

## **EASTMAN KODAK**

### **3rd Quarter Sales & Earnings November 1, 2007**

**Operator:** Good day everyone and welcome to this Eastman Kodak third quarter sales and earnings conference call. Today's conference is being recorded.

At this time for opening remarks and introductions, I'd like to turn the conference over to the Director and Vice President of Investor Relations, Ms. Ann McCorvey.

**Ann McCorvey:** Good morning and welcome to our discussion of third quarter earnings.

I'm here this morning with Antonio Perez, Kodak's Chairman and Chief Executive Officer; as well as Chief Financial Officer, Frank Sklarsky. Antonio will begin this morning with his observations on the quarter and then Frank will provide a review of the quarterly financial performance.

As usual, before we get started, I have some housekeeping activity to complete. Certain statements during this conference call may be forward-looking in nature or forward-looking statements as defined in the United States Private Securities Litigation Reform Act of 1995. For example, references to the company's expectations for revenues, earnings, digital earnings, net cash generation, entertainment imaging film revenue, earnings from operation, digital revenue growth, working capital, consumer inkjet units and revenue, gross profit margin, operating margin, restructuring charges, target cost model and capital expenditures are forward-looking statements.

These forward-looking statements are subject to a number of important risk factors and uncertainties which are fully enumerated in our press release this morning. Listeners are advised to read these important cautionary statements in their entirety, as forward-looking statements need to be evaluated in light of these important factors and uncertainties.

Also, Kodak has significantly reduced its references to non-GAAP measures. In those instances where they are used, they are fully reconciled to the nearest GAAP equivalent in the documentation release this morning, which can also be found on our Web site.

Now I'd like to turn the call over to Antonio Perez.

**Antonio Perez:** Thank you, Ann, and good morning everybody. I'm pleased that we were able to continue to achieve in the third quarter the strategic objectives we set ourselves for this year. We had good market success with our new digital products contributing to the 12-percent digital revenue growth and we created value for our shareholders by growing net earnings from continuing operations by \$117 million year over year.

Another highlight for the quarter was that earnings from our digital businesses nearly tripled year over year and in the quarter were roughly equal to the earnings from our traditional businesses.

Our cash usage of \$95 million in the third quarter was slightly more than plan. This largely reflects the timing of receipts of proceeds and certain working capital actions, which will now happen in the fourth quarter. As in previous years, the fourth quarter is critical from a cash flow perspective and I am confident each business team is very clear on the actions they need to take to deliver net cash generation of \$100 million for the full year.

I believe our third quarter performance gives us the momentum we need going into the very important fourth quarter.

Everything is in motion to achieve our full year key strategic objectives. I'm specifically pleased by the positive results we're seeing from our expanded digital portfolio together with our solid cost performance as well as our significant progress in continuously improving supply chain management and platform design efficiencies.

Now I would like to summarize my thoughts on each of the business segments. Let's start with FPG, the Film Products Group.

PG continues to perform. During the third quarter, earnings from operations improved six percent despite an 18-percent decline in revenue. The FPG team truly understands how to manage a business with a decline in revenue.

As we forecasted, entertainment imaging film revenue softened from the strong first half industry performance and it was down 5 percent for the third quarter. Because of the seasonality, our expectation is that entertainment imaging film revenue will end the year in line with last year's as per our original forecast.

In anticipation of FPG's seasonality, we began adjusting production rates late in the third quarter to ensure we achieve our fourth quarter working capital targets.

Based on the strong third quarter earnings performance and the plans for the fourth quarter, we now expect FPG to end the year with earnings from operations as a percentage of revenue in the 20-percent range as compared to the upper end of this 13 to 16-percent range previously forecasted. FPG's year-to-date earnings performance gave me more confidence in the future sustainability of double-digit earnings from operations as a percentage of revenue for this segment.

Kodak is and will continue to be a leader in film. We continue to provide new innovative products to the market. Earlier this month at PhotoPlus in New York, we introduced the world finest grain and sharpest 400 speed black and white film. Product T-MAX 400 affirms our commitment to professional photographers who see this film as a very powerful tool.

Next GCG, the Graphic Communications Group. GCG's third quarter performance confirmed that the momentum we saw in the second quarter was real and gives us confidence for the fourth quarter. GCG's third quarter digital revenue grew 9 percent year over year driven by digital printing, enterprise workflow, and digital prepress consumables.

Digital Printing growth included a double-digit increase in consumables, as year-over-year NexPress page volume grew 38 percent.

Our enterprise workflow business is growing on the strength of the fully integrated solutions we're bringing to the market. Our customers tell us that Kodak is the first to deliver a real Web-to-print solution that encompasses all the steps from order entry to print.

One of the strategic objectives this year is to expand our product lines in the market we serve and GCG is delivering. The expanded GCG product line was very well received at Graph Expo, where our sales exceeded our expectations.

In September, we introduced a new digital flexographic system called Kodak Flexcel NX. Customers at both Graph Expo in the US and LabelExpo in Europe were very impressed by the offset light quality this system can produce. The Kodak Flexcel NX system represents a significant step for the industry and further improves Kodak's position in the large and growing digital packaging market. We are delivering on the promise we had in mind when we created this group. We have a strong GCG team, who understands what they have to do to achieve both the targeted 6 to 9-percent digital revenue growth for the full year and their working capital targets.

Next, CDG, the Consumer Digital Imaging Group.

CDG achieved another milestone in the third quarter by growing both revenue and earnings from operations. This progress was achieved while the company made a significant investment in the introduction of consumer inkjet printers and managed declines in CDG's traditional products.

CDG's digital revenue grew 16 percent year over year driven by consumer inkjet printers, Kiosks and related media, and digital capture and devices.

Digital Captures growth is evidence that consumers are embracing our improved digital product portfolio. Digital camera unit volume grew 35 percent year over year while gross margins improved. We have strong growth in our digital picture frames, which was partially offset by the continuing industry decline in snapshot printing.

This quarter's results also include continued growth in our recurring ongoing intellectual property royalties, as well as a new non-recurring licensing agreement comparable in size to the one non-recurring agreement we had last year in this quarter.

Our focus for digital cameras over the last four quarters has been on margin expansion. The third quarter demonstrates our ability to deliver profitable revenue growth. Additional evidence of our success is the significant improvement in inventory turns for digital cameras due to the improvements in our supply chain.

We believe we have the right portfolio of products in CDG to sustain this momentum of profitable growth into the fourth quarter and beyond.

I continue to be pleased with the progress of consumer inkjet. We have a strong value proposition; unique in the market, a better-printed page at about half the cost and the introduction is moving ahead according to plan. Our consumer inkjet products are now available at more than 7,600 retail outlets worldwide.

As I have said before, we are experiencing the typical challenges associated with a startup of a major product line. In the third quarter, to support the strong channel acceptance, we applied additional resources to resolve manufacturing and software connectivity issues, made improvements to our marketing program to enhance our in-store presence, and took actions to accelerate the release of future generations of products.

We are committed to developing a business with one billion in revenue in 2010. That's the target and everything we're doing now is designed to achieve this goal. We have a disruptive technology, which gives consumers a wonderful value proposition of premium printing at up to 50-percent savings while providing a

significant margin opportunity for Kodak. Achieving our goal of selling 500,000 units by year-end is one milestone in that journey.

This quarter we expanded as well the profitable and growing Kiosk product line by introducing the Kodak Picture Kiosk GS Compact, an entry-level self-service digital picture printing solution, which open business opportunities for new retail locations, including smaller and non-traditional environments. This new product provides growth opportunity for retailers and for Kodak.

And finally, before I turn the call over to Frank who will provide a financial overview, I would like to make you aware of an organizational change that will allow us to better manage Kodak's silver halide products.

As you will remember last year, we consolidated all of our output product offerings to retailers and the one go-to-market structure within the consumer digital imaging group. That single go-to-market structure is working well and will not change. But with the restructuring program behind us, we can now go further and leverage these businesses to maximize performance and drive faster decision making by managing all silver halide based products in one place.

So effective January 1st, 2008, the Film Products Group will be renamed the Film, Photofinishing and Entertainment Group, FPEG. It will be led by Mary Jane Hellyar, who has an exceptional track record for delivering results. FPEG will include the current FPEG portfolio of consumer, professional, entertainment, and industrial films and it will add responsibility for graphic films, silver halide photographic paper and chemistry, and retail and wholesale photofinishing.

The change that I have just described today, in conjunction with the digital businesses led by Phil Faraci represent a new Kodak that is better prepared to increase shareholder value by more effectively managing both our traditional and our digital businesses.

Now I will turn over to Frank.

**Frank Sklarsky:** Thanks, Antonio, and good morning everyone. Today I will share with you some highlights of the third quarter financial results and then Antonio and I will happy to take your questions.

Overall, we are pleased with the company's third quarter results, particularly the strong revenue performance in several of our key digital businesses and with the continued progress on our cost reduction initiatives including SG&A expenses. We also have continued efforts underway related to working capital reduction, which are required to achieve our goals for net cash generation for the total year.

With respect to financial results, earnings from continuing operations for the third quarter were \$29 million pre-tax and \$34 million after tax, or \$.12 cents per share, compared to a loss from continuing operations of \$53 million pre-tax and \$83 million after tax for a loss of \$.29 cents per share in the third quarter of 2006. This represents a pre-tax improvement of \$82 million versus the prior year and an after tax improvement of \$117 million, or \$.41 cents per share.

Third quarter results include items of expense impacting comparability totaling \$94 million after tax, or \$.33 cents per share. This is comprised mainly of restructuring charges of \$96 million after tax. The prior year's third quarter included items of expense impacting comparability totaling \$137 million after tax, or \$.48 cents per share, primarily reflecting restructuring costs.

Total consolidated revenue declined by 1 percent and included a 2-percent favorable foreign exchange impact. Third quarter digital revenue grew by 12 percent while traditional revenue declined by 16 percent.

Third quarter gross profit margin was 26.4 percent versus 25.1 percent last year, an improvement of 1.3 percentage points. This improvement in gross profit margin was driven primarily by continued progress in reducing manufacturing and supply chain costs along with just over one percentage point of favorability from foreign exchange. This was partially offset by pricing impacts and approximately \$26 million of increases in aluminum and silver costs.

While gross profit margins can be seasonable in nature, we still expect to achieve our previously communicated gross profit margin between 25 and 26 percent for the total year.

SG&A was reduced by \$37 million, or 8 percent, and declined as a percent of revenue from about 18 percent in the year-ago quarter to under 17 percent in the current quarter. Year to date, the company has reduced SG&A costs by \$230 million or over 15 percent.

Our R&D costs totaled \$129 million for the quarter, or about 5 percent of revenue and in line with our plans. R&D's percent of revenue is higher if applied to the revenue associated with our digital businesses, where we focus most of our spending.

Our restructuring efforts continued through the quarter with pre-ax restructuring charges totaling \$127 million as compared to \$181 million in the year-ago quarter. Year to date through the third quarter, pre-tax restructuring charges totaled \$594 million compared to \$621 million for the first three quarters of last year. In the third quarter, restructuring related payments from corporate cash were approximately \$110 million.

We had previously communicated that total restructuring charges to the P&L for the year would run between \$900 million and \$1 billion. Based upon our progress to date, along with our analysis of actions to be completed for the remainder of the year, we now believe total restructuring charges for 2007 will be in the range of \$750 to \$850 million. This reduction is due to a variety of factors. These include efficiencies associated with reductions in our manufacturing footprint, along with our ability to outsource or sell certain operations thereby reducing employee severance requirements. Payments made in 2007 related to restructuring actions from corporate cash for the current and prior years may be lower than the previously stated \$600 million. At the same time, a good portion of any cash payment savings we do achieve will come from funding for US-based actions which would have been dispersed from the company's over funded US pension assets.

We would like to emphasize that we have been able to effectively manage restructuring costs to be somewhat lower than originally anticipated, as just described. And, the pace of restructuring activity, the efficiency with which it has been carried out, and the reductions in the company's overall cost structure to date gives us confidence that we will still complete the major restructuring this year and make significant progress toward achieving our target cost model according to plan as previously communicated.

Third quarter digital EFO almost tripled to \$82 million as compared to \$28 million in the year-ago quarter, an improvement of \$54 million. Year-to-date digital earnings improved by \$185 million to \$43 million compared to year-to-date losses of \$142 million in the prior year.

Consumer Digital Imaging Group improved their EFO by \$13 million to 10 million from a \$3-million loss in last year's third quarter. It is particularly noteworthy that improvements in both our digital cameras and kiosk businesses along with licensing revenues more than offset the significant costs associated with the ramp-up of our consumer inkjet business. The enhanced product portfolio and go-to-market structure changes in digital cameras and digital frames implemented over the last several quarters contributed to substantially improved performance in those businesses.

Earnings from operations in the Graphic Communications Group for the current quarter were \$42 million as compared to \$26 million in the year-ago quarter, an improvement of \$16 million driven primarily by higher equipment placements for our NexPress color production presses, higher volume in workflow software, digital printing consumables, and digital plates, cost control initiatives in SG&A, and favorable foreign exchange. These benefits were partially offset by the negative impacts of aluminum, along with product mix and workflow software and pre-press solutions.

Film Products Group posted earnings from operations of \$122 million for the third quarter versus \$115 million in the year-ago quarter. This EFO, at 25 percent of revenue demonstrates that FPG continues to achieve strong operating margins despite experiencing double-digit revenue declines. This is due to a disciplined focus on maintaining revenue and margin in key product areas while driving cost reductions across the board. We are now forecasting full year FPG operating margins to be the range of about 20 percent.

Overall total company traditional earnings were \$91 million for the current quarter versus \$110 million in the prior year quarter, down \$19 million mostly due to lower volumes in our film, paper and photofinishing businesses. Separately, other income and interest expense improved by \$51 million versus the prior year quarter. This is driven primarily by the benefits to both interest income and interest expense from the impact on cash and debt balances resulting from the Health Group divestiture.

Turning to cash, our net cash generation for the third quarter reflected a use of \$95 million, an increase in usage versus the prior year quarter. Our year-over-year increase in trade receivables is largely attributable to the timing and mix of product revenues across our various businesses. Inventories for the quarter were a bit higher in preparation for growth in fourth quarter digital revenues. In addition, we have already begun to adjust production rates in FPG to reduce inventories in that area by the end of the year. We also had some timing differences as compared to the prior year, related to cash receipts associated with non-recurring licensing agreements and asset sales. Lastly, we had cash payments in this year's third quarter to settle certain tax and legal obligations. Our goal is to deliver a strong fourth quarter for net cash generation by carefully managing our inventories consistent with our revenue and working capital goals, by continuing our focus on driving down past due receivables, improving our payable cycle, and by delivering a strong earnings performance from our more seasonal digital businesses.

We ended the third quarter with \$1.847 billion in cash and cash equivalents and our debt currently stands at \$1.626 billion. We are very pleased with our strong balance sheet and a significant liquidity position it provides us.

As stated in our press release, we continue to stay focused on our goal of \$100 million in net cash generation for 2007 and remain confident in our ability to complete the major restructuring this year and make significant progress toward our targeted cost model. With the success we are achieving in growing our digital businesses, we now believe that 2007 digital revenue growth for the company will be at the upper

end of the 3 to 5 percent previously communicated and total company revenue for 2007 will decline at the lower end of the 4- to 7-percent range previously messaged. We continue to forecast the company's digital earnings of \$150 to \$250 million, which corresponds to total company earnings from operations of \$300 to \$400 million.

Thanks very much and now Antonio and I will be happy to take your questions.

**Antonio Perez:** Thank you again for joining us today. The pieces are all coming together and we are delivering on our strategic objectives for 2007. We have an expanding digital product portfolio that customer are embracing, great people in the right jobs and a much more cost-efficient business model, plus significant intellectual property and a powerful brand. This is the platform from which we will launch and sustain profitable growth. This is the new Kodak that is quickly emerging. Thanks again for your interest.

**Operator:** Thank you, Mr. Perez. The question-and-answer session will be conducted electronically. If you would like to ask a question, you may do so by pressing the star key followed by the digit one on your touch-tone telephone. If you are using a speakerphone, we do ask that you please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, ladies and gentlemen, that is star one for questions. We'll pause just a moment to assemble our roster.

We'll take our first question from Carol Sabbagha, Lehman Brothers.

**Carol Sabbagha:** Thanks very much. Just a couple of quick questions. The first is on use of cash.

Antonio, is there any more clarity around what the potential uses are or the timing of when we're going to hear about Kodak's plans on HG proceeds?

**Antonio Perez:** Not yet, Carol, but come February when we have our meeting in New York we hope to have a little more clarity of what we're going to do. For the moment, we still, have the three possibilities that we've been evaluating which are the internal investments commercializing the technology that we have in-house.

Obviously, we are looking to see if there are any M&A opportunities that are appropriate and valuable, and they are the right price, and fit with our product portfolio expansion. And then we continue to look at the possibility of share buyback. No decision has been made yet. We talk in every board meeting about these possibilities and we'll keep evaluating them.

**Carol Sabbagha:** OK, and a couple more questions on inkjet. When do you expect sort of a new product line to come out and after that, how quickly do you expect to continue to refresh the product portfolio?

**Antonio Perez:** I don't understand the first part of the question, Carol. What did you say?

**Carol Sabbagha:** I know you talked about introducing new products by year end when you first introduced the three inkjet products. Do you know when we may see more additions to the 5100, 5300 and the 5500 printers?

**Antonio Perez:** Well, if I said by the year end, I guess it will be by year end. I don't recall saying that, but if I did say that, then it's because it's going to be before year-end .

We will be introducing new products to refresh the product line. It will be around that time. This is a very high season with a lot of volumes. It's very important for us to manage our inventories into the channel and the supply chain. But obviously we've been working very hard to create the new product line and we are getting close to introduce something when it's appropriate.

**Carol Sabbagha:** And how would you characterize the pricing environment in inkjet in the third quarter broadly for the market and specifically for you? And it looks like some of the new channel partners that you've announced like Wal-Mart and Sam's Club typically reach the lower-end consumer. How would you within those channels try to reach the higher ink usage customer that you're targeting?

**Antonio Perez:** Actually, I don't agree with that statement. That's a very generic statement, Carol. I mean most of the high ink consumers go and buy there and they are very high use ink consumption so you cannot make that statement that is such a generic way. So I think they are very good channels for us.

What is going to drive the right customer is the business model. It's not the channel. The right consumer has to be confronted with either you pay slightly less for the printer and a lot more for the ink and I mean a lot more for the ink, or you might be more comfortable paying very little more for the printer but getting a printed page because of our premium inks and savings a lot of money when you print. So I think that's going to define who's going to buy this printer.

**Carol Sabbath:** And my last question is for Frank. Can you talk about how much of a headwind silver and aluminum were in this quarter and also how much lower D&A there was in the quarter versus a year ago that ran through the operating numbers?

**Frank Sklarsky:** Right. Yes, if I look at the commodity impact from the silver and aluminum, while we don't split it out between silver and aluminum, the total of the two was \$26 million and a lot of that was aluminum and it had a pretty significant impact on the margins for GCG. So I guess what I would say is if it were not for the net impact of aluminum GCG gross margins would have -- would have been up. On the G&A, yes, our G&A was down Q3 versus Q3 by that \$37 million or eight percent.

**Carol Sabbagha:** I'm sorry; did you say G&A? I meant depreciation and amortization. Sorry about that.

**Frank Sklarsky:** Oh, OK. All right.

**Frank Sklarsky:** Depreciation and amortization was down, oh, I guess about -- a little over \$100 million Q3 to Q3 but we're still on track. So, we've had about \$600 million year to date and about 100 million of that was what I'd characterize as accelerated depreciation.

**Carol Sabbagha:** Thank you very much.

**Operator:** And we'll take our next question from Jay Vleeschhouwer, Merrill Lynch.

**Jay Vleeschhouwer:** Thanks. Good morning. Antonio, with CDG driving the bulk of the revenue upside at least versus our model, I'd like to ask for a longer-term perspective on how you see the end game playing out, particularly on the digital printing side in the consumer market. Given there were a number of interesting trends going on right now I'm curious to see how you think it'll all come together.

We see, for instance, that total print volume growth seems to be decelerating although the market has substantially shifted to retail and online, then used digital camera growth lately has held up very well and seems to be meeting or exceeding print growth -- again, that's recent data -- and so when you put all that together in your exposure across different venues what do you think the ultimate structure of the market might look like, and perhaps most importantly, your share of the profit pool available with all of that printing in different venue, and then a couple of follow-ups.

**Antonio Perez:** So digital camera market is growing actually faster than we thought it was going to grow and we're benefiting from it. We have a very flexible supply chain that allowed us to move up and down very quickly with volumes and this has been critical not only with the growth we are experiencing but as well the great improvement in the bottom line of this business. So we're very pleased with that.

We still see looking forward we cannot expect this growth to continue. We believe that multifunction devices such as cell phones in which we are participating, as you know we have a deal with Motorola and part of that growth although it's not clear.

We know that there is room for improvement in the cell phones to make a better commerce and we're not sure that the total digital camera single function device would go down, but in our assumption of the numbers, we're going to assume that it's going to go down. That is not going to grow as fast as it is growing today. We're very focused in certain segments of our market. We feel very comfortable with the fourth quarter and with portfolio we have for next year and that business is doing pretty well.

With printing, we are participating in the different elements of printing. We are still in photofinishing although that is the silver halide base printing. We have an important participation there. That business is going down and is being replaced by all the methodologies, all the technologies such as kiosks, that's why we were enjoying such a nice growth on the top line and bottom line, with our kiosks and we are expanding the portfolio because, as you said it seems like that more and more people are getting comfortable with getting those prints in the stores, which is great for us.

And we see that growing because we believe eventually the silver halide products will be replaced at the appropriate time for more flexible, more economical technologies that we call dry labs and we are already offering those dry labs and we will continue to offer those. That is a possibility for growth for us because, as you know we are not participating in the classic silver halide based equipment businesses. Since that business we believe is going to be transforming into dry labs, we see a very interesting opportunity for growth.

And then within the homes since we have so little of the market, a small part of the market, I mean, everything is growth for us and, we just have to get the word to the right people that we have a different value proposition that will be in my view unbeatable for someone that prints a lot. So that's what we're after. We're after those people that print a lot and they like a better-printed page.

We believe we have a better printed page because it doesn't fade, because it's more robust, because of the type of inks that we use, and we do it at half the price so we have to keep passing that message and it's going to take a while to get to everywhere that we want to go but it's moving along. So what happened with the overall marketing at this point it's all growth for us and we're going to get a piece of it. That's for sure.

I don't know if I answered the question right. I went through all the topics I thought, but, if I didn't let me know what I missed.

**Jay Vleeschhouwer:** Well, we can bring it up maybe at the analyst meeting in more depth.

Second question is within GCG what is the best evidence that you can offer that the multi-product or blended analog digital portfolio strategy is really working incrementally? Where's the one-plus-one-equals-three evidence that having that kind broad product line is in fact giving you a competitive advantage for a material part of orders within GCG?

**Antonio Perez:** OK, well, first I forgot to say to your statement that most of the progress was done in GCG I do not agree with it. The progress in GCG for me is phenomenal and it's in line with what we expected. You know, remember that it's never going to be that easy to come into this market displacing the phenomenal companies that we are working with and I did mention in my speech that the number of pages printed with color grew by 38 percent. You know, that's where the money is.

And now going back to the proof, the proof is that look at our workflow software progress. That is a very important product line. It is the glue of the whole industry. We are making tremendous progress with that. We are recognized as the most complete -- maybe the only, I wouldn't say universal but comprehensive workflow that deals with most of the issues whether it's production workflow, telemanagement workflow, or business workflow and we are integrating all of that and we don't know of anybody that is doing that certainly as well as we do. .

And then the continuous improvement in the product line. You see GCG, it keeps quarter after quarter after quarter performing better and it's because of the whole, not because of any particular part. They all contribute.

We still expand in the portfolio. We still have a lot -- that is a huge market and we have our product portfolio we applied to several parts of the business. But within each one, we have very small portfolios so we have to expand the portfolios. We have to expand the portfolio of inkjet printing in which we will be announcing things this summer, very fundamental things for us. In Drupa we will be, increasing the portfolio of our workflow, of our scanning, all of that. So you will see a very steady growth and steady progress in the top line and in the bottom line of this business, which is what we want because the traction we have is a solid traction for this business.

**Jay Vleeschhouwer:** And finally, if I may, a geography test for you. In the consumer digital business on a currency-adjusted basis, your US business in CDG is outperforming your non-US business. On the other hand within GCG, your non-US business is materially outperforming your domestic business both in the quarter and year to date. There's a pretty wide spread there, particularly in GCG.

**Antonio Perez:** Very good, very good so we'd have work to do. I agree. I agree that we have to -- I will talk to Phil tomorrow morning and tell him that he has to improve his performance outside the US. Believe me; he's been hearing that from me. Yes, we have to improve. I see that as an opportunity more than an issue but it is an opportunity for us to increase our CDG results outside the US.

You know, I'll tell you the reasons for this: there's a reason for all these things, and then as far as GCG, there are different parts. The EP is actually doing better in the US than doing outside the US. Plates is probably slightly better outside the US so you can't take the whole GCG as one and say that we're better in one place for the other. But, for the consumer market the logical thing for us is introducing in the US

tune up the value proposition and then move. So obviously, it seems we are new in this market.

You're going to see first the impact in the US market and then hopefully we can move into the rest of the world. We always introduce products sometimes six months or nine months after the US so you can possibly see the same revenue stream.

**Jay Vleeschhouwer:** OK, thank you very much.

**Antonio Perez:** Thank you.

**Operator:** And our next question comes from Matt Troy, Citigroup.

**Matt Troy:** A question for Frank, kind of a counter to Antonio's commentary on the usage of cash or deployment of cash.

Frank, you've been there for about a year now, observed the different seasonalities of the old business and the new business. When the dust settles on Antonio's plan at year end and you think about the run rate business model targets being achieved that you've articulated clearly for us in margins and growth rates, I was wondering how much cash so you think you need to run the business over the course of a year? If I go back in history, Kodak was a company that could very efficiently run with three, \$400 million of cash on balance sheet, you obviously have several multiples and more than that today. How should we think about the cash operating needs of the business?

**Frank Sklarsky:** That's a good question and we've thought about that quite a bit. I think over time as we raise the overall water level of profitability beyond the major restructuring, you know, once we get beyond the end of the year, the overall profitability level will go up and the cash needs obviously for major restructuring go away. So the water level goes up and so the seasonality won't be as much of an impact on us as it is today where we dip in the first half of the year and then recover later in the year. Clearly, at some point in time, we don't anticipate that we're going to need a billion dollars on the balance sheet to run the business.

Currently, we want to make sure we get through the restructuring, we demonstrate the growth that we've messaged in the digital businesses, and the other thing, as you're obviously aware of is, given our current rating category, we have to make sure we have that cushion as we complete this transformation. But obviously, your point is right on that at some point in time, whether it's later next year or the early part of the following year, we don't expect to require that same level of cash on the balance sheet just as a cushion.

**Antonio Perez:** Just another point, Matt, is that we only have really two or three digital product lines that mature, which their running rate of capital use is going to be low. Many of the product lines are new and it's better to have a little more cash on hand than not because you're going to be making single moves in there to speed up the maturity of the product line.

When you look at the volume -- the relative volumes of the product lines, there's only two or three there I will consider were already there and we're managing this business with certain growth and all that. But many of them are in need of some kind of investment. Again, whether it is a significant internal investment when we get to the right package and all the technology or when we get to the right application, or maybe an M&A acquisition here and there. So, you know, we're still building.

The first four-year plan was about two things basically; cleaning up the film business, deal with the excess assets that we had there and the excess number of people that we had there, make sure that it is a sustainable business and we've done that very much. I mean that is done.

And, you know, second objective of the first four years, we are finishing now, was to create a group of nascent digital business with a lot of possibilities for the future. We've done that very well, too, if you allow me to be the judge of this.

Second phase, which we're starting now, is to scale those businesses, and out of those businesses, we have I believe phenomenal properties in the digital space that have enormous possibilities for expansion and I understand the complexity of the market, but we have six, seven digital properties that have phenomenal capabilities for value creation and this is why you see us I won't say tentative but prudently looking about where do we put our resources, which one of those are the ones that we're going to go forward which obviously we know a little more than we're telling you but this is the process right now.

**Matt Troy:** Thank you. I understand. I'm in the camp that there is no quick lightning bolt use either. I'm just trying to get a sense for, you know, what kind of cash needs the business have. Obviously, structurally lower than what you've got today, which is a good thing.

My second question I guess would be for you, Antonio, and Frank. The silver halide paper and chemistry business has moved around. You've indicated you're putting it back into a newly bundled group with film. I was wondering if you could just help me understand the thought process there a little bit more clearly. Are you seeing a change in the way that retailers are buying product? Certainly, I think if you talk to retailers today there seems to be a greater willingness to invest in onsite photofinishing whatever the technology in form. I was wondering if you could maybe share with us that the thought process or the reasoning behind recoupling that with the film business.

**Matt Troy:** What did you learn in the last 12 months?

**Antonio Perez:** ... yes -- the go-to-market is going to remain the same. The same people that are talking to the retail stores they have to -- they have to be able to contemplate the whole ecosystem of printing in retail, whether it's kiosks or home printers, web-based to the stores, to mini labs, all those options, so there has to be -- so the go-to-market has no change.

What we have found though in the last year is that we want to manage very efficiently the resources we have dedicated to silver halide and you can imagine that when a business -- some part of the businesses are going down, and others are stable like EI, others in a phase that might start going down. You want to manage all that capacity in a unified way, in an integrated way. That's why we've done what we've done. We have not changed the go-to-market so none of the trends that you were describing that we are aware of have made a dent to influence the decision. The go-to-market is the same. It's the same people that are going to deal with the customer issues and try to make the most appropriate deal for those customers, it's the back office business. That's the one where we can improve by putting it all under -- on the one head and managing those assets in the most effective way.

Why didn't we do that before? With all the work that we're doing with the restructuring it was something that we wanted to do. It was just not possible. It was not just the prudent thing to do. We think this is the right time for the restructuring,

it's over so we're ask Mary Jane to run this and get the maximum efficiency of those assets that we have.

**Frank Sklarsky:** And Matt, an additional benefit to the investment community is at least at the business unit level there'd be the transparency between our digital and traditional performance.

**Matt Troy:** Right, right. Last question, Antonio, in terms of just messaging and to make sure expectations are level set, in terms of the stream technology, you've previously indicated we can expect to see something at Drupa in 2008, is that a demonstration technology? What is the product path there in terms of commercialization? Is it a demonstration to be followed by launch later in the year, or is it more a 2009/2010 launch?

And then second question would be just simply product breadth. You've taken the Cannon product and made it your own. Wondering about your trajectory there and thoughts on expanding the portfolio further, either build verse buy, if you could just talk about breath.

That's all I've got. Thanks.

**Antonio Perez:** As far as the inkjet stream, you're going to see both in Drupa. You're going to see products that will be starting to sell at that time and you're going to see demonstrations of technology that whose really volumes will come the year after or six months after that. You're going to see both. You're going to see as well the possibilities of the technology so maybe those three things. They're going to be real products that you could take or some people will take. I don't think you will buy one. But you're going to see as well products that are not ready to ship but they're going to be demonstrated and will be shipping a few months after that. And then you're going to see the power of the technology and the role -- the possible role that this technology could have within the world of printing. I mean, you're going to see those three things.

As far as portfolio, we didn't take a product from Canon; we took an engine. We took an engine and with that and a lot of things that we put in, we created a product. That is not the end of our activities. We will continue to do things like that and we'll continue to do our own engines as well. We're looking all sorts of possibilities. We will expand. We have to expand the portfolio or EP to be a better participant and we're doing very well with NexPress but we're not taking advantage of the whole EP market. But again, we didn't get a product from Canon to make it our own; we just -- we did not do that. There is a component that comes from Canon and from that component we made a product, which has a lot more than that component, and actually, we believe that our product is significantly different than the Canon product.

**Matt Troy:** And you've been pleased with sell-through trends thus far? These are early days, I realize, but the initial traction has been good?

**Antonio Perez:** I am never pleased with any of my sales. I always say to my people that we should be selling a lot more. But having said that, it's moving well. We're getting into markets and into deals that we couldn't get before. So I'm happy with the product. I'm happy with the product but there's so much in EP that we can -- that we can have access to that I'm not happy with the whole idea of our EP portfolio yet, but, you know, it's an opportunity.

**Matt Troy:** Understand. Thank you very much for the time.

**Operator:** And we'll take our next question from Shannon Cross, Cross Research.

**Shannon Cross:** Hi. Good morning or we're getting close to afternoon. Anyway, just a few questions. First, can you talk a little bit, Antonio, on the inkjet side? I'm just curious. You had some advertisements when you launched. There were TV commercials and that we're trying to explain the value proposition. I would have thought you might be out more with that so if you can talk a little bit about that and then I have a couple of follow-ups.

**Antonio Perez:** Yes, we do spend a lot on advertising, Shannon, but it's not so much in the type of media. We do a lot and spend a lot of money in store. At this point of time with the capacity and the volumes that we have, our business thrust is to get our products in the channel and make sure that when they're in the channel they are well presented. So we have to make enough, we have to put them in all the channels and they have to be well presented in the channels.

We know that the traffic to buy a printer is basically done for us by the other guys, the HPs of the world and the Canons of the world, the Epson's of the world. They're already luring you into going and buying a new printer so all we have to do for now is wait for you at the store and when you come into the store we'll call you aside and say, ma'am, did you consider the fact that we have this phenomenal value proposition, so if you print a lot this will be useful. There will be a time that you will see us more public to create traffic to our own product. This is the most efficient way right now. We're basically selling the products that we make, so clearly, more traffic is not going to help us. What we have to do is increase the number of people that we can attract once they get to the store attracted to our products so we can improve the velocity in the store. That's the whole effort but we are spending a lot of money doing that.

**Shannon Cross:** OK, that brings me to another question. With regard to inkjet manufacturing, I mean, it appears that there have been some issues in terms of ramping production. Can you give us any more specifics in things that you're doing to change because I would have thought you were manufacturing at flex and it seems to me that you had a new technology with the print head side but, in terms of reinventing the wheel where have the issues come up and how can we be confident that you've alleviated them enough to hit the 500,000 target?

**Antonio Perez:** Yes, there are bunch of things that you said there, Shannon. Flextronics is one of our partners.

**Shannon Cross:** Right.

**Antonio Perez:** It's not the largest partner we have. I don't know if you know that but it's not. So it's not just Flex. We have several partners and they have many other lines and to get this volume of printers there are a lot of issues that happen when you try to raise volumes. We don't have -- in my experience in inkjets, we don't have any problem that I haven't seen in any other companies that I've worked for when you're trying to increase the volumes of a complex product like that. We do have those issues. We had some connectivity issues because we missed some of the connection of the business and the homes are very different that we were expecting. So there were some connectivity issues where we dealt with those, we're dealing with those.

When you strive to create certain sub-assembly, it works very well when you have to make, I don't know, 2,000 a week. It's not as good when you're going to move to 4,000 a week so you keep improving those. It's just the everyday thing to scale manufacturing. There is nothing specific that I can mention that will be different than normal issues that you will have when you do that. That's why we actually set ourselves for a number of 500,000. Honestly we could have gone and said, well, we're sure that we can make a lot more. We should go for a higher number.

We looked at it, and since I make few mistakes in this business as in the past, said, well, let's put a number that we can make, let's make sure that this year, the objective is get our market -- get some market share out there, get our notion in the market, get customers to understand who we are and our value proposition. You know, 500,000 is a good number -- it's a good number to start and learn a lot from and things that you have to do. Like, for instance, we didn't want to introduce the next generation of products, which you can imagine we've been working on for the last two years already. We didn't work in just one. We work on several as any other company does. I'm not saying anything silly.

We're not going to ship them until we are sure that we understood the issues that came when we introduce the first one. So the second one should not have any of those issues and be a better product overall. So we are right on that track. We are planning to make and sell 500,000, learn a lot, not only from the manufacture for review.

Suppliers -- we'll have new suppliers. They have to learn to give us more parts and higher volumes. Sometimes they do and sometimes they don't so you have to look for another supplier that is able to scale better and so on and so forth. So this is the year of doing what I just described. The year of scale is going to be the year after and the year after.

**Shannon Cross:** OK and then can you give us an update on your CMOS business? I didn't see much discussion on it within the MD&A.

**Antonio Perez:** .. we'll make the announcement about the process. The progress we're making low light in technology we made some public announcement about, low light capabilities which are fundamental. One of the objectives of our CMOS team is to make sure that eventually we make a camera that doesn't need a flash which as you know is one of the gating elements of a digital camera and cause of a lot of trouble for color management and many other things, ie. battery power and all of that. So we've made a lot of progress there.

We are working. The large volume product that you're going to see will be in a cell phone and this is a project that we're working intensely with a leader in the industry, Motorola. You will see the effect of that.

And then the other one is that in the fourth quarter you're going to see -- we just introduced it about a month ago -- one of our digital cameras at very low end that has one of our CMOS sensors. Again, this is a long-cycle business. We have our plans there for volumes but the two places where you can see this CMOS business coming to --reality, relative volumes in our low-end digital camera and in the first and second Motorola phones. That's what you're going to see. We're working in all the deals but those are things that you're going to see soon.

**Shannon Cross:** OK and I just have two quick questions. The first one: you talked about earlier in the year 250 million in IP licensing revenue, about 70 percent of which would be nonrecurring. **Antonio Perez:** I never said that, never said that. I said 250 was

recurring. I said at least 250 from the deals that we have already signed. That's what I said.

**Frank Sklarsky:** \$250 million.

**Antonio Perez:** Yes, yes, 250 million at least I said from the deals that we have already signed and I didn't want to do any other forecasts for any because I don't know what deals we're going to have. We might have deals that are going to be based on cash or we might have deals that are going to be a relationship for a new business or we might have deals that will be very different like this. So I can't -- we can't and we don't want to and it wouldn't be helpful for anybody, especially for us, to set a forecast of royalties. All I said is the only thing I could say which is the deals that we have signed so far I know they're going to deliver in 2007. At least \$250 million.

**Shannon Cross:** OK, and then my last question is can you just talk about when we can expect -- maybe this is for Frank -- GAAP earnings to equal pro forma from the standpoint of the 250 within that number was there a portion that was nonrecurring of the deals you had signed at the beginning of the year? Just if you can answer that ...

**Frank Sklarsky:** We're not really characterizing a split in the amount that goes in either on a quarterly basis or a year to date to split between recurring and nonrecurring. I think we want to stick to for now is at least 250 for the year as Antonio had characterized and then look at additional licensing deals as they might occur.

**Shannon Cross:** OK, and then just a last question. With regard to GAAP equals pro forma, any idea when we can start to see that from an earnings standpoint and you said major restructuring, I assume. I mean -- we've seen this with a number of companies like Xerox and others -- restructuring can go on for a long time ...

**Frank Sklarsky:** Yes ...

**Frank Sklarsky:** ... I think that the best way to characterize that one is the major restructuring will be completed this year. We are still holding to that and very confident of that. Every company in the world has ongoing initiatives to further drive its efficiency and costs and so on and so forth. You know, we'll be no different. I think what we had said back in February is that there would be about \$100 million in potential cash payments in 2008 as it related to what I'll call the flop-over, associated with 2007 and prior actions. We're still holding to that.

In terms of any P&L impact of any actions we might take in the future, nowhere in any realm nor order of magnitude that we've seen over the last four years. What we're talking about well under \$100 million and whether we characterize that -- how we characterize that on the P&L, we haven't specifically landed on that just yet, but very, very little. So you'll start to see a much closer connection between pro forma and GAAP earnings going forward after the fourth quarter.

**Shannon Cross:** OK, thank you.

**Frank Sklarsky:** OK, thanks very much.

**Operator:** And that does conclude today's question-and-answer session. At this time, I'd like to turn the call over to you, Mr. Perez, for any additional or closing remarks.

**Antonio Perez:** Well, thank you very much for joining us. Thank you for your questions. They're always useful -- very useful.

In my view, all the pieces are coming together and we are delivering the objectives that we set ourselves for 2007. First, we have an expanding digital product portfolio that customers are embracing. We have created a great team of people not only at the top level like Phil and Mary Jane but as well underneath those managers we have very strong people that manages the P&Ls, you know, and I feel very comfortable with the level of expertise and their commitment. We have created, with all this work, a much more cost-effective business model and then we have the IP and we have the brand to work with. So this is the platform from which we can launch and sustain profit overall and this is the new Kodak that we have been saying that will emerge after these four years of restructuring.

Thank you very much.

**Operator:** And again that does conclude today's conference call. We do thank you for your participation. You may disconnect at this time.

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