EASTMAN KODAK

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1st Quarter 2006

Operator: Good day everyone and welcome to the Eastman Kodak first 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, Mr. Don Flick. Mr. Flick, please go ahead.

Don Flick: Good morning and welcome to this morning's conference call. I'm here with Antonio Perez, Kodak's Chairman and CEO and Bob Brust, our Chief Financial Officer.

Antonio will begin this morning's call with his observations on the quarter and the other important announcements that we've made this morning and then Bob will provide a review of our first quarter financial performance.

Before we begin, I have the usual housekeeping activities to complete. First, certain statements during this conference call may be forward-looking in nature, or forward-looking in statements as defined in the United States Private Securities Litigation Reform Act of 1995. For example, references to expectations for the company's earnings, revenue and cash are such forward-looking statements. Actual results may differ from those expressed or implied in these forward-looking statements and 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 cautionary statements in their entirety. Lastly, although 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 that we have released this morning.

Now, let me turn the conference call over to Antonio Perez.

Antonio Perez: Thank you, Don. Good morning and welcome to our call. As you know, we have a number of important announcements this morning, which I will discuss first and then Bob will go into more detail about our first quarter financial results.

In my view, the first quarter continues to show the progress we're making in our transformation as well as the strong seasonality of our business. Having said that, my outlook for the year remains essentially unchanged.

The summary of our performance is as follows. In CDG, the consumer digital group, we face a slightly higher than normal industry channel inventory position caused by the fourth quarter that created temporary price impressions for old models and some transient inventory build up.

Strategically I'm pleased with the fact that our Digital Capture business improved earnings from year to year in line with our strategy of expanding margins and that our media pricing is more competitive now.

GCG, the Graphic Communications Group, performed much better than expected based on the strong momentum created last year. I feel great about this performance, which is a little earlier than expected, ahead of the bulk of cost synergies planned for the year; and is based on good market acceptance.

FPG, the Film and Photofinishing revenue decline was an expectation, but FPG performed slightly better than our internal plan for earnings, while the Health Imaging Group was slightly behind its EFO goals. Overall, our digital earnings have improved year to year in-line with the strategy. In my view, a balanced result that keeps us on track for the year.

I'll come back with more detail on the businesses later.

On the strategic front, I have been working to accelerate our transformation to a digital company ever since becoming CEO last June.

To this end, last July, we accelerated and deepened the restructuring actions for our traditional businesses, with major facility closures in Australia, Canada, Brazil, the UK, and significant reductions in the other facilities located in the U.S., the UK and France. We will continue to retain margins in the traditional portfolio through cost reduction, while working aggressively to monetize the assets made surplus.

I also announced in January that having achieved significant scale in our digital businesses, we are rebalancing our focus more toward margin expansion. That would take a bit of time to implement, but it's a key priority for the year, with results becoming more visible in the later part of the year.

This morning's announcements are therefore the next step in completing the creation of the new Kodak per the plan presented to you in January. As I said before, we intend to finish the re-structuring during 2007, with 2006 being the year with the highest restructuring cost. As always, our focus remains on driving shareholder value.

On the other announcements, the first is the decision to pursue strategic alternatives for our Health Group. This is a very valuable business, with an extremely strong brand, excellent products with market leading positions, a tremendous heritage in the health imaging market, employees with unrivalled experience, a global customer base and strong cash flow.

However, industry dynamics in this industry are re-defining the business model and the scale required for sustained success and leadership.

Because of this, we have decided that now is the appropriate time to explore alternatives. And we have initiated the actions necessary to do so. We have been preparing for this possibility for some time and we'll move this process forward as rapidly as possible.

Our principal objective, as you would, expect is to find the strategic option to reach the full potential of this business; becoming an even stronger supplier to our customers and create a more valuable business with increased shareholder value.

We announced today two additional strategic actions to further implement my vision for our operational model. That vision is to align the company around empowered segment general managers, who have the clearest line of site to their markets and can quickly and effectively create a winning value for proposition for their customers, as well as the infrastructure levels necessary to profitably support those markets. Obviously, I'm pushing the decision rights to those best able to choose the appropriate investment levels.

The first of these additional announcements is the re-alignment of our Global Manufacturing and Logistics organization, by integrating these assets and operations into the relevant business segments. This action, which was a pivotal element in our plans, has been made possible today thanks to and enabled by the rapid and effective restructuring actions we have taken, leaving us with a manufacturing structure that can now be rationalized into the businesses they support. These actions will be completed by July 1st.

This is very significant, operationally and in one sense, marks the last break with the past business model – the end of the 19th century "economy of the scale" manufacturing model, which served our traditional business so well for over 120 years.

However, this must give way to the new dynamics of today's fast-moving markets and new supply chain models. This action is consistent with my vision of aligning assets with the manager closest to the market being served. This will result in an inherently lower cost model overall, faster execution, as well as more fine-tuned distribution and logistic models.

The other announcement is the next significant step toward achieving our target business model by the end of 2007.

As you know, to accomplish this, we must efficiently remove a significant amount of cost from SG&A, which ultimately, is all about business simplification. Again, now that we have clearly defined business segments, the segment managers have defined how much cost is appropriate and are quickly moving to that level. The effort at the business unit level must be matched by significant reductions at the corporate level. By removing layers of management that once were appropriate for our previous model, I can reduce organizational complexity and achieve the reductions in corporate costs that we need.

To that end, we are implementing now an aggressive plan to reduce corporate costs. We will replicate the success we have had in reducing costs and assets in manufacturing but now, on the SG&A side of the business.

It's important to mention that all of these decisions and the costs associated with them were in our plan and part of this year's restructuring budget. We are now in full implementation phase.

Today's announcement will result in the retirement of three senior officers and the re-alignment of three organizational entities and their associated infrastructure. Charles Brown, Charles Barrentine and Dan Meek are strong supporters of our transformation strategy, which they helped me create, and have been extremely effective supporting and executing the transformation. I thank them for their contribution to Kodak past and present and for the unselfish support that I have received from them in the last two years. We wish them well in their retirement.

Now, let's go back to my perspective on our business performance in the first quarter.

CDG **-** While our market position remains very strong in CDG. You remember the great results in the fourth quarter and we expect good results in the first quarter too. Today's results largely reflect the normal impact of the retailers selling through excess inventories, as well as the impact of significant price decreases taken last year in our thermal media portfolio.

From a longer-time perspective, you will recall that I announced in January the primary goal for our Consumer Digital Business in 2006 is margin expansion. Plans are in place to achieve that goal and you can see results of this operating model already and we will see more during the balance of the year.

Phil Faraci and his management team are fully engaged in this process with a number of initiatives moving through the system, including our go-to-market model and supply chain management.

These include using the current 61 countries served directly by Kodak so less than 20 countries, with sufficient scale to permit profitable Kodak's direct participation, with a balance served more effectively by distributors. This is a very typical, well-proven, distribution model for low-margin digital products and we are moving rapidly to have this model largely in place before the end of this year.

We have been focused on driving revenue and scale expansion for the last two years. We are now moving quickly to convert that scale into cost synergies and margin expansion by effectively implementing platform designs, fine-tuned go-to-market strategies and improved logistics. It is possible that these steps could end up limiting our growth in the short-term, but will position the Consumer Digital Group for sustained growth on a more profitable basis. In fact, we now expect that with these improvements, our entire Digital Portfolio will be profitable during the third quarter, a full quarter earlier than last year.

The Film & Photofinishing Systems segment performed essentially on expectation, as we rapidly reduce our manufacturing assets and employment in line with revenue decline.

While the first quarter results reflect the expected low first quarter of revenue seasonality, we anticipate a rebound throughout the remainder of the year. I am very pleased with the better-than-expected EFO performance in the first quarter, helped by operational productivity in the face of higher commodity prices.

The Health Group experienced continued growth in its key digital businesses for the future; the digital capture and the health care information businesses, offset by declines in traditional radiography and digital output products.

The output business, although using a digital printer, is attached to the analogue workflow of the Hospital and therefore, are declining. Digital Capture and Health Information Systems will continue to have a strong market growth.

In this business, in parallel with our investigation of strategic options, we will work on adjusting its cost structure to improve its overall margin performance and continuing to drive the growth of its digital workflow portfolio.

Again, this is a very valuable business and by exploring all the strategic options we will be able to reach its full potential and the maximum shareholder value.

Obviously, the best news from the first quarter came from the Graphic Communications Group. This is a great example of an ongoing success story. This is a business I envisioned when I first came to Kodak and it has become a reality within two years, thanks to a powerful strategy and an excellent implementation. I have great expectations for this business as we continue to take advantage of cost and revenue synergies and the strong acceptance we are experiencing in the market.

The integration of acquired businesses and the associated cost reductions are proceeding better than planned. We continue to see healthy industry growth for our array of digital businesses and even more importantly, customers have embraced the breadth of the Kodak portfolio as one that is unmatched in the industry. You may recall, we recently announced that we significantly exceeded our sales goals again at the IPEX printing conference in Europe. Therefore, we have raised our expectations for the year for this business.

Before I turn the discussion over to Bob, I'd like to reiterate our three critical methods for success in 2006. Digital earnings from operations of $350 million to $450 million, digital revenue growth of 16% to 22% and investable cash of $400 million to $600 million. We remain confident in delivering these numbers for the year.

In summary, we are sharpening the focus of the company, while continuing to create the digital business model I have described for you. And, while we are fully aware of the challenges we have in front of us, we feel reassured by the clear progress we have achieved so far.

Thank you. And now I will turn the call over to Bob for more details about the quarter.

Bob Brust: Thanks, Antonio. I will provide a bit more information around our first quarter financial results and then Antonio and I will be happy to take your questions.

As Antonio indicated, the quarter's performance reflects the seasonality of our transformation, particularly of our Consumer Digital Business, plus the impact of several unusual headwinds. However, I will repeat Antonio's comment, that our view of the full year is unchanged from our January New York meeting.

Let me discuss three of the headwinds in the quarter.

First on the list are commodity prices. We're all dealing with oil-based increases, both business and personal but for Kodak, the most dramatic of these are accelerating increases in silver pricing, with the average price of silver in 2005 at approximately $7.30 an ounce, increasing to an average of $9.73 per ounce during the first quarter, and currently at about $14.00 an ounce.

Due to the rapid increase in silver prices, it has been very difficult to take a significant hedge position in this commodity.

Silver is used across a broad range of our product portfolio, from consumer film to motion picture film to X-ray and digital output film to color paper. As one measure, at $14.00 an ounce, the negative year over year impact on earnings for the balance of this year would be in the range of $200 to $225 million.

During the first quarter, the year over year negative pre-tax impact on earnings due to silver was approximately $19 million. Pressures also exist with aluminum pricing – a key raw material in manufacturing printing plates in our Graphics Communications Group, as well as petrochemical based resins and general energy costs. In order to offset some of this pressure, we have recently announced broad price increases across our silver halide portfolio, as well as previously announced price increases for graphic plate products. These price increases will help us recover some lost margin as we go forward.

The second headwind is on the tax line. For the quarter, we recorded a tax charge of $3 million versus a tax credit of $57 million in the year ago quarter, representing an unfavorable change of $60 million dollars, despite a higher pre-tax loss in the current quarter. With the higher pre-tax loss, you would expect a higher year over year tax credit in the current quarter. However, since the initial recording of the valuation allowance in the third quarter of 2005, we are no longer recording tax benefits and therefore, 100% of our U.S. pre-tax losses are falling to the bottom line. This unfavorable year over year comparison will end in the third quarter as we anniversary the initial recognition of the valuation allowance.

Lastly, I will remind everyone that we have shortened our asset useful life assumptions at mid-year last year, which has a meaningful non-cash negative impact on earnings, particularly in the Film & Photofinishing Group. Due in large part to this change, the depreciation charges are up $83 million, year over year. This significant, unfavorable comparison will also end in the second quarter as we have made this change July 1st of last year.

The total unfavorable impact of these three items represent a substantial portion of our year over year earnings decline. As it looks today, higher commodity prices, and in particular, silver will remain a negative past the second quarter, partially offset by selling price increases. So, with these known issues impacting us in the quarter, as well as the nature of the company transformation, our first quarter results were about where we expected.

One last item before we get started - you will notice the year ago results used today for comparison do not align with results reported in the year ago quarter. We adjusted previous year numbers to reflect the current reporting structure such that the performance is on a comparable basis. Most of these changes reflect the movement of costs and/or allocations between business segments were digital/traditional product categories. These changes include: re-allocation of costs between business segments where the acquired Graphic Communications subsidiaries were added to the company's corporate allocation process, resulting in additional expense allocations to GCG while reducing allocations to the other business segments.

Movement of strategic product groups between traditional and digital product categories.

Impact of U.S. inventory costing changes from LIFO to average cost, which was implemented on January 1st this year and unfavorably impacted the first quarter of 2005 by $8 million on a pre-tax basis.

Now, to the first quarter, consolidated revenue growth for the company was 2%, which included a negative foreign exchange impact of $55 million, or a 2% negative impact. Digital revenue growth was 29% year over year primarily driven by the recent acquisitions within the Graphic Communications Group, while our traditional product portfolio declined 20%.

In the quarter, the company's gross profit margin was 23.5% versus 24.4% last year – a decline of $13 million or approximately 1 percent each point.

First quarter gross profit was negatively impacted by lower volumes, increased depreciation due to shortened useful life assumptions, negative price/mix, unfavorable foreign exchange and higher material – raw material costs, partially offset by significant gains from acquired businesses and manufacturing productivity.

In the quarter, SG&A increased $28 million or 5% but remained essentially unchanged as a percentage of sales at 21%. This increase in dollars was primarily driven by SG&A related to acquired businesses of $117 million, which was largely offset by cost reduction activities of nearly $90 million during the quarter. This reflects the heavy emphasis on this category by Antonio and the team.

In another area of our ongoing cost reduction efforts, the company recorded first quarter pre-tax restructuring charges of $145 million and accelerated depreciation inventory writedowns of $83 million -- totaling $228 million pre-tax or $.69 per share. This was $.10 per share more than a year ago. This includes severance associated with the elimination of 1,175 positions during the quarter, bringing our total employment reduction against the goal of 25,000 to approximately 19,000. The cash restructuring payments in the quarter were $135 million versus $128 million last year. We will manage full year cash restructuring payments to not exceed $650 million this year.

On a segment basis, revenues in the Consumer Digital Imaging group declined 10% as a result of lower volumes and adverse foreign exchange and lower price/mix.

In the quarter, Digital Capture sales declined 11%. Home printing revenue was down 13% and kiosk sales decreased 9%.

The revenue declines were the result of slower sales into the channels as retailers sold through generally higher-than normal inventory positions, while kiosk and home printing were significantly impacted by price reductions of thermal media implemented during the second half of last year.

However, we remain pleased with our kiosk media burn rate and the prospects for these businesses in 2006.

Losses from the consumer digital imaging group were $94 million versus $58 million in last year's first quarter. The year over year decline in earnings, resulting from lower earnings from Kiosks, Kodak Gallery and home printing, partially offset by a strategically important improvement in digital capture earnings.

As Antonio mentioned, we are in the midst of a major overhaul of the operating model for this business. As a result, we expect improving our earnings performance as we move through the second half, particularly in the fourth quarter.

On an organization note, our Inkjet systems continue to be reported in All Other.

Moving onto the Film and Photo-finishing Group, revenues declined 28%, as a result of continuing secular declines in consumer film and photo finishing. In the quarter, the motion picture film portfolio was down 7%, largely due to unfavorable foreign exchange, more conservative release strategies by the major studios, and an increase in the proportion of independent versus studio feature film releases.

However, even with a 28% revenue decline, FPG earnings declined only $42 million, year over year, with more than half attributable to the non-cash impact of higher depreciation resulting from shortened useful assumption. This validates our cost reduction efforts in this area.

Health revenues declined 7% in the quarter, as a result of continued declines in the digital output and traditional radiography portfolios, partially offset by growth in Digital Capture and Health Care Information Systems.

Earnings in the Heath Group decreased from $78 million last year to $46 million this year, primarily as a result of lower earnings contributions from traditional radiology film and digital output, partially offset by improved earnings performance in digital capture and Health Care Information Systems. In addition, it's important to note that the Health represents our most silver-intensive business. Operating margins declined to approximately 8% as a result of these factors.

As Antonio mentioned, given the industry dynamics within the segment, we are now exploring alternatives to strengthen this business.

GCG revenue growth was 136%, driven by the CREO and KPG acquisitions. Cost synergies remain ahead of plan and our comprehensive portfolio of pre-pressed products continues to be well received by the market. Earnings in Graphic Communications Group increased $65 million from a loss of $34 million last year to earnings of $31 million in this year's first quarter, driven by the contribution from the plate businesses and strong year over year earnings improvements in NexPress.

The other income and charges category had a negative year over year swing of $9 million. The biggest contributor to the year over year change is the elimination of KPG equity income, which is now reported within Graphic Communications Group. This is the last quarter of this unfavorable comparison as the KPG acquisition was closed on April 1st of last year.

Interest expense was $62 million in the current quarter, an increase of $24 million from the first quarter of last year as a result of increased levels of debt associated with recent acquisitions and higher interest costs. Interest costs will decline later in the year as we pull down debt.

Total corporate traditional earnings were slightly better than expected at $46 million for the first quarter versus $105 million last year, which represents the seasonal low point for the year.

Consolidated first quarter digital losses from operations were $37 million, a strategically important improvement form last year's quarter loss of $51 million, while New Technology spending showed a slight year over year decline.

As a result, Kodak reported a GAPP loss of $1.04 per share on a continuing operation basis.

This quarter's results continue to place the company well within the range needed to ensure compliance with our debt covenants. In the quarter, the ratio of debt to EBITDA was 2.76 against a covenant of 4.50, for this one, lower is better. The ratio of EBITDA to interest was 5.80, against a covenant of 3.00 - for this one, higher is better. These measurements are calculated on our rolling 4-quarter average.

First quarter investable cash flow was a negative of $576 million compared to a negative $258 million in the year ago quarter. It was essentially on our plan. The plan anticipated several significant negatives from last year's first quarter. We assumed the following: No asset sales in the first quarter, Higher restructuring cash outflows, Incentive compensation of payments in the first quarter versus the second quarter of last year, A larger operating loss, An inventory build which ended up being higher than planned, and Some effect from last Demceber’s push for cash in receivables, where we had aggressive collection actions across the company.

All of that added up to more than $300 million negative from last year.

A lot has to do with the shifting working capital needs of the new digital business versus our traditional business, especially inventories. We'll discuss more in a minute. Net cash from operating activities as determined in accordance with GAAP was a negative $481 million versus a negative $223 million in the year ago quarter, primarily as a result of the decrease in trade payables and other liabilities, earlier payment of the wage dividend, lower asset sales, higher restructuring cash costs and lower earnings. Cash on hand at the end of the quarter totaled $1.077 billion, which compares to $1.031 billion in the year ago period. That is consistent with our desire to maintain approximately $1 billion of cash on hand.

Although we have had a slower start on cash performance this year, we are still comfortable in achieving our investable cash performance for the year, in the range of $400 million to $600 million, equating to $800 million to $1 billion in net cash provided by operating activities.

We are taking actions that make our first half cash performance essentially even with last year. It includes the following initiatives: Inventories increased in the first quarter as a result of not keeping up with the decline in traditional products and the slow sales in consumer digital. We plan to decrease inventory levels by approximately $200 million in the second quarter, as opposed to the second quarter seasonal inventory build of approximately $200 million or so million that we experienced over the years. Our focus here is to begin to change the historic seasonal pattern. We need to make lower first half inventory balance part of the new seasonality of the company. We also have continued tight discipline on capital expenditures, a tight discipline on restructuring cash expenditures and we expect improving earnings performance during the second quarter.

These actions are expected to drive little usage of investable cash in this year's second quarter versus a use of $297 million in the second quarter of last year.

As a result, we should essentially be equal to the year over year cash performance trajectory by the end of the second quarter and on track for our full year expectation.

As you know, we have $500 million of debt due in June. Because of our commitment to maintain a cash balance of around $1 billion, and the strong seasonality of our cash flow, we will likely use some or all of the delayed draw option on our term loan for this $500 million of debt. I would like to remind you that this is not an increase of our debt level, but rather a substitution of maturing debt with debt that will be paid in the second half of the year, when cash flow will be seasonally stronger. We remain committed to reducing our debt level by about $800 million by year-end.

All in all, I feel we are well positioned to deliver our plans for the balance of the year.

In summary, as always, we will work hard on cash, especially in changing this historic inventory seasonality and levels, but we know what to do and how to do it. The second quarter should be materially better than last year and to move us closer to the goals for the year.

On earnings, many of the negative year over year comparisons we saw in the first quarter will be improved by the third quarter as we reach the anniversaries of the changes in taxes and useful life. Some headwinds in other factors will most likely improve, such as foreign exchange, selling prices, volume and interest expenses we begin to retire debt. And those that were positive contributors in the first quarter, such as manufacturing cost, acquisitions synergies, SG&A and R&D costs should strengthen as the year goes on. Silver is the big wildcard and we've been increasing prices to lower the impact.

And now, Antonio and I would be happy to take your questions.

Operator: … Ladies and gentlemen, 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, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, that's star one for questions and I will pause for just a moment to allow everyone an opportunity to signal for questions.

And we'll take our first question from Jay Vleeschhouwer, with Merrill Lynch.

Jay Vleeschhouwer: Thanks. Good morning. I'd like to ask you first about your comments regarding the Health business, which has been, by and large, under-performing for about a year now, in terms of revenue and margin. Are you, in fact, going to be treating that as a discontinued operation, even though you won't necessarily report it that way? You know, you had in mind to perhaps start putting some money back into business, perhaps next year, if not this year and perhaps start to grow it again. Is that now not your plan to try to re-invest and re-stimulate that business? And then, assuming you sell some or all of it, what might be your use of proceeds from the Health business?

Secondly, Antonio, you mentioned the changes in your manufacturing and logistics and to try to integrate more to the business groups. Would that, in part, make it easier to disaggregate the Health business by having a line to the assets and the logistics more according to the segments?

Antonio Perez: First, we haven't said we are going to sell the group. What we said is that the BOD has authorized us to explore strategic alternatives. And we will explore them all and selling will be one of them - but it's not the only one. So, we cannot conclude at this point of time that we're going to sell the group.

Second, the manufacturing question, we've been working on carving out the different parts of the business in an effort to have a much leaner organization that will be fully dedicated to customer segment with full accountability and focus and the ability to make decisions fast and take care of %all the elements of the P&L. I'm talking about inventory. I'm talking about supply chain so we can be more effective. The business, as of July 1, will be, by and large, independent in the sense that we'll have control over every single element of the value chain.

Bob Brust: It's far too premature to decide how we're going to change any accounting because we have just entered into this evaluation with our advisers as to the strategic alternatives for the business. So there's no accounting change.

Jay Vleeschhouwer: … I'd like to ask about your digital EFO expectations for the year, which you are maintaining. If we strip out the consumer digital loss from the total digital profitability in Q1, that looks like about a $57 million earnings from a combined GCG and Health businesses in digital - about a five percent margin for those two businesses together. Assuming you do improve your consumer digital profitability over the remainder of the year, however, what are your assumptions for the margins for Graphics and Health? Do you need to get to a high single digit or 10% or more margins for the non-consumer businesses to get your numbers for the year?

Antonio Perez: Yes. The Health Group will be trending up from the first quarter as it did last year and you can expect somewhere in the teens. 12 to 14 will be a good number. In GCG, the original plan was only to be between five and eight. As I said in my talk at the beginning, we are actually raising the expectation because they are doing much better than we thought.

Jay Vleeschhouwer: Thank you.

Operator: Thank you. We'll take our next question from Matt Troy with Citigroup.

Matt Troy: Good morning. Just following up to Jay's question. I know you're not going to put specifics around what might occur with Health Imaging, but I wondering, Bob, if you could just help us broadly. If I look at that portfolio, could you break it up between what I view as the three primary buckets: 1. The traditional X-ray products and related; 2. The digital output; 3. The remaining digital technologies. Just on a percentage of revenue basis, that would be helpful. I have one follow-up. Thanks.

Bob Brust: You know, I really don't know those off the top of my head. We'll have to get back to you on that.

Matt Troy: OK.

Bob Brust: … Don knows. OK.

Don Flick: Yes and just really broad sweeps?

Matt Troy: Yes.

Don Flick: … The traditional x-ray business is something in the $800 to $1 billion type of range. Digital Output is probably a little bit smaller. You can divide the rest out. We don't split it any further but those are just rough figures.

Matt Troy: OK. Second question would be just an update on the inkjet strategy. Specifically, we're approaching the back-to-school period with stocking logistics probably having to begin in earnest in June - July timeframe, admittedly anecdotal channel checks are saying. Retailers aren't telling anything in terms of seeing product from Kodak. I was wondering if you could give us an update. Are we still on track for back-to-school or is it more of a seasonal issue?

Antonio Perez: Well that could be because they're keeping confidentiality.

Matt Troy: Exactly. I said admittedly anecdotal. But I'm just looking for an update. Are we still on track for back-to-school?

Antonio Perez: I never said we're going to be back-to-school. We'll still on target with our project. I have no news ready to report and you know why I don't want to report news until the closest possible time, the latest possible time. We are accelerating things and I feel that we are in good shape but there's nothing else to report.

Matt Troy: OK, the last question would be on the thermal media. Obviously, you know the pricings were largely a function of people like HP and other inkjet players bringing down their pricing on a bulk basis into the key holiday selling period last year. We should stabilize, or have stabilized on a sequential basis, but what's to say we won't see another step down? Where do you see thermal pricing stabilizing in the next holiday period? Thanks.

Antonio Perez: Well, I can't speak for the others. We did very significant price reductions anywhere between 38 and 50 percent. That was a very significant price reduction that we took. The idea was to be more competitive. At the same time, we've been working to reduce our own cost. We feel that the number of units that have sold through is high, so we think that we are very competitive now. I can't tell you this is going to happen again. So far, so good.

Matt Troy: Thanks, guys.

Operator: And we'll take our next question from Laura Starr with Equinox Capital Management.

Laura Starr: I just wanted to ask a question about the film - the Entertainment Imaging business. It was down seven percent in the first quarter. When you look to the second quarter, the line-up of blockbuster sort of movies coming out over the next three months is much higher than last year. Are you expecting the comparison this year in second quarter versus last year to be much higher?

Antonio Perez: Hi, Laura. Yes. It went down in the first quarter. We think this is caused by poor content – content that hasn't been accepted by the audiences. This is factual data: in North America, the attendance has grown two to three percent this year. The number of people going to see movies has gone up.

Laura Starr: Right. And the box office is up too, this year.

Antonio Perez: Yes. And their revenue is about five percent up. This is before Memorial Day weekend, which is normally the time when all the blockbusters that you mentioned are ready to come into play. So, I don't know how those are going to be received. We're optimistic but we keep saying the same thing we said before – we expect this business to re-flourish. We don't expect this business to grow significantly or go down significantly. On the other hand, we have seen a shortening in what is called the theatrical window - the time from movies going to the theatres and then coming into DVD's. It does not seem to affect the number of attendees to the theatres. We're doing well with our digital program. Our pre-show digital – we are actually the largest supplier of independent theatres as far as pre-show digital projection. We have about 2,000 installations already in place. We have a system that can actually perform through HD. We are ready for whatever happens - although it's going to happen slowly. There are going to be some pilots this year and next year and the year after. This is going to be, in our view, a long process and a hybrid industry and we'll be working through it.

Laura Starr: OK. Thank you very much.

Operator: And we'll take our next question from Jack Kelly with Goldman Sachs.

Jack Kelly: Good morning. Antonio, could you just go back to consumer digital and talk about the first quarter? You mentioned, inventory back up at retail. In terms of consumer digital cameras, could we be seeing a flattening or decline? It sounded like camera sales went down, so have we reached penetration maybe sooner rather than later?

Antonio Perez: Let me give you the best answer that I know. We did very well in the fourth quarter and in fact, I can tell you that we're doing very well in sell-through in the first quarter. Sell-to is a different story.

Obviously, the inventory and the channel have to clear up in the first quarter. We expect that we will be cleared up by the second quarter. Our pricing points are moving up. We're moving a lot more the V-Series. Our V-Series have been incredibly successful. We're very proud of it and it's a much higher price than the original cameras. And, as you probably noticed, we have introduced new models starting with the second quarter. We know that what happens in the first quarter is a clean up of the old models. On top of that, we have been careful as far as picking what market share we want to gain and what we don't want to gain. So, during the first quarter, you have all these pricing deals. We only decided to participate in the ones that we thought were appropriate for us – following the strategy of margin expansion.

Now overall, the market is flattening and we knew that. There's going to be some growth but nothing compared to the last three years. We are on track. We are making more money than last year and I feel optimistic for the year.

Jack Kelly: So, versus a down decline in your shipments of digital cameras, you're saying the sale of Kodak cameras at retail was up?

Antonio Perez: The sell-through was up. The sell-to was lower.

Jack Kelly: Yes, yes. That's what I'm saying. So, we're down 10 percent plus selling to retailers. You're saying retail sales of cameras to consumers were up for Kodak.

Antonio Perez: That's right. Very strong. And that's really what counts. I mean, when you send these things to the retailer is irrelevant. What matters at the end of the day is when the retailer finally sells these products to a final consumer.

Jack Kelly: OK. This question is for Bob. On the potential divestiture, or partial sale, or whatever you might do on health care, I thought there was a provision in the new bank loan deal that you negotiated last year that up to $1.1 billion of asset sales would be required to pay down debt. Is that just triggered by an outright sale? So if you did something less than that, that provision wouldn't be triggered?

Bob Brust: Yes. If the option is a sale, we would be required to make payment of the covenant debt, which is about $1.2 billion. Any other options we would choose, we would have to view at that time. We're talking about strategic alternatives, here. We have not made a decision. If we did opt to sell, we'd pay the debt.

Jack Kelly: OK. And just finally, Bob. On the restructuring you mentioned, or was it Antonio that described it as being kind of already in the plan. I guess this year we're going to have restructuring charges of $1.1 billion and then maybe another $500 million next year? So maybe you could just talk about those numbers and what the cash implications of those numbers would be?

Bob Brust: Yes. Jack, the cash, this year, that we've been talking about is around $650 million and we are tightly controlling ourselves at that rate and it was close – it was $138 million in the first quarter. It tends to build-up toward the third quarter and then diminishes a little bit in the fourth quarter. Next year though, will be a fairly sharp reduction in restructuring. There will still be significant charges but the cash will probably be down around $200 to $300 million. So it'll probably be less than half of this year. Once we get through this year, we're through the lion share of this.

Jack Kelly: OK. So the $650 million in cash this year would be equivalent to the expense, the charges of $1.1 billion or so and then next year?

Bob Brust: … $1.3 billion, depending on how we estimate this when we start the year. When you actually get to the actual assets, you have to write them down, so I'd say $1.1 to $1.3 billion would be the financial charge.

Jack Kelly: OK. And the two to three next year might gross up to five? The $200 to $300 million?

Bob Brust: Yes. Somewhere around there. I don't know yet. We'll have to give you some more guidance on that in September. After this year, what's left will be materially lower and it will be early in the year. As we come out of '07 we should have this pretty well cleaned up.

Jack Kelly: On the announced price increases implemented May 1, did you see any build up in shipments in April or in the first quarter as people try to anticipate those price increases?

Antonio Perez: No, no. We didn't see that. That market is not a growing market where those things tend to happen. This is a pretty well established market. Now we don't know what the rest of the industry will do. As material costs go higher significantly, we feel this is the right thing to do.

Jack Kelly: OK. Thank you.

Operator: And we'll take our next question from Chris Whitmore with Deutsche Bank. Mr. Whitmore, your line is open. Please go ahead with your question.

And we'll go ahead and move onto our next question with Ulysses Yannas with Buckman, Buckman & Reid.

Ulysses Yannas: Hi, Antonio. You are talking about price decline of 38 to 50 percent in thermal media. You had a decline of nine percent in overall revenue. That means that your sell through rate was what? Over 50 percent?

Antonio Perez: Yes. Ulysses, say again?

Ulysses Yannas: … to come down to the burn rate at kiosks. The media.

Bob Brust: Burn rate?

Antonio Perez: Oh, the burn rate continues to be very good. It's excellent. We haven't seen any reduction in burn rate. Actually it's going up. Burn rate is going up. We put the price at that point because of the other systems that come into play. We have to put a price that is competitive to the mini-labs, to the home printing and to the other kiosks. We did an analysis looking for the impact on our customers. Our market share was the best. We feel very strong about our kiosk burn rate going up. We don't have a problem there.

Ulysses Yannas: How about the package deals you are doing? Cameras and the printer docks?

Antonio Perez: Yes. You're going to be seeing less bundling. Normally when you bundle, you set a very attractive price for both. That plays a role when you're trying to build your install base. You reinforce the value of the connection. Obviously it's not as attractive financially as when you sell them separately. So you're going to see less bundling this year than last year.

Ulysses Yannas: You were talking last year about Versamark doing extremely well. Is that continuing to be strong, besides NexPress?

Antonio Perez: Yes. They tend to be very large orders. This first quarter they were weak compared to last year. You know, they don't have a true competitor. You ask me, they have a very specific technology.

Ulysses Yannas: Did your products beat the competitor?

Antonio Perez: Which one?

Ulysses Yannas: I'm sorry. Xerox …

Antonio Perez: Our competitor has a different technology.

Ulysses Yannas: OK.

Antonio Perez: You know, inkjet has very specific characteristics and for the jobs that have been designed, I think it's the best alternative. We have very good prospects for Versamark for the year. It's just that this first quarter was weaker than last first quarter. That doesn't have any negative signal for the year.

Ulysses Yannas: How about the cost reduction out of the KPG and the Creo acquisitions. Where do you stand there? You were talking about $150 million.

Antonio Perez: Yes, over a few years. They're on track - maybe slightly better. The bulk of those synergies are going to come later this year, but they're on track. That organization is executing beautifully. I have full confidence that we'll get those numbers.

Ulysses Yannas: You haven't started yet on Creo, have you?

Antonio Perez: Yes. We have started on Creo. Those cost reductions have a lot to do within those two organizations working together to eliminate dualities and improve productivity. Those numbers apply primarily to KPG and Creo, with a small portion of savings from the rest of GCG.

Ulysses Yannas: OK. Thanks a lot.

Antonio Perez: Thanks, Ulysses.

Operator: And we'll take our next question form Carol Sabbagha, with Lehman Brothers.

Carol Sabbagha: Thanks. Just a couple follow-ups on the consumer digital businesses. You kept your digital revenue growth for the year the same, although it looks like consumer digital may come in lower than expected for the year. Is something else within that going to do better as the year progresses? To make up for, I'm guessing, some more muted expectations around consumer digital?

Antonio Perez: I don't know that we changed the expectations on anything yet, Carol. What are you referring to?

Carol Sabbagha: Well, given how you talked about digital revenue - consumer digital revenues as the year progresses – doesn't sound like you're looking for significant growth coming from that business as a whole.

Antonio Perez: What I tried to say is that the most important objective for that organization for this year is margin expansion. If we have to sacrifice growth to get the margin expansion that we want, we will do so. Hopefully we won't have to sacrifice a lot of growth to do that. We think it's the right thing to do because there are a lot of deals out there that could be questionable.

Carol Sabbagha: So on consumer digital cameras, you mentioned that the retailer sell-through to the customer was up in the quarter. Can you give us kind of a feel what that was?

Antonio Perez: It's a little too early. We have daily and weekly information of what's going on at some of the key retailers. We don't get every single retailer in the world so I don't want to give you a number. This takes a little longer. We have a sample of key retailers – it's a very good sample. It gives you an idea of what's going on, but I wouldn't make that number public. I just know that our sell-through this quarter is fine. It is doing fine even though our sell-to is lower than last year.

Carol Sabbagha: OK. And then in the kiosk business, just so we're not surprised for the year, it seems like you said your media unit sales were strong but pricing declined? Were your hardware sales down or is it mostly pricing and therefore it could take another couple of quarters to anniversary out of the numbers?

Antonio Perez: I basically think it is the price of the media and that we created large packages sold in the third and the fourth quarter. Some of those haven't gone through yet. There was an expectation of a certain amount of printing by our retailers and every company offered large packages - moving from 40 to 160 pages. I believe some of those packages still haven't been used. So, it's some of that in the price and it's not the real usage. The real usage is going up - maybe not as fast as the industry predicted.

Carol Sabbagha: OK. Do you think the kiosk business for the year will be up in revenues?

Antonio Perez: Yes. That's the plan we have today, yes.

Carol Sabbagha: OK. Continuing on consumer digital – I think you mentioned that digital capture profits improved or losses improved year over year while the total segment's losses widened. What was the main factor there? And then, Bob, in his comments mentioned kind of a major overhaul of the consumer digital businesses to get to profitability. What are the key points in that overhaul? Is it simply just walking away from bad business?

Antonio Perez: No. It was a combination of things. Digital capture did better than last year as far as EFO. Kiosk and home printing did worse than last year. It doesn't mean much for us in the first quarter. I mean, obviously we would like it better, but the first quarter is very small. Because of the changes we made to the thermal media, this is understandable and predictable. The other element that Bob was referring to is that we have been investing in SG&A in the consumer digital group. By the end of the year it will be reduced as compared to last year. We have more SG&A synergy than last year. Splitting DFIS in two is pretty complicated and we don't want to lose sales dramatically. We had to get ourselves right before we started to reduce SG&A. It will happen during the second and the third and the fourth quarters. I described a plan of moving from basically 61 countries where we directly sell with our own office and our own people to 20 countries. We're not going to abandon the other markets. It's just that it's much more efficient to pick those 20 where there is sufficient size and do it by ourselves. In the rest, we're going to use distributors, which is a very typical thing to do. We are in the process of doing this and by and large, it will be done by the end of the year. So, the SG&A will go down. In the first quarter it's up because of the split of DFIS into the digital and the non-digital.

Carol Sabbagha: OK. One last question and thank you for taking so many. On the price increases that you instated across the board on your silver based products – it might be too early to say but if you can walk through the major segments and tell me if any are sticking and how the feeling is around customer acceptance and whether they'll be able to go through.

Antonio Perez: I think they're going to stick because we're not going to move them down. So, I don't know how the world is going to react. This is the right thing to do. It doesn't make sense in any way, shape or form to absorb this enormous cost. It doesn't make any sense. So, I don't know what our competitors are going to do but we're going to stick with those.

Carol Sabbagha: Thank you very much.

Operator: And we'll take our next question from Sam Doctor, with JP Morgan.

Sam Doctor: thank you. I have a couple of questions. Most of them have been answered but can you give us a sense of spend on advertising? Was it up year on year? You said it was up in CDG. Was that an absolute increase or was it a re-allocation of advertising expense?

Antonio Perez: The advertising was higher in CDG, yes.

Sam Doctor: Was it up in aggregate for Kodak?

Antonio Perez: I don't know that, Sam. Yes, we're looking at it. We'll tell you in a second. I expect you guys to look at this by segments. It was up slightly, like four percent. It was up four million. That's practically nothing.

Sam Doctor: All right. On the digital GCG plan, you said you are raising the target from the original five to eight percent operating margin. What is the new target for earnings from operations for GCG?

Antonio Perez: Oh. We're going to raise the target. I'm still negotiating with my team. They're over-performing. It's very clear that they're over-performing. It's very clear that the opportunity is better than what we had in the plan. We don't have a number yet.

Sam Doctor: OK. And a final question from me – what is your philosophy on the cash balance? I know you said that at the moment, you're looking at $1 billion minimum. But if you're looking at reducing debt by about $800 million, are you looking at that contingent on asset sales or is this reduction looking at proceeds from what you might do with health care?

Bob Brust: It's the exact same story that we gave in the January meeting. We started the year with about $1.7 billion of cash. We anticipate generating about $500 million, including asset sales. So that would be $500 million plus a $1.7 billion. We are planning on paying down about $800 million of debt so I envision ending the year at about $1.3 billion to $1.4 billion - so no change at all.

Sam Doctor: OK. Thanks.

Operator: At this time, I'd like to turn the call back over to you for any additional remarks or closing comments.

Antonio Perez: Well, thank you very much. I really appreciate the time that you take to listen to the call. Again, I want to reiterate that this is a very typical first quarter. There are a lot of strategic wins for us. There's some issues that we have to work on, specifically, inventory build-up. We're going to deal with that in the second quarter. Otherwise, I see the year the way we planned it at the beginning. We have the same goals and we're ready to execute. Thank you very much.

Operator: And ladies and gentlemen, this does conclude today's teleconference. You may now disconnect and have great day.