

# New Challenges

Over the last three years, we have worked to regain our customers' trust. Building on this progress, we are now aiming to make the next three years a period of higher growth and returns. Fiscal 2007 must therefore be a transformational year for Fujitsu. This feature highlights some of the initiatives we will be taking in the current fiscal year to realize this goal.

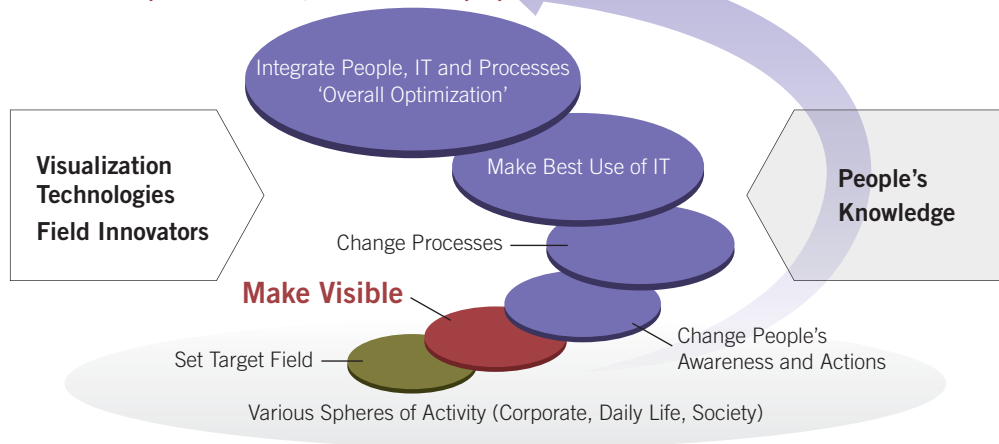


## What is the background to your new “field innovation” approach?

There is no letup in the pace of IT innovation. Today, we can realize many more opportunities by fully utilizing a whole range of IT products and services. However, as IT has evolved, so too has the complexity and impenetrability of systems knowledge, with the result that related business processes and the role of people in these processes have become harder to identify. Some customers even tell us that it is now more difficult to understand what is going on in their businesses and work sites. It is clear that focusing on IT alone will not help customers to improve their businesses. Originally, introducing IT was meant to help companies upgrade business processes and use the knowledge of their employees more effectively. I believe we now have to return to this starting point. First, we must make the relationships between people, processes and IT more visible. This is essential if we are to truly take the customer’s viewpoint. This is what we call “field innovation.” This idea is an important factor in our new medium-term strategic plan, which is explained later in this report.

### ■ Field Innovation—Converting IT-enabled Innovation into Business Value

Bring innovation to companies, people’s daily lives and society at large through the continual improvement of processes and IT, with a focus on people



### How did Fujitsu perform in fiscal 2006?

In the year under review, consolidated net sales increased 6.4%, to ¥5,100.1 billion. Operating income, although short of our initial target of ¥190.0 billion, rose 0.3% year on year, to ¥182.0 billion. As a result, we maintained the trend of higher sales and earnings.

Looking at our sales performance, while certain areas of the electronic devices market slowed, sales were favorable overall, as sales of services and UNIX servers grew strongly overseas and unit shipments of hard disk drives (HDDs) reached an all-time high.

However, the rise in operating income was limited compared to the rate of sales growth. Global price competition intensified, especially in product areas, and although we worked to cut costs, we were not able to fully offset the drop in prices. Other factors impacting profitability included higher expenses related to new business acquisitions and other initiatives to expand our business in Europe and North America, investment in advanced logic LSI technologies, and heavier upfront strategic expenditures in both hardware and software.

### As a backdrop to your new medium-term strategic plan, could you first review the last three years at Fujitsu?

Our management focus during the last three years was centered on regaining the trust of customers and improving the viability of various businesses. We put particular effort into helping employees regain the will and ability to take on our rivals with confidence. Specifically, we concentrated on initiatives to fix problematic areas by reducing the incidence of project failures, raising quality, and boosting operational efficiency. We have made real progress, illustrated by an approximate 50% drop over the last three years in the number of Group companies reporting operating losses. Although challenges remain with respect to earnings growth, we were able to increase sales and earnings during this period.

Operating income has now exceeded the ¥180 billion level for the past two fiscal years, up from around ¥160 billion in fiscal 2004, while the operating income margin rose from 3.2% in fiscal 2003, to 3.6% in fiscal 2006. However, this increase of only 0.4 of a percentage point stands in contrast with a sales growth rate of 7.0% over the same period.

Meanwhile, other expenses have declined and the monthly inventory turnover rate has improved from 0.64 in fiscal 2003 to 0.93 in fiscal 2006. Our financial position is clearly better, and I believe Fujitsu has regained its underlying strength.

### What are the objectives and key elements of your new medium-term strategic plan?

Our new medium-term strategic plan covers the three fiscal years through fiscal 2009, ending March 31, 2010. Based on a review of our performance over the last three years, our foremost

#### ■ New Medium-term Goals (FY 2007–2009)

		FY 2006 Results	Medium-term Targets (FY 2009)
Operating Income	Consolidated	3.6%	Over 5%
Margins	Technology Solutions	5.2%	Over 7%
Overseas Sales Ratio		36%	Over 40%
Monthly Inventory Turnover		0.93 times	2 times*

\*Set as medium- to long-term target level



objective will be to boost operating income margins. Specifically, we are aiming to raise our overall operating income margin to more than 5.0% in fiscal 2009, compared with 3.6% in fiscal 2006. We also want to raise the operating income margin in our core Technology Solutions segment to above 7.0%.

Another goal is to step up our business expansion in overseas markets that are growing strongly. Our aim is to increase the proportion of overseas sales from the current 36% of consolidated net sales to more than 40% by fiscal 2009.

Over the same period, we are also aiming to improve the monthly inventory turnover rate to approximately 2.0 times, compared with 0.93 in fiscal 2006.

In terms of business development, we plan to focus on the services business to drive earnings growth in our mainstay Technology Solutions segment. We will also build an operating structure to ensure that higher sales in our HDD and device businesses translate into stronger earnings.



### **What management initiatives will you pursue in order to achieve the goals of the new medium-term strategic plan?**

The key phrase for the next three fiscal years is “boost earnings and growth.” Under our medium-term strategic plan, we will focus on reinforcing areas of our business that are already strong—the services business being one example. We will also implement constructive, Group-wide organizational realignment and work to extend our business domain from IT solutions into business solutions.

Naturally, we remain committed to four key principles that have underpinned our management approach at Fujitsu for many years, namely: to always think and act from the customer’s perspective, to maintain and improve timely delivery and quality, to increase the speed of our business operations, and to think and act on frontline realities.

We have now added three new management principles to this list. First, we will work to enhance collaboration between sales and product development functions in order to create competitive product and service offerings that will allow us to increase market share and raise profitability. Second, we will follow the principle of cash flow-conscious management to encourage each Fujitsu business to be more self-sufficient. And third, recognizing that people

are our greatest asset, we will pursue management that seeks to realize the full potential of our human resources.

### **Could you give some more details on how you plan to create a competitive product lineup by enhancing collaboration between sales and product development?**

The kind of value customers seek from IT products and services is becoming exceptionally diverse. In servers, for example, the days when providing high-performance systems was enough to please customers are over. Today, their requirements may include quiet, compact servers for office environments, models that consume less power and have other environmentally friendly features, and systems that are easier to operate and reduce the potential for operational errors. The key to staying ahead in this market is creating products that offer customers real added value, or more specifically, developing and launching products with value that makes them stand out in the marketplace as quickly as possible. Another trend is shorter product life cycles, which means manufacturers have to sell out products in a very short time frame. In this context, we have to carefully predict demand to ensure we are not left with excess inventories.

To make all this happen, our product development engineers have to work more closely with our sales people in order to listen to customers' feedback and experience the actual workplace environments where our products will be used. At the same time, our marketing units, customer support units and, in fact, our entire organization, have to rebuild systems and development processes centered on product and service offerings. In this way, through an operational approach that brings us closer to customers and their actual businesses, we will be able to create a lineup of more competitive products and services.

#### ■ New Management Principles

Recurring themes over the past 3 years:

- Think and act from the customer's viewpoint
- Continue to maintain timely delivery and quality
- Continue to increase speed
- Think and act on frontline realities

#### ■ Competitive Product & Service Offerings

##### *Enhancing collaboration between sales and product development*

- Focus management efforts on creating competitive product and service offerings that can drive up market share and profits
- Align organization and processes to create product and service offerings from the customer's perspective

#### ■ Self-sufficiency

##### *Cash-flow-conscious management*

- Business operations should subsist on the cash flow they generate

#### ■ Human Knowledge as an Asset

##### *Management for realizing full potential of human resources*

- Allocation and cultivation of human resources that make fullest use of people's value (potential)
- Promote Group management and Group-wide HR management

## ■ Four Challenges for FY 2007–2009

- Create a new Group management structure
- Strengthen strategic thinking based on JQA\*
- Think and act more thoroughly from a Group-wide perspective

**Strengthen Our Management**

**Improve Our Product and Service Offerings**

- Reform product and service development processes (enhance collaboration with sales)
- Pursue new types of product and service value
- Develop easy-to-implement systems that do not require extensive system engineering resources to deploy or maintain

**As a partner to our customers, strive to contribute to their business success and grow together with them**

- Place importance on frontline operational realities
- Take advantage of people's frontline expertise and promote teamwork
- Implement field innovation in our own operations

**Enhance Our Frontline Operational Capabilities**

**Empower Our People**

- Cultivate lifelong learners (encourage self-improvement)
- Foster field innovators
- Nurture global human resources

\*JQA: Japan Quality Award

## Could you tell us about the four key challenges that you intend to tackle in the new medium-term strategic plan?

Simply put, we will vigorously pursue management that focuses on people and product and service offerings. In so doing, we will tackle four key challenges: improve our product and service offerings, empower our people, enhance our frontline operational capabilities, and strengthen our management. In strengthening our product and service competitiveness, we have to carefully identify the new types of value customers are seeking. Enhancing collaboration between sales and product development functions is one way of doing this. In addition, until now, we have supplied many products based on the assumption of having teams of system engineers to manage them. Going forward, we must challenge ourselves to develop and provide more products that do not rely on system engineers, in other words, systems that are easier to deploy and manage and will therefore enable us to increase sales volumes. In regard to the challenge of empowering our people, a key theme will be to develop people capable of supporting our field innovation approach by helping our employees acquire more specialist skills. Enhancing our frontline operational capabilities will focus on pursuing field innovation in our own operations, as well as on encouraging better teamwork. Finally, strengthening management capability will be crucial to ensure that operational reforms going forward are implemented effectively. Two key themes will be enhancing the strategic thinking of senior managers based on our existing JQA program designed to raise the quality of management, and creating a new Group management structure.

**You mentioned the medium-term target of raising the ratio of overseas sales to consolidated net sales from 36% to more than 40%. How will you do this?**

We plan to further grow our business overseas by developing strategies tailored to each market and building on the Fujitsu Group's capabilities. In Europe, the Middle East and Africa (EMEA), we are building a strong presence in the public-sector IT market, especially in the UK. We also plan to expand our business in the commercial sector and enhance our capabilities in markets across continental Europe. In the Americas, along with working to strengthen our individual businesses in fields such as photonics, servers, PCs and services, we will strive to enhance Fujitsu's overall presence in the market.

In the Asia Pacific (APAC) and China regions, our business is currently centered on the local operations of Japanese companies. Going forward, we will work to grow our business with indigenous companies. We obviously see China and India as growing markets for our products and services, and we will also focus on these countries as strategic offshore sites for our services operations.





■ Expanding Global Business Capabilities ~Grasp market characteristics and steadily expand opportunities for growth~

<b>EMEA</b>	<p><b>Head:</b> Corporate Sr. VP Richard Christou (Also serves as FS Chairman)  <b>FY06 Sales:</b> 795.8 billion yen (+15.4%)  <b>Mid-term regional goal:</b> 8% growth/year  <b>FS sales:</b> (FY05) £2,294M→(FY07) £2,700M (About ¥600.0 billion)</p>	<ul style="list-style-type: none"> <li>■ Fujitsu Services: Build on strength as top-tier services company for UK government/public sector • Work to expand business in continental Europe and with private-sector clients               <ul style="list-style-type: none"> <li>• Acquired TDS of Germany in Jan. '07</li> </ul> </li> <li>■ Expand TRIOLE deployment (including for services)</li> </ul>
<b>The Americas</b>	<p><b>Head:</b> Corporate Sr. VP Tetsuo Urano  <b>FY06 Sales:</b> 472.9 billion yen (+21.9%)  <b>Mid-term regional goal:</b> 14% growth/year  <b>FC sales:</b> (FY05) \$384M→(FY07) \$700M (About ¥80.0 billion)</p>	<ul style="list-style-type: none"> <li>■ Fujitsu Consulting: Expand services capabilities through M&amp;A               <ul style="list-style-type: none"> <li>• Acquired Rapidigm in Mar. '06</li> </ul> </li> <li>■ Reorganize global retail business</li> <li>■ Develop vertically integrated solutions business</li> </ul>
<b>APAC and China</b>	<p><b>Head (China):</b> Corporate First Sr. VP Takashi Igarashi  <b>Head (APAC):</b> Corporate Sr. VP Kyung-soo Ahn  <b>FY06 Sales:</b> 556.4 billion yen (+8.3%)  <b>Mid-term regional goal:</b> 11% growth/year</p>	<ul style="list-style-type: none"> <li>■ Expand Fujitsu Australia's SAP business               <ul style="list-style-type: none"> <li>• Expand outsourcing services business</li> </ul> </li> <li>■ Strengthen local management in China market</li> <li>■ Full-fledged start-up of business in India</li> </ul>

\* FY06 sales are regional net sales to unaffiliated customers; FS=Fujitsu Services, FC=Fujitsu Consulting; FY07 figures are estimates.



## How do you plan to strengthen the struggling System Platforms sub-segment?

System Platforms is struggling now, but it is an extremely important part of our business, because these platforms support and help us to differentiate our services business.

We plan to strengthen System Platforms in a number of ways. First, we will push forward with reforms to our product development process based on enhancing collaboration between sales and product development functions. This will allow us to more accurately identify the needs of customers and sales channels, and then reflect these needs in our product offerings. Second, we will streamline the number of models and product options in our lineup so we can use resources more effectively and speed up product development.

We will also change our approach to system proposals. One of our key assets in System Platforms is the vast amount of sales data we have accumulated. By analyzing around 9,000 business deals to date, we were able to identify 25 different usage scenarios, which we then categorized into six optimization levels. For example, we have divided the area of data backup management into six optimization levels ranging from “on-site data backup on an *ad hoc* basis” to “data backup with disaster countermeasures.”

Based on this exercise, we learned that proposals that simply offer servers or storage systems will not satisfy customers. In server integration, for example, network optimization is always required too. In this way, we can get a more accurate overall picture of customer needs, and bring together specialists from each related area to create proposals from the customer’s perspective. This, I believe, is one way we can leverage our unique strengths as a company.

## What is Fujitsu’s policy on returning profits to shareholders?

I believe we can boost shareholder value by delivering sustained growth. Our basic policy on the payment of dividends is to offer a stable return to shareholders while ensuring a healthy level of retained earnings to strengthen our financial position and actively develop our business.

In fiscal 2006, we reported consolidated net income of ¥102.4 billion. However, on an unconsolidated basis, which provides the legal basis for dividends, we posted a net loss. Nevertheless, in light of the fact that future financial risks would be reduced by posting the loss, that the loss is not associated with an actual outflow of cash, and that earnings are on a recovery path, we decided to pay an annual dividend of ¥6.00 per share, the same as the previous fiscal year, to maintain our policy of providing a stable return to shareholders. By continuing to increase profits, we hope to pay shareholders substantial dividends going forward.

