

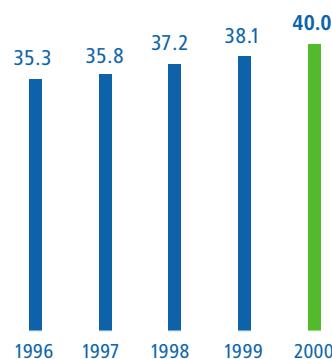


The P&G logo, consisting of the letters 'P&G' in a blue, stylized, italicized font.

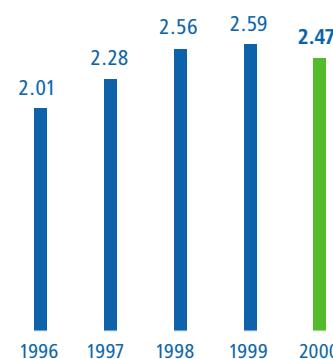
2000 ANNUAL REPORT

# Financial Summary

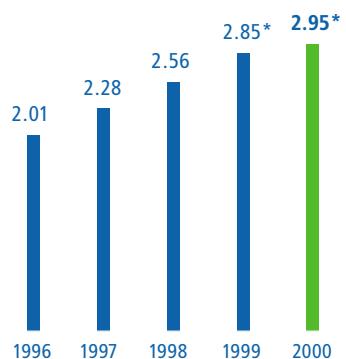
**NET SALES**  
billions of dollars



**DILUTED NET EARNINGS**  
per common share



**CORE DILUTED NET EARNINGS**  
per common share



\* Excluding Organization 2005 program costs of \$.48 per share after tax in 2000 and \$.26 per share after tax in 1999.

Amounts in millions except per share amounts

	Years ended June 30		
	2000	1999	% change
Net Sales	<b>\$39,951</b>	\$38,125	5%
Operating Income	<b>5,954</b>	6,253	-5%
Core Operating Income <sup>†</sup>	<b>6,768</b>	6,734	1%
Net Earnings	<b>3,542</b>	3,763	-6%
Core Net Earnings <sup>†</sup>	<b>4,230</b>	4,148	2%
Per Common Share			
Diluted Net Earnings	<b>2.47</b>	2.59	-5%
Core Diluted Net Earnings <sup>†</sup>	<b>2.95</b>	2.85	4%
Dividends	<b>1.28</b>	1.14	12%

<sup>†</sup> Excludes Organization 2005 program costs.

## Dear Shareholders,

Fiscal 2000 was a tough year. Earnings came in below the goals we had originally established and felt we could achieve. In our drive to meet changes in the marketplace – globalization, the Internet, consolidation among retailers – we tried to do too much too fast. As a result, we lost critical balance in several key areas:

- > We grew top-line sales more than we had over the past few years, but bottom-line earnings growth came in below historical rates.
- > We introduced more new brands than during any other period in our history, but our biggest, most profitable brands didn't grow at acceptable rates.
- > We invested for the future – in new businesses and developing markets – but some costs grew faster than revenues.
- > We made important leadership changes, placing people into new jobs as part of our organizational restructuring, but we lost continuity in some parts of the business.

Even in the face of these challenges, our core earnings were above a year ago – delivering record results.

- > Net sales grew 5% on 4% unit volume growth – very strong improvement over last year, when volume was flat.
- > Net earnings were \$3.5 billion or \$2.47 per share, compared to \$3.8 billion or \$2.59 per share in 1999.
- > Core net earnings, which exclude \$688 million of Organization 2005 costs, were \$4.2 billion. Core earnings per share grew 4% to \$2.95.

While these results demonstrate progress, P&G is capable of delivering better results. We are confident we can reestablish the balance needed to deliver top-line revenue growth and bottom-line earnings growth. We have the core competencies and strengths to win; our new organizational design remains fundamentally right; and we have a focused plan to drive both sales and profit growth.

### FUNDAMENTALS TO WIN

Our goal is simple: to create the most successful global brands in every category everywhere we compete. And we have the strengths to do it.

Today P&G has more leading brands than any other consumer products company in the world. We have strong relationships with our retail customers around the world. And our innovative people continue to set industry standards.



*A. G. Lafley and John E. Pepper*



#### TEN P&G BRANDS HAVE BILLION-DOLLAR SALES

**Big Leadership Brands** P&G's megabrands generate significant sales and hold strong leadership positions. Eight brands are global leaders in their categories. Ten P&G brands each generate over a billion dollars in sales a year – far more billion-dollar brands than our key competitors. Our 10 largest brands, together, would be a Fortune 100 company. And we have several other brands already in the market that we believe have billion-dollar potential.

**Superior Customer Relationships** In a recent U.S. survey by Cannondale Associates, retailers were asked to rank manufacturers on a number of competencies. P&G was ranked number one in virtually every category:

- > “Clearest Company Strategy”
- > “Brands Most Important to Retailers”
- > “Best Brand Marketers Overall”
- > “Most Innovative Marketing Programs”

This high regard by our customers is increasingly important. Today, our top 30 customers represent nearly 45% of our total volume, and we expect them to account for more than half of our volume by 2005. More importantly, these customers contributed about two-thirds of our recent volume growth and have a strong potential to drive future growth.

**Innovation Leadership** The quality of our people continues to be our most valuable asset. And that quality is demonstrated by the innovation of our organization.

- > More than 8,000 scientists and researchers are accelerating the pace of new product and technology invention.
- > We have a global innovation network of 18 technical centers in nine countries on four continents.
- > P&G holds more than 27,000 patents and applies for 3,000 more each year – or roughly 10 a day! In fact, we are among the top 10 patent-producing companies in the world – well ahead of any other consumer products company.

Importantly, innovation isn't limited to products alone. P&G people are innovative leaders in every part of our business. For example:

- > We are pioneering new Internet-based business models. Last year, we launched our initial Internet brand, reflect.com, the first to offer truly personalized beauty care products online. This venture

is enabling us to get valuable experience in both Internet marketing and mass customization of products.

> We led the formation of a consortium of more than 50 companies to create a consumer products industry marketplace called Transora. This business-to-business portal will enable companies in our industry to buy and sell more than \$200 billion of supplies and services annually, and will result in substantial savings for P&G.

What we hope you see from these examples is that P&G – through the men and women who make up our Company – is more than ever an industry innovator and leader.

### RIGHT ORGANIZATION DESIGN

To gain even more value from our basic strengths, we have changed the way we're organized and the way we work. Our goals were to make it easy for innovation to flow across the enterprise and around the world; to learn directly from consumers as early as possible; and to profitably commercialize the best ideas and inventions quickly.

We're doing all that. Global Business Units flow product innovations across categories and geographic markets. Market Development Organizations get initiatives to local markets faster, more creatively, at less cost. And our Global Business Services organization leverages our size to deliver better-quality services internally at significantly lower cost to the Company.

We designed our new organization to be global and local at the same time – a paradoxical challenge that we believe is key to our future success.

### OUR ACTION PLAN FOR PROFITABLE GROWTH

We have learned a lot from our experience over the past year, and have applied this learning to a four-point plan to drive both sales and profit growth.

First, we are focusing sharply on *building our biggest, strongest global brands*, the core of our business. We need to be sure we are consistently growing our market share on these brands.

Second, we are *making tougher choices about investing in new products and new businesses*. We'll use fast-cycle learning techniques to get rapid consumer validation of our biggest ideas, and commercialize those ideas more quickly worldwide.

Third, we are *working hard to get even more value from our strong customer relationships*. We'll build on this strength by collaborating more closely with customers. The result will be even more innovative marketing programs for new and established brands alike.

### P&G'S ACTION PLAN FOR GROWTH

01

BUILD BIG BRANDS

02

INVEST IN INNOVATION

03

DEEPEN CUSTOMER PARTNERSHIPS

04

REDUCE COSTS AND IMPROVE  
CASH MANAGEMENT

Fourth, we are *placing greater emphasis on rigorous cost control and cash management*. We deployed teams to drive out waste and to find new efficiencies in overhead management, marketing support and product costs. In addition, we've renewed our emphasis on capital investment and working-capital efficiency.

We highlight some of our efforts in these areas on pages 8 – 11.

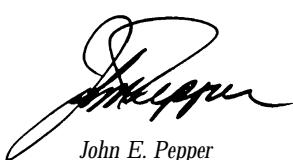
#### **A PASSION FOR WINNING**

P&G people are accustomed to being winners and to doing what we commit to do – or better. We take great pride in our brands, our innovation leadership, our customer relationships, the trust we've earned from consumers – and our ability to deliver steady, reliable growth for our shareholders.

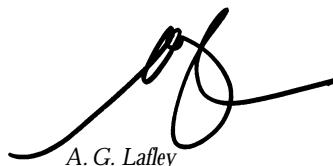
Whenever our leadership in any of these areas is challenged, we take it seriously. And personally. For example, in the mid-'80s, we faced a significant financial setback. Earnings for fiscal 1985 declined 29% from the previous year. Back then we addressed the issues head-on, just as we're doing now. In the 15 years since, sales have grown from \$13.6 billion to \$40 billion – a rate of 7% per year. And profits have increased from a little more than \$600 million to \$4.2 billion, an average growth rate of more than 13% per year.

We don't point to these numbers as any kind of forecast, but they do underscore that we've faced major problems in the past and have overcome them. By addressing those problems just as we are tackling present issues, we continued to deliver the leadership levels of growth that both you and we expect from P&G.

We are at our best when working on tough challenges because P&G people have such a tremendous passion for winning. In fact, that passion is our defining characteristic as an organization. And it is that passion that will ensure P&G maintains its rightful place as the preeminent consumer products company in the world.



John E. Pepper  
Chairman of the Board  
August 1, 2000



A. G. Lafley  
President and Chief Executive  
August 1, 2000

#### **MANAGEMENT CHANGE**

After 30 years of service, Durk I. Jager retired July 1 as chairman, president, chief executive and a director of P&G. His visionary leadership and many contributions accelerated the pace of product innovation for the Company. He has left a legacy of innovation, not only in new brands, but also in areas such as use of the Internet and strengthening of customer relations. His emphasis on a culture that reaches out for breakthroughs has provided a strong foundation for future progress.

# Up-front with A.G.

**ON JUNE 8, A.G. LAFLEY WAS NAMED PRESIDENT AND CHIEF EXECUTIVE OF P&G. HERE HE ANSWERS SOME OF THE QUESTIONS HE'S BEEN ASKED SINCE THEN ABOUT THE STATE OF P&G'S BUSINESS AND HIS PLANS FOR THE FUTURE.**



*A.G. Lafley, President and Chief Executive*

**Q: Will P&G's growth strategy change under the new leadership?**

*A: No. The basic building blocks of our growth strategy remain unchanged:*

- > *Building our established and most profitable brands*
- > *Introducing new brands and entering new categories*
- > *Acquiring brands that can help us strengthen existing businesses or enter new businesses and markets*
- > *Improving the mix of our brand portfolio with more premium-performance, higher-priced products*

*In any given year, the contribution from each of these elements will vary. But taken together, these building blocks provide the basis for balanced growth in top-line sales and bottom-line profits.*

**Q: How will you balance investment in big, established brands and new brands?**

*A: Our biggest flagship brands are popular with consumers, often are the leader in their product category and are the greatest, sustainable source of profits and cash flow. Consequently, we must always ensure that these brands are strong and growing. At the same time, our future depends on our ability to continually create tomorrow's big brands. To do that, we will judiciously invest in new brands that we believe have global leadership potential.*

*The key is striking the right balance. We did it in our fabric & home care business in North America this past year, where we delivered double-digit sales growth, with gains on big brands like Tide and Downy, and we increased profits, while making significant investments in new brands like Febreze and Swiffer.*

**Q: How will you sharpen P&G's ability to control costs?**

*A: Over the past year, some of our costs grew faster than sales. A number of factors were responsible, including big investments in new brands and the overall impact of massive organizational change.*

*We've now redoubled our efforts to leverage a traditional P&G strength – tough cost control. We're focusing on:*

- > *Making more choiceful investments in innovation*
- > *Tying marketing spending more tightly to sales potential*
- > *Using new approaches to target consumers more efficiently*
- > *Holding the rate of increase in product costs below the rate of inflation*
- > *Working aggressively to contain overhead costs*

*All of this is meant to ensure that we don't ask consumers to pay for costs that don't add value.*

**Q: What do you see as P&G's core source of competitive advantage?**

*A: P&G's core strength is its ability to build big, leadership brands. Our goal is to continue doing that better and more consistently than any other company in the world.*

*Our success in building brands is based on three factors:*

- > *Understanding consumer needs. We talk with more than 5.5 million consumers worldwide every year. We use a variety of approaches, from in-home visits to concept and product testing via the Internet. In this way, we're able to discover new, unmet and often unarticulated consumer needs.*
- > *Inventing new product technologies. This is what we call "connecting what's needed with what's possible." We have more than 27,000 patented technologies and, as a result, can simply find more innovative ways to turn our best ideas into improved products that better meet consumer needs.*
- > *Commercializing and expanding new products globally. On the strength of our marketing and distribution partnerships, we can introduce big, new ideas faster than ever before.*

*These capabilities have helped us win with consumers around the world. Shoppers buy P&G products more than 20 billion times a year – which is the basis for a great deal of our confidence in the Company's future, and in the strength of P&G's core competencies as an innovator and marketer.*

**Q: Why do you believe the new organization design you implemented last year is still right for the future?**

*A: It's right because it extends the competitive advantages that I just talked about. It also positions us to adapt to changes in the external environment.*

*The Internet, globalization and the consolidation of the retail industry have combined to create a dynamic global marketplace. To lead in such an environment, you have to be big and small at the same time. More specifically, you have to be a global company that can operate like a small local business in every part of the world. Our new structure helps us to do that.*

*Swiffer is a good example. This brand is built on a global marketing and technology platform – meaning the product and the marketing programs supporting it can be rolled out worldwide. We've expanded Swiffer faster than any other brand in our history. Our local Market Development Organizations were essential to this. They worked with retail customers and tailored marketing plans to win with local consumers. As a result, we've created a brand with billion-dollar potential.*

*The transition to this new organizational design is proving more challenging than we expected. But it is fundamentally the right approach and we're on track to get the benefits we envisioned.*



**Q: What criteria guide your acquisition plans?**

*A: We look for acquisitions that will provide a good financial return for our shareholders, while considering key strategic issues:*

- > *We want brands that can help expand our leadership in existing categories. Tampax, for example, strengthened our feminine care business by getting us into the tampon segment.*
- > *We also look for opportunities that help us enter entirely new businesses, such as Iams, which took us into premium pet health and nutrition.*

*In addition to these basic criteria, we look for acquisitions with which we can leverage our considerable strengths in marketing, distribution scale and customer relationships. Iams is actually a great example of all of this: It brings us product technology that leverages our own competencies in health and nutrition, and a brand that we can expand worldwide with our superior marketing and distribution know-how.*

*Historically, we've focused on small-to-medium size acquisitions. Of course, if much larger opportunities emerge, we'll look at them, but they're not essential to our growth goals.*

**Q: Why should I invest in P&G when companies in other sectors, like technology, are growing at a faster rate?**

*A: Investment decisions require an assessment of risk. Many high-growth, high-return stocks come with a relatively high risk. Investors willing to absorb that risk will pay a share price premium.*

*P&G, on the other hand, delivers real profits and significant cash flow today with an expectation of steady growth in the years ahead – a combination we have proven can result in meaningful share price appreciation.*

*We're not trying to be a high-risk, high-growth company. We're committed to delivering the same kind of reliable shareholder returns that we've delivered historically – and that is precisely the reason many people will continue to invest in us. In fact, it may be the reason why we've added more than 200,000 new shareholders in the past year alone.*

# Global Laundry Leader



*P&G is focusing on four areas that are critical to moving our business ahead: building our biggest, most established brands; making good investment choices in innovation and new businesses; deepening our relationships with customers; and managing costs and cash more rigorously. The following examples demonstrate how we are doing this:*

## ACTION PLAN

10

## BUILD BIG BRANDS

### CASE IN POINT > TIDE AND ARIEL

**Investing in our largest brands is providing an engine for growth. Continuous innovation in products and marketing is paying off.**

- > Tide and its sister brand outside the U.S., Ariel, together have more sales than any other P&G brand.
- > In the last 18 months, P&G has introduced several breakthrough innovations in Tide and Ariel: Tide with Bleach Sanitization in the U.S. and Ariel Bleach Plus in Japan; Tide with Activated Hydrogen Peroxide in the U.S. and Ariel Hygiene in Europe; Tide Deep Clean, TideKick, Tide WearCare in the U.S. and Ariel

Essentials in Europe; and soon Tide Rapid Action Tablets, which follow Ariel Tablets in Europe.

- > All of these initiatives have been designed to do one thing: delight consumers. And what's the result? U.S. Tide ended last fiscal year with a market share more than four times larger than the nearest competitor, contributing to record results for North America fabric and home care. Ariel is sold in 115 countries and is the first or second leading brand in more than 25 of them.



## A New Way to Grow

**INVEST IN INNOVATION AND NEW BUSINESS**  
**CASE IN POINT > IAMS**

02

**ACTION PLAN**

**We are focusing on making optimal choices for our investments in new brands and product categories, to maximize commercial success and financial return.**

- > In September 1999, after careful scrutiny, P&G entered an entirely new business when it acquired the Iams Company, a world leader in pet health and nutrition. Iams is very similar to P&G in its core values, strong brand names, research investment for superior products, and history of leading innovation.
- > We quickly assessed the growth opportunity. Globally, we are only scratching the surface of

Iams' potential with about a 4% share of the \$25 billion commercially prepared pet food market. Iams sells its Eukanuba and Iams brands of dog and cat food in 77 countries.

- > In the six months following the acquisition, P&G expanded the Iams brand to 25,000 additional retail outlets in North America. (Its super-premium Eukanuba brand continues to be sold only in pet specialty stores.)
- > The results of this expansion have been outstanding. This year, the Iams Company reached \$1 billion in sales, up 25% from when P&G acquired it.



## Partnering for a Winning Launch

### ACTION PLAN



### DEEPEN CUSTOMER RELATIONSHIPS

#### CASE IN POINT > PHYSIQUE

**P&G is partnering with customers to build strategic relationships that create a strong return on investment for both.**

> In January 2000, P&G launched a revolutionary line of hair care products based on our best science and a deep understanding of Physique's target consumer. This understanding enabled the brand to reach its audience in very different ways – where they live, where they work, where they play and where they shop. In-store consultants helped consumers find the right products for the style they wanted.

- > Working closely with retailers to create a prestige shopping experience, we created store displays and point-of-sale materials. These addressed a key source of dissatisfaction for consumers – not enough information in the store to help them select the right product.
- > The result? Within six months of its launch, Physique was already one of the top 10 hair care brands in the U.S. This was the fastest new brand introduction in this \$7 billion market.

# Smart Savings



## REDUCE COSTS AND IMPROVE CASH MANAGEMENT

GBS employees Maricarmen Pijem and Miguel Pantoja

CASE IN POINT > GBS

04

**ACTION PLAN**

**P&G has a long history of cost control, and we have focused on this issue again as a key part of our Action Plan.**

- > Global Business Services (GBS) has designed, and now is putting in place, an internal system of Web-based services to deliver the right level of service at the right price and at significantly lower overall cost to the Company.
- > Business activities which previously were dispersed across many business units – such as employee

services, workplace services, purchasing, customer logistics, accounting and financial reporting, and information technology – are being consolidated in key service centers around the world.

- > GBS already has generated significant savings by simplifying, standardizing and automating the way we work. It is on track to deliver at least \$200 million in after-tax savings annually by 2004.

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## RESULTS OF OPERATIONS

The Company's results reflected strong sales growth, with earnings impacted by higher spending on product initiatives and Organization 2005 costs.

The Company introduced several new brands, expanded strong established brands into new markets, acquired new businesses and introduced significant product upgrades on major brands. The increased innovation resulted in significant investments at a time when commodity costs also increased, currency had a negative impact, the Company incurred additional costs to transition into its new global organizational structure and competition reacted strongly to business initiatives.

Net earnings were \$3.54 billion or \$2.47 per share compared to \$3.76 billion or \$2.59 per share in 1999. Results included charges of \$688 million after tax for current year costs of the Organization 2005 program. Organization 2005 is the Company's multi-year program designed to realign the organization into global product-based segments from a geographic structure and change the work processes and culture.

For the fiscal year, core net earnings, which exclude Organization 2005 costs, increased 2% to \$4.23 billion. Core net earnings per share were \$2.95, an increase of 4% from the prior year. Volume and sales progress drove core earnings growth, but were partially offset by higher spending, primarily behind new product initiatives.

Worldwide net sales for the current year were \$39.95 billion, an increase of 5% versus last year. Excluding a negative 2% exchange rate impact, net sales increased 7% on 4% unit volume growth. This growth reflects strong product initiative activity, the acquisition of the Iams pet health and nutrition business and progress on flagship brands, largely in fabric and home care.

Worldwide gross margin was 46.1%, compared to 44.8% in the prior year. Gross margin includes \$496 million in charges related to the Organization 2005 program. These charges consisted primarily of accelerated depreciation, asset write-downs and employee separation

costs. Excluding these charges, gross margin increased to 47.4%, reflecting the impact of high-performance, premium-priced initiatives and effective cost management in the face of rising material costs.

Worldwide marketing, research and administrative expense was \$12.48 billion versus \$10.85 billion in the prior year. The increase to 31.2% of net sales from 28.4% was primarily due to increased spending on product initiatives. Organization 2005 costs increased marketing, research and administrative expense by \$318 million, primarily due to employee separation expenses. Excluding these charges, marketing, research and administrative expense increased 13% over 1999.

Operating income declined by 5%. Excluding the charges for Organization 2005, operating income improved 1% as business results were supplemented by lower employee benefit costs reflected in the Corporate segment.

Interest expense increased 11% to \$722 million on increased debt, primarily due to acquisitions and share repurchases. Other income, net, which consists primarily of interest and investment income, contributed \$304 million in the current year compared to \$235 million in the prior year, including impacts of the Company's ongoing minor brand divestiture program.

The Company's effective tax rate for the year was 36.0%, compared to 35.5% in the prior year. This change reflects a reduction in the core earnings rate, more than offset by the impact of tax rate effects from the Organization 2005 program. Excluding Organization 2005 costs and related tax effects, the effective tax rate was 33.4% compared to 34.4% in the prior year.

Net earnings margin was 8.9% versus 9.9% in the prior year. Excluding the Organization 2005 charges, core net earnings margin was 10.6%, down from 10.9% last year, reflecting the strong top-line growth offset by increased spending.

The Company's action plan for the next year focuses on balancing top-line and bottom-line progress: growing big brands in core categories, investing smartly in commercialization of innovation, driving out costs and improving cash flow.

**The following provides perspective on the year ended June 30, 1999, versus June 30, 1998:**

Worldwide net earnings were \$3.76 billion in 1999, flat versus \$3.78 billion in 1998.

Worldwide net sales in 1999 were \$38.13 billion, up 3% from \$37.15 billion in the prior year on flat unit volume. The increase in sales was attributable to improved pricing in all regions and favorable volume and product mix in North America, partially offset by exchange impacts. Unfavorable exchange rates, primarily in Asia and Latin America, depressed sales by 1% for the year.

Worldwide gross margin increased to 44.8% from 43.8% in 1998, reflecting effective cost savings, primarily in North America. Organization 2005 charges increased cost of products sold by \$443 million in 1999, as a result of asset write-downs and accelerated depreciation. Excluding these charges, gross margin increased to 46.0%.

Worldwide marketing, research and administrative expense was 28.4% of net sales, compared with 27.5% in 1998. The 6% increase in total spending was primarily due to increased research spending, primarily in the paper and health care businesses, and increased spending for new initiatives. Organization 2005 charges increased marketing, research and administrative expense by \$38 million, related primarily to employee separation expenses.

Operating income grew 3% in 1999. Excluding the charges for Organization 2005, operating income grew 11%. These trends reflected sales growth and cost control efforts. Net earnings margin was 9.9% in 1999 versus 10.2% in 1998. Excluding the Organization 2005 charges, core net earnings margin in 1999 was 10.9%, the highest in 58 years.

Interest expense increased 19% to \$650 million in 1999, on increased debt, due mainly to share repurchases. In 1998, interest expense was \$548 million. Other income, net, was \$235 million in 1999, versus \$201 million in 1998.

The Company's effective tax rate for the year was 35.5%, compared to 33.8% in 1998. The increase reflected a reduction in benefits for research and development tax credits in North America, which were included in 1998 results, as well as the impact of various country tax rates on Organization 2005 program costs. Excluding Organization 2005 program costs and related tax effects, the tax rate was 34.4%.

Over the last several years, the Company maintained an ongoing program of simplification and standardization, which included projects to consolidate selected manufacturing facilities, re-engineer manufacturing and distribution processes, redesign organizations, simplify product line-ups and divest non-strategic brands and assets. This program did not have a significant impact on 1999 or 1998 net earnings. Beginning with the fourth quarter of 1999, the restructuring aspects of this program were superseded by Organization 2005.

Certain reclassifications of the prior years' amounts have been made to conform with the current year presentation.

**FINANCIAL CONDITION**

Cash flow from operations was \$4.68 billion, \$5.54 billion and \$4.89 billion in 2000, 1999 and 1998, respectively. Operating cash flow provided the primary source of funds to finance operating needs, capital expenditures and shareholder dividends. Supplemented by additional borrowings, cash flow from operations also provided funds to finance acquisitions and the share repurchase program.

Cash and cash equivalents decreased \$879 million in the current year to \$1.42 billion, reflecting acquisition spending and lower net earnings, partially offset by the issuance of debt. In the prior year, cash and cash equivalents increased by \$745 million to \$2.29 billion, reflecting improved earnings, primarily concentrated in Europe.

Capital expenditures were \$3.02 billion in 2000, \$2.83 billion in 1999 and \$2.56 billion in 1998. Current year expenditures included initiatives and capacity increases in fabric and home care and paper, including spending on Organization 2005 projects. Capital expenditures are expected to increase in the upcoming year, behind the Organization 2005 program, including increased capacity. In 1999, capital spending was driven by standardization projects in paper and capacity expansions in the paper and food and beverage businesses.

Net cash used for acquisitions completed during 2000 totaled \$2.97 billion, primarily related to the acquisitions of The Iams Company and Affiliates, Recovery Engineering, Inc. and a joint venture ownership increase in China. This compares to acquisition spending of \$137 million in 1999 and \$3.27 billion in 1998. Transactions in fiscal 1998 were largely concentrated in paper businesses and included Tambrands, Inc., the Loreto y Peña paper company in Mexico and the Ssangyong Paper Company in Korea. The Company also increased ownership of various joint ventures in Asia and Latin America in 1998.

The Company continues its program to divest certain non-strategic brands in order to focus resources on core businesses. The proceeds from these and other asset sales generated \$419 million in cash flow in the current year, compared to \$434 million and \$555 million in 1999 and 1998, respectively.

The Company maintains a share repurchase program, which authorizes the Company to purchase shares annually on the open market to mitigate the dilutive impact of employee compensation programs. The Company also has a discretionary buy-back program under which it currently intends to repurchase additional outstanding shares of up to \$1 billion per year. Current year purchases under the combined programs were \$1.77 billion, compared to \$2.53 billion in 1999 and \$1.93 billion in 1998. The Company issued equity put options in 2000 for 12 million shares at prices ranging from \$60 to \$71 per share, which reduce the Company's cash outlay for share repurchases.

Common share dividends grew 12% to \$1.28 per share in 2000, compared to \$1.14 and \$1.01 in 1999 and 1998, respectively. For the coming year, the annual dividend rate will increase to \$1.40 per common share, marking the 45th consecutive year of increased common share dividend payments. Total dividend payments, to both common and preferred shareholders, were \$1.80 billion, \$1.63 billion and \$1.46 billion in 2000, 1999 and 1998, respectively.

Total debt was up \$2.75 billion to \$12.13 billion, due to the issuance of long-term debt to fund acquisitions and share repurchases.

Long-term borrowing available under the Company's shelf registration statement filed in 1995, as amended in July 1997 and September 1999, was \$1.87 billion at June 30, 2000. Additionally, the Company is able to issue commercial paper at favorable rates and to access general bank financing.

**The following pages provide perspective on the Company's business segments. The Company moved to a global product-based structure from a geographic structure effective July 1, 1999, and prior years' results have been restated for the change. Product-based segment results exclude items that are not included in measuring business performance for management reporting purposes, most notably certain financing, investing and employee benefit costs, goodwill amortization and costs related to the Organization 2005 program.**

**Sales in companies over which the Company exerts significant influence, but does not control the financial and operating decisions, are reported for segment purposes in a manner similar to consolidated subsidiaries. Taxes are reflected in the businesses at local statutory tax rates. The effects of these conventions are eliminated in the Corporate segment to reconcile to accounting principles generally accepted in the United States of America.**

#### **FABRIC AND HOME CARE**

Net sales for fabric and home care were \$12.16 billion, an increase of 7% over the prior year. Unit volume grew 5%. Excluding foreign exchange impacts, primarily in Western Europe, sales grew 9%. Net earnings for the segment were \$1.45 billion, down 3% versus year ago.

Fabric and home care represents the Company's largest business segment, accounting for nearly one third of sales and an even greater percentage of earnings.

Strong sales growth was spurred by the introduction of new brands and solid base business performance in North America and Northeast Asia, as well as continued expansion within the Southern Cone (Brazil, Chile, Argentina) of Latin America. Despite volume and sales progress, earnings were down, primarily due to significant investments in product initiatives.

Strong unit volume and sales growth was achieved in North America versus the prior year. Several new brand initiatives were launched, including Swiffer, Dryel and Mr. Clean Wipes, along with product upgrades on established brands, such as Tide. New business sales accounted for approximately half of the growth.

Western Europe posted slight volume increases behind the introductions of Swiffer and Dryel, as well as the expansion of laundry tablets. Sales declined as pricing lagged unfavorable exchange trends. Progress in Central and Eastern Europe was strong following last year's economic crisis in Russia and reflecting an improved cost structure.

Northeast Asia delivered high double-digit growth on volume and sales, despite a challenging economic environment. Strength on Ariel and Joy, as well as the introduction of Febreze in Japan and South Korea, drove the increases.

In 1999, net sales increased 4% over 1998, on flat unit volume. Net earnings were \$1.50 billion, a 6% increase. North America was a strong contributor to segment results, driving both sales and earnings gains.

**PAPER**

The paper segment had net sales of \$12.04 billion, down 1% from the prior year on flat unit volume. Excluding the impact of exchange rates, primarily the euro, sales were up 1%. Excluding the impact of the prior year divestiture of the Attends adult incontinence brand, unit volume increased 2%.

Net earnings were \$1.07 billion, down 16%, reflecting tissues and towel expansion in Western Europe, investments in new product initiatives on Charmin, a tough competitive environment in baby care and feminine care businesses, increased capacity and unfavorable raw and packing material cost trends.

In the current year, tissues and towel volume and sales grew 9% and 7%, respectively, behind geographic expansion, as well as a major product upgrade on Charmin. Volume growth was broad-based in all major markets, led by the North America expansion of Charmin and Bounty. Product introductions in the United Kingdom contributed to volume progress in Western Europe. In 1999, volume and sales increased 7%, primarily due to gains in North America and Northeast Asia.

Tissues and towel earnings declined despite volume growth, as rising pulp and energy prices, combined with investments in geographic expansions and product initiatives, more than offset volume gains. In addition, two new paper machines in North America and another in the United Kingdom provided needed capacity, but resulted in higher start-up costs. Commodity-driven pricing actions were taken during the last quarter of the year, but were not sufficient to offset the full year impact of cost increases.

Baby care volume was flat, as significant competitive challenges in Western Europe offset increases in other markets. Excluding a 3% negative exchange impact, sales increased 1%. Earnings were affected by increased marketing and administrative expense. The recent introductions of Pampers One-Ups! wipes and Luvs Splashwear, the expansion of Pampers into China and planned product improvements are expected to better position the baby care business by restoring consumer value in the face of the current price premium versus competition. For fiscal 1999, pricing actions drove sales up 5% on flat unit volume.

Feminine care volume declined 9%, due primarily to the impact of the prior year divestiture of the Attends adult incontinence brand. Excluding the divestiture, volume declined by 3% primarily driven by competitive activity in Northeast Asia, China and Latin America. Sales decreased 7%. Excluding exchange impacts, sales declined 4%. Earnings were down due to lower volumes, combined with product initiative related cost increases primarily in North America and Western Europe. While unit volume declined 3% in 1999, sales increased marginally.

In 1999, paper net sales increased 4% to \$12.19 billion on 1% unit volume growth, led by tissues and towel and baby care. Net earnings were \$1.28 billion, a 29% increase over 1998, primarily driven by baby care results.

**BEAUTY CARE**

Net sales in beauty care were \$7.39 billion, comparable to the prior year, but up 1% excluding the impact of unfavorable exchange rates, primarily in Western Europe. Unit volume declined 2%, impacted by a difficult competitive environment in key European markets and significant contraction of the market in China. Net earnings were \$894 million, a 3% decrease from the prior year.

Sales in the current year were slightly ahead of volume due to the focus on high-performance, premium-priced initiatives, including the launch of the Physique styling-led line, cosmetics and skin care product initiatives and the expansion of Secret Platinum.

Earnings for the current year reflected the weakness in China and Western Europe and higher marketing costs associated with the introduction of new products and initiatives on established brands, which more than offset gains from minor brand divestitures.

Western Europe was negatively impacted by competitive factors and the euro devaluation. Plans to restore growth include improved focus on cost control, as well as the expansion of premium-priced initiatives such as the VS Sassoon and Head and Shoulders restages and expansion of Olay Total Effects.

China, especially hair care, was challenged by a worsening economic situation, which fueled the growth of low cost local brands and a higher incidence of branded product counterfeiting. Going forward, the business will continue to focus on strengthening brand equities through several upgrades on large brands.

North America increased volume behind premium product introductions. Physique, positioned as a salon-quality brand, was launched in the last half of the year and achieved solid share results. The introduction of Old Spice Red Zone and expansion of Secret Platinum also provided good share results.

In 1999, net sales declined 1% to \$7.38 billion on a 5% unit volume drop. Sales were negatively affected by the financial crisis in Eastern Europe, as well as competitive activity and the impact of divestitures of non-strategic brands in Western Europe. Net earnings were \$917 million, a 9% increase from 1998, reflecting favorable pricing and steady progress on cost control.

**HEALTH CARE**

Health care net sales were \$3.91 billion, with growth primarily coming from acquisitions. Volume and sales increased 34% and 36%, respectively, versus the prior year. Unfavorable exchange rates impacted sales by 2%. Net earnings were \$335 million, a 38% increase over 1999. Excluding the impact of acquisitions, health care delivered sales growth of 4% despite a 2% volume decline, while earnings increased 17%.

The Iams Company posted record results, doubling distribution with the expansion into new retail channels. Beyond the channel expansion, Iams introduced several successful product initiatives.

Health care sales in North America grew behind strong consumption, favorable pricing and volume progress in pharmaceuticals. Oral care volume gains were driven by the launches of Crest MultiCare Advanced Cleaning and other premium dentifrice products.

Actonel (risedronate sodium tablets) 5 mg., the Company's first major prescription drug, was launched in the fourth quarter. Actonel is a bisphosphonate for the prevention and treatment of osteoporosis and is the only therapy proven to significantly reduce spinal fractures in one year. A milestone payment received upon FDA approval of Actonel was essentially offset by launch costs in the current year. The launch is off to a good start in the United States, United Kingdom and Germany, with launches planned shortly in four more countries.

Western Europe depressed sales, primarily due to the weak euro and lower volume. The Actonel launch is expected to impact Western Europe results more significantly next fiscal year.

In 1999, net sales were flat versus the prior year at \$2.88 billion on a 3% unit volume reduction. Net earnings were \$242 million, a 4% increase over 1998. Earnings progress reflected a shift toward higher-margin pharmaceutical sales and pricing, mitigated by investments in product launches.

#### **FOOD AND BEVERAGE**

Food and beverage net sales were flat versus last year at \$4.63 billion, including a 1% negative exchange impact. Unit volume also was flat. Excluding the prior year divestiture of Hawaiian Punch, unit volume increased 5% behind strong growth in Western Europe and Northeast Asia, partially due to the expansion of Pringles. Net earnings increased to \$364 million, up 11% versus last year, primarily due to gross margin improvement.

Results in North America reflected significant competitive activity, particularly in coffee and snacks. Initiative launches helped drive volume, partially offsetting the impact of the Hawaiian Punch divestiture. Despite product cost savings, earnings were impacted by marketing costs and other spending increases.

Unit volume in Western Europe achieved double-digit growth with the successful expansion of Pringles. Juice volume suffered due to a temporary public relations setback with Sunny Delight in the United Kingdom that has now been addressed. Recent launches in France and Spain are expected to improve volume progress, along with additional launches in Western Europe.

Northeast Asia posted double-digit progress on volume and sales driven by renewed strength in the snacks business, as well as strengthening of the Japanese yen.

In 1999, net sales increased 1% to \$4.66 billion, on a 4% volume increase. Net earnings were \$328 million, a 12% increase versus \$294 million in 1998, which included significant initiative related spending.

#### **CORPORATE**

The Corporate segment includes both operating and non-operating elements, such as: financing and investing activities, goodwill amortization, employee benefit costs, charges related to restructuring (including the Organization 2005 program), segment eliminations and other general corporate items.

Corporate sales reflected adjustments to reconcile management reporting conventions to accounting principles generally accepted in the United States of America.

Corporate results reflected increased charges from Organization 2005 and goodwill amortization, partially offset by lower corporate costs, including reduced employee benefit costs and the proceeds of a patent litigation settlement with Paragon Trade Brands, Inc.

**HEDGING AND DERIVATIVE FINANCIAL INSTRUMENTS**

The Company is exposed to market risks, such as changes in interest rates, currency exchange rates and commodity prices. To manage the volatility relating to these exposures, the Company nets the exposures on a consolidated basis to take advantage of natural offsets. For the residual portion, the Company enters into various derivative transactions pursuant to the Company's policies in areas such as counterparty exposure and hedging practices. The financial impacts of these hedging instruments are offset in part or in whole by corresponding changes in the underlying exposures being hedged. The Company does not hold or issue derivative financial instruments for trading purposes. Note 6 to the consolidated financial statements includes a discussion of the Company's accounting policies for financial instruments.

Derivative positions are monitored using techniques including market value, sensitivity analysis and value at risk modeling. The tests for interest rate and currency rate exposures discussed below are based on a variance/co-variance value at risk model using a one year horizon and a 95% confidence level. The model incorporates the impact of correlation and diversification from holding multiple currency and interest rate instruments, assumes that financial returns are normally distributed and approximates the financial return for options and other non-linear instruments. Estimates of volatility and correlations of market factors are drawn from the RiskMetrics™ dataset as of June 30, 2000. In cases where data is unavailable in RiskMetrics™ a reasonable proxy is included.

The Company's market risk exposures relative to interest and currency rates, as discussed below, have not changed materially versus the previous reporting period. In addition, the Company is not aware of any facts or circumstances that would significantly impact such exposures in the near term.

**INTEREST RATE EXPOSURE**

Interest rate swaps are used to hedge underlying debt obligations. Certain currency interest rate swaps are designated as hedges of the Company's foreign net investments.

Based on the Company's overall interest rate exposure as of and during the year ended June 30, 2000, including derivative and other instruments sensitive to interest rates, a near-term change in interest rates, at a 95% confidence level based on historical interest rate movements, would not materially affect the Company's financial statements.

**CURRENCY RATE EXPOSURE**

The Company manufactures and sells its products in a number of countries throughout the world and, as a result, is exposed to movements in foreign currency exchange rates. The Company's major foreign currency exposures involve the markets in Western and Eastern Europe, Asia and Mexico. The primary purpose of the Company's foreign currency hedging activities is to manage the volatility associated with foreign currency purchases of materials and other assets and liabilities created in the normal course of business. Corporate policy prescribes the range of allowable hedging activity. The Company primarily utilizes forward exchange contracts and purchased options with maturities of less than eighteen months.

In addition, the Company enters into certain foreign currency swaps to hedge intercompany financing transactions. The Company also utilizes purchased foreign currency options with maturities of generally less than eighteen months and forward exchange contracts to hedge against the effect of exchange rate fluctuations on royalties and income from international operations.

Based on the Company's overall currency rate exposure as of and during the year ended June 30, 2000, including derivative and other instruments sensitive to foreign currency movements, a near-term change in currency rates, at a 95% confidence level based on historical currency rate movements, would not materially affect the Company's financial statements.

#### **COMMODITY PRICE EXPOSURE**

Raw materials used by the Company are subject to price volatility caused by weather, supply conditions, political and economic variables and other unpredictable factors. The Company uses futures and options contracts, primarily in food and beverage products, to manage the volatility related to certain of these exposures. Commodity hedging activity is not material to the Company's financial statements.

#### **ORGANIZATION 2005**

As also discussed in Note 2 to the consolidated financial statements, effective July 1, 1999, the Company reorganized its operations, moving from a geographic structure to product-based Global Business Units.

This Organization 2005 program is designed to realign the organizational structure, work processes and culture to commercialize innovations faster and drive growth. This involves Global Business Units streamlining decision making to quickly flow innovation across categories and geographies, Market Development Organizations getting initiatives to market faster and more efficiently, and Global Business Services leveraging scale to deliver services at significantly lower cost.

To achieve this, changes are required to administrative and manufacturing operations. As announced in June 1999, the Company has undertaken a multi-year program to consolidate and standardize manufacturing operations, reduce enrollment and effect other actions integral to the Organization 2005 objectives.

The cost of this program is estimated to be \$2.1 billion after tax over a six year period. Based on the nature and duration of the Organization 2005 program, costs incurred in future years are subject to varying degrees of estimation for key assumptions, such as normal employee attrition levels, the actual timing of the execution of plans and other variables. The estimated cost of the program has increased approximately \$200 million after tax since its announcement, primarily due to refinement of estimates associated with the legal and organizational restructuring of the Company and expansion of certain manufacturing consolidation plans.

Significant savings are expected to begin accruing next fiscal year, reaching going annual levels of approximately \$1.2 billion after tax by fiscal 2004. This annual savings estimate has increased by approximately \$300 million since announcement of the program, primarily due to the savings associated with the legal and organizational restructuring, which yields substantial tax and other savings.

The Company recorded Organization 2005 charges of \$814 million (\$688 million after tax) and \$481 million (\$385 million after tax) in 2000 and 1999, respectively. These charges were recorded in the Corporate segment for management and external reporting purposes, although they affected substantially all business units. Savings for the current year were approximately \$65 million after tax, with no individual business unit significantly impacted. Estimated costs for fiscal 2001 are \$750 million (\$550 million after tax). The balance of the charges are not expected to materially affect any single year, and savings are expected to offset the charges.

Costs under Organization 2005 were related primarily to separation and relocation of employees as well as streamlining manufacturing facilities, including consolidations, closures and standardization projects. Certain other costs directly related to Organization 2005 also were included.

The non-cash costs of the program primarily were related to manufacturing consolidations and asset write-downs. These accounted for 62% and 88% of charges in 2000 and 1999, respectively. Approximately 30% of future charges are expected to be non-cash. Cash requirements of the program, including capital spending requirements, will be met through normal operating cash flow.

Approximately 45% of the plant and production module closings have occurred to date, with the majority of the remainder expected to be completed in fiscal 2001.

Employee separation charges were \$153 million (\$102 million after tax) and \$45 million (\$29 million after tax) in 2000 and 1999, respectively. These costs related to severance packages for approximately 2,800 people in 2000 and 400 people in 1999, with all geographies and businesses impacted. The predominantly voluntary packages were formula driven, based on salary levels and past

service. Severance costs related to voluntary separations were charged to earnings when the employee accepted the offer and were reflected in cost of products sold for manufacturing employees and in marketing, research and administrative expense for all other employees.

The streamlined work processes and manufacturing consolidations under Organization 2005 are expected to affect approximately 15,000 jobs over six years (fiscal 1999 through 2004). The majority of the remaining separation costs are expected to occur by 2002, although additional costs will continue throughout the program. Net enrollment is expected to decline by less than the total separations, as terminations will be partially offset through increased enrollment at remaining sites and acquisition impacts.

Asset write-downs were \$64 million (\$43 million after tax) in 2000 and \$217 million (\$142 million after tax) in 1999. The 2000 charges related to assets held for sale or disposal and represented excess capacity that is in the process of being removed from service. Such assets were written down to the lower of their current carrying basis or net amounts expected to be realized upon disposal. In the prior year, the charges primarily related to manufacturing assets that were expected to operate at levels significantly below their capacity because of a shift in global strategy enabled by Organization 2005, as well as demand trends below expectations. Because the expected cash flows of those assets were estimated to be less than their carrying values, the assets were written down to estimated fair value as determined using discounted cash flows. The remainder of the 1999 charges related to assets held for sale. Asset write-downs will not have a significant impact on future depreciation charges.

Charges for accelerated depreciation were \$386 million (\$335 million after tax) in 2000 and \$208 million (\$206 million after tax) in 1999. The charges for accelerated depreciation related to long-lived assets that will be taken out of service prior to the end of their normal service period due to manufacturing consolidations, technology standardization and plant closures. The Company has shortened the estimated useful lives of such assets, resulting in an acceleration of depreciation. The underlying plant closures and consolidations will impact substantially all businesses. Accelerated depreciation charges are expected to be approximately \$250 million in 2001. Both asset write-downs and accelerated depreciation are charged to cost of products sold.

Other costs were \$211 million (\$208 million after tax) and \$11 million (\$8 million after tax) in 2000 and 1999, respectively. These costs were incurred as a direct result of Organization 2005 and were expensed as incurred. The nature of the costs included training, relocation, tax and other incremental costs relating to establishment of Global Business Services and the new legal and organizational structure of Organization 2005. Such before-tax costs were primarily charged to marketing, research and administrative expense and were included in the Corporate segment. Charges for other costs are expected to be approximately \$225 million in 2001.

Most charges under Organization 2005 are paid shortly after accrual or charged directly to the related assets. The reserve balances at June 30, 2000 and 1999 were \$88 million and \$44 million, respectively.

#### FORWARD-LOOKING STATEMENT

The Company has made and will make certain forward-looking statements in the Annual Report and in other contexts relating to volume growth, increases in market shares, Organization 2005, financial goals and cost reduction, among others.

These forward-looking statements are based on assumptions and estimates regarding competitive activity, pricing, product introductions, economic conditions, technological innovation, currency movements, governmental action and the development of certain markets. Among the key factors necessary to achieve the Company's goals are: (1) the successful implementation of Organization 2005, including achievement of expected cost and tax savings and successful management of organizational and work process restructuring; (2) the ability to achieve business plans, including volume growth and pricing plans, despite high levels of competitive activity; (3) the ability to maintain key customer relationships; (4) the achievement of growth in significant developing markets such as China, Mexico, the Southern Cone of Latin America and the countries of Central and Eastern Europe; (5) the ability to successfully manage regulatory, tax and legal matters, including resolution of pending matters within current estimates; (6) the successful execution of planned minor brand divestitures; (7) the ability to successfully implement cost improvement plans in manufacturing and overhead areas; and (8) the ability to successfully manage currency, interest rate and certain commodity cost exposures. If the Company's assumptions and estimates are incorrect or do not come to fruition, or if the Company does not achieve all of these key factors, then the Company's actual performance could vary materially from the forward-looking statements made herein.

Consolidated financial statements and financial information included in this report are the responsibility of Company management. This includes preparing the statements in accordance with accounting principles generally accepted in the United States and necessarily includes estimates based on management's best judgments.

To help insure the accuracy and integrity of Company financial data, management maintains internal controls designed to provide reasonable assurance that transactions are executed as authorized and accurately recorded and that assets are properly safeguarded. These controls are monitored by an ongoing program of internal audits. These audits are supplemented by a self-assessment program that enables individual organizations to evaluate the effectiveness of their controls. Careful selection of employees and appropriate divisions of responsibility are designed to achieve control objectives. The Company's "Worldwide Business Conduct Manual" sets forth management's commitment to conduct its business affairs with the highest ethical standards.

Deloitte & Touche, independent public accountants, have audited and reported on the Company's consolidated financial statements. Their audits were performed in accordance with auditing standards generally accepted in the United States of America.

The Board of Directors, acting through its Audit Committee composed entirely of outside directors, oversees the adequacy of internal controls. The Audit Committee meets periodically with representatives of Deloitte & Touche and internal financial management to review internal control, auditing and financial reporting matters. The independent auditors and the internal auditors also have full and free access to meet privately with the Audit Committee.



John E. Pepper  
Chairman of the Board



A.G. Lafley  
President and Chief Executive



Clayton C. Daley Jr.  
Chief Financial Officer

#### INDEPENDENT AUDITORS' REPORT



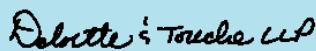
250 East Fifth Street  
Cincinnati, Ohio 45202

To the Board of Directors and Shareholders of The Procter & Gamble Company:

We have audited the accompanying consolidated balance sheets of The Procter & Gamble Company and subsidiaries as of June 30, 2000 and 1999 and the related consolidated statements of earnings, shareholders' equity and cash flows for each of the three years in the period ended June 30, 2000. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company at June 30, 2000 and 1999 and the results of its operations and cash flows for each of the three years in the period ended June 30, 2000, in conformity with accounting principles generally accepted in the United States of America.



August 1, 2000

## The Procter &amp; Gamble Company and Subsidiaries

Amounts in millions except per share amounts

	Years ended June 30		
	2000	1999	1998
<b>Net Sales</b>	<b>\$39,951</b>	<b>\$38,125</b>	<b>\$37,154</b>
Cost of products sold	21,514	21,027	20,896
Marketing, research and administrative expense	12,483	10,845	10,203
<b>Operating Income</b>	<b>5,954</b>	<b>6,253</b>	<b>6,055</b>
Interest expense	722	650	548
Other income, net	304	235	201
<b>Earnings Before Income Taxes</b>	<b>5,536</b>	<b>5,838</b>	<b>5,708</b>
Income taxes	1,994	2,075	1,928
<b>Net Earnings<sup>(1)</sup></b>	<b>\$ 3,542</b>	<b>\$ 3,763</b>	<b>\$ 3,780</b>
<b>Basic Net Earnings Per Common Share<sup>(1)</sup></b>	<b>\$ 2.61</b>	<b>\$ 2.75</b>	<b>\$ 2.74</b>
<b>Diluted Net Earnings Per Common Share<sup>(1)</sup></b>	<b>\$ 2.47</b>	<b>\$ 2.59</b>	<b>\$ 2.56</b>
<b>Dividends Per Common Share</b>	<b>\$ 1.28</b>	<b>\$ 1.14</b>	<b>\$ 1.01</b>

<sup>(1)</sup>Net earnings include an after-tax charge for Organization 2005 of \$688 in 2000 and \$385 in 1999. Basic and diluted net earnings per share include Organization 2005 charges of \$.52 and \$.48 in 2000 and \$.29 and \$.26 in 1999, respectively.

See accompanying Notes to Consolidated Financial Statements.

## CONSOLIDATED BALANCE SHEETS

The Procter &amp; Gamble Company and Subsidiaries

Amounts in millions

	June 30	
	2000	1999
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 1,415	\$ 2,294
Investment securities	185	506
Accounts receivable	2,910	2,940
<b>Inventories</b>		
Materials and supplies	1,254	1,176
Work in process	394	375
Finished goods	1,842	1,787
<b>Total Inventories</b>	<b>3,490</b>	<b>3,338</b>
Deferred income taxes	309	621
Prepaid expenses and other current assets	1,760	1,659
<b>Total Current Assets</b>	<b>10,069</b>	<b>11,358</b>
<b>Property, Plant and Equipment</b>		
Buildings	4,259	3,885
Machinery and equipment	18,366	16,953
Land	596	562
	23,221	21,400
Accumulated depreciation	(9,529)	(8,774)
<b>Total Property, Plant and Equipment</b>	<b>13,692</b>	<b>12,626</b>
<b>Goodwill and Other Intangible Assets</b>		
Goodwill	9,080	7,062
Trademarks and other intangible assets	1,305	1,115
	10,385	8,177
Accumulated amortization	(1,599)	(1,355)
<b>Total Goodwill and Other Intangible Assets</b>	<b>8,786</b>	<b>6,822</b>
<b>Other Non-Current Assets</b>		
	1,647	1,307
<b>Total Assets</b>	<b>\$34,194</b>	<b>\$32,113</b>

See accompanying Notes to Consolidated Financial Statements.

Amounts in millions

	June 30	
	2000	1999
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 2,209	\$ 2,300
Accrued and other liabilities	3,721	4,083
Taxes payable	925	1,228
Debt due within one year	3,210	3,150
<b>Total Current Liabilities</b>	<b>10,065</b>	<b>10,761</b>
Long-Term Debt	8,916	6,231
Deferred Income Taxes	625	362
Other Non-Current Liabilities	2,301	2,701
<b>Total Liabilities</b>	<b>21,907</b>	<b>20,055</b>
<b>Shareholders' Equity</b>		
Convertible Class A preferred stock, stated value \$1 per share (600 shares authorized)	1,737	1,781
Non-Voting Class B preferred stock, stated value \$1 per share (200 shares authorized)	—	—
Common stock, stated value \$1 per share (5,000 shares authorized; shares outstanding: 2000 – 1,305.9 and 1999 – 1,319.8)	1,306	1,320
Additional paid-in capital	1,794	1,337
Reserve for Employee Stock Ownership Plan debt retirement	(1,418)	(1,552)
Accumulated other comprehensive income	(1,842)	(1,606)
Retained earnings	10,710	10,778
<b>Total Shareholders' Equity</b>	<b>12,287</b>	<b>12,058</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$34,194</b>	<b>\$32,113</b>

See accompanying Notes to Consolidated Financial Statements.

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

The Procter &amp; Gamble Company and Subsidiaries

Dollars in millions/ Shares in thousands	Common Shares Outstanding	Common Stock	Preferred Stock	Additional Paid-in Capital	Reserve for ESOP Debt Retirement	Accumulated Other Comprehensive Income	Retained Earnings	Total	Total Comprehensive Income
<b>Balance June 30, 1997</b>	1,350,843	\$1,351	\$1,859	\$ 559	\$(1,634)	\$ (819)	\$10,730	\$12,046	
Net earnings							3,780	3,780	\$3,780
Other comprehensive income:									
Currency translation, net of \$25 tax						(536)		(536)	(536)
Other, net of tax						(2)		(2)	(2)
Total comprehensive income									\$3,242
Dividends to shareholders:									
Common							(1,358)	(1,358)	
Preferred, net of tax benefit							(104)	(104)	
Treasury purchases	(24,716)	(25)					(1,904)	(1,929)	
Employee plan issuances	8,777	9		312				321	
Preferred stock conversions	2,557	2	(38)	36				–	
ESOP debt guarantee reduction				18				18	
<b>Balance June 30, 1998</b>	1,337,461	1,337	1,821	907	(1,616)	(1,357)	11,144	12,236	
Net earnings							3,763	3,763	\$3,763
Other comprehensive income:									
Currency translation, net of \$4 tax						(232)		(232)	(232)
Other, net of tax						(17)		(17)	(17)
Total comprehensive income									\$3,514
Dividends to shareholders:									
Common							(1,517)	(1,517)	
Preferred, net of tax benefit							(109)	(109)	
Treasury purchases	(29,924)	(30)					(2,503)	(2,533)	
Employee plan issuances	9,605	10		393				403	
Preferred stock conversions	2,612	3	(40)	37				–	
ESOP debt guarantee reduction				64				64	
<b>Balance June 30, 1999</b>	1,319,754	1,320	1,781	1,337	(1,552)	(1,606)	10,778	12,058	
Net earnings							3,542	3,542	\$3,542
Other comprehensive income:									
Currency translation, net of \$88 tax						(299)		(299)	(299)
Other, net of tax						63		63	63
Total comprehensive income									\$3,306
Dividends to shareholders:									
Common							(1,681)	(1,681)	
Preferred, net of tax benefit							(115)	(115)	
Treasury purchases	(24,296)	(24)		72 <sup>(1)</sup>			(1,814)	(1,766)	
Employee plan issuances	7,592	7		344				351	
Preferred stock conversions	2,817	3	(44)	41				–	
ESOP debt guarantee reduction				134				134	
<b>Balance June 30, 2000</b>	1,305,867	\$1,306	\$1,737	\$1,794	\$(1,418)	\$(1,842)	\$10,710	\$12,287	

<sup>(1)</sup>Premium on equity put options.

See accompanying Notes to Consolidated Financial Statements.

## The Procter &amp; Gamble Company and Subsidiaries

Amounts in millions

	Years ended June 30		
	2000	1999	1998
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b>\$ 2,294</b>	<b>\$ 1,549</b>	<b>\$ 2,350</b>
<b>Operating Activities</b>			
Net earnings	3,542	3,763	3,780
Depreciation and amortization	2,191	2,148	1,598
Deferred income taxes	463	(60)	(101)
Change in accounts receivable	64	(207)	42
Change in inventories	(176)	(96)	(229)
Change in accounts payable, accrued and other liabilities	(883)	792	(3)
Change in other operating assets and liabilities	(404)	(926)	(65)
Other	(122)	130	(137)
<b>Total Operating Activities</b>	<b>4,675</b>	<b>5,544</b>	<b>4,885</b>
<b>Investing Activities</b>			
Capital expenditures	(3,018)	(2,828)	(2,559)
Proceeds from asset sales	419	434	555
Acquisitions	(2,967)	(137)	(3,269)
Change in investment securities	221	356	63
<b>Total Investing Activities</b>	<b>(5,345)</b>	<b>(2,175)</b>	<b>(5,210)</b>
<b>Financing Activities</b>			
Dividends to shareholders	(1,796)	(1,626)	(1,462)
Change in short-term debt	243	689	1,315
Additions to long-term debt	4,196	986	1,970
Reductions of long-term debt	(1,409)	(334)	(432)
Proceeds from stock options	336	212	158
Treasury purchases	(1,766)	(2,533)	(1,929)
<b>Total Financing Activities</b>	<b>(196)</b>	<b>(2,606)</b>	<b>(380)</b>
<b>Effect of Exchange Rate Changes on Cash and Cash Equivalents</b>	<b>(13)</b>	<b>(18)</b>	<b>(96)</b>
<b>Change in Cash and Cash Equivalents</b>	<b>(879)</b>	<b>745</b>	<b>(801)</b>
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 1,415</b>	<b>\$ 2,294</b>	<b>\$ 1,549</b>
<b>Supplemental Disclosure</b>			
Cash payments for:			
Interest, net of amount capitalized	\$ 700	\$ 640	\$ 536
Income taxes	1,712	1,743	1,873
Liabilities assumed in acquisitions	236	38	808

See accompanying Notes to Consolidated Financial Statements.

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation:** The consolidated financial statements include The Procter & Gamble Company and its controlled subsidiaries (the Company). Investments in companies over which the Company exerts significant influence, but does not control the financial and operating decisions, are accounted for using the equity method. These investments are managed as integral parts of the Company's business units, and segment reporting reflects such investments as consolidated subsidiaries.

**Use of Estimates:** Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying disclosures. These estimates are based on management's best knowledge of current events and actions the Company may undertake in the future. Actual results may ultimately differ from estimates.

**New Pronouncements:** In June 1998, the FASB issued Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities." This statement will be adopted effective July 1, 2000, but is not expected to materially impact the Company's financial statements.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101, "Revenue Recognition in Financial Statements." The effective date has been deferred pending additional interpretive guidance. Based on current interpretations, no material impact on the Company's financial statements is anticipated.

**Currency Translation:** Financial statements of subsidiaries outside the U.S. generally are measured using the local currency as the functional currency. Adjustments to translate those statements into U.S. dollars are accumulated in a separate component of shareholders' equity. For subsidiaries operating in highly inflationary economies, the U.S. dollar is the functional currency. Remeasurement adjustments for highly inflationary economies and other transactional exchange gains and losses are reflected in earnings.

**Cash Equivalents:** Highly liquid investments with maturities of three months or less when purchased are considered cash equivalents.

**Inventory Valuation:** Inventories are valued at cost, which is not in excess of current market price. Cost is primarily determined by either the average cost or the first-in, first-out method. The replacement cost of last-in, first-out inventories exceeded carrying value by approximately \$83 and \$100 at June 30, 2000 and 1999, respectively.

**Goodwill and Other Intangible Assets:** The cost of intangible assets is amortized, principally on a straight-line basis, over the estimated periods benefited, generally forty years for goodwill and periods ranging from three to forty years for other intangible assets. The realizability of goodwill and other intangibles is evaluated periodically when events or circumstances indicate a possible inability to recover the carrying amount. Such evaluation is based on various analyses, including cash flow and profitability projections that incorporate the impact of the Company's existing businesses. The analyses necessarily involve significant management judgment to evaluate the capacity of an acquired business to perform within projections. Historically, the Company has generated sufficient returns from acquired businesses to recover the cost of the goodwill and other intangible assets.

**Property, Plant and Equipment:** Property, plant and equipment are recorded at cost reduced by accumulated depreciation. Depreciation expense is based on estimated useful lives using the straight-line method. Estimated useful lives are periodically reviewed, and where warranted, changes are made that result in an acceleration of depreciation.

**Fair Values of Financial Instruments:** Fair values of cash equivalents, short and long-term investments and short-term debt approximate cost. The estimated fair values of other financial instruments, including debt, equity and risk management instruments, have been determined using available market information and valuation methodologies, primarily discounted cash flow analysis. These estimates require considerable judgment in interpreting market data, and changes in assumptions or estimation methods may significantly affect the fair value estimates.

**Reclassifications:** Certain reclassifications of prior years' amounts have been made to conform with the current year presentation.

**NOTE 2 ORGANIZATION 2005**

In June 1999, the Board of Directors approved a multi-year restructuring program in conjunction with the Company's Organization 2005 initiative.

Due to the nature and duration of this program, the timing and amount of estimated costs and savings require significant judgment and may change over time. Based on current expectations, the total cost of the program is estimated to be \$2.7 billion (\$2.1 billion after tax) over a six year period (fiscal 1999 through fiscal 2004).

The costs of this program primarily relate to separation and relocation of employees and streamlining manufacturing capabilities, including consolidation and closure. Certain other costs directly related to Organization 2005 also are included.

## The Procter &amp; Gamble Company and Subsidiaries

Charges for the program were \$814 (\$688 after tax) and \$481 (\$385 after tax) in 2000 and 1999, respectively. Estimated costs for fiscal 2001 are \$750 (\$550 after tax). The balance of the charges are not expected to materially affect any single year, and savings are expected to offset the charges. All charges for the program are reflected in the Corporate segment for management and external reporting.

The before-tax amounts consisted of the following:

	Separations	Asset Write-Downs	Accelerated Depreciation	Other	Total
<b>1999:</b>					
Charges	\$ 45	\$ 217	\$ 208	\$ 11	\$ 481
Cash spent	(10)	–	–	(2)	(12)
Charged against assets	–	(217)	(208)	–	(425)
Reserve balance					
June 30, 1999	35	–	–	9	44
<b>2000:</b>					
Charges	153	64	386	211	814
Cash spent	(100)	–	–	(220)	(320)
Charged against assets	–	(64)	(386)	–	(450)
Reserve balance					
June 30, 2000	88	–	–	–	88

Employee separation charges related to severance packages for approximately 2,800 people in 2000 and 400 people in 1999. The packages are predominantly voluntary and are formula driven based on salary levels and past service. Severance costs related to voluntary separations are charged to earnings when the employee accepts the offer.

Asset write-downs in 2000 related to assets held for sale or disposal and represented excess capacity that is in the process of being removed from service or disposed. These assets were written down to the lower of their current carrying basis or amounts expected to be realized upon disposal, less minor disposal costs. Asset write-downs in 1999 related primarily to manufacturing assets that are expected to operate at levels significantly below their capacity. The projected cash flows from such assets over their remaining useful lives are now estimated to be less than their current carrying values; therefore, the assets were written down to estimated fair value as determined using discounted cash flows. The asset write-downs charged to earnings will not have a significant impact on future depreciation charges.

Charges for accelerated depreciation related to long-lived assets that will be taken out of service prior to the end of their normal service period due to manufacturing consolidations, technology standardization and plant closures. The Company has shortened the estimated useful lives of such assets, resulting in accelerated depreciation.

Other costs included primarily relocation, training costs and legal entity restructuring costs directly related to the Organization 2005 initiative.

### NOTE 3 ACQUISITIONS

In 2000, the Company acquired The Iams Company and Affiliates for approximately \$2,222 in cash. Other acquisitions in 2000 totaled \$745 and consisted primarily of Recovery Engineering, Inc. and a joint venture ownership increase in China. The 2000 acquisitions were accounted for using the purchase method, and resulted in goodwill of \$2,508. Purchase acquisitions in 1999 totaled \$137. In 1998, the Company acquired Tambrands, Inc., and its leading brand, Tampax, for approximately \$1,844 in cash. Other acquisitions in 1998 totaled \$1,425 and included the acquisition of paper businesses and increased ownership in various ventures in Latin America and Asia. The 1998 acquisitions, all of which were accounted for using the purchase method, resulted in goodwill of \$3,335.

### NOTE 4 SUPPLEMENTAL FINANCIAL INFORMATION

	June 30	
	2000	1999
<b>Accrued and Other Liabilities</b>		
Marketing expenses	\$ 1,142	\$ 1,094
Compensation expenses	462	449
Other	2,117	2,540
	3,721	4,083
<b>Other Non-Current Liabilities</b>		
Other postretirement benefits	\$ 824	\$ 1,081
Pension benefits	975	926
Other	502	694
	2,301	2,701

### Selected Operating Expenses

Research and development costs are charged to earnings as incurred and were \$1,899 in 2000, \$1,726 in 1999 and \$1,546 in 1998. Advertising costs are charged to earnings as incurred and were \$3,667 in 2000, \$3,538 in 1999 and \$3,704 in 1998.

**Net Earnings Per Common Share**

Net earnings less preferred dividends (net of related tax benefits) are divided by the weighted average number of common shares outstanding during the year to calculate basic net earnings per common share. Diluted net earnings per common share are calculated to give effect to stock options and convertible preferred stock.

Basic and diluted net earnings per share are reconciled as follows:

	Years ended June 30		
	2000	1999	1998
Net earnings available to common shareholders	<b>\$3,427</b>	<b>\$3,654</b>	<b>\$3,676</b>
Effect of dilutive securities			
Preferred dividends, net of tax benefit	<b>115</b>	109	104
Preferred dividend impact on funding of ESOP	<b>(18)</b>	(22)	(25)
Diluted net earnings	<b>3,524</b>	<b>3,741</b>	<b>3,755</b>

Shares in thousands	Years ended June 30		
	2000	1999	1998
Basic weighted average common shares outstanding	<b>1,313.2</b>	1,328.1	1,343.4
Effect of dilutive securities			
Conversion of preferred shares	<b>94.3</b>	97.2	99.8
Exercise of stock options	<b>19.7</b>	21.5	22.3
Diluted weighted average common shares outstanding	<b>1,427.2</b>	<b>1,446.8</b>	<b>1,465.5</b>

**Equity Put Options**

During 2000, the Company entered into a series of equity put options on its common stock. These agreements will be settled on a physical or net-share basis at the Company's option and expire in the October-December 2000 quarter. The premium received from the sale of the instruments was credited to equity and reduces the Company's cash outlay for share repurchases.

As of June 30, 2000, put options equivalent to 12 million common shares were outstanding at prices ranging from \$60 to \$71 per share. The impact on diluted earnings per share is immaterial.

**NOTE 5 SHORT-TERM AND LONG-TERM DEBT**

	June 30	
	2000	1999
<b>Short-Term Debt</b>		
U.S. obligations	<b>\$2,142</b>	<b>\$2,308</b>
Foreign obligations	<b>785</b>	375
Current portion of long-term debt	<b>283</b>	467
	<b>3,210</b>	<b>3,150</b>

Millions of dollars except per share amounts

The weighted average short-term interest rates were 4.8% and 5.7% as of June 30, 2000 and 1999, respectively.

	Average Rate	Maturities	June 30	
			2000	1999
<b>Long-Term Debt</b>				
U.S. notes and debentures	5.73%	2000–2049	<b>\$7,664</b>	\$3,760
ESOP Series A	8.33%	2000–2004	<b>392</b>	472
ESOP Series B	9.36%	2007–2021	<b>1,000</b>	1,000
U.S. commercial paper			–	1,019
Foreign obligations			<b>143</b>	447
Current portion of long-term debt			<b>(283)</b>	(467)
			<b>8,916</b>	<b>6,231</b>

Long-term weighted average interest rates in the preceding table are as of June 30, 2000, and include the effects of related interest rate swaps discussed in Note 6.

The fair value of the long-term debt was \$8,929 and \$6,517 at June 30, 2000 and 1999, respectively. Long-term debt maturities during the next five years are as follows: 2001–\$283; 2002–\$472; 2003–\$534; 2004–\$1,139 and 2005–\$973.

**NOTE 6 RISK MANAGEMENT ACTIVITIES**

The Company is exposed to market risks, such as changes in interest rates and currency exchange rates. To manage the volatility relating to these exposures, the Company nets the exposures on a consolidated basis to take advantage of natural offsets. For the residual portion, the Company enters into various derivative transactions pursuant to the Company's policies in areas such as counterparty exposure and hedging practices. The financial impacts of these hedging instruments are offset in part or in whole by corresponding changes in the underlying exposures being hedged. The Company does not hold or issue derivative financial instruments for trading purposes.

**Interest Rate Management**

The Company's policy is to manage interest cost using a mix of fixed and variable rate debt. To manage this mix in a cost-efficient manner, the Company enters into interest rate swaps in which the Company agrees to exchange, at specified intervals, the difference between fixed and variable interest amounts calculated by reference to an agreed-upon notional principal amount. These swaps are designated to hedge underlying debt obligations. For qualifying hedges, the interest rate differential is reflected as an adjustment to interest expense over the life of the swaps.

Certain currency interest rate swaps are designated as hedges of the Company's foreign net investments. Currency effects of these hedges are reflected in the accumulated other comprehensive income section of shareholders' equity, offsetting a portion of the translation of the net assets.

The following table presents information for all interest rate instruments. The notional amount does not necessarily represent amounts exchanged by the parties and, therefore, is not a direct measure of the Company's exposure to credit risk. The fair value approximates the cost to settle the outstanding contracts. The carrying value includes the net amount due to counterparties under swap contracts, currency translation associated with currency interest rate swaps and any marked-to-market value adjustments of instruments.

	June 30	
	2000	1999
<b>Notional amount</b>	<b>\$7,955</b>	<b>\$1,614</b>
Fair value	\$ 105	\$ 7
Carrying value	149	15
Unrecognized loss	(44)	(8)

The increase in notional amount is due primarily to increased emphasis on matching the currency component of assets and liabilities on the Company's consolidated balance sheet. This activity hedges currency exposures in two ways. It hedges the Company's net investment position in major currencies and generates foreign currency interest payments which offset other transactional foreign exchange exposures in these currencies.

Although derivatives are an important component of the Company's interest rate management program, their incremental effect on interest expense for 2000, 1999 and 1998 was not material.

#### Currency Rate Management

The Company manufactures and sells its products in a number of countries throughout the world and, as a result, is exposed to movements in foreign currency exchange rates.

The Company's major foreign currency exposures involve the markets in Western and Eastern Europe, Asia and Mexico. The primary purpose of the Company's foreign currency hedging activities is to manage the volatility associated with foreign currency purchases of materials and other assets and liabilities created in the normal course of business. Corporate policy prescribes the range of allowable hedging activity. The Company primarily utilizes forward exchange contracts and purchased options with maturities of less than eighteen months.

In addition, the Company enters into certain foreign currency swaps to hedge intercompany financing transactions. The Company also utilizes purchased foreign currency options with maturities of generally less than eighteen months and forward exchange contracts to hedge against the effect of exchange rate fluctuations on royalties and income from international operations.

Gains and losses related to qualifying hedges of foreign currency firm commitments or anticipated transactions are deferred in prepaid expense and are included in the basis of the underlying transactions. To the extent that a qualifying hedge is terminated or ceases to be effective as a hedge, any deferred gains and losses up to that point continue to be deferred and are included in the basis of the underlying transaction. All other foreign exchange contracts are marked-to-market on a current basis, generally to marketing, research and administrative expense. To the extent anticipated transactions are no longer likely to occur, the related hedges are closed with gains or losses charged to earnings on a current basis.

Currency instruments outstanding are as follows:

	June 30	
	2000	1999
<b>Notional amount</b>		
Forward contracts	\$1,822	\$1,988
Purchased options	1,147	1,358
Currency swaps	0	33
<b>Fair value</b>		
Forward contracts	4	(6)
Purchased options	18	19
Currency swaps	0	5

The reduction in the notional amount of currency instruments outstanding reflects the increased efficiencies of our centralized global hedge program, including the foreign exchange exposure offsets generated by foreign currency interest payments. The deferred gains and losses on these currency instruments were not material.

In addition, in order to hedge currency exposures related to the net investments in foreign subsidiaries, the Company utilizes local currency financing entered into by the subsidiaries, currency interest rate swaps and other foreign currency denominated financing instruments entered into by the parent. Gains and losses on instruments designated as hedges of net investments are offset against the translation effects reflected in shareholders' equity.

Currency interest rate swaps, foreign currency instruments and foreign currency denominated debt that have been designated as hedges of the Company's net investment exposure in certain foreign subsidiaries have notional amounts totaling \$7,276 and \$826 at June 30, 2000 and 1999, respectively. These hedges resulted in gains of \$150 and \$5, net of \$88 and \$4 in tax effects, respectively, reflected in shareholders' equity.

#### Credit Risk

Credit risk arising from the inability of a counterparty to meet the terms of the Company's financial instrument contracts is generally limited to the amounts, if any, by which the counterparty's obligations exceed the obligations of the Company. It is the Company's policy to enter into financial instruments with a diversity of creditworthy counterparties. Therefore, the Company does not expect to incur material credit losses on its risk management or other financial instruments.

#### NOTE 7 STOCK OPTIONS

The Company has stock-based compensation plans under which stock options are granted annually to key managers and directors at the market price on the date of grant. The 2000 and 1999 grants are fully exercisable after three years and have a fifteen year life, while prior years' grants are fully exercisable after one year and have a ten year life. Beginning in 1998, the Company began granting stock options to all eligible employees not covered by the key manager and director plans. These one-time grants, which comprised 8.7 million of the 20.3 million options granted in 1998, are fully exercisable after five years and have a ten year life. The Company issues stock appreciation rights in countries where stock options are not permitted by local governments.

Pursuant to FASB Statement No. 123, "Accounting for Stock-Based Compensation," the Company has elected to account for its employee stock option plans under APB Opinion No. 25, "Accounting for Stock Issued to Employees." Under these plans, stock options have been issued at fair value and therefore, compensation cost has not been recognized. Had compensation cost for the plans been

determined based on the fair value at the grant date consistent with FASB Statement No. 123, the Company's net earnings and earnings per share would have been as follows:

	Years ended June 30		
	2000	1999	1998
Net earnings			
As reported	\$ 3,542	\$ 3,763	\$ 3,780
Pro forma	3,363	3,683	3,472
Net earnings per common share			
Basic			
As reported	\$ 2.61	\$ 2.75	\$ 2.74
Pro forma	2.47	2.69	2.51
Diluted			
As reported	2.47	2.59	2.56
Pro forma	2.34	2.53	2.35

The fair value of each option grant is estimated on the date of grant using a binomial option-pricing model with the following assumptions:

	Options Granted in Years ended June 30		
	2000	1999	1998
Interest rate	6.0%	5.4%	5.6%
Dividend yield	1.5%	1.5%	2.0%
Expected volatility	28%	26%	26%
Expected life in years	9	7	6

Stock option activity was as follows:

	Options in Thousands		
	2000	1999	1998
Outstanding, July 1	76,810	79,918	68,514
Granted	14,360	7,026	20,315
Exercised	(7,401)	(9,397)	(8,477)
Canceled	(1,025)	(737)	(434)
Outstanding, June 30	82,744	76,810	79,918
Exercisable	54,667	61,664	59,610
Available for grant	41,387	39,874	31,558
Average price:			
Outstanding, beginning of year	\$52.11	\$45.58	\$31.00
Granted	96.10	89.72	83.26
Exercised	25.21	22.36	18.57
Outstanding, end of year	61.73	52.11	45.58
Exercisable, end of year	46.67	43.79	32.74
Weighted average fair value of options granted during the year	37.21	32.23	24.56

## The Procter &amp; Gamble Company and Subsidiaries

The following table summarizes information about stock options outstanding at June 30, 2000:

Range of prices	Options Outstanding		
	Number Outstanding (Thousands)	Weighted Avg. Exercise Price	Weighted Avg. Remaining Contractual Life
\$20 to 30	19,517	\$25.61	2.2 years
33 to 46	15,124	37.89	5.1
57 to 85	28,044	75.52	7.3
86 to 107	20,059	95.59	13.5

The following table summarizes information about stock options exercisable at June 30, 2000:

Range of prices	Options Exercisable	
	Number Exercisable (Thousands)	Weighted Avg. Exercise Price
\$20 to 30	19,517	\$25.61
33 to 46	15,124	37.89
57 to 85	19,547	73.41
86 to 107	479	91.14

#### NOTE 8 EMPLOYEE STOCK OWNERSHIP PLAN

The Company maintains The Procter & Gamble Profit Sharing Trust and Employee Stock Ownership Plan (ESOP) to provide funding for two primary postretirement benefits: a defined contribution profit sharing plan and certain U.S. postretirement health care benefits.

The ESOP borrowed \$1,000 in 1989, which has been guaranteed by the Company. The proceeds were used to purchase Series A ESOP Convertible Class A Preferred Stock to fund a portion of the defined contribution plan. Principal and interest requirements are \$117 per year, paid by the trust from dividends on the preferred shares and from cash contributions and advances from the Company. The shares are convertible at the option of the holder into one share of the Company's common stock. Annual credits to participants' accounts are based on individual base salaries and years of service, and do not exceed 15% of total participants' annual salaries and wages. The liquidation value is equal to the issue price of \$13.75 per share.

	Years ended June 30		
	2000	1999	1998
ESOP preferred shares allocated			
at market value	\$313	\$279	\$235
Company contributions	1	18	35
Benefits earned	314	297	270

In 1991, the ESOP borrowed an additional \$1,000, also guaranteed by the Company. The proceeds were used to purchase Series B ESOP Convertible Class A Preferred Stock to fund a portion of retiree health care benefits. Debt service requirements are \$94 per year, funded by preferred stock dividends and cash contributions from the Company. Each share is convertible at the option of the holder into one share of the Company's common stock. The liquidation value is equal to the issue price of \$26.12 per share.

	Shares in Thousands		
	2000	1999	1998
Outstanding, June 30			
Series A	55,925	58,342	60,635
Series B	37,085	37,485	37,805

Shares of the ESOP are allocated at original cost based on debt service requirements, net of advances made by the Company to the trust. Dividends on all preferred shares, net of related tax benefit, are charged to retained earnings. The preferred shares held by the ESOP are considered outstanding from inception for purposes of calculating diluted net earnings per common share.

The fair value of the Series A shares serves to reduce the Company's cash contribution required to fund the profit sharing plan contributions earned. The Series B shares are considered plan assets of the other retiree benefits plan.

#### NOTE 9 POSTRETIREMENT BENEFITS

The Company offers various postretirement benefits to its employees.

##### Defined Contribution Retirement Plans

Within the U.S., the most significant retirement benefit is the defined contribution profit sharing plan described in Note 8.

##### Other Retiree Benefits

The Company also provides certain health care and life insurance benefits for substantially all U.S. employees who become eligible for these benefits when they meet minimum age and service requirements. Generally, the health care plans require contributions from retirees and pay a stated percentage of expenses, reduced by deductibles and other coverages. Retiree contributions change annually in line with health care cost trends. These benefits are partially funded by an ESOP, as well as certain other assets contributed by the Company.

Certain other employees, primarily outside the U.S., are covered by local defined benefit pension, health care and life insurance plans.

The elements of the net amount recognized for the Company's postretirement plans are summarized below:

	Years ended June 30			
	Pension Benefits		Other Retiree Benefits	
	2000	1999	2000	1999
<b>Change in Benefit Obligation</b>				
<b>Benefit obligation</b>				
at beginning of year	<b>\$2,488</b>	<b>\$2,282</b>	<b>\$ 1,199</b>	<b>\$ 1,465</b>
Service cost	120	111	39	49
Interest cost	151	140	90	97
Participants' contributions	4	4	16	17
Amendments	9	(5)	20	(1)
Actuarial loss (gain)	35	164	(7)	(356)
Acquisitions	47	4	0	0
Curtailments and settlements	(20)	(3)	0	0
Currency exchange	(79)	(73)	(3)	(1)
Benefit payments	(128)	(136)	(84)	(71)
Benefit obligation at end of year	<b>2,627</b>	<b>2,488</b>	<b>1,270</b>	<b>1,199</b>
<b>Change in Plan Assets</b>				
<b>Fair value of plan assets</b>				
at beginning of year	<b>1,555</b>	<b>1,523</b>	<b>2,516</b>	<b>2,611</b>
Actual return on plan assets	198	111	(1,178)	(49)
Acquisitions	28	4	0	0
Employer contributions	73	95	4	8
Participants' contributions	4	4	16	17
Settlements	(2)	0	0	0
Currency exchange	(37)	(46)	0	0
Benefit payments	(128)	(136)	(84)	(71)
Fair value of plan assets at end of year	<b>1,691</b>	<b>1,555</b>	<b>1,274</b>	<b>2,516</b>
<b>Funded Status</b>				
Funded status at end of year	(936)	(933)	4	1,317
Unrecognized net actuarial loss (gain)	(30)	17	(828)	(2,384)
Unrecognized transition amount	21	27	0	0
Unrecognized prior service cost	39	37	1	(21)
Net amount recognized	<b>(906)</b>	<b>(852)</b>	<b>(823)</b>	<b>(1,088)</b>
Prepaid benefit cost	\$ 59	\$ 59	\$ 2	\$ 1
Accrued benefit cost	(990)	(936)	(825)	(1,089)
Accumulated other comprehensive income	25	25	0	0
Net liability recognized	<b>(906)</b>	<b>(852)</b>	<b>(823)</b>	<b>(1,088)</b>

The Company's stock comprised \$1,123 and \$2,346 of other retiree plan assets, net of Series B ESOP debt, as of June 30, 2000 and 1999, respectively.

Assumptions for the postretirement benefit calculations are as follows:

	Years ended June 30			
	Pension Benefits		Other Retiree Benefits	
	2000	1999	2000	1999
<b>Weighted average assumptions</b>				
Discount rate				
Expected return on plan assets	6.1%	6.0%	8.0%	7.5%
Rate of compensation increase	8.1%	7.9%	10.0%	10.0%
Initial health care cost trend rate*	4.5%	4.6%	—	—
Initial health care cost trend rate*	—	—	5.8%	6.0%

\*Assumed to decrease to 5.0% by 2006 and remain at that level thereafter.

Components of the net periodic benefit cost are as follows:

	Years ended June 30					
	Pension Benefits			Other Retiree Benefits		
	2000	1999	1998	2000	1999	1998
<b>Components of Net Periodic Benefit Cost</b>						
Service cost						
Interest cost	\$ 120	\$ 111	\$ 106	\$ 39	\$ 49	\$ 42
Expected return on plan assets	151	140	148	90	97	102
Amortization of prior service cost	(122)	(105)	(103)	(294)	(218)	(171)
Amortization of transition amount	7	8	7	(2)	(2)	(2)
Settlement (gain)	4	3	3	0	0	0
Curtailment loss (gain)	(6)	0	0	0	0	0
Recognized net actuarial loss (gain)	(3)	0	12	0	0	0
Gross benefit cost	4	4	0	(92)	(58)	(41)
Dividends on ESOP preferred stock	155	161	173	(259)	(132)	(70)
Net periodic benefit cost	0	0	0	(77)	(78)	(78)

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the pension plans with accumulated benefit obligations in excess of plan assets were \$1,368, \$1,073 and \$189, respectively, as of June 30, 2000, and \$1,382, \$1,122 and \$233, respectively, as of June 30, 1999.

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

	One Percentage Point Increase	One Percentage Point Decrease
Effect on total of service and interest cost components	\$ 23	\$ (18)
Effect on postretirement benefit obligation	167	(138)

#### NOTE 10 INCOME TAXES

Earnings before income taxes consist of the following:

	Years ended June 30		
	2000	1999	1998
United States	\$ 3,006	\$ 3,474	\$ 3,632
International	2,530	2,364	2,076
	5,536	5,838	5,708

The income tax provision consists of the following:

	Years ended June 30		
	2000	1999	1998
<b>Current Tax Expense</b>			
U.S. Federal	\$ 648	\$ 1,080	\$ 996
International	816	934	918
U.S. State & Local	67	121	115
	1,531	2,135	2,029
<b>Deferred Tax Expense</b>			
U.S. Federal	241	(74)	51
International & other	222	14	(152)
	463	(60)	(101)
	1,994	2,075	1,928

Taxes credited to shareholders' equity for the years ended June 30, 2000 and 1999 were \$59 and \$222, respectively. Undistributed earnings of foreign subsidiaries that are considered to be reinvested indefinitely were \$8,828 at June 30, 2000.

The Company's effective income tax rate was 36.0%, 35.5% and 33.8% in 2000, 1999 and 1998, respectively, compared to the U.S. statutory rate of 35.0%. Excluding the Organization 2005 program costs and related tax effects, the effective tax rate was 33.4% in 2000 and 34.4% in 1999. This change reflects the execution of tax planning opportunities which is offset by the impact of various country tax rates on Organization 2005 program costs.

Deferred income tax assets and liabilities are comprised of the following:

	June 30	
	2000	1999
Current deferred tax assets	\$ 309	\$ 621
Non-current deferred tax assets (liabilities)		
Depreciation	\$ (951)	\$ (979)
Other postretirement benefits	273	392
Loss and other carryforwards	332	206
Other	(279)	19
	(625)	(362)

Included in Other above are valuation allowances of \$207 and \$140 in 2000 and 1999, respectively.

#### NOTE 11 COMMITMENTS AND CONTINGENCIES

The Company has purchase commitments for materials, supplies and property, plant and equipment incidental to the ordinary conduct of business. In the aggregate, such commitments are not at prices in excess of current market.

The Company is subject to various lawsuits and claims with respect to matters such as governmental regulations, income taxes and other actions arising out of the normal course of business. The Company is also subject to contingencies pursuant to environmental laws and regulations that in the future may require the Company to take action to correct the effects on the environment of prior manufacturing and waste disposal practices. Accrued environmental liabilities for remediation and closure costs at June 30, 2000 and 1999 were \$47 and \$58, respectively, and, in management's opinion, such accruals are appropriate based on existing facts and circumstances. Current year expenditures were not material.

While considerable uncertainty exists, in the opinion of management and Company counsel, the ultimate liabilities resulting from such claims will not materially affect the Company's financial statements.

**NOTE 12 SEGMENT INFORMATION**

On July 1, 1999, as part of the Organization 2005 initiative, the Company changed its internal management structure to product-based global business units. Previously, the Company had been organized on a geographic basis. The segments manufacture and market products as follows:

- Fabric and home care includes laundry care, dish care, fabric conditioners and hard surface cleaners.
- Paper aggregates tissues and towel, feminine care and baby care, which contains diapers and wipes.
- Beauty care includes cosmetics, hair care, deodorants, fragrances and other beauty products.

- Health care includes personal health care, oral care, prescription drugs and pet health and nutrition.

- Food and beverage includes coffee, snacks, commercial services, juice, peanut butter and shortening and oil.

The Corporate segment includes both operating and non-operating elements such as financing and investing activities, goodwill amortization, employee benefit costs, charges related to restructuring (including the Organization 2005 program), segment eliminations and other general corporate items. The segment eliminations adjust management reporting principles to accounting principles generally accepted in the United States of America and primarily affect the treatment of unconsolidated investees and income taxes, which are reflected in the business segments using applicable local statutory tax rates. Corporate assets primarily include cash, investment securities and goodwill.

	Fabric and Home Care	Paper	Beauty Care	Health Care	Food and Beverage	Corporate	Total
<b>Net Sales</b>	<b>2000</b>	<b>\$12,157</b>	<b>\$12,044</b>	<b>\$7,389</b>	<b>\$3,909</b>	<b>\$4,634</b>	<b>\$(182)</b>
	1999	11,415	12,190	7,376	2,876	4,655	(387)
	1998	11,019	11,685	7,469	2,889	4,620	(528)
<b>Net Earnings</b>	<b>2000</b>	<b>1,450</b>	<b>1,069</b>	<b>894</b>	<b>335</b>	<b>364</b>	<b>(570)</b>
	1999	1,497	1,278	917	242	328	(499)
	1998	1,406	990	845	232	294	13
<b>Before-Tax Earnings</b>	<b>2000</b>	<b>2,318</b>	<b>1,817</b>	<b>1,393</b>	<b>540</b>	<b>566</b>	<b>(1,098)</b>
	1999	2,417	2,195	1,457	372	528	(1,131)
	1998	2,240	1,772	1,379	381	477	(541)
<b>Depreciation and Amortization</b>	<b>2000</b>	<b>354</b>	<b>664</b>	<b>194</b>	<b>159</b>	<b>153</b>	<b>667</b>
	1999	293	638	198	107	149	763
	1998	295	611	198	105	135	254
<b>Total Assets</b>	<b>2000</b>	<b>5,477</b>	<b>8,415</b>	<b>3,497</b>	<b>2,229</b>	<b>2,611</b>	<b>11,965</b>
	1999	5,047	8,184	3,754	1,556	2,598	10,974
<b>Capital Expenditures</b>	<b>2000</b>	<b>807</b>	<b>1,282</b>	<b>310</b>	<b>195</b>	<b>235</b>	<b>189</b>
	1999	638	1,327	285	143	237	198

The Company had net sales in the United States of \$20,038, \$18,314 and \$17,848 for the years ended June 30, 2000, 1999 and 1998, respectively. Assets in the United States totaled \$17,227 and \$15,142 as of June 30, 2000 and 1999, respectively.

The Company's largest customer, Wal-Mart Stores, Inc. and its affiliates, accounted for 14%, 12% and 11% of consolidated net sales in 2000, 1999 and 1998, respectively. These sales occurred primarily in the United States.

## NOTE 13 QUARTERLY RESULTS (UNAUDITED)

		Quarters Ended			Total Year
		Sept. 30	Dec. 31	Mar. 31	
Net Sales	1999–2000	\$9,919	\$10,588	\$9,783	\$9,661
	1998–1999	9,510	9,934	9,231	9,450
Operating Income*	1999–2000	1,847	1,842	1,320	945
	1998–1999	1,874	1,837	1,665	877
Net Earnings*	1999–2000	1,147	1,126	753	516
	1998–1999	1,167	1,142	1,040	414
Diluted Net Earnings Per Common Share*	1999–2000	.80	.78	.52	.36
	1998–1999	.80	.78	.72	.29

## FINANCIAL HIGHLIGHTS

	2000	1999	1998	1997	1996
Net Sales	\$39,951	\$38,125	\$37,154	\$35,764	\$35,284
Operating Income*	5,954	6,253	6,055	5,488	4,815
Net Earnings*	3,542	3,763	3,780	3,415	3,046
Core Net Earnings	4,230	4,148	3,780	3,415	3,046
Net Earnings Margin*	8.9%	9.9%	10.2%	9.5%	8.6%
Core Net Earnings Margin	10.6%	10.9%	10.2%	9.5%	8.6%
Basic Net Earnings Per Common Share*	2.61	2.75	2.74	2.43	2.14
Diluted Net Earnings Per Common Share*	2.47	2.59	2.56	2.28	2.01
Diluted Core Net Earnings Per Common Share	2.95	2.85	2.56	2.28	2.01
Dividends Per Common Share	1.28	1.14	1.01	.90	.80
Research and Development Expense	1,899	1,726	1,546	1,469	1,399
Advertising Expense	3,667	3,538	3,704	3,466	3,254
Total Assets	34,194	32,113	30,966	27,544	27,730
Capital Expenditures	3,018	2,828	2,559	2,129	2,179
Long-Term Debt	8,916	6,231	5,765	4,143	4,670
Shareholders' Equity	12,287	12,058	12,236	12,046	11,722

\*2000 and 1999 amounts include Organization 2005 program costs.

## DIRECTORS

**Norman R. Augustine**

Chairman of the Executive Committee, Lockheed Martin Corporation (aerospace, electronics, telecommunications, information management and energy systems)

**Donald R. Beall**

Retired Chairman and Chief Executive Officer, Rockwell International Corporation (industrial automation, avionics and communications and electronic commerce) and Chairman of the Executive Committee, Rockwell International Corporation

**Gordon F. Brunner**

Former Chief Technology Officer

**Richard B. Cheney**

Former Chairman of the Board and Chief Executive Officer, Halliburton Company (energy services, engineering and construction) and currently on leave of absence from the board

**Richard J. Ferris**

Retired Co-Chairman, Doubletree Corporation

**Joseph T. Gorman**

Chairman and Chief Executive Officer, TRW Inc. (automotive, aerospace and information systems)

**A. G. Lafley**

President and Chief Executive

**Charles R. Lee**

Chairman and Co-Chief Executive Officer, Verizon Communications (telecommunication services)

**Lynn M. Martin**

Professor, J. L. Kellogg Graduate School of Management, Northwestern University

**John E. Pepper**

Chairman of the Board

**John F. Smith Jr.**

Chairman of the Board, General Motors Corporation (automobile and related businesses)

**Ralph Snyderman**

Chancellor for Health Affairs, Executive Dean, School of Medicine at Duke University, and

President/CEO of Duke University Health Systems

**Robert D. Storey**

Partner in the law firm of Thompson, Hine & Flory, L.L.P.

**Marina v.N. Whitman**

Professor of Business Administration and Public Policy, University of Michigan

***In Memory***

*John Sawhill, a member of P&G's Board since 1996 and President and Chief Executive Officer of The Nature Conservancy, died unexpectedly on May 18. His character, spirit and leadership will be deeply missed by all who knew and worked with him.*

## CORPORATE OFFICERS

**John E. Pepper**

Chairman of the Board

**A. G. Lafley**

President and Chief Executive

**Fernando Aguirre**

President – Global Feminine Care

**Susan E. Arnold**

President – Personal Beauty Care

**Antonio Belloni**

President – Western Europe

**Charles V. Bergh**

President – ASEAN, Australasia & India

**Wolfgang C. Berndt**

President – Global Fabric & Home Care

**Bruce L. Byrnes**

President – Global Beauty Care and Global Health Care

**R. Kerry Clark**

President – Global Market Development Organization

**Michael Clasper**

President – Global Home Care and New Business Development

**Stephen P. Donovan Jr.**

President – Global Beverage and North America Food & Beverage

**Mark D. Ketchum**

President – Global Baby Care and Global Feminine Care

**Fuad O. Kuraytim**

President on Special Assignment

**Gary T. Martin**

President – Global Tissues & Towel

**Robert A. McDonald**

President – Northeast Asia

**Jorge P. Montoya**

President – Global Food & Beverage and Latin America

**Martin J. Nuechtern**

President – Global Hair Care

**Dimitri Panayotopoulos**

President – Greater China

**Paul Polman**

President – Global Fabric Care

**Herbert Schmitz**

President – Central & Eastern Europe, Middle East, Africa & General Export

**Robert A. Steele**

President – North America Market Development Organization

**Richard L. Antoine**

Global Human Resources & Product Supply Officer

**Gordon F. Brunner**

Former Chief Technology Officer (External Technical Ventures)

**G. Gilbert Cloyd**

Chief Technology Officer

**Clayton C. Daley Jr.**

Chief Financial Officer

**Stephen N. David**

Chief Information Officer and Business-to-Business Officer

**James J. Johnson**

Chief Legal Officer

**Charlotte R. Otto**

Global External Relations Officer

**Robert L. Wehling**

Global Marketing and Government Relations Officer

**Michael J. Power**

Vice President – Global Business Services

**Gretchen W. Price**

Vice President & Treasurer

**David R. Walker**

Vice President & Comptroller

**Terry L. Overby**

Secretary

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### PERSON TO PERSON

Shareholder Services representatives available

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1-800-742-6253

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Automated service available after U.S. business hours

### OR WRITE

The Procter & Gamble Company

Shareholder Services Department

P.O. Box 5572

Cincinnati, Ohio 45201-5572

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### CORPORATE HEADQUARTERS

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### TRANSFER AGENT/SHAREHOLDER SERVICES

The Procter & Gamble Company

Shareholder Services Department

P.O. Box 5572

Cincinnati, Ohio 45201-5572

### REGISTRAR

Chase Manhattan Trust Company, N.A.

255 East Fifth Street, Suite 2115

Cincinnati, Ohio 45202

### EXCHANGE LISTING

New York, Cincinnati, Amsterdam, Paris, Basle, Geneva, Lausanne, Zurich, Frankfurt, Brussels, Tokyo

### SHAREHOLDERS OF COMMON STOCK

There were 291,965 Common Stock shareholders of record, including participants in the Shareholder Investment Program, as of July 21, 2000.

### FORM 10-K

Shareholders may obtain a copy of the Company's 2000 report to the Securities and Exchange Commission on Form 10-K by going to P&G's investor Web site at [www.pg.com/investor](http://www.pg.com/investor) or by calling us at 1-800-764-7483. This information is also available at no charge by sending a request to Shareholder Services at the address listed above.

### SHAREHOLDERS' MEETING

The next annual meeting of shareholders will be held on Tuesday, October 10, 2000. A full transcript of the meeting will be available from Linda D. Rohrer, Assistant Secretary, at a cost of \$10. Ms. Rohrer can be reached at One P&G Plaza, Cincinnati, Ohio 45202-3315.

### COMMON STOCK PRICE RANGE AND DIVIDENDS

Quarter ended	Price Range				Dividends	
	1999-2000		1998-1999			
	High	Low	High	Low	1999-2000	1998-1999
September 30	\$104.13	\$84.56	\$ 94.00	\$65.13	\$ .32	\$ .2850
December 31	115.63	92.00	94.81	69.63	.32	.2850
March 31	118.38	52.75	101.81	82.00	.32	.2850
June 30	72.75	53.25	103.81	84.13	.32	.2850

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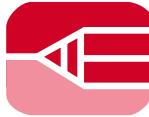
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