

Summary Translation of Question & Answer Session at Electronic Devices Business Strategy Briefing for Analysts

Date: April 4, 2007
Location: Grand Prince Hotel Akasaka, Tokyo
Presenter: Shigeru Fujii
Corporate Senior Vice President, Fujitsu Limited

***Questioner A:** I understand that the distinction between standard and advanced technology devices has to do with cost structure, but I would like to know how long your 90nm devices will remain in the advanced tech category.*

Mr. Fujii: We will keep 90nm in the advanced tech category at least through fiscal 2007, and we will review that categorization regularly thereafter. We consider products to be standard tech once the investment is fully depreciated and profits begin to materialize. Before they reach that point, they are considered advanced tech. With respect to 90nm production in fiscal 2007, although we will start to see profits from Mie Fab No. 1 beginning this fiscal year, there will be development of IP for new applications this year. Once the bulk of our engineers shift to work on 65nm and 45nm, we will reconsider reclassifying 90nm as standard tech.

***Questioner B:** Could you please tell us about your capital expenditure figure for LSI Devices in fiscal 2006 as well as the expected figure for fiscal 2007, reflecting your new revisions?*

Mr. Fujii: We have lowered our original projection, which was in excess of 100 billion yen, by about 10 billion yen. I am not able to discuss projected fiscal 2007 numbers today, but as far as basic direction is concerned, I can say that with the downward revision due to the postponement of investment in advanced tech capacity expansion, we do not expect overall LSI Devices capital expenditure to surpass the 100 billion yen level in fiscal 2007.

***Questioner B:** What is your view of the current market environment?*

Mr. Fujii: Orders hit bottom in November, but there appears to have been a slight rebound in the fiscal 2006 fourth quarter. Nevertheless, we are expecting severe conditions to continue into the first quarter of fiscal 2007. The book-to-bill ratio has risen above 1, but it is too early to determine whether this will be a true recovery.

***Questioner B:** How soon will you be able to post a quarterly operating profit for LSI Devices?*

Mr. Fujii: I consider it my responsibility to restore profitability sometime within fiscal 2007. Our current plan is at a tipping point, and results could go either way. The overall Device Solutions segment is generating profit. However, within the LSI Devices sub-segment, even though we have built Fab No. 2 at our Mie Plant and are incurring depreciation expenses, we have no output there yet, so it is squeezing our profits. We are planning to increase income generated by standard tech products in fiscal 2007 to cover this area.

***Questioner C:** It seems that for 45nm technology you completed investment on your own, but what about 32nm technology and beyond? Will you continue to pursue development on your own, or will you collaborate with other companies?*

Mr. Fujii: We have not made any decisions at this point with respect to 32nm and beyond. Before then, we have to continue R&D on 45nm, and we do not yet have a clear picture of the type of 45nm devices would make economic sense and what new functions they will need to have. When it comes to 32nm technology, we still do not have a good understanding of what the applications would be. We are at the level of doing R&D on materials and so forth. Collaborating with another company on 32nm development is one option. I think that it is very difficult for companies to make very large investments in development without having a clear picture of the market in mind. In terms of miniaturization and differentiation, for example, just as we are doing with 65nm devices, each of the major players – Toshiba, Renesas, NEC, IBM, etc. – is continuing process development work while developing applications in their areas of expertise. In Fujitsu's case, for 90nm, we have developed ultra-high-end technology to incorporate in our PRIMEPOWER UNIX servers as well as ultra low power processes. At the same time, we have avoided generic technology for PCs and other applications that are positioned in the middle. In this way, we are pursuing development with clear targets in terms of applications. For this reason, because processes and technologies differ on the basis of what applications you are aiming for, some companies are candidates for collaboration and some are not. Considerations about collaborating with another company in volume production are separate from considerations about what application technology to pursue.

Questioner C: Have there been changes in regard to specific customers that have impacted your 65nm investment plan?

Mr. Fujii: I cannot comment about specific customers.

Questioner C: In regard to standard tech logic production, what are your plans for production capacity of 8-inch wafer lines, including those that your new subsidiary FSET will handle? Also, what is your capacity utilization rate for standard tech products?

Mr. Fujii: Monthly production capacity for standard tech 8-inch wafer lines will rise from about 80,000 to about 110,000 wafers, an increase of about 40%. The capacity utilization rate varies according to the production line. The rate is becoming higher for FRAM for security applications and for microcontrollers for automotive applications. The overall rate for standard tech lines is around 80%.

Questioner C: Please comment on the profitability of your fabs.

Mr. Fujii: Our 8-inch wafer lines are generating a profit even with the 80% capacity utilization rate. In fiscal 2007, Fab No. 1 at the Mie plant (300mm, 90nm) will generate a profit. We will strive to also make Fab No. 2 (65nm) generate a profit as soon as possible.

Questioner D: I have the impression that dependence on TSMC is increasing for the industry as a whole. What are your thoughts about this issue?

Mr. Fujii: I cannot comment on other companies, but, as I explained, from the perspective of our production capacity, depending upon how our business develops, I would not rule out using TSMC. We would only consider working together in our areas of strength, but among our applications, if there is one that TSMC is particularly adept in, contracting out to TSMC is one option we would obviously consider. At present we are not using TSMC, but we are working with companies in Taiwan and Shanghai in a fabless/foundry relationship.

Questioner D: Recently I have heard rumors about another Japan foundry plan, except this time it would be driven by the private sector rather than the government, and an 8-inch facility that has already been fully depreciated would be purchased. Do you have any comments about this?

Mr. Fujii: I do not comment on rumors.

Questioner D: Could you tell us about the status of Fujitsu's pool of semiconductor engineers?

Mr. Fujii: Let me respond with respect to designers and process engineers. Right now the biggest needs are for designers; there is a shortage of analog designers, in particular. Japan used to be very strong in the analog field, but many of the engineers have retired, and many of the younger engineers have little training in the analog field. So in Japan, overall, there are not many analog designers. In that sense, this may be the area with the greatest shortages, but it is still a source of competitiveness, so we are doing what we can to increase our resources in this area.

In that respect, I feel that the labor market in Japan, including our universities, are not adequately addressing and responding to the human resource needs of corporations. The places where we can get those human resources are Israel, India, and parts of China, so the fact is that we are having now to go overseas for these resources.

Regarding process engineers, formerly companies were able to secure sufficient numbers of process engineers, including younger ones, but as the baby boom generation begins to retire, this is another area in which resources will become tight. On the other hand, the production equipment manufacturers are now doing quite well, and they are now performing many of the tasks that used to be performed by process engineers, so we are not yet feeling a pinch. An area in which we need to enhance our level of skill is in people who can bridge the areas of process and design.

Questioner E: I understand that demand for 65nm chips has been pushed out into the future because customers do not yet understand the economic merits, but how do you intend to get them to understand the merits going forward?

Mr. Fujii: I think our customers understand the value that we provide. In general, and including at Fujitsu, pricing for each service level—foundry, COT and ASIC—is quite clear, so value is also very transparent.

Questioner E: What ratio of production is for internal use and how significant is it?

Mr. Fujii: The ratio for internal use is currently about 10-20%, so it is really not the focus of our business. We are supplying chips for our PRIMEQUEST servers, and we have done many things to enable this chip to enhance server reliability. I think Fujitsu is the only company that has this kind of technology.

Questioner E: At present, your earnings are being held down by depreciation expenses associated with your investments in the Mie Plant, but what level of operating income margin are you targeting once depreciation comes down to a more normal level?

Mr. Fujii: Our target operating income margin level is 10%. Initially we thought we could attain a 10% operating income margin in fiscal 2009, but since we have postponed the start-up for the Fab No. 2, we will also have to push back our projections a bit. On the other hand, if the applications we are focusing on happen to take off, we may be able to target even higher margins.

***Questioner E:** You mentioned that set makers are shifting production to EMS/ODMs in Asia. What kind of business will you have with EMS/ODMs in Asia?*

Mr. Fujii: It is not as if this is the first time that we are entering Asian markets. For example, in the case of MPEGs for set-top boxes, two years ago we had an 80% of this segment in the China market. We are continuing to provide solutions to design houses and ODMs. But we have no intention of approaching every ODM for business. We will do business with ODMs that are strong in particular areas.

***Questioner F:** Your original plan had Mie Fab No. 1 becoming profitable in the first half of fiscal 2007, but under present circumstances when do you expect it will become profitable? Likewise, Mie Fab No. 2 was expected to be profitable in fiscal 2008, but given these latest revisions to your plan, when do you now expect it to turn a profit?*

Mr. Fujii: We are planning for Fab No. 1 to be profitable in the first half of fiscal 2007. Regarding Fab No. 2, because of the revision to planned production capacity, we now expect to generate profits around 2009 or after.

***Questioner F:** According to your plan of a year ago, you expected sales of standard tech products to decline; however, you see them rising under the current plan. Please explain the reason for the change.*

Mr. Fujii: The reason for the change is the expected contribution to sales resulting from the September 2006 purchase of a plant from Spansion with monthly production capacity of 30,000 wafers.

***Questioner F:** You planned for Mie Fab No. 2 to have monthly production capacity of 5,000 wafers in the first half of fiscal 2007 and 10,000 wafers in the second half. In light of your revised investment plans, what levels are you currently planning?*

Mr. Fujii: We are planning for 1,000 wafers for the first half and at least 2,000 for the second half.

***Questioner F:** Why has your standard tech strategy become clearer over the past year?*

Mr. Fujii: In the field of Flash microcontrollers, it has become clearer that our areas of specialty are in synch with market growth areas. Also, we have been better able to predict growth in the DC/DC converter market.