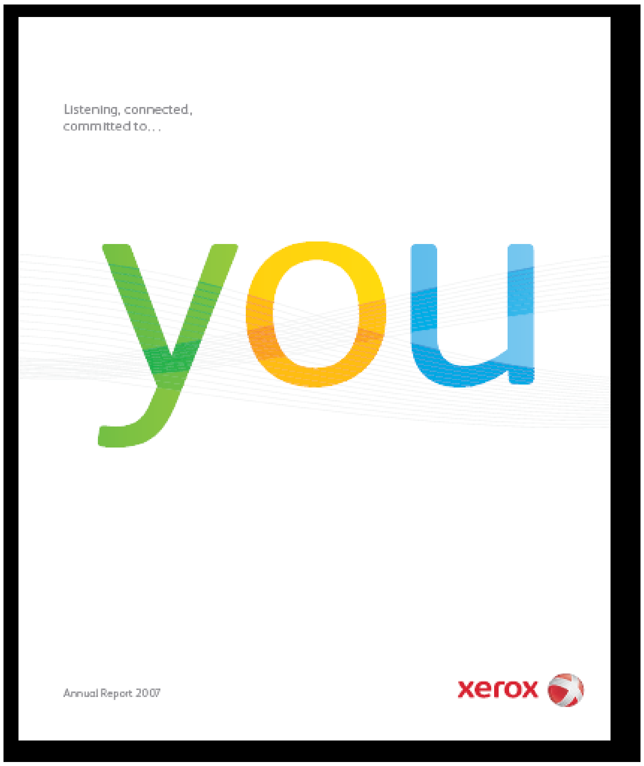
Report of the Month

Xerox

Norwalk, CT, **U.S.A.**



Report Facts

Company name: Xerox Corporation

Fiscal year end: December 31, 2007

Report title: *Listening, connected, committed to… you*

Chairman and CEO: Anne M. Mulcahy

Number of books: One

Report length: 136 pages

Auditors: PricewaterhouseCoopers LLP

Design: Pappas MacDonnell Inc.

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Report Rating: ★★★(★)

(Rating scale below)

Profile-Mission (Excerpts, as from the report)

We are a $17.2 billion technology and services enterprise and a leader in the global document market. We develop, manufacture, market, service and finance a complete range of document equipment, software, solutions and services. We operate in more than 160 countries… 28% of revenue from equipment sales; 72% from post sale, maintenance, supplies and financing.

(Annual Report p 30, p 46) (Italics are own company's words)

Key Figures

Total revenue: $ 17,228 million

Net income: $ 1,135 million

Earnings per share: $ 1.19 (diluted)

Dividend per share: $ 0.0425 (common stock)

Equity: $ 8,588 million

Gross margin: 40.3%

Operating margin: 9.3%

(Source: 2007 figures sourced from the annual report)

Major Competitors

- **Canon**
- **HP (Hewlett-Packard)**
- **Ricoh**
- **Océ**
- **Konica Minolta**
- **Lexmark**

Report Rating: ★★★(★)

Triple A

> *Fellow shareholders* receive a solid ten-page *Letter* from Chairman and CEO Anne M. Mulcahy, that reminds the past strategic bets, convincingly argues about progress made, substantiates the message with six well-picked five-year charts, and tells *what excites* her and how the company is *playing offense*.

> Extremely clear *Operations Review* written in plain English, laid out in a two-column grid, paced with tables, and made reader-friendly through an intensive use of bullet points (see e.g. *Costs, Expenses and Other Income* in our selected page below, including a matter-o-fact gross margin analysis).

Double A

> Though coming a bit late, the business profile, revenue streams and segments are clearly defined.

> Four case studies describe *What we heard* and *What we did* and sustain the Listening, committed cover theme, with a few pictorial breathers.

> Emphasis placed on research and development.

Simple A

> Though coming a bit late, the business profile, revenue streams and segments are

> *Five years in review* recap is finely structured and includes key ratios such as gross margin (broken down also for finance services), working capital and current ratio. But a number of major indicators are left out.

Some Bs

> Is there a good reason for not highlighting dividends? An answer comes only on… p 135!

> The page one *Financial overview* is lacking in details: 8 items only, over two years, no balance sheet one…

> Liquidity analysis and indicators lag far behind the operating performance review. ROE and debt-to-equity are not in print and are left to readers with a calculator.

> Governance matters are left out of the core annuals, like in mainstream U.S. annuals.

> Stripes and lines do not make up the snazziest visual thread. Even the cover is quite dull.

Cautionary Statement Triple and other A ratings have nothing to do with and were not approved by official ratings agencies!

Rating Scale
★★★★★: First-rate ★★★★(★): Excellent ★★★★: Very good ★★★(★): Sound ★★★: Average
★★(★): Uneven ★★: Common ★(★): Substandard ★: Poor (★): Uncompetitive
The rating is based on ReportWatch internal desk research and does not take into account the independent Rating Panel's judgment. It may therefore differ from ratings (to be) published in the ***Annual Report on Annual Reports***.

partially offset by higher interest expense and lower gains on the sales of businesses and assets.

2006 Operating profit of $31 million decreased $120 million from 2005, reflecting:

- The absence of the following items that occurred in 2005: $93 million gain related to the sale of Integic and the $57 million interest benefit from the finalization of the 1996-1998 Internal Revenue Service tax audit.
- $13 million pre-tax write-off resulting from the termination of a previous credit facility.
- Lower interest income of $12 million and increased non-financing interest expense of $8 million.

The above were partially offset by the following:

- Increased paper profit due to increased sales and reduced SAG expenses resulting from organizational streamlining.
- $44 million in gains on sale of assets.

Costs, Expenses and Other Income

Gross Margin

Gross margins by revenue classification were as follows:

(in millions)	Year Ended December 31, 2007	2006	2005
Total Gross margin	40.3 %	40.6 %	41.2 %
Sales	35.9 %	35.7 %	36.6 %
Service, outsourcing and rentals	42.7 %	43.0 %	43.3 %
Finance income ...	61.6 %	63.7 %	62.7 %

2007 Total Gross margin was down slightly as compared to 2006 as cost improvements were offset by price and product mix.

- Sales gross margin increased 0.2-percentage points primarily as cost improvements and other variances more than offset the 2.0-percentage point impact of price declines.
- Service, outsourcing and rentals margin decreased 0.3-percentage points as cost improvements and other variances did not fully offset price declines and unfavorable product mix of approximately 2.0-percentage points.
- Financing income margin declined 2.1-percentage points reflecting additional interest expense due to higher interest rates. Equipment financing interest is determined based on an estimated cost of funds, applied against an estimated level of debt required to fund our net finance receivables on a 7 to 1 debt to equity leverage ratio (refer to Note 11- Debt in the Consolidated Financial Statements for further information).

2006 Total Gross margin decreased by 0.6-percentage points from 2005 due to product mix. Price declines of 1.4-percentage points were offset by productivity improvements and other variances of 1.4-percentage points.

- Sales gross margin decreased 0.9-percentage points from 2005 as price declines of 2.1-percentage points exceeded the combined impacts of productivity improvements, product mix and other variances of 1.2-percentage points.
- Service, outsourcing and rentals margin decreased 0.3-percentage points from 2005 as product mix decline of 1.3-percentage points exceeded the impact of productivity improvements, price and other variances of 1.0-percentage points.
- Financing income margin increased 1.0-percentage points due to changes in interest costs specific to equipment financing.

Research, Development and Engineering Expenses ("R,D&E")

(in millions)	Year Ended December 31, 2007	2006	2005	Change 2007	2006
Total R,D&E expenses ..	$912	$922	$943	$ 10	$ (21)
R,D&E % Revenue ...	5.3 %	5.8 %	6.0 %	(0.5)pts	(0.2)pts

2007 R,D&E of $912 million decreased $10 million from 2006. We expect our 2008 R,D&E spending to approximate 5% to 5.5% of total revenue.

- R&D of $764 million increased $3 million from 2006. We invest in technological development, particularly in color, and believe our R&D spending is sufficient to remain technologically competitive. Our R&D is strategically coordinated with that of Fuji Xerox, which invested $672 million and $660 million in R&D in 2007 and 2006, respectively.