

*In this difficult market environment, Konica is working to steadily achieve such basic goals as increasing operating income, decreasing interest-bearing debt, and boosting corporate value. We are also pushing forward with efforts to dramatically reform our business structure in line with the trend toward digitization.*

### ***Transformation Is the Key to Konica's Future***

The key to Konica's future is to dramatically transform the Company's business structure. Meeting this challenge will require us all to work together with relentless determination. Since assuming the position of president and chief executive officer in April 2001, I have emphasized this point at every possible opportunity. The report you are now reading is intended to clarify Konica's business position to you, our shareholders, and to rally the support of everyone involved in Konica's management and business operations.

In my few months of serving as president, I have become convinced that our company is poised to move in a positive direction.

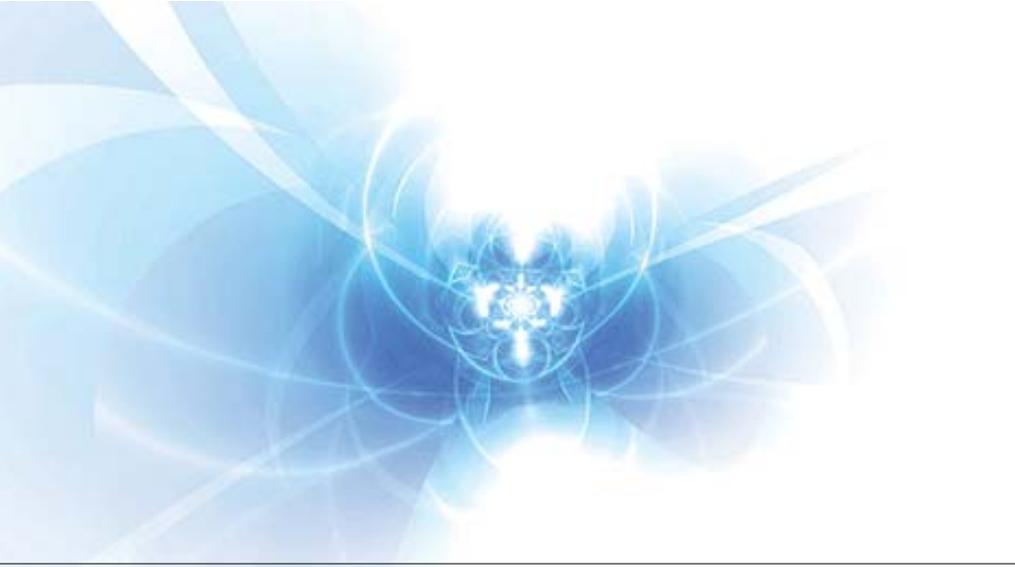
In February 2001, the Company formulated a new medium-term management plan for the period from the fiscal year ending March 2002 to March 2005. Called SAN Plan 2004, the plan maps out a course for Konica's growth during this age of rapid change, consistent with the

challenge mentioned above. An outline of the plan follows. First, however, I would like to report on the Company's business performance during fiscal 2001, ended March 31, 2001.

### ***Business Results for Fiscal 2001***

Despite the fact that the fiscal year under review saw a largely inhospitable business environment, the Company's performance went almost as planned. We recorded net sales of ¥543.7 billion and net income of ¥6.5 billion. While I would greatly prefer to deliver a more positive report on our performance, I regret to say that we fell short of some of our goals compared with the previous fiscal year. Key factors behind the adverse results included unfavorable exchange rates, with the yen's appreciation during the year having a significant dampening effect on sales and operating income, and an extraordinary loss resulting from mandatory retirement benefit payments. However, looking back at the consolidation of our product line and the cost-reduction measures the Company undertook, we can claim a certain degree of success for the year.

In business related to the photographic materials segment, the Medical and Graphic Company managed to post gains by shifting early on to digital products, leading to development and marketing of such systems as to record, transmit and store X-ray images (the Konica Direct Imaging System). In addition, the EM & ID Business Group saw increased sales of triacetyl cellulose (TAC film), a key material for making the polarizing filters used in liquid crystal displays (LCDs). Operations went into full swing in March 2000. Due to the high production capacity at our dedicated facility—the industry's first—we succeeded in meeting the growing market demand. At the same time, the Consumer Imaging Company, which handles color film and photographic paper, recorded steady growth in markets such as Russia, India, China and Brazil. Due to sluggish domestic demand, falling prices, and unfavorable exchange rates, revenue and profit declined. The Inkjet Business Group, which handles inkjet paper products, continued to cultivate large-scale business in its sector with



President  
**Fumio Iwai**

*Alliance, and Network. The Speed concept has been applied in all operating areas by means of structural reform. In June 1999, we implemented new policies to refine our internal company system, and in June 2000 we introduced new management and decision-making structures.*

the highly regarded Konica Inkjet Paper Photolike QP.

Sales and operating income from the business machines segment, which is managed by the Office Document Company, were heavily affected by the exchange rate and saw drops in both revenue and profit. The Optics Technology Company, which handles products such as pickup lenses used in CDs and DVDs, saw steady growth overall but experienced a temporary slowdown, mainly due to the rapid cooling of the U.S. personal computer market in the latter half of the year.

The Camera & Digital Imaging Business Group, which markets products such as cameras and digital cameras, was affected by the downturns in the film and camera markets of Japan and Western countries, which saw significant decreases in both sales amounts and volumes. On the other hand, digital camera sales continued to grow, centering largely on original equipment manufacturing (OEM) supply.

**Results of the Company's Medium-Term Business Plan**

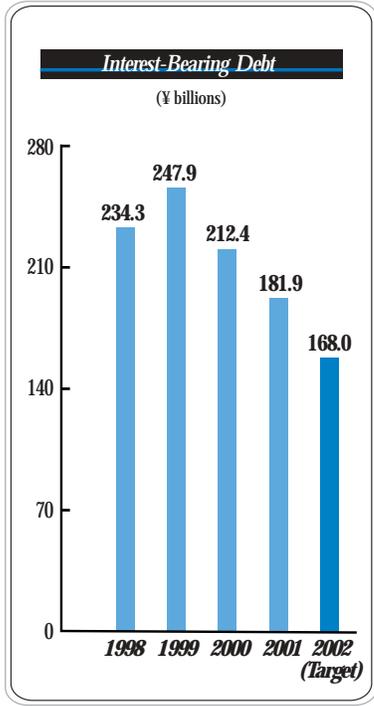
Before outlining the contents of our new SAN Plan 2004 medium-term management plan and our future strategies for growth, I would like to review the policies Konica has followed over the past several years.

Beginning in 1998, the Company moved forward with two new medium-term business initiatives, V Plan 2000 AAA and SAN Plan 2003.

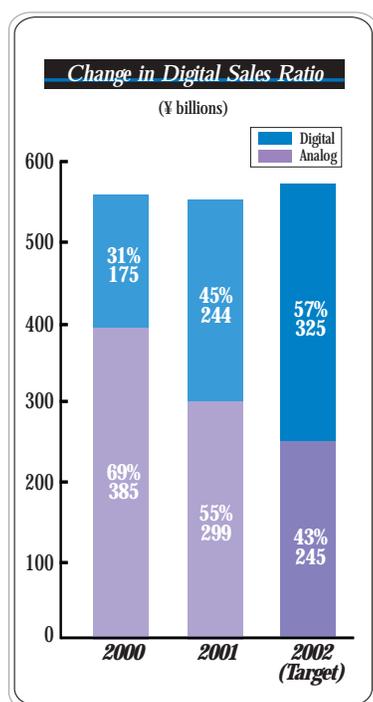
Our V Plan 2000 AAA set the basic approach for restructuring our photographic materials segment, with the goals of improving profits and strengthening cash flow management to reduce interest-bearing debt.

Guided by the plan, we succeeded in raising our operating margin from 4% in March 1998 to 5.6% in March 2001 and in slashing interest-bearing debt from ¥234.3 billion to ¥181.9 billion.

Meanwhile, the primary goal of SAN Plan 2003 was to boost corporate value, guided by the key words *Speed,*



***From 31% to 45%. As of March 2001, the shift to digitization has continued to proceed swiftly. Guided by our medium-term business plan, we will keep focusing investment, staff, and technical strategies to push ahead with digital networking***



Under the *Alliance* theme, in April 2000 Konica formed a business tie-up with Minolta Co., Ltd., in the office document business. The combination of our high-speed digital technology and materials development with Minolta's digital color image processing technology and printers gives both companies a number of highly competitive products and greater technical strengths. The alliance will provide consumers with

a host of attractive new products that offer unprecedented features, while helping us bolster operations and significantly boost profits.

Under the Network theme, we focused on increasing sales of the digital products in our product line. These efforts paid off, with the sales percentage of digital products climbing dramatically, from 31% in March 2000 to 45% one year later.

Moreover, we have reallocated Konica's resources and sought to promote the development of products and services for digital network systems and expanded strategic business lines such as optics technology, inkjets, and electronic materials. Combining these three strategic business fields proved highly successful, as the Company's sales rose from ¥71.3 billion in March 2000 to ¥80.7 billion in March 2001.

### ***Transforming Our Business Structure under SAN Plan 2004***

At the outset of this report, I described how dramatic transformation was the key to Konica's future. By this, I mean

the transformation of our business structure itself. While transformation has been the underlying theme of the Company's medium-term management plans for the past several years, our business structure has mainly revolved around film, photographic paper and other analog products. The continued swift advancement in digital technology, however, requires a more profound shift—from the previous business structure to one that better accommodates digital systems and creates new business opportunities.

Accordingly, we studied the progress made under SAN Plan 2003 during the previous year, added new management tasks, and upgraded to SAN Plan 2004 in a move designed to achieve steady implementation of the medium-term management plan. SAN Plan 2004 stipulates a policy of focusing investment, human resources and technical strategies on promoting the Company's shift in emphasis toward the newly developing areas centered on digital networks while also reinforcing strategic business areas.

***Solid Growth Expected in the Business Machines Segment and for the Office Document Company***

We anticipate significant growth in the business machines segment, and for the Office Document Company in particular. With many companies now providing office document services, competition in this field has intensified. Accordingly, many of the Company's shareholders must have questions about our optimistic expectations for the Office Document Company. I believe the following points will provide a clear answer to these questions.

First, it is a fact that high-speed copiers are the focus of keen attention. As digitization continues to increase, the business structure of the Office Document Company will remain the same—that is, profits will continue to come from sales of consumables. Eventually, however, high-speed copiers will generate greatly increasing sales. Also, note that some major technological advances are necessary to develop high-speed copiers that can operate around the clock and sustain

productivity of at least 75 copies per minute (as with the Konica Sitis 7075). Konica's high-speed copiers already enjoy high regard in this area, with levels of reliability and durability that give us a strong competitive edge.

Backed by the performance of our high-speed copiers, we are considering introducing print-on-demand (POD) to the near-print industry. Although we have possessed the functional ability to handle POD, certain technical problems with the image continued to hamper development, such as detailed control of the print position. These problems have now been resolved, and we expect to launch the product at a price of several million yen. There is a large market for near-print POD that requires high-volume copying, and we believe this will contribute significantly to expanding sales. For example, developing a controller that can interface with the IBM AS/400 for computer network systems would greatly improve networking capabilities.

Second, consider the subject of cost reduction in digital copiers. To obtain clear success at a time of intensifying price competition, Konica has focused on comprehensive cost reductions. We expanded our manufacturing base in China, then continued finding other innovative ways to drive down costs.

Third, I would like to mention sales of polymerization toner, whose development is unique to Konica. Following the establishment of our business alliance with Minolta in December 2000, we jointly formed the Konica Minolta Supplies Manufacturing Co., Ltd. The new company brought to market a practical polymerization toner, which debuted as a consumable that delivers superior picture quality at a competitive price.

By making best use of our competitive strengths in the years ahead, we have our sights set on boosting sales from ¥174.1 billion in March 2001 to ¥277.0 billion by March 2005.

### ***Expanding Our Technological Sphere with Optics Technology***

We are also optimistic about the future prospects of the Optics Technology Company, one of our strategic business operations. To this point, the Optics Technology Company's mainstay product has been the aspherical plastic lenses used in optical discs, with our CD/DVD aspherical plastic objective lenses capturing a market share of around 70%. We expect to maintain a healthy market share and high profitability, particularly in lenses for DVDs and the next-generation HD-DVDs. Plans are also under way to reinforce our lens unit business, especially for products such as VTRs and digital cameras.

Further, we expect that opto-mechatronics technology, which we developed for zoom lenses used in cameras/VTRs and 3.5-inch magneto-optical (MO) disk drives, will find applications in micro-camera units, such as those used in the personal digital assistant field. With these areas as our focal points, our goal in optics technology, including camera and digital imaging operations, is to boost

sales from ¥64.4 billion in March 2001 to ¥83.0 billion by March 2005.

### ***The Inkjet Business Group Uses High Technology to Create New Markets***

The Inkjet Business Group and the EM & ID Business Group have been designated as strategic business fields in photosensitive materials-related operations. Sales of media (paper) have been the driving force behind the business volume and profits of the Inkjet Business Group. In particular, sales of our highly regarded Photolike QP, a Konica photo-quality inkjet paper with an excellent glossy base and microporous technology for fast drying, have doubled every six months. This has led to our capturing around a 60% share of the market for high-quality glossy paper.

In addition, printer heads are achieving both higher speeds and higher density as the number of nozzles has increased from 128 to 512. The Company has set a goal of 512 nozzles and is following a three-pronged approach that calls for developing media, printer heads and

ink. While combined sales of the Inkjet Business Group were ¥4.1 billion in fiscal 2001, we have set an ambitious sales target of ¥36.0 billion by March 2005.

### ***Advances in High-Value-Added Products from the EM & ID Business Group***

The EM & ID Business Group is focusing its energies on LCD polarizer TAC film. Demand for this film, a key component in making polarized film for LCDs, should continue to expand. As thin film and high-value-added services continue to grow, we project that sales of the EM & ID Business Group will rise sharply from ¥12.2 billion in March 2001 to ¥30.0 billion by March 2005.

### ***Focusing on Investment, Human Resources and R&D Strategy***

To guide our efforts in fields with high growth potential, we are focusing on our investment, human resources and R&D strategy as outlined above. All capital investment possible within the limitations of cash flow is being directed toward these fields. Specifically, the LCD polarizer TAC film business is creating high-value-added

products, the Optics Technology Company is expected to see operations expand as it finds new applications for optics technology, and the Inkjet Business Group has developed a strategic plan to use its advanced technology to open new markets. In addition, the Medical and Graphic Company is constructing a new medical dry film production facility, the Consumer Imaging Company is investing in a digital photo network service, and the Office Document Company is undertaking investment in polymerization toner. In these ways, we are concentrating intensively on investment and R&D in digital imaging fields, with expectations of solid future growth.

We are well aware of the vital importance of allocating human resources effectively, especially in light of the technical expertise it takes to shift focus to fields with the highest growth potential. To meet this challenge, we have established a committee to mobilize human resources. We will also continue to apply our unique technology and exploit our competitive strengths to broaden our strategic business alliances, such as the office

document business joint venture formed with Minolta in April 2000.

### *Plans to Establish Separate Corporations and a Holding Company in April 2003*

In closing, I would like to touch on our plans to establish separate corporations and a holding company. Details of these plans are outlined in SAN Plan 2004.

Konica introduced an internal company system in 1999, and our structure now encompasses four companies and three business groups. Our business covers a variety of fields, and each operation has a diverse customer base with its own unique needs. To accelerate the development of these operations, it is necessary to transfer a considerable amount of power and authority to each company. Consequently, in April 2003 we plan to make each existing company a separate corporate entity and to study the transfer of Konica to a holding company. These changes will increase management flexibility, allow us to focus more sharply on maximizing corporate value, and help ensure that management remains shareholder-oriented.

SAN Plan 2004 also outlines our environmental accounting systems. Konica believes that global environmental preservation is one of the most critical issues management must address, and accordingly has devised a set of Environmental Guidelines to promote harmonious coexistence between our operations and the natural environment. Under these guidelines, we created environmental accounting systems in March 2000 and established environmental performance goals that take effect following the year ending March 31, 2002.

I believe that the 21st century will be an era of profound change and intense competition. Konica stands ready to respond swiftly, decisively and effectively to new challenges as they arise, moving into the future with courage and determination.



June 28, 2001

Fumio Iwai, *President*