockholders	$ 121,876	$ 73,436	$ (9,230)
Net income (loss) per basic common share	$ 1.98	$ 1.23	$ (.16)
Weighted average number of basic common shares	61,506	59,860	58,254
Net income (loss) per diluted common share	$ 1.84	$ 1.14	$ (.16)
Weighted average number of diluted common shares and equivalents	66,316	64,642	58,254

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year Ended December 31 (In thousands)	1999	1998	1997
Cash flows from operating activities:			
Net income (loss)	$122,318	$ 74,399	$ (8,288)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Deferred income taxes	3,407	(10,366)	(5,891)
Depreciation and amortization	28,947	27,248	20,010
Amortization of debt issuance costs	737	1,240	1,085
Compensatory stock option expense	220	220	220
Tax benefit related to stock option plans	9,747	7,623	2,976
Expensed in-process research and development	—	—	55,000
Revaluation of acquired inventory	—	16,500	16,500
Change in operating assets and liabilities, net of acquisitions:			
(Increase) in accounts receivable	(15,566)	(21,978)	(8,127)
(Increase) in inventories	(1,474)	(8,230)	(2,270)
Increase in accounts payable and other current liabilities	4,343	14,034	11,399
Increase in deferred revenue and customer advances	2,406	4,284	5,375
Other, net	(4,877)	5,196	8,377
Net cash provided by operating activities	150,208	110,170	96,366
Cash flows from investing activities:			
Additions to property, plant and equipment	(19,399)	(15,040)	(18,216)
Software capitalization and other intangibles	(5,017)	(5,576)	(5,177)
Business acquisitions, net of cash acquired	(2,412)	(3,157)	(160,985)
Loans to officers	1,098	187	(136)
Net cash (used in) investing activities	(25,730)	(23,586)	(184,514)
Cash flows from financing activities:			
Net (repayment) borrowings of bank debt	(127,240)	(90,225)	87,452
Redemption of preferred stock	(9,500)	—	—
Proceeds from stock plans	11,173	6,588	2,491
Other, net	—	—	1,113
Net cash (used in) provided by financing activities	(125,567)	(83,637)	91,056
Effect of exchange rate changes on cash and cash equivalents	(605)	(563)	(434)
(Decrease) increase in cash and cash equivalents	(1,694)	2,384	2,474
Cash and cash equivalents at beginning of period	5,497	3,113	639
Cash and cash equivalents at end of period	$ 3,803	$ 5,497	$ 3,113

CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

Year Ended December 31 (In thousands)	1999	1998	1997
Supplemental cash flow information:			
Income taxes paid	$ 29,014	$ 14,993	$ 10,022
Interest paid	$ 12,214	$ 19,601	$ 12,754
Supplemental noncash transactions:			
Issuance of common stock for acquisition	$ —	$ —	$ 11,241
Issuance of notes for acquisition	$ —	$ —	$ 9,975

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands)	Common Stock	Additional Paid-in Capital	Deferred Stock Option Compensation	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total	Statement of Comprehensive Income
Balance December 31, 1996	$ 578	$145,428	$ (826)	$ (87,808)	$ 408	$ 57,780	
Comprehensive (loss), net of tax:							
Net (loss)	—	—	—	(8,288)	—	(8,288)	$ (8,288)
Other comprehensive (loss):							
Foreign currency translation adjustments	—	—	—	—	(3,181)	(3,181)	(3,181)
Other comprehensive (loss)	—	—	—	—	(3,181)	(3,181)	(3,181)
Comprehensive (loss)	—	—	—	—	—	—	$ (11,469)
Accretion of preferred stock	—	(342)	—	—	—	(342)	
Dividend payable on preferred stock	—	(600)	—	—	—	(600)	
Issuance of common stock for acquisition	6	11,235	—	—	—	11,241	
Issuance of common stock for Employee Stock Purchase Plan	2	316	—	—	—	318	
Compensatory stock option expense	—	—	220	—	—	220	
Stock options exercised	6	2,167	—	—	—	2,173	
Tax benefit related to stock option plans	—	2,976	—	—	—	2,976	
Balance December 31, 1997	$ 592	$161,180	$ (606)	$(96,096)	$ (2,773)	$ 62,297	

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (CONTINUED)

(In thousands)	Common Stock	Additional Paid-in Capital	Deferred Stock Option Compensation	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total	Statement of Comprehensive Income
Balance December 31, 1997	$ 592	$161,180	$ (606)	$(96,096)	$ (2,773)	$ 62,297	
Comprehensive income, net of tax:							
Net income	—	—	—	74,399	—	74,399	$ 74,399
Other comprehensive (loss):							
Foreign currency translation adjustments	—	—	—	—	(45)	(45)	(45)
Other comprehensive (loss)	—	—	—	—	(45)	(45)	(45)
Comprehensive income	—	—	—	—	—	—	$ 74,354
Accretion of preferred stock	—	(363)	—	—	—	(363)	
Dividend payable on preferred stock	—	(600)	—	—	—	(600)	
Issuance of common stock for Employee Stock Purchase Plan	2	864	—	—	—	866	
Compensatory stock option expense	—	—	220	—	—	220	
Stock options exercised	12	5,710	—	—	—	5,722	
Tax benefit related to stock option plans	—	7,623	—	—	—	7,623	
Balance December 31, 1998	$ 606	$174,414	$ (386)	$ (21,697)	$ (2,818)	$150,119	
Comprehensive income, net of tax:							
Net income	—	—	—	122,318	—	122,318	$122,318
Other comprehensive (loss):							
Foreign currency translation adjustments	—	—	—	—	(973)	(973)	(973)
Other comprehensive (loss)	—	—	—	—	(973)	(973)	(973)
Comprehensive income	—	—	—	—	—	—	$121,345
Accretion of preferred stock	—	(92)	—	(230)	—	(322)	
Dividend payable on preferred stock	—	(153)	—	(350)	—	(503)	
Gain on redemption of preferred stock	—	383	—	—	—	383	
Issuance of common stock for Employee Stock Purchase Plan	1	1,250	—	—	—	1,251	
Compensatory stock option expense	—	—	220	—	—	220	
Stock options exercised	16	9,906	—	—	—	9,922	
Tax benefit related to stock option plans	—	9,747	—	—	—	9,747	
Balance December 31, 1999	$ 623	$195,455	$ (166)	$100,041	$ (3,791)	$292,162	

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(IN THOUSANDS, EXCEPT PER SHARE DATA)

1. DESCRIPTION OF BUSINESS, ORGANIZATION AND BASIS OF PRESENTATION

Waters Corporation ("Waters" or the "Company"), an analytical instrument manufacturer, is the world's largest manufacturer and distributor of high performance liquid chromatography ("HPLC") instruments, chromatography columns and other consumables, and related service. HPLC, the largest product segment of the analytical instrument market, is utilized in a broad range of industries to detect, identify, monitor and measure the chemical, physical and biological composition of materials, and to purify a full range of compounds. Through its Micromass Limited ("Micromass") subsidiary, the Company is also a market leader in the development, manufacture, and distribution of mass spectrometry ("MS") instruments, which are complementary products that can be integrated and used along with other analytical instruments, especially HPLC. Through its TA Instruments, Inc. ("TAI") subsidiary, the Company is also the world's leader in thermal analysis, a prevalent and complementary technique used in the analysis of polymers.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect (i) the reported amounts of assets and liabilities, (ii) disclosure of contingent assets and liabilities at the dates of the financial statements and (iii) the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, most of which are wholly owned. All material intercompany balances and transactions have been eliminated.

translation of foreign currencies

For most of the Company's foreign operations, assets and liabilities are translated into U.S. dollars at exchange rates prevailing on the balance sheet date while revenues and expenses are translated at average exchange rates prevailing during the period. Any resulting translation gains or losses are included in accumulated other comprehensive (loss) in the consolidated balance sheets.

cash and cash equivalents

Cash equivalents primarily represent highly liquid investments, with original maturities of 90 days or less, in repurchase agreements and money market funds that are convertible to a known amount of cash and carry an insignificant risk of change in value. The Company has periodically maintained balances in various operating accounts in excess of federally insured limits.

concentration of credit risk

The Company sells its products to a significant number of large and small customers throughout the world, with approximately 61% of 1999 net sales to the pharmaceutical industry. None of the Company's individual customers accounts for more than 2% of annual Company sales. The Company performs continuing credit evaluation of its customers and generally does not require collateral, but in certain circumstances may require letters of credit or deposits. Historically, the Company has not experienced significant bad debt losses.

inventory

The Company values all of its inventories at the lower of cost or market on a first-in, first-out basis (FIFO).

income taxes

Deferred income taxes are recognized for temporary differences between financial statement and income tax bases of assets and liabilities.

property, plant and equipment

Property, plant and equipment is recorded at cost. Expenditures for maintenance and repairs are charged to expense while the costs of significant improvements are capitalized. Depreciation is provided using the straight-line method over the following estimated useful lives: buildings and improvements — thirty years, leasehold improvements — fifteen years or life of lease, and production and other equipment — three to ten years. Upon retirement or sale, the cost of assets disposed and the related accumulated depreciation are eliminated from the balance sheet and related gains or losses are reflected in income.

software development costs

The Company capitalizes software development costs for products offered for sale in accordance with Statement of Financial Accounting Standard ("SFAS") 86. Capitalized costs are amortized to cost of sales on a straight-line basis over the estimated useful lives of the related software products, generally three to five years. Capitalized software included in other assets, net of accumulated amortization, was $15,430 and $14,191 at December 31, 1999 and 1998, respectively.

The Company capitalizes internal software development costs in accordance with Statement of Position 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. Capitalized internal software development costs are amortized on a straight-line basis over ten years. For the years ended December 31, 1999 and 1998, capitalized internal software included in property, plant and equipment, net of accumulated amortization, totaled $3,275 and $3,375, respectively.

purchased technology and goodwill

Purchased technology amounts are recorded at their fair market value as of the acquisition date and amortized over estimated useful lives ranging from four to fifteen years. Goodwill is amortized on a straight-line basis over its useful life, forty years for current goodwill components. Under SFAS 121, impairment of purchased technology and goodwill are measured on the basis of whether anticipated future undiscounted operating cash flows expected from the acquired business will recover the recorded respective intangible asset balances over the remaining amortization period. At December 31, 1999, no amounts have been determined to be impaired. Purchased technology included in other assets totaled $27,105 and $30,034, net of accumulated amortization of $14,282 and $11,360, at December 31, 1999 and 1998, respectively.

debt issuance costs

Debt issuance costs are amortized over the life of the related debt using the effective interest method. At December 31, 1999 and 1998, debt issuance costs included in other assets amounted to $1,072 and $1,809, net of accumulated amortization of $2,591 and $1,854, respectively.

stockholders' equity

On February 25, 1999, the Board of Directors approved a two-for-one common stock split, in the form of a 100% stock dividend, contingent upon shareholder approval of a charter amendment increasing authorized common stock. At the Company's Annual Meeting on May 4, 1999, shareholders approved the charter amendment. Shareholders of record on May 27, 1999 received the stock dividend on or about June 10, 1999. All share and per share amounts have been retroactively restated to reflect the stock split.

hedge transactions

The Company maintains debt swap agreements which hedge the U.S. dollar value of the Company's investment in the net assets of certain foreign subsidiaries. The Company records any unrealized or realized gains or losses on these transactions in accumulated other comprehensive income (loss) in the consolidated balance sheets.

In June 1999, the Financial Accounting Standards Board issued SFAS 137, Accounting for Derivative Instruments and Hedging Activities — Deferral of the Effective Date of SFAS 133. SFAS 137 amends SFAS 133, Accounting for Derivative Instruments and Hedging Activities, which was issued in June 1998 and previously was to be effective for all fiscal quarters of fiscal years beginning after June 15, 1999. SFAS 137 defers the effective date of SFAS 133 to fiscal years beginning after June 15, 2000. Earlier application is permitted. SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. While management has not determined the impact of the new standard, it is not expected to be material to the Company.

revenue recognition

Sales of products and services are recorded based on product shipment and performance of service, respectively. Proceeds received in advance of product shipment or performance of service are recorded as deferred revenue in the consolidated balance sheets.

product warranty costs

The Company provides for estimated warranty costs at the point of sale.

field service expenses

All expenses of the Company's field service organization are included in selling, general and administrative expenses in the consolidated statements of operations.

reclassification

Certain amounts in previous years' financial statements have been reclassified to conform to current presentation.

income (loss) per share

In accordance with SFAS 128, Earnings Per Share, the Company presents two earnings per share ("EPS") amounts. Income (loss) per basic common share is based on income available to common shareholders and the weighted average number of common shares outstanding during the periods presented. Income (loss) per diluted common share includes additional dilution from potential common stock, such as stock issuable pursuant to the exercise of stock options outstanding and the conversion of debt. Accretion, cumulative dividends and gain on redemption of preferred stock have been included in computing income (loss) per share.

comprehensive (loss) income

The Company accounts for comprehensive (loss) income under SFAS 130, Reporting Comprehensive Income. The statement establishes standards for reporting and displaying comprehensive income and its components (revenues, expenses, gains, and losses) in a full set of general-purpose financial statements. The statement requires that all components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements.

retirement plan

The Company adopted SFAS 132, Employers' Disclosures about Pensions and Other Postretirement Benefits. The statement standardizes employer disclosure requirements about pension and other postretirement benefit plans by requiring additional information on changes in the benefit obligations and fair values of plan assets and eliminating certain disclosures that are no longer useful. It does not change the measurement or recognition of those plans.

business segments

The Company discloses business segments under SFAS 131, Disclosures about Segments of an Enterprise and Related Information. The statement establishes standards for reporting information about operating segments in annual financial statements of public business enterprises and in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers.

3. BUSINESS COMBINATIONS

micromass limited acquisition

On September 23, 1997, the Company acquired all of the capital stock of Micromass Limited, a company headquartered in England, for approximately $175,000 in cash, common stock (750 shares) and promissory notes. The acquisition principally was financed through borrowings under the Company's Bank Credit Agreement. Micromass develops, manufactures, and distributes mass spectrometry instruments, products that are complementary to Waters' existing product offering. Micromass offers products ranging from high-end stand-alone instruments to smaller, easier-to-use detectors that can be integrated and used along with other analytical instruments, especially HPLC. Micromass is a global market leader in the field of mass spectrometry. Net sales for Micromass were approximately $76,600 for the period from January 1, 1997 to September 30, 1997.

The acquisition of Micromass was accounted for by the purchase method and the results of its operations have been consolidated with the Company's results from September 30, 1997, the effective accounting date of the acquisition. In conjunction with the acquisition, the Company recorded a nonrecurring charge of $55,000 for the write-off of acquired in-process research and development and revalued acquired inventory by $33,000, which amount was amortized to cost of sales over a period of approximately six months commencing October 1, 1997. The technological feasibility of in-process research and development projects had not been established at the date of acquisition and had no alternative future use. The Company recorded purchased technology in the transaction of $24,200 and goodwill of $66,914, which will be amortized for a period of fifteen and forty years, respectively, on a straight-line basis. The Company recorded $8,500 of purchase accounting liabilities in conjunction with the acquisition in 1997, and reversed $4,000 of those purchase accounting liabilities against goodwill in 1998.

ymc, inc. acquisition

On July 31, 1997, the Company acquired all of the capital stock of YMC, Inc. ("YMC"), a U.S.-based company for approximately $9,000 in cash. The acquisition of YMC was accounted for by the purchase method. YMC is a manufacturer and distributor of chromatography chemicals and supplies, which augment the Waters consumables product line. Net sales for YMC were approximately $4,300 for the period from January 1, 1997 to July 31, 1997.

pro forma results of operations

The following unaudited Pro Forma results of operations for the year ended December 31, 1997 give effect to the Company's acquisitions as if the transactions had occurred at the beginning of that period. The financial data are based on the historical consolidated financial statements for the Company, Micromass and YMC and include related adjustments. The Pro Forma results of operations exclude the nonrecurring charges that were recorded in conjunction with the Micromass acquisition in 1997 and do not purport to represent (i) what the Company's results of operations actually would have been if the acquisitions had occurred as of the beginning of the period or (ii) what such results will be for any future periods. The financial data are based upon assumptions that the Company believes are reasonable and should be read in conjunction with the consolidated financial statements and accompanying notes thereto included elsewhere in this report. As there were no significant acquisitions made in 1998 and 1999, reference is hereby made to the consolidated statements of operations for 1998 and 1999 financial data.

Unaudited Pro Forma Results for the Year Ended	December 31, 1997
Net sales	$542,045
Income before extraordinary item	67,204
Net income	66,262
Net income per basic common share	$ 1.13
Net income per diluted common share	$ 1.02

4. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following:

December 31	1999	1998
Land and land improvements	$ 3,887	$ 3,146
Buildings and leasehold improvements	35,321	34,087
Production and other equipment	103,855	92,592
Construction in progress	5,190	4,625
Total property, plant and equipment	148,253	134,450
Less: accumulated depreciation and amortization	(56,412)	(45,421)
Property, plant and equipment, net	$ 91,841	$ 89,029

5. INVENTORIES

Inventories are classified as follows:

December 31	1999	1998
Raw material	$ 27,155	$ 27,327
Work in progress	14,446	9,572
Finished goods	38,762	43,382
Total inventories	$ 80,363	$ 80,281

6. DEBT

The Company has a Bank Credit Agreement ("Agreement") that was renegotiated in 1997 and provides a $450,000 line of credit through June 2002. Loans under the Agreement bear interest for each calendar quarter at an annual rate equal to, at the Company's option, i) the applicable LIBOR rate plus a varying margin between .30% and 1.00% or ii) prime rate. Margins on LIBOR borrowings vary with Company financial performance. At December 31, 1999 and 1998, the Company had aggregate borrowings outstanding under the Agreement of $81,105 and $208,275, respectively, and had additional amounts available to borrow of $354,978 and $228,617, respectively, after outstanding letters of credit. The weighted average interest rate on the borrowings at December 31, 1999 and 1998 was 6.54% and 5.64%, respectively. Borrowings are collateralized by substantially all of the Company's assets. The Company is also required to meet certain covenants, none of which is considered restrictive to operations. The Company was in compliance with all covenants as of December 31, 1999 and 1998. The Company's foreign subsidiaries also had available short-term lines of credit totaling $32,413 at December 31, 1999 and $31,616 at December 31, 1998. At December 31, 1999 and 1998, related short-term borrowings were $4,183 at a weighted average interest rate of 5.25% and $4,144 at a weighted average interest rate of 3.1%, respectively. In addition, the Company has promissory notes of $9,975 due in September 2000 in conjunction with the Micromass acquisition. These notes bear interest at a fixed rate of 6.25% payable semiannually.

In November 1999, the Company closed an interest swap agreement with Bankers Trust Company and entered into a new agreement with decreased notional amounts. During 1999 and 1998, the Company swapped $103,000 and $135,000, respectively, in notional amount of floating rate LIBOR borrowings for an equivalent notional amount of borrowings at a fixed interest rate of 6.3%. The new interest swap agreement reduces notional amounts progressively to zero over a thirteen-month period and expires on December 29, 2000. The notional amount of the interest swap exceeded the aggregate borrowings at December 31, 1999 by $21,895. At December 31, 1999 and 1998, the fair value of this agreement was an unrealized loss of $16 and $4,437, respectively.

In February 1999, the Company closed certain outstanding debt swap agreements and entered into new debt swap agreements in European currencies which hedged foreign exchange exposures. These new debt swap agreements also extended the time period of the agreements until February 2001. These agreements combined with other outstanding debt swap agreements that the Company maintained at December 31, 1999 effectively swapped higher U.S. dollar fixed rate borrowings for lower fixed rate borrowings denominated in the respective currencies. The effect of these debt swap agreements lowers overall annual interest cost by approximately $3,348 over the lives of the swap agreements at interest rates in effect under the respective contracts on December 31, 1999. The Company could incur higher or lower principal payments over the term of the swap agreements. At currency exchange rates in effect on December 31, 1999, the fair market value of those instruments was an unrealized gain of $6,104. Details of these swap agreements are as follows:

Geography	Notional Amount	Composite Interest Rate	Expiration Dates
Japan	$ 32,933	1.10%	January 2001
Europe	73,000	4.20%	February 2001
Canada	6,400	4.05%	January 2000
Total	$112,333		

7. INCOME TAXES

Income tax data for 1999, 1998 and 1997 follow in the tables below:

Year Ended December 31	1999	1998	1997
The components of income from operations before income taxes were as follows:			
Domestic	$ 66,082	$ 62,873	$ 64,751
Foreign	101,479	38,674	(57,284)
Total	$167,561	$101,547	$ 7,467
The components of the current and deferred income tax provision from operations were as follows:			
Current	$ 41,560	$ 34,264	$ 20,280
Deferred	3,683	(7,116)	(4,525)
Total	$ 45,243	$ 27,148	$ 15,755
The components of the provision for income taxes from operations were as follows:			
Federal	$ 16,428	$ 6,001	$ 9,383
State	1,187	1,336	878
Foreign	27,628	19,811	5,494
Total	$ 45,243	$ 27,148	$ 15,755
The differences between income taxes computed at the United States statutory rate and the provision for income taxes are summarized as follows:			
Federal tax computed at U.S. statutory income tax rate	$ 58,646	$ 35,541	$ 2,613
Foreign sales corporation	(3,075)	(2,333)	(1,826)
State income tax, net of federal income tax benefit	772	868	570
Deferred tax assets (benefited)	(4,891)	(13,254)	(12,307)
Net effect of foreign operations	(7,243)	(191)	1,005
Nondeductible acquisition costs	—	5,775	25,025
Other	1,034	742	675
Provision for income taxes	$ 45,243	$ 27,148	$ 15,755
The tax effects of temporary differences and carryforwards which gave rise to deferred tax assets and deferred tax (liabilities) were as follows:			
Acquired net operating loss carryforwards	$ —	$ 608	$ 2,516
Tax benefit of net operating loss and credits	27,778	18,006	4,133
Goodwill amortization	8,588	10,598	10,866
Deferred compensation	9,908	7,984	3,605
Inventory	2,586	6,388	2,452
Other	645	(68)	2,296
Depreciation and capitalized software	(9,890)	(7,620)	(6,481)
Valuation allowance	(22,565)	(15,439)	(9,296)
Total deferred taxes	$ 17,050	$ 20,457	$ 10,091

At December 31, 1999, the Company had foreign net operating loss carryforwards of approximately $1,570, some of which begin to expire in the year 2001 and some of unlimited duration. The goodwill amortization represents the difference between the book and tax treatment for both goodwill and in-process research and development. Deferred tax assets included in other current assets totaled $5,591 and $7,865 at December 31, 1999 and 1998, respectively. Deferred tax assets included in other assets totaled $11,459 and $12,592 at December 31, 1999 and 1998, respectively. The valuation allowance relates to foreign net operating losses and foreign tax credits, the realization of which is contingent upon future taxable income.

The Company's effective tax rate before the nondeductible acquisition related expenses for the years ended December 31, 1999, 1998 and 1997 was 27%, 23% and 20%, respectively.

8. LEASES

Lease agreements, expiring at various dates through 2019, cover buildings, office equipment and automobiles. Rental expense was approximately $11,812 in 1999, $10,766 in 1998 and $8,666 in 1997. Future minimum rents payable as of December 31, 1999 under non-cancelable leases with initial terms exceeding one year were as follows:

2000	$11,230
2001	9,064
2002	6,400
2003	4,637
2004	3,870
Thereafter	9,521

9. REDEEMABLE PREFERRED STOCK

In conjunction with the August 18, 1994 acquisition of the predecessor HPLC business of Millipore Corporation ("Millipore"), the Company authorized and issued one hundred shares of Redeemable Preferred Stock ("Preferred Stock") with a par value of $.01 per share. The Preferred Stock had a liquidation value of $10,000 and earned an annual 6% cumulative dividend on the liquidation value. Any accumulated but unpaid dividends added to the liquidation value. The Company could, at any time, redeem the Preferred Stock at the current liquidation value but in no event later than August 18, 2006. The Preferred Stock was recorded at its estimated fair value of $5,000 on the date of issuance. The excess of the liquidation value over the fair market value was being accreted by periodic charges to additional paid-in capital or available retained earnings since the date of issue.

On November 2, 1999, the Company redeemed all outstanding shares of Preferred Stock, including cumulative unpaid dividends, for $9,500 in cash. The carrying value of the one hundred shares of Preferred Stock and cumulative dividends payable was $9,883 on that date and the transaction resulted in a gain on redemption of $383 which was credited to additional paid-in capital.

During the years ended December 31, 1999, 1998 and 1997, $322, $363 and $342, respectively, for accretion, and $503, $600 and $600, respectively, for unpaid dividends were charged against additional paid-in capital or available retained earnings.

10. STOCK COMPENSATION AND PURCHASE PLANS

basis of accounting

The Company has four stock-based compensation plans, which are described below. The Company uses the intrinsic value method of accounting prescribed by the Accounting Principles Board Opinion 25, Accounting for Stock Issued to Employees, and related interpretations for its plans. Accordingly, no compensation expense has been recognized for its fixed stock option plans and its stock purchase plan under SFAS 123, Accounting for Stock-Based Compensation. Had compensation expense for the Company's four stock-based compensation plans been recorded based on the fair value of awards at grant date consistent with the alternative method prescribed by SFAS 123, the Company's pro forma net income (loss) for 1999, 1998 and 1997 would have been $115,857, $70,043 and $(10,821), respectively. Basic income (loss) per share for 1999, 1998 and 1997 would have been $1.88, $1.17 and $(0.19), respectively. Diluted income (loss) per share for 1999, 1998 and 1997 would have been $1.75, $1.09, and $(0.19), respectively. The pro forma amounts include amortized fair values attributable to options granted after December 31, 1994 only and, therefore, are not likely to be representative of the effects on reported net income for future years.

The fair value of each option grant under SFAS 123 was estimated on the date of grant using the Black-Scholes option-pricing model. Relevant data are described below:

Significant Assumptions Used to Estimate Option Fair Values	1999	1998	1997
Options issued	934	1,056	998
Risk-free interest rate	6.2%	4.7%	5.8%
Expected life in years	7.5	7.5	7.2
Expected volatility	0.437	0.454	0.609
Expected dividends	0	0	0

Weighted Average Exercise Price and Fair Values of Options on the Date of Grant	1999	1998	1997
Options exercise prices are less than the market price			
Exercise price			$15.75
Fair value			$ 6.75
Options exercise prices are equal to the market price			
Exercise price	$46.13	$39.27	$21.38
Fair value	$26.62	$21.86	$14.58

The following table details the weighted average remaining contractual life of options outstanding at December 31, 1999 by range of exercise prices:

Exercise Price Range	Number of Shares Outstanding	Exercise Price	Remaining Contractual Life of Options Outstanding	Number of Shares Exercisable	Exercise Price
$ 0.00 to $ 4.00	754	$ 2.04	4.7 years	703	$ 2.04
$ 4.01 to $ 10.00	5,609	$ 7.33	4.7 years	5,457	$ 7.37
$10.01 to $ 20.00	605	$17.08	6.4 years	327	$17.10
$20.01 to $ 30.00	898	$21.36	7.9 years	333	$21.34
$30.01 to $ 40.00	1,041	$39.37	8.9 years	209	$39.37
$40.01 to $ 50.00	934	$46.13	9.9 years	0	$ 0.00
	9,841	$15.87	6.1 years	7,029	$ 8.90

stock option plans

On May 7, 1996, the Company's shareholders approved the 1996 Long-Term Incentive Plan ("1996 Plan"), which provides for the granting of 2,000 shares of Common Stock, in the form of incentive or non-qualified stock options, stock appreciation rights ("SARs"), restricted stock or other types of awards. Under the 1996 Plan, the exercise price for stock options may not be less than the fair market value of the underlying stock at the date of grant. On December 2, 1997, the Board of Directors approved an additional 4,000 shares of Common Stock for issue under the 1996 Plan. The 1996 Plan is scheduled to terminate on May 7, 2006, unless extended for a period of up to five years by action of the Board of Directors. Options generally will expire no later than ten years after the date on which they are granted and will become exercisable as directed by the Compensation Committee of the Board of Directors. An SAR may be granted alone or in conjunction with an option or other award. No SARs, restricted stock, or other types of awards were outstanding as of December 31, 1999.

The Company's 1994 Stock Option Plan ("1994 Plan") provided for the granting of 10,070 options to purchase shares of common stock to certain key employees of the Company. The exercise price of the options was determined by a committee of the Board of Directors of the Company. Options granted have a term of ten years and vest in five equal installments on the first five anniversaries after the grant.

On May 7, 1996, the Company's shareholders approved the 1996 Non-Employee Director Deferred Compensation Plan ("Deferred Compensation Plan") and the 1996 Non-Employee Director Stock Option Plan ("Director Stock Option Plan"). Under the Deferred Compensation Plan, outside directors may elect to defer their fees and credit such fees to either a cash account which earns interest at a market-based rate or to a common stock unit account, for which two hundred shares of Common Stock have been reserved. Under the Director Stock Option Plan, each outside director will receive an annual option to purchase two thousand shares of Common Stock. One hundred thousand shares of Common Stock may be issued under the plan. Options have a term of ten years and, with the exception of options granted in 1996, which vest in one year, vest in five equal installments on the first five anniversaries following the date of grant and have option prices no less than fair market value at the date of grant.

The following table summarizes stock option activity for the plans:

		Number of Shares	Price Per Share	Weighted Average Exercise Price
	Outstanding at December 31, 1996	10,524	$ 2.04 to $ 17.25	$ 6.66
Granted		998	$16.10 to $ 21.38	$ 21.20
Exercised		(530)	$ 2.04 to $ 17.11	$ (3.95)
Canceled		(72)	$ 4.75 to $ 17.11	$(10.03)
	Outstanding at December 31, 1997	10,920	$ 2.04 to $ 21.38	$ 8.10
Granted		1,056	$18.78 to $ 39.38	$ 39.27
Exercised		(1,388)	$ 2.04 to $ 21.38	$ (4.13)
Canceled		(14)	$16.10 to $ 21.38	$(19.84)
	Outstanding at December 31, 1998	10,574	$ 2.04 to $ 39.38	$ 11.71
Granted		934	$46.13	$ 46.13
Exercised		(1,636)	$ 2.04 to $ 39.38	$ (6.06)
Canceled		(31)	$17.11 to $ 39.38	$(24.57)
	Outstanding at December 31, 1999	9,841	$ 2.04 to $46.13	$ 15.87

Options exercisable at December 31, 1999, 1998 and 1997 were 7,029, 6,564 and 6,056, respectively. The weighted average exercise prices of options exercisable at December 31, 1999, 1998 and 1997 were $8.90, $7.33 and $6.22, respectively. Available stock options for grant at December 31, 1999 were 2,527.

employee stock purchase plan

On February 26, 1996, the Company adopted the 1996 Employee Stock Purchase Plan under which eligible employees may contribute up to 15% of their earnings toward the quarterly purchase of the Company's Common Stock. The plan makes available 500 shares of the Company's Common Stock commencing October 1, 1996. As of December 31, 1999, approximately 123 shares have been issued under the plan. Each plan period lasts three months beginning on January 1, April 1, July 1, and October 1 of each year. The purchase price for each share of stock is the lesser of 90% of the market price on the first day of the plan period or 100% of the market price on the last day of the plan period. No compensation expense is recorded in connection with the plan.

11. EARNINGS PER SHARE

Basic and diluted EPS calculations are detailed as follows:

	Year Ended 1999		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Net income	$122,318		
Accretion of and 6% dividend on preferred stock	(825)		
Gain on redemption of preferred stock	383		
Income per basic common share from operations	$ 121,876	61,506	$ 1.98
Effect of dilutive securities:			
Options outstanding		4,394	
Options exercised		416	
Income per diluted common share from operations	$ 121,876	66,316	$ 1.84

	Year Ended 1998		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Net income	$ 74,399		
Accretion of and 6% dividend on preferred stock	(963)		
Income per basic common share from operations	$ 73,436	59,860	$ 1.23
Effect of dilutive securities:			
Options outstanding		4,404	
Options exercised		378	
Income per diluted common share from operations	$ 73,436	64,642	$ 1.14

	Year Ended 1997		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Net (loss)	$ (8,288)		
Accretion of and 6% dividend on preferred stock	(942)		
(Loss) per basic common share from operations	$ (9,230)	58,254	$ (.16)
Effect of dilutive securities		—	
(Loss) per diluted common share from operations	$ (9,230)	58,254	$ (.16)

For the years ended December 31, 1999, 1998 and 1997, the Company had 0, 1,050 and 10,920 stock option securities that were antidilutive, respectively. These securities were not included in the computation of diluted EPS.

12. COMPREHENSIVE INCOME

Comprehensive income details follow:

Year Ended December 31	1999	1998	1997
Net income (loss)	$122,318	$74,399	$ (8,288)
Foreign currency translation adjustments before income taxes	(1,333)	(58)	(3,976)
Income tax (benefit)	(360)	(13)	(795)
Foreign currency translation adjustments, net of tax	(973)	(45)	(3,181)
Other comprehensive (loss)	(973)	(45)	(3,181)
Comprehensive income (loss)	$121,345	$74,354	$(11,469)

13. RETIREMENT PLANS

The Company has two retirement plans for employees: the Waters Employee Investment Plan, a defined contribution plan, and the Waters Retirement Plan, a defined benefit cash balance plan.

In conjunction with its 1994 acquisition of the predecessor HPLC business of Millipore, the Company had asserted a claim contending that Millipore had understated the amount of assets it was obligated to transfer from the Millipore retirement plan to the Waters Retirement Plan. The Federal court subsequently ruled in favor of Millipore's position with respect to the claim. On appeal, the Federal court ruling was upheld, and $2,440 was transferred to the Waters Retirement Plan on June 2, 1998.

U.S. employees are eligible to participate in the Waters Employee Investment Plan after one month of service. Employees may contribute from 1% to 20% of eligible pay on a pre-tax basis. The Company makes a matching contribution of 50% for contributions up to 6% of eligible pay. Employees are 100% vested in company matching contributions after one year of service. For the years ended December 31, 1999, 1998 and 1997, the Company's matching contributions amounted to $1,984, $1,839 and $1,559, respectively. Effective January 1, 1998, the Micromass, Inc. 401(k) Plan was merged into and YMC employees joined the Waters Employee Investment Plan.

U.S. employees are eligible to participate in the Waters Retirement Plan after one year of service. The Company makes an annual contribution to each employee's account as a percentage of eligible pay based on years of service. In addition, each employee's account is credited for investment returns at the beginning of each year for the prior year at the average 12-month Treasury Bill rate plus 0.5%, limited to a minimum rate of 5% and a maximum rate of 10%. An employee does not vest until the completion of five years of service at which time the employee becomes 100% vested.

The net periodic pension cost under SFAS 87 is made up of several components that reflect different aspects of the Company's financial arrangements as well as the cost of benefits earned by employees. These components are determined using the projected unit credit actuarial cost method and are based on certain actuarial

assumptions. The Company's accounting policy is to reflect in the projected benefit obligation all benefit changes to which the Company is committed as of the current valuation date; use a market-related value of assets to determine pension expense; amortize increases in prior service costs on a straight-line basis over the expected future service of active participants as of the date such costs are first recognized; and amortize cumulative actuarial gains and losses in excess of 10% of the larger of the market-related value of plan assets and the projected benefit obligation over the expected future service of active participants. Summary data for the Waters Retirement Plan are presented in the following tables:

Reconciliation of Projected Benefit Obligation	1999	1998
Benefit obligation, January 1	$ 20,930	$ 15,904
Service cost	2,878	2,513
Interest cost	1,696	1,369
Employee rollovers	45	160
Actuarial (gain) loss	(2,544)	1,312
Disbursements	(295)	(328)
Benefit obligation, December 31	$ 22,710	$ 20,930

Reconciliation of Fair Value of Assets	1999	1998
Fair value of assets, January 1	$ 17,162	$ 16,008
Actual return on plan assets	1,896	1,322
Company contributions	4,078	—
Disbursements	(295)	(328)
Employee rollovers	45	160
Fair value of assets, December 31	$ 22,886	$ 17,162

Reconciliation of Funded Status, December 31	1999	1998
Projected benefit obligation	$(22,710)	$(20,930)
Fair value of plan assets	22,886	17,162
Projected benefit obligation less than (in excess of) fair value of plan assets	176	(3,768)
Unrecognized prior service cost	(1,225)	(1,324)
Unrecognized net actuarial (gain) loss	(2,597)	198
Accrued benefit (liability)	$ (3,646)	$ (4,894)
The projected benefit obligation was calculated using the following weighted average assumptions:		
Discount rate	8.00%	7.00%
Return on assets	9.00%	9.00%
Increases in compensation levels	4.75%	4.75%

Components of Net Periodic Pension Cost, Year Ended December 31	1999	1998	1997
Service cost	$ 2,878	$ 2,513	$ 2,043
Interest cost	1,696	1,369	1,054
Return on plan assets	(1,645)	(1,391)	(1,190)
Net amortization:			
Prior service cost	(99)	(99)	(99)
Net actuarial (gain)	—	—	(39)
Net periodic pension cost	$ 2,830	$ 2,392	$ 1,769

Reconciliation of (Accrued) Pension Cost	1999	1998	1997
(Accrued) pension cost, January 1	$ (4,894)	$ (2,502)	$ (1,208)
FAS 87 (cost)	(2,830)	(2,392)	(1,769)
Contributions made during the year	4,078	—	475
(Accrued) pension cost, December 31	$ (3,646)	$ (4,894)	$ (2,502)

The Company also sponsors several unfunded defined benefit post-retirement plans covering U.S. employees. The plans provide medical insurance benefits and are, depending on the plan, either contributory or non-contributory. The Company's accrued post-retirement benefit obligation was $2,596 and $2,532 at December 31, 1999 and 1998, respectively, and is included in other liabilities in the consolidated balance sheets.

14. RELATED PARTY TRANSACTIONS

In 1996 and 1995, the Company made loans to certain executive officers of the Company. The loans are collateralized by a pledge of shares of common stock held by these executive officers. The 1995 loans bear interest at 5.83% per annum and mature on December 1, 2000. The 1996 loans bear interest at 5.65% per annum and mature on January 8, 2001. Loans receivable of $1,337 at December 31, 1999 and $2,436 at December 31, 1998 are included in other assets in the consolidated balance sheets.

In connection with the acquisition of the predecessor HPLC business on August 18, 1994, the Company and Millipore entered into a Transition Support and Service Agreement ("Transition Agreement") whereby Millipore agreed to (i) lease office space, (ii) transfer certain personnel, (iii) provide management information systems, administrative, distribution and facilities management support, (iv) provide access to its telephone network and (v) supply professional support services. The Transition was substantially complete as of December 31, 1996. The Company believes that the costs incurred under the Transition Agreement were representative of charges that would have been levied by independent third parties for similar services. The Company incurred net expenses, primarily rent, pursuant to this agreement of $875, $1,178 and $1,273, for the years ended December 31, 1999, 1998 and 1997, respectively. These expenses are included in selling, general and administrative expenses in the consolidated statements of operations.

During the years ended December 31, 1999, 1998 and 1997, the Company sold products and service totaling $66, $148 and $32, respectively, to Millipore. These sales are included in net sales in the consolidated statements of operations.

15. BUSINESS SEGMENT INFORMATION

SFAS 131 establishes standards for reporting information about operating segments in annual financial statements of public business enterprises. It also establishes standards for related disclosures about products and service, geographic areas and major customers. The Company evaluated its business activities that are regularly reviewed by the Chief Executive Officer for which discrete financial information is available. As a result of this evaluation, the Company determined that it has three operating segments: Waters, TAI and Micromass.

Waters is in the business of manufacturing and distributing HPLC instruments, columns and other consumables, and related service; Micromass is in the business of manufacturing and distributing mass spectrometry instruments that can be integrated and used along with other analytical instruments, particularly HPLC; and TAI is in the business of manufacturing and distributing thermal analysis and rheology instruments. For all three of these operating segments within the analytical instrument industry; economic characteristics, production processes, products and services, types and classes of customers, methods of distribution, and regulatory environments are similar. Because of these similarities, the three segments have been aggregated into one reporting segment for financial statement purposes. The accounting policies of the reportable segment are the same as those described in the Summary of Significant Accounting Policies. Please refer to the consolidated financial statements for financial information regarding the one reportable segment of the Company. The Company sells products and service within this reportable segment, detailed as follows:

Revenue	1999	1998	1997
Products	$ 569,504	$ 504,956	$ 371,928
Service	134,896	113,857	93,542
Total	$ 704,400	$ 618,813	$ 465,470

Geographic information is presented below:

1999	United States	Europe	Japan	Asia	Other Int'l	Elimination	Total
Sales:							
Unaffiliated sales	$289,538	$ 228,181	$65,137	$ 27,603	$ 51,134	$ —	$661,593
Unaffiliated export sales to Japan	—	16,119	—	—	—	—	16,119
Unaffiliated export sales to Asia	5,831	5,007	—	—	—	—	10,838
Unaffiliated export sales to Other Int'l	14,326	1,524	—	—	—	—	15,850
Transfers between areas	182,471	59,510	—	—	—	(241,981)	—
Total sales	$492,166	$ 310,341	$65,137	$ 27,603	$ 51,134	$ (241,981)	$704,400
Long-lived assets:							
Unaffiliated	$ 221,907	$ 100,516	$ 3,279	$ 192	$ 11,213	$ —	$337,107
Between affiliates	227,246	24,011	2,181	—	3,795	(257,233)	—
Total long-lived assets	$449,153	$ 124,527	$ 5,460	$ 192	$ 15,008	$ (257,233)	$337,107

Geographic information (continued):

1998	United States	Europe	Japan	Asia	Other Int'l	Elimination	Total
Sales:							
Unaffiliated sales	$ 258,050	$ 208,168	$ 46,098	$ 21,923	$ 44,578	$ —	$ 578,817
Unaffiliated export sales to Japan	—	12,199	—	—	—	—	12,199
Unaffiliated export sales to Asia	5,276	6,896	—	—	—	—	12,172
Unaffiliated export sales to Other Int'l	12,347	3,278	—	—	—	—	15,625
Transfers between areas	153,666	49,148	—	—	—	(202,814)	—
Total sales	$ 429,339	$ 279,689	$ 46,098	$ 21,923	$ 44,578	$ (202,814)	$ 618,813
Long-lived assets:							
Unaffiliated	$ 225,811	$ 98,058	$ 2,775	$ 367	$ 11,658	$ —	$ 338,669
Between affiliates	234,652	20,963	2,180	—	3,790	(261,585)	—
Total long-lived assets	$ 460,463	$ 119,021	$ 4,955	$ 367	$ 15,448	$ (261,585)	$ 338,669

1997							
Sales:							
Unaffiliated sales	$ 187,136	$ 138,591	$ 46,077	$ 29,635	$ 37,744	$ —	$ 439,183
Unaffiliated export sales to Japan	74	4,132	—	—	—	—	4,206
Unaffiliated export sales to Asia	8,009	1,792	—	—	—	—	9,801
Unaffiliated export sales to Other Int'l	12,280	—	—	—	—	—	12,280
Transfers between areas	131,441	12,471	—	—	—	(143,912)	—
Total sales	$ 338,940	$ 156,986	$ 46,077	$ 29,635	$ 37,744	$ (143,912)	$ 465,470
Long-lived assets:							
Unaffiliated	$ 230,258	$ 103,500	$ 2,444	$ 550	$ 5,808	$ —	$ 342,560
Between affiliates	219,149	20,550	2,181	—	24	(241,904)	—
Total long-lived assets	$ 449,407	$ 124,050	$ 4,625	$ 550	$ 5,832	$ (241,904)	$ 342,560

The United States category includes Puerto Rico. The Other category includes Canada, South America, Australia, India, Eastern Europe and Central Europe. Transfer sales between geographical areas are generally made at a discount from list price. None of the Company's individual customers accounts for more than 2% of annual Company sales.

16. QUARTERLY RESULTS

The Company's unaudited quarterly results are summarized below:

1999	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Net sales	$160,362	$172,280	$171,090	$200,668	$704,400
Cost of sales	60,622	63,712	61,903	70,899	257,136
Gross profit	99,740	108,568	109,187	129,769	447,264
Selling, general and administrative expenses	54,504	55,537	57,075	59,477	226,593
Research and development expenses	8,686	9,021	8,634	9,753	36,094
Goodwill and purchased technology amortization	2,045	2,034	1,999	1,990	8,068
Operating income	34,505	41,976	41,479	58,549	176,509
Interest expense, net	3,033	2,379	1,794	1,742	8,948
Income from operations before income taxes	31,472	39,597	39,685	56,807	167,561
Provision for income taxes	8,498	10,691	10,715	15,339	45,243
Net income	22,974	28,906	28,970	41,468	122,318
Accretion of and dividend on preferred stock	(244)	(245)	(247)	(89)	(825)
Gain on redemption of preferred stock	—	—	—	383	383
Net income available to common stockholders	$ 22,730	$ 28,661	$ 28,723	$ 41,762	$121,876
Net income per basic common share	$ .37	$ .47	$ .47	$ .67	$ 1.98
Weighted average number of basic common shares	60,894	61,222	61,754	62,204	61,506
Net income per diluted common share	$ .35	$ .43	$ .43	$ .63	$ 1.84
Weighted average number of diluted common shares and equivalents	65,840	66,167	66,611	66,621	66,316
Stock price range	36 1/4 – 54 1/8	46 1/2 – 56 1/2	48 3/4 – 67 5/8	37 – 66 1/8	36 1/4 – 67 5/8

1998	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Net sales	$138,725	$149,311	$151,793	$178,984	$618,813
Cost of sales	51,920	55,848	57,832	66,897	232,497
Revaluation of acquired inventory	16,500	—	—	—	16,500
Gross profit	70,305	93,463	93,961	112,087	369,816
Selling, general and administrative expenses	49,988	51,952	49,276	54,995	206,211
Research and development expenses	8,372	8,246	8,512	9,303	34,433
Goodwill and purchased technology amortization	2,275	2,231	2,537	2,304	9,347
Operating income	9,670	31,034	33,636	45,485	119,825
Interest expense, net	5,063	4,888	4,416	3,911	18,278
Income from operations before income taxes	4,607	26,146	29,220	41,574	101,547
Provision for income taxes	4,363	6,033	7,264	9,488	27,148
Net income	244	20,113	21,956	32,086	74,399
Accretion of and dividend on preferred stock	(239)	(240)	(241)	(243)	(963)
Net income available to common stockholders	$ 5	$ 19,873	$ 21,715	$ 31,843	$ 73,436
Net income per basic common share	$ .00	$ .33	$ .36	$ .53	$ 1.23
Weighted average number of basic common shares	59,416	59,754	60,028	60,330	59,860
Net income per diluted common share	$ .00	$ .30	$ .33	$ .49	$ 1.14
Weighted average number of diluted common shares and equivalents	66,322	67,038	64,822	65,228	64,642
Stock price range	18 1/4 – 26	24 21/32 – 31 7/16	26 3/16 – 34 5/32	26 9/16 – 43 3/4	18 1/4 – 43 3/4

SELECTED FINANCIAL DATA

	The Company						Predecessor Business (A)		
(In thousands, except per share and employees data)	Year Ended December 31, 1999	Year Ended December 31, 1998	Year Ended December 31, 1997	Year Ended December 31, 1996	Year Ended December 31, 1995	August 19 to December 31, 1994	January 1 to August 18, 1994	Year Ended December 31, 1993	Year Ended December 31, 1992
STATEMENT OF OPERATIONS DATA:									
Net sales	$704,400	$618,813	$465,470	$391,113	$332,972	$131,057	$176,097	$304,927	$309,287
Cost of sales	257,136	232,497	173,275	145,254	126,216	49,740	73,446	124,387	123,342
Revaluation of acquired inventory (B)	—	16,500	16,500	6,100	925	38,424	—	—	—
Gross profit	447,264	369,816	275,695	239,759	205,831	42,893	102,651	180,540	185,945
Selling, general and administrative expenses	226,593	206,211	167,290	148,513	132,746	44,522	85,216	132,452	138,318
Research and development expenses	36,094	34,433	25,750	20,898	17,681	6,790	13,399	18,525	19,142
Goodwill and purchased technology amortization	8,068	9,347	6,468	5,219	3,629	1,227	—	—	—
Expensed in-process research and development (B)	—	—	55,000	19,300	—	53,918	—	—	—
Management fee (B)	—	—	—	—	5,393	552	—	—	—
Restructuring charge (B)	—	—	—	—	—	3,500	—	13,000	—
Operating income (loss)	176,509	119,825	21,187	45,829	46,382	(67,616)	4,036	16,563	28,485
Interest expense, net (C)	8,948	18,278	13,720	14,740	30,315	12,011	828	2,072	2,107
(Gains) on cash flow hedges (B)	—	—	—	—	(1,175)	(923)	—	—	—
Income (loss) from operations before income taxes	167,561	101,547	7,467	31,089	17,242	(78,704)	3,208	14,491	26,378
Provision for income taxes	45,243	27,148	15,755	11,230	3,129	1,487	916	4,169	6,180
Income (loss) from operations	122,318	74,399	(8,288)	19,859	14,113	(80,191)	2,292	10,322	20,198
Income (loss) from discontinued operations, net of tax (B)	—	—	—	—	—	(7,213)	(448)	(9)	108
Income (loss) before extraordinary item	122,318	74,399	(8,288)	19,859	14,113	(87,404)	1,844	10,313	20,306
Extraordinary item-(loss) on early retirement of debt (B)	—	—	—	(22,264)	(12,112)	—	—	—	—
Income (loss) before cumulative effect of change in accounting principle	122,318	74,399	(8,288)	(2,405)	2,001	(87,404)	1,844	10,313	20,306
Cumulative effect of change in accounting principle (B)	—	—	—	—	—	—	—	—	(2,228)
Net income (loss)	122,318	74,399	(8,288)	(2,405)	2,001	(87,404)	$ 1,844	$ 10,313	$ 18,078
Less: Accretion of and dividend on preferred stock, net of gain	442	963	942	921	902	330			
Net income (loss) available to common stockholders	$121,876	$ 73,436	$ (9,230)	$ (3,326)	$ 1,099	$(87,734)			

SELECTED FINANCIAL DATA (CONTINUED)

	The Company						Predecessor business (A)		
(In thousands, except per share and employees data)	Year Ended December 31, 1999	Year Ended December 31, 1998	Year Ended December 31, 1997	Year Ended December 31, 1996	Year Ended December 31, 1995	August 19 to December 31, 1994	January 1 to August 18, 1994	Year Ended December 31, 1993	Year Ended December 31, 1992
Income (loss) per basic common share:									
Income (loss) per common share before extraordinary item	$ 1.98	$ 1.23	$ (.16)	$ .33	$ .30	$ (1.87)			
(Loss) per common share from discontinued operations	—	—	—	—	—	(.17)			
Extraordinary (loss) per common share	—	—	—	(.39)	(.27)	—			
Net income (loss) per common share	$ 1.98	$ 1.23	$ (.16)	$ (.06)	$ .03	$ (2.04)			
Weighted average number of basic common shares	61,506	59,860	58,254	57,682	44,652	42,964			
Income (loss) per diluted common share:									
Income (loss) per common share before extraordinary item	$ 1.84	$ 1.14	$ (.16)	$ .30	$ .27	$ (1.87)			
(Loss) per common share from discontinued operations	—	—	—	—	—	(.17)			
Extraordinary (loss) per common share	—	—	—	(.35)	(.25)	—			
Net income (loss) per common share	$ 1.84	$ 1.14	$ (.16)	$ (.05)	$ .02	$ (2.04)			
Weighted average number of diluted common shares and equivalents	66,316	64,642	58,254	63,256	49,164	42,964			
BALANCE SHEET AND OTHER DATA (D):									
Working capital	$ 49,489	$ 53,459	$ 45,843	$ 61,227	$ 56,385	$ 87,357		$100,528	$112,905
Total assets	$584,437	$577,701	$552,059	$365,502	$299,816	$331,598		$189,592	$199,513
Long term debt, including current maturities (C)	$ 91,080	$218,250	$305,340	$210,470	$158,500	$275,000		$ —	$ —
Redeemable preferred stock	—	$ 9,058	$ 8,096	$ 7,153	$ 6,232	$ 5,330		$ —	$ —
Stockholders' equity (deficit)/parent company investment	$292,162	$150,119	$ 62,297	$ 57,780	$ 58,118	$(22,670)		$149,095	$163,157
Employees	2,968	2,758	2,640	2,135	1,934	2,021	2,069	2,009	2,180
Depreciation and amortization for the period	$ 28,947	$ 27,248	$ 20,010	$ 16,709	$ 13,774	$ 4,394	$ 6,323	$ 9,265	$ 8,857
Capital expenditures for the period	$ 24,416	$ 20,616	$ 23,393	$ 13,822	$ 9,878	$ 2,191	$ 5,935	$ 8,439	$ 10,739

(A) Results of predecessor HPLC business of former parent Millipore Corporation acquired by Company on August 18, 1994.
(B) Nonrecurring charges and (gains).
(C) Interest expense through August 18, 1994 was an allocation of Millipore's worldwide net interest expense based upon the ratio of the Predecessor's net assets to Millipore's net assets. No debt obligations of Millipore were reflected on the Predecessor's balance sheets.
(D) As a publicly held company, the Company has not declared or paid any dividends on common stock.

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directors

Douglas A. Berthiaume
**Chairman, President
and Chief Executive Officer
Waters Corporation**

Joshua Bekenstein
**Managing Director
Bain Capital, Inc.**

Dr. Michael J. Berendt
**Senior Vice President
Bayer Corporation**

Philip Caldwell
**Chairman of the Board
and Chief Executive Officer (Retired),
Ford Motor Company**

Edward Conard
**Managing Director
Bain Capital, Inc.**

Dr. Laurie H. Glimcher
**Professor of Immunology and Medicine
Harvard School of Public Health
and Harvard Medical School**

William J. Miller
Independent Investor and Consultant

Thomas P. Salice
**President and Chief Executive Officer
AEA Investors, Inc.**

officers

Douglas A. Berthiaume
**Chairman, President
and Chief Executive Officer**

Arthur G. Caputo
**Senior Vice President
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Thomas W. Feller
**Senior Vice President
E-Business Initiative**

John R. Nelson
**Senior Vice President
Research, Development and Engineering**

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**Senior Vice President
Finance and Administration
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Brian K. Mazar
**Vice President
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Devette W. Russo
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John Ornell
**Vice President
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stockholders' meeting

**Date: May 4, 2000, 11 a.m.
Place: Waters Corporation
34 Maple Street
Milford, Massachusetts
Directions: Call 800-252-4752 Ext. 3314**

stocklist symbol

**NYSE: WAT
Form 10K**

A copy of the Company's 10K, filed with the Securities and Exchange Commission, is available without charge upon written request to:

**Waters Corporation
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Milford, Massachusetts 01757**

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Waters

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