

## Our Business

We are a \$17.6 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.

### Overview

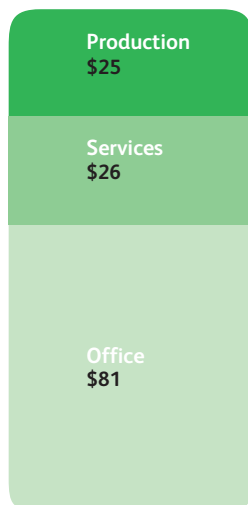
References in this section to “we,” “us,” “our,” the “Company” and “Xerox” refer to Xerox Corporation and its subsidiaries unless the context specifically states or implies otherwise.

We provide the document industry’s broadest portfolio of document systems and services for businesses of any size. Digital systems include high-end printing and publishing systems; digital presses, advanced and basic multifunctional devices (“MFD’s”) which can print, copy, scan and fax; digital copiers; laser and solid ink printers and fax machines. We provide software and workflow

solutions with which businesses can easily and affordably print books, create personalized documents for their customers, and scan and route digital information. Our services expertise is unmatched and includes helping businesses develop online document archives, analyzing how employees can most efficiently share documents and knowledge in the office, operating in-house print shops or mailrooms, and building Web-based processes for personalizing direct mail, invoices, brochures and more. We also offer software, support and supplies, such as toner, paper and ink.

## We serve a \$132 billion market

(in billions)



### ■ \$25 Production

We are the leading provider in the market that offers a complete family of monochrome and color production systems, business development tools and workflow solutions. We are creating new market opportunities in targeted application areas with digital printing as a complement to traditional offset printing.

### ■ \$26 Services

Our value-added services deliver solutions, which not only optimize enterprise output spend and infrastructure, but also streamline, simplify and digitize our customers’ document-intensive business processes.

### ■ \$81 Office

We are well positioned to capture growth by leading the transition to color and by reaching new customers with our broad offerings and expanded distribution channels.

This estimate, and the market estimates that follow, are calculated by leveraging third-party forecasts from firms such as International Data Corporation and InfoSource in conjunction with our assumptions about our markets.

The document industry is transitioning to digital systems, to color, and to an increased reliance on electronic documents. More and more, businesses are creating and storing documents digitally and using the Internet to exchange electronic documents. We believe

these trends play to the strengths of our product and service offerings and represent opportunities for future growth in the \$132 billion market we serve.

## Our Strategy



We are well-positioned to lead in this large and growing market through:

### Executing on Growth Initiatives

- **Accelerating the transition to color** – We have the broadest color portfolio in the industry and leading technologies.
  - Color is the fastest growing portion of our market and estimated at \$44 billion.
  - Economic cost and quality improvements are driving the transition from black-and-white to color.
  - We continue to capture growth opportunities within the black-and-white segment of our core markets, which we estimate is a \$62 billion market.
- **Building on services leadership** – We lead the industry with end-to-end Document Management Services and we participate in three areas of the outsourcing services market:
  - **Infrastructure Outsourcing**, where we help our customers to reduce their enterprise spend through differentiated technology, skills and automation.
  - **Application Outsourcing**, where we help our customers to streamline their document intensive business processes through automation and deployment of software applications and tools.
  - **Business Process Outsourcing**, where our customers leverage our global delivery capability and proprietary production imaging software to manage both high volume standardized activities as well as lower volume complex workflows.
- **Driving the New Business of Printing®** – We continue to create new market opportunities with digital printing as a complement to traditional offset printing through a market transition we call the “New Business of Printing”.

- We are driving the New Business of Printing opportunity by identifying applications which are suitable for digital production.
- Our leading business development tools, workflow and digital technology, led by our market-making Xerox iGen® technology, uniquely positions us to meet the increasing demand for short-run, customized and quick-turnaround offset quality printing.

### Expanding our Distribution Channels

- We continue to expand our presence in the small and mid-size business (“SMB”) market through the acquisition of Veenman B.V. in the European market, as well as additional acquisitions made by Global Imaging Systems, Inc. in the U.S. markets.
- We are maintaining our investments in Developing Markets, a high-growth market opportunity.
- We are capitalizing on our Graphic Arts coverage investments to capture the opportunity associated with the New Business of Printing.

### Securing Future Technology Leadership

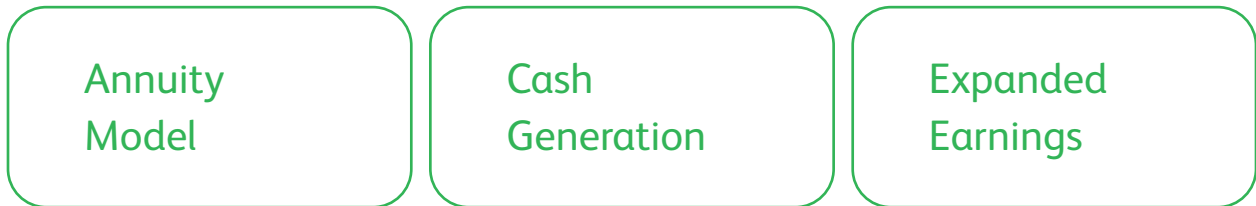
- Through advancing our heritage of innovation, we are yielding a broad technology portfolio.
- We are capitalizing on breakthrough ink technologies such as Solid Ink and Cured Gel Ink.
- Expanding our Document Management Technologies that optimize the capabilities of our products and streamline customers’ processes.

### Optimizing Productivity and Infrastructure

- We are improving the efficiency and effectiveness of our infrastructure and
- Optimizing our resources to support innovation and growth.

# Our Business

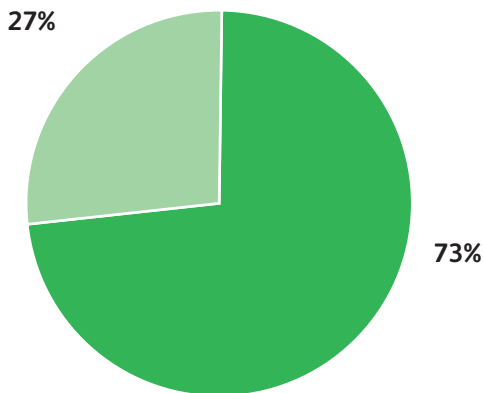
## Our Business Model Fundamentals



One fundamental of our business model is our annuity model. Post sale revenue growth is driven by increasing equipment installation which increases the number of page-producing machines in the field ("MIF") and by expanding the document management services we offer our customers. 73% of our 2008 total revenue

was post sale revenue that includes equipment maintenance and consumable supplies, among other elements. We sell the majority of our equipment through sales-type leases that we record as equipment sale revenue. Equipment sales represented 27% of our 2008 total revenue.

## Revenue stream



■ **73%**  
Approximately 73% of our revenue, "post sale" includes annuity-based revenue from maintenance, services, supplies and financing, as well as revenue from rentals and operating lease arrangements.

■ **27%**  
The remaining 27% of our revenue comes from equipment sales, from either lease arrangements that qualify as sales for accounting purposes or outright cash sales.

The number of equipment installations and the growth in document management services are key indicators of post sale revenue trends. The mix of color pages is also a significant indicator of post sale revenue trends because color pages use more consumables per page than black-and-white. In addition, expanding our market, particularly within the New Business of Printing, is key to increasing pages and we have developed tools and resources to be the leader in this large market opportunity.

Our consistent cash flow from operations is driven by recurring revenues; this, along with modest capital investments, enables us to provide a return to shareholders through:

- Expanding our distribution through acquisitions;
- Buying back shares under our share repurchase program and
- Maintaining our quarterly dividend.

We anticipate expanding our future earnings through:

- Modest revenue growth;
- Driving cost efficiencies to balance gross profit and expense;
- Leveraging our share repurchase and
- Making accretive acquisitions.

## Acquisitions

To further strengthen our distribution capacity, in 2008 we completed several acquisitions.

We acquired Veenman B.V. (“Veenman”), expanding our reach into the small and mid-size business market in the Netherlands. Veenman is the Netherlands’ leading independent distributor of office printers, copiers and multifunction devices serving small and mid-size businesses.

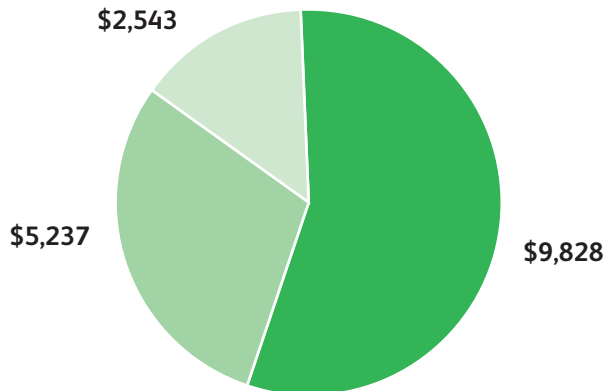
Global Imaging Systems, Inc. (“GIS”) acquired Saxon Business Systems, an office equipment supplier with offices throughout Florida and three smaller acquisitions: Better Quality Business Systems, Precision Copier Service Inc. DBA Sierra Office Solutions and Inland Business Systems of Chico.

## Segment Information

Our reportable segments are Production, Office and Other. We present operating segment financial information in Note 2 – Segment Reporting in the Consolidated Financial Statements, which we incorporate by reference here. We have a very broad and diverse base of customers by both geography and industry, ranging from SMB to graphic communications companies, governmental entities, educational institutions and large fortune 1000 corporate accounts. None of our business segments depends upon a single customer, or a few customers, the loss of which would have a material adverse effect on our business.

## Revenues by business segment

(in millions)



### ■ \$9,828 Office

Our Office segment serves global, national and small to mid-size commercial customers, as well as government, education and other public sector customers.

### ■ \$5,237 Production

Our Production segment provides high-end digital monochrome and color systems designed for customers in the graphic communications industry and for large enterprises.

### ■ \$2,543 Other

Our Other segment primarily includes revenue from paper sales, wide-format systems, value-added services and Global Imaging Systems network integration solutions and electronic presentation systems.

# Our Business

## Production

We provide high-end digital monochrome and color systems designed for customers in the graphic communications industry and for large enterprises. These high-end devices enable digital on-demand printing, digital full-color printing and enterprise printing. We are the only manufacturer in the market that offers a complete family of cut sheet monochrome production systems from 65 to 288 pages per minute (“ppm”), color production systems from 40 to 110 ppm and a complete line of continuous feed printers from 250 to 1,064 ppm. In addition, we offer a variety of pre-press and post-press options and the industry’s broadest set of workflow software.

With our Freeflow® digital workflow collection of software technology solutions, our customers can improve all aspects of their processes, from content creation and management to production and fulfillment. Our digital technology, combined with total document solutions and services that enable personalization and printing on demand, delivers value that improves our customers’ business results.

### 2008 Production Goals

Our 2008 goals for the Production segment were to continue to strengthen our leadership position in monochrome and color and to build on the power of digital printing. Our New Business of Printing strategy complements the traditional offset market and continues to transform our industry. We are enabling print providers in graphic communications and large enterprises to profit and grow by meeting their customers’ specific business needs with just-in-time, one-to-one and e-based services – rather than simply manufacturing a printed piece. Having the right business model<sup>SM</sup>, the right workflow<sup>SM</sup> and the right technology<sup>SM</sup> are fundamental to this transformation.

We continued our application-focused approach to assist our customers in implementing solutions in four major categories. This approach provided our customers end-to-end applications for Collaterals by Request, Books, Transactional/Promotional and Direct Mail.

During the 2008 drupa tradeshow that is held every four years, we announced 12 new offerings and 50 applications; building on our heritage of innovation and our in-depth understanding of both the printing industry and customer requirements.

We continued to increase installations of our flagship Digital Color Production Presses. We are the industry leader in the number of pages produced on digital production color presses, with our flagship Xerox iGen4® Digital Production Press, iGen3® Digital Production Press and DocuColor® Digital Presses. Over 325 customers have installed two or more iGen presses to meet their increased demand.

In 2008, we continued to build on our unmatched product breadth, world class market and business development tools and integrated end-to-end applications. Below are some of the key accomplishments that enabled us to achieve our goals:

### Our 2008 Production Accomplishments

#### Right Business Model

Our commitment to our customers starts before technology is discussed and extends long after a solution is installed. It includes sharing with them resources, strategies and tools that will help them grow their businesses with digital printing.

- **ProfitAccelerator®:** This robust set of tools and programs designed to maximize our customers’ investment in digital printing equipment expanded in 2008 and now includes more than 80 tools. It brings together Xerox’s unparalleled experience and expertise, world-class resources and industry-leading support. Some of the newest additions include a “Value-Based Pricing Guide,” the “Picture Me Profitable Kit” to assist customers in pursuing the personalized photo products opportunity, and the “ProfitQuick® Investment Planner” financial modeling tool that will help customers increase productivity and achieve cost and efficiency savings.
- **New Business of Printing Services:** Business Development Services was created in direct response to customer demand and provides both training and professional services to help print providers increase page volume and revenue. Service offerings are available to support Sales & Marketing, Workflow and Application Development efforts, and are delivered at the customers’ location or via the web. These offerings include creating marketing and sales management plans, sales force training, designing for digital, color management, implementing direct mail/marketing campaigns, Transpromo applications and more. The offerings are deployed by a dedicated team of Xerox business development consultants and industry experts.

#### Right Workflow

We lead the digital production workflow market by helping customers become more profitable – reducing costs, streamlining operations and enabling new applications. Our FreeFlow Digital Workflow Collection makes it easy for customers to complement traditional offset printing through the integration of digital printing into existing environments for efficient hybrid print manufacturing. In 2008 we enhanced our collection to include:

- **Xerox FreeFlow Process Manager®:** Software that provides automated, “touchless” file preparation and decision making to automate prepress and eliminate manual production steps.

- **Xerox FreeFlow Variable Information Suite:** Software that delivers the maximum productivity for personalized and customized documents including the award winning specialty effects that help print providers minimize document security concerns. These effects include MicroText marks, Correlation Marks, Glossmark®, FlorescentMark, and InfraRed text.
- **FreeFlow Print Server:** A powerful print server that delivers superior performance, advanced workflow interoperability, state-of-the-art color management, and a common workflow for Xerox production printers.
- **FreeFlow Express to Print:** A simple prepress automation tool designed specifically for the light and mid production environments. Easily add tabs, covers, inserts, barcodes, page numbers and more and see changes through the robust visual interface. Simple automation is provided with over 50 pre-built templates that make Express to Print easy to use and easy to install on a computer.

### Right Technology

For more than two decades, we have delivered innovative technologies that have revolutionized the production printing industry. In 2008 we continued to bring innovative products to the markets that included:

- **Xerox iGen4 Digital Production Press:** We unveiled in May at drupa the new iGen4, the industry's most productive and highest quality cut sheet digital press. The iGen4 features advanced color management that allows print providers to consistently achieve and maintain offset and photo image quality. With new patented technologies, the iGen4 automates many operator tasks for greater uptime. With productivity gains of 25-35 percent, the iGen4 increases the run-length to be break-even with offset for greater press utilization and capacity. For commercial printers, photo finishers, book printers, direct mail houses and digital service providers, the iGen4 delivers a more efficient and cost-effective way to produce more pages and achieve greater profits.
- **Xerox 700 Digital Color Press:** We expanded our full color offerings with the launch of the Xerox 700 Digital Color Press at drupa in May. The Xerox 700 at 70 ppm offers enhanced color reproduction capabilities as well as an exceptional matte finish that is winning over customers worldwide. A wide range of feeding and finishing options at an entry level price enables print providers to adopt digital technology or expand their digital printing business.
- **Xerox DocuColor 5000AP:** In July we launched a 50 ppm full-color production system which provides excellent print resolution, color reproduction and reliability for a wide range of application and weights, all at rated speed.
- **Automated Color Quality Suite:** In May, we introduced the Automated Color Quality Suite ("ACQS") Press Matching System for our flagship Xerox iGen3 90 and 110 Digital Production Presses, offering high performance plus quality that match offset printing. The new ACQS enables faster press set up, quicker time to production, greater color stability and automated Pantone color matching. In November, we launched this offering on the Xerox 8000AP and 7000AP, bringing these new quality capabilities to these Digital Color Presses.
- **Xerox 490/980 Color Continuous Feed Printing System:** We launched the world's fastest toner based full color roll fed printer that produces up to 986 full color duplex images per minute in May for Europe and part of developing markets and in November for North America and the rest of developing markets. With its Flash Fusing Technology, this system is ideal for the Transactional/Promotional and Direct Mail market segments that require high speed, high volume variable data printing.
- **Xerox 650/1300 Continuous Feed Printing System:** In February, this new monochrome continuous feed printer was made available worldwide. This monochrome roll feed printer also leverages flash fusing technology to print a wide variety of substrates up to 1300 images per minute. This system supports numerous applications within the transactional/promotional and direct mail segments and is ideal for books and manuals.
- **Xerox Nuvera® 288 Digital Perfecting System:** In October, the fastest cut sheet monochrome duplex printer in the market expanded its sheet feed capability up to 12.6" x 19.3" and added a new Roll Feed DocuConverter with Grain Rotation supporting a host of new applications. This system, with its benchmark image quality, flexibility of substrates and reliability, enables applications such as book publishing.
- **Xerox Nuvera 100/120/144 EA Digital Production Systems:** With its Emulsion Aggregate ("EA") toner for greater reliability and image quality, the Nuvera EA family expanded its portfolio of finishing alternatives. In October we announced the availability of Xerox Tape Bind, CEM DocuConverter and C.P. Bourg/Watkiss Power Square 200® Booklet Maker. This modular, scalable print engine also expands digital printing applications due to its high quality and flexibility of substrates.

# Our Business

## Office

Xerox develops and manufactures a range of color and black-and-white multifunction, printer, copier and fax products. Our Office segment serves global, national and small to mid-size commercial customers as well as government, education and other public sector customers. Office systems and services, which include monochrome devices at speeds up to 95 ppm and color devices up to 70 ppm, include our family of CopyCentre®, WorkCentre® and WorkCentre Pro digital multifunction systems, Phaser® desktop printers and MFD's as well as DocuColor printer/copiers for the specific needs of graphic intensive organizations and facsimile products.

We offer a complete range of services and solutions in partnership with independent software vendors that allow our customers to analyze, streamline, automate, secure and track their digital workflows, which we then use to identify the most efficient, productive mix of office equipment and software for that business, helping to reduce the customer's document-related costs.

### 2008 Office Goals

Our 2008 Office goals were to drive to a leadership position in color to extend our market reach, particularly in the SMB market and continue to expand our Office Services and Solutions business. We broadened our product line and complemented our industry-leading product offerings with expanded distribution in order to increase our machines-in-field ("MIF") and capture more pages, building the foundation for future post sale revenue growth.

We continued to drive color in our Office segment by significantly enhancing our already strong color product portfolio, making color more affordable, easier to use, faster and more reliable while maintaining our leadership position in black-and-white. The breadth of our product portfolio is unmatched. Our color-capable laser devices provide an attractive color entry point, our patented solid ink technology offers unmatched ease of use, vibrant color image quality and economic color run costs, and our top of the line color laser products provide superior image quality coupled with industry-leading productivity and reliability. Below are some of the key accomplishments that enabled us to achieve our goals:

### 2008 Office Accomplishments

- **Phaser 6125:** In February, we announced the Phaser 6125, a 12 ppm color, 16 ppm black-and-white printer. This product is an extension of the Phaser 6130 line, and offers a small footprint, strong processing capability and Emulsion Aggregate High Quality ("EA-HQ") toner technology for clear, crisp printing.
- **Phaser 3635 MFP:** Launched in May, the Phaser 3635MFP is a 35 ppm printer that provides advanced security options such as image overwriting, encryption and authentication. This product is designed for small and mid-size business workgroups, and offers features like a color touchscreen user interface and robust scanning features to promote ease-of-use and productivity.
- **Phaser 5550:** Launched in May, this 50 ppm printer offers tabloid and letter/legal printing, as well as advanced software features like PhaserSMART®. PhaserSMART is an online troubleshooting tool that helps diagnose and solve potential issues, prevent maintenance calls and increase reliability. This product also offers duplex printing and optional additional paper handling features.
- **WorkCentre 5016/5020:** In May, Xerox introduced its first sub-\$1,000 A3/tabloid MFD family in developing markets. The 16/20 ppm family offers basic copying, printing and scanning capabilities for small workgroups that are price sensitive.
- **WorkCentre 5222/5225/5230:** In May, we introduced a new 25/30 ppm monochrome platform designed to help SMB and enterprise workgroups increase productivity on an entry-level device with high-end features such as our Extensible Interface Platform, full-system common criteria certification, and booklet making capabilities. In September, the 5200 series was expanded with the addition of a 22 ppm configuration as well as color scanning capability on the Workcentre 5225A/5230A configurations.
- **WorkCentre 5600 Series:** We refreshed the 5600 series monochrome platform with updated controller software to keep pace with today's ever changing IT standards and protocols. With support for IPv6 and compatibility with Microsoft's Web Services on Devices, the WorkCentre 5600 series – with speeds ranging from 32 ppm to 87 ppm – becomes even more powerful for IT professionals.
- **WorkCentre Bookmark 40/55 Multifunction Copier/Printer:** A robust book copier at its core, it is the ideal solution for libraries, universities, and other public vending environments. It features an angled side panel support that protects books' spines while copying, and offers solid durability, ease-of-use and powerful solutions for streamlining unique workflows.
- **WorkCentre 7346 Multifunction Printer & EFI Workflows:** In May we introduced a high-end version of the WorkCentre 7300 series system featuring fast print speeds of up to 40 ppm in color and 45 ppm in black-and-white for busy workgroups. The WorkCentre 7300 series was also enhanced with optional EFI workflow capabilities.

- **Xerox 700 Digital Color Press:** Launched in May, this light production color device with an embedded controller brings productivity, excellent print quality and flexibility to those looking to adopt digital technology or expand their digital capabilities.
- **WorkCentre 4260:** Launched in September, the WC 4260 is Xerox's fastest desktop multifunction system with speeds up to 55 ppm. It offers workflow tools such as ID Copy Card, Fax Forward to Email, automatic two sided printing and competitive security features. This product is designed to promote productivity in small and medium business workgroups.
- **Phaser 3300 MFP:** Launched in September, the Phaser 3300 MFP offers print/copy speeds up to 30 ppm and offers automatic two-sided printing. This product offers color scanning to USB, email or the network. It is equipped with Xerox Scan to PC Desktop® which allows users to send a document from the MFP to their desktop for viewing, editing or storing.

## Other

The Other segment primarily includes revenue from paper sales, value-added services, wide-format systems and GIS network integration solutions and electronic presentation systems.

We sell cut-sheet paper to our customers for use in their document processing products. The market for cut-sheet paper is highly competitive and revenues are significantly affected by pricing. Our strategy is to charge a premium over mill wholesale prices, which is adequate to cover our costs and the value we add as a distributor, as well as to provide unique products that enhance the New Business of Printing and color output.

An increasingly important part of our offering is value-added services, which utilizes our document industry knowledge and experience. Our value-added services deliver solutions that optimize our customers' document output and infrastructure costs while streamlining, simplifying, and digitizing their document-intensive business processes. Through Xerox's imaging centers, a company can scan and digitize documents to create secure, accessible and searchable online information archives, such as a library of car-rental contracts or construction blueprints. Often our value-added services solutions lead to larger managed services contracts which include our equipment, supplies, service, and labor. We report revenue from managed services contracts in the Production or Office segments. In 2008, the combined value-added services and managed services revenue, including equipment, totaled \$3.8 billion.

In our wide-format systems business, we offer document processing products and devices designed to reproduce large engineering and architectural drawings up to three feet by four feet in size. In 2008 we launched:

- **Xerox 8254E and 8264E Wide Format Printers:** Introduced in June, further enables customers to print robust, colorful large format graphic applications on a broad range of substrates quickly and easily.
- **Xerox 6279 Wide Format Printer:** This printer continues our successful tradition in the CAD environment with its unsurpassed ease of operation and benchmark image quality.

# Our Business

## Revenue

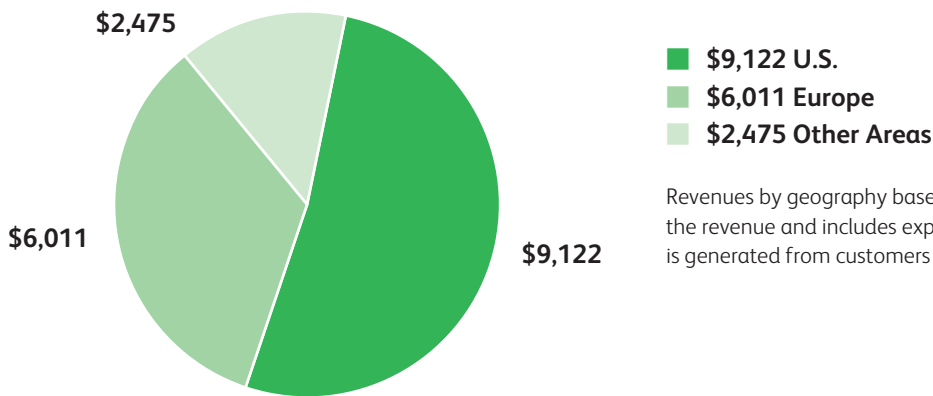
We sell the majority of our products and services under bundled lease arrangements, in which our customers pay a monthly amount for the equipment, maintenance, services, supplies and financing over the course of the lease agreement. These arrangements are beneficial to our customers and to us since, in addition to customers receiving a bundled offering, these arrangements allow us to maintain the customer relationship for future sales of equipment and services.

We analyze these arrangements to determine whether the equipment component meets certain accounting requirements such that the equipment fair value should be recorded as a sale at lease

inception, that is, a sales-type lease. We allocate the remaining portion of the monthly minimum payments to the various elements of the lease based on fair value – service, maintenance, supplies and financing – that we generally recognize over the term of the lease agreement, and that we report as “post sale revenue”. In those arrangements that do not qualify as sales-type leases, which have increased as a result of our services-led strategy, we recognize revenue over the term of the lease agreement, whether rental or operating lease, and report it in “post sale revenue.” Our accounting policies for revenue recognition for leases and bundled arrangements are included in Note 1 – Summary of Significant Accounting Policies in the Consolidated Financial Statements in our 2008 Annual Report.

## Revenues by geography

(in millions)



Revenues by geography based on the location of the unit reporting the revenue and includes exports sales. About 50% of our revenue is generated from customers outside the U.S.

## Research and Development

Our R&D is strategically coordinated with Fuji Xerox, which invested \$788 million in R&D in 2008, \$672 million in 2007 and \$660 million in 2006.

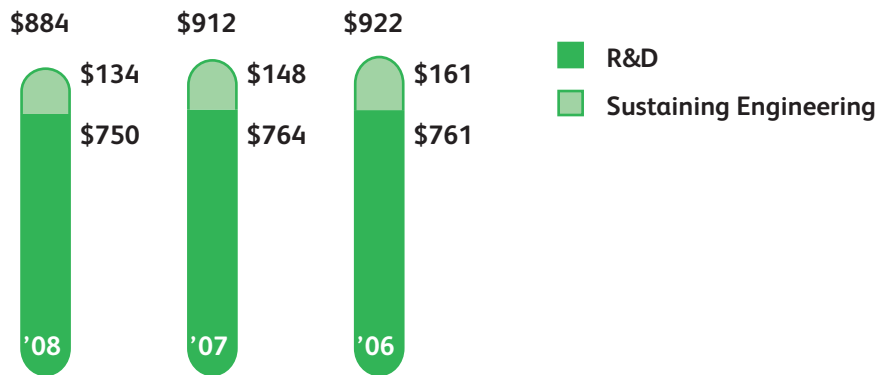
Investment in R&D is critical for competitiveness in our fast-paced markets where more than two-thirds of our equipment sales are from products launched during the past two years. Research activities are conducted in the United States, Canada and Europe – often in collaboration with Fuji Xerox Co., Ltd. (“Fuji Xerox”).

Our R&D drives innovation and customer value by:

- Creating new differentiated products and services;
- Enabling cost competitiveness through disruptive products and services;
- Enabling new ways to serve customers and
- Creating new business opportunities that drive future growth and reach new customers.

## R,D&E expenses

(in millions)



To ensure our success, we have aligned our R&D investment portfolio with our growth initiatives of accelerating the transition to color, enhancing customer value by building on our services leadership and by driving the New Business of Printing. 2008 R&D spending focused primarily on the development of high-end business applications to drive the New Business of Printing, extending our color capabilities, expanding our services offerings and delivering lower-cost platforms and customer productivity enablers. The Xerox iGen family, advanced next-generation digital printing presses that produce photographic-quality prints

indistinguishable from offset, the Xerox Nuvera 288 Digital Perfecting System which boasts the fastest (288 duplex impressions per minute) digital duplex monochrome cut-sheet printer in the industry, and Xerox’s proprietary Solid Ink technology for the office are examples of the type of breakthrough technology we have developed and that we expect will drive future growth. Sustaining engineering expenses, which are the hardware engineering and software development costs we incur after we launch a product, are included in our R,D&E expenses.

## Our Business

### Patents, Trademarks and Licenses

We are a technology company. Including our Xerox Palo Alto Research Center ("PARC") and XMPie subsidiaries, we were awarded 609 U.S. utility patents in 2008. We were ranked 31st on the list of companies that were awarded the most U.S. patents during the year and would have been ranked about 27th with the inclusion of PARC and XMPie patents. Including our research partner Fuji Xerox Co., Ltd ("Fuji Xerox"), we were awarded over 940 U.S. utility patents in 2008. Our patent portfolio evolves as new patents are awarded to us and as older patents expire. As of December 31, 2008, we held approximately 8,900 design and utility U.S. patents. These patents expire at various dates up to 20 years or more from their original filing dates. While we believe that our portfolio of patents and applications has value, in general no single patent is essential to our business or any individual segment. In addition, any of our proprietary rights could be challenged, invalidated, or circumvented or may not provide significant competitive advantages.

In the U.S., we are party to numerous patent-licensing agreements and, in a majority of them, we license or assign our patents to others, in return for revenue and/or access to their patents. Most patent licenses expire concurrently with the expiration of the last patent identified in the license. In 2008, we added 11 agreements to our portfolio of patent licensing agreements, and either we or PARC was a licensor in all 11 of the agreements. We are also a party to a number of cross-licensing agreements with companies that hold substantial patent portfolios, including Canon, Microsoft, IBM, Hewlett Packard, Océ, Sharp, Samsung and Seiko Epson. These agreements vary in subject matter, scope, compensation, significance and time.

In the U.S., we own approximately 570 trademarks, either registered or applied for. These trademarks have a perpetual life, subject to renewal every ten years. We vigorously enforce and protect our trademarks.

**Our brand is a valuable resource** and continues to be ranked among the top percentile of the most valuable global brands.

### Competition

Although we encounter aggressive competition in all areas of our business, we are the leader or among the leaders in each of our principal business segments. Our competitors range from large international companies to relatively small firms. We compete on the basis of technology, performance, price, quality, reliability, brand, distribution and customer service and support. To remain competitive we invest in and develop new products and services and continually improve our existing offerings. Our key competitors include Canon, Ricoh, Hewlett-Packard, and, in certain areas of the business, Pitney Bowes, Kodak, Océ, Konica-Minolta and Lexmark.

We believe that our brand recognition, reputation for document knowledge and expertise, innovative technology, breadth of product offerings, global distribution channels, customer relationships and large customer base are important competitive advantages. We and our competitors continue to develop and market new and innovative products at competitive prices, and, at any given time, we may set new market standards for quality, speed and function.

### Marketing and Distribution

We manage our business based on the principal business segments described earlier. However, we have organized the marketing, selling and distribution of our products and solutions according to geography and channel type. We sell our products and solutions directly to customers through our worldwide sales force and through

a network of independent agents, dealers, value-added resellers, systems integrators and the Web. In the U.S. GIS continues to expand its network of office technology suppliers to serve an ever-expanding base of small and mid-size businesses. We utilize our direct sales force to address our customers' more advanced technology, solutions and services requirements, and use cost-effective indirect distribution channels for basic product offerings.

In large enterprises, we follow a services-led approach that enables us to address two basic challenges facing large enterprises:

- How to optimize infrastructure to be both cost effective and globally consistent.
- How to improve the value proposition and communication with their customers.

In response to these needs, we offer a go-to-market approach that leads with the largest direct sales and service delivery force in the industry available on a globally consistent manner. This can range from hardware, software or services in whatever combination is necessary to meet the needs of that customer.

We market our Phaser line of color and monochrome laser-class and solid ink printers primarily through office information technology resellers, who typically access our products through distributors. We continue to expand our distribution partnerships in North America through additional information technology resellers and by enhancing our network of independent agents. We also continued to increase product offerings available through a two-tiered distribution model in Europe and developing markets.

We operate in over 160 countries worldwide. We develop, manufacture, market and support document management systems, supplies and services through a variety of distribution channels around the world.



■ **North American Operations**

North American Operations includes the United States and Canada.

■ **Xerox Europe**

Xerox Europe covers 17 countries across Europe.

■ **Developing Markets**

Developing Markets supports more than 130 countries.

■ **Fuji Xerox**

Fuji Xerox, an unconsolidated entity of which we own 25%, develops, manufactures and distributes document management systems, supplies and services.

Our reselling relationship with key partners contributed to our market coverage expansion and new business penetration. Through our global reseller alliance with Fujifilm, we distribute our production products and solutions to graphic communications customers as well as photo specialty markets spanning Retail, Professional Lab and Processing Center businesses. In 2008, we signed additional country-level contracts with Fujifilm Graphics Systems in Europe and developing markets to extend Xerox digital production systems reach to new commercial print customers and prospects. We continue to use our alliances to integrate “best in class” information technologies and services to deliver improved workflow and document output management enabling our customers to accelerate profitable revenue growth in their businesses. Through the world-class Xerox Business Partner Program we are able to deliver an extensive portfolio of products

which streamline our customers’ workflows enabling them to reduce costs, improve operational efficiencies and drive new business opportunities.

In Europe, Africa, the Middle East, India, and parts of Asia, we distribute our products through Xerox Limited, a company established under the laws of England, and related non-U.S. companies which we refer to collectively as Xerox Limited. Xerox Limited enters into distribution agreements with unaffiliated third parties to provide distribution of our products in many of the countries located in these regions, and previously entered into agreements with unaffiliated third parties providing distribution of our products in Iran, Sudan, and Syria. Iran, Sudan and Syria, among others, have been designated as state sponsors of terrorism by the U.S. Department of State and are subject to U.S. economic

## Our Business

sanctions. We maintain an export and sanctions compliance program and believe that we have been and are in compliance with U.S. laws and government regulations for these countries. In addition, we have no assets, liabilities, or operations in these countries other than liabilities under the distribution agreements. After observing required prior notice periods, Xerox Limited terminated its distribution agreements with distributors servicing Sudan and Syria in August 2006 and terminated its distribution agreement with the distributor servicing Iran in December 2006. Now, Xerox only has legacy obligations to third parties such as providing spare parts and supplies to these third parties. In 2008, we had total revenues of \$17.6 billion, of which approximately \$7.4 million was attributable to Iran and less than \$0.2 million in total was attributable to Sudan and Syria.

In January 2006, Xerox Limited entered into a five-year distribution agreement with an unaffiliated third party covering distribution of our products in Libya. Libya is also designated as a state sponsor of terrorism by the U.S. Department of State. The decision to enter into this distribution agreement was made in light of recent U.S. federal government actions that have lifted the countrywide embargo previously imposed on Libya. Our sales in Libya through this distribution agreement will be subject to our export and sanctions compliance program and will be conducted according to the U.S. laws and government regulations that relate to Libya.

### Customer Financing

We finance a large portion of customer purchases of Xerox equipment through our bundled lease arrangements. We believe that financing facilitates customer acquisition of Xerox technology and enhances our value proposition to the customer while providing Xerox a profitable revenue stream and a strong return on equity.

As a result of our customer financing program, we benefit by gaining in-depth knowledge of the products being leased and a deep understanding of the customer base and their use of our technology. This knowledge allows us to effectively manage the credit and residual value risk normally associated with financing. Our financing risk is further mitigated because the majority of our lease contracts are non-cancelable and include cancellation penalties approximately equal to the full value of the lease receivables.

Because our lease contracts permit customers to pay for equipment over time rather than at the date of installation, we maintain a certain level of debt to support our investment in these lease contracts. We fund our customer financing activity through a combination of cash generated from operations, cash on hand, borrowings under bank credit facilities and proceeds from capital market offerings. At December 31, 2008 we had \$7.3 billion of



**Globally, we have 57,100 direct employees.** We have over 7,500 Sales Professionals, over 13,000 Managed Service Employees at customer sites and over 13,000 Technical Service Employees. In addition, we have over 6,500 Agents and Concessionaires and over 10,000 resellers.

finance receivables and \$0.6 billion of equipment on operating leases, or Total Finance assets of \$7.9 billion. We maintain an assumed 7:1 leverage ratio of debt to equity as compared to our Finance assets and therefore a significant portion of our \$8.4 billion of debt is associated with our financing business.

In addition to being an excellent customer retention vehicle, our customer financing program also achieves an attractive gross margin which provides us a reasonable return on our investment in this business. This program is also a strong value proposition for our customers because it provides them a bundled monthly payment for their document management needs and an attractive financing alternative.

## Service

As of December 31, 2008, we had a worldwide service force of approximately 13,000 employees and an extensive variable contract service force. We continue to expand our use of cost-effective remote service technology for basic product offerings while utilizing our direct service force and a variable contract service force to address customers' more advanced technology requirements. The increasing use of a variable contract service force is consistent with our strategy to reduce service costs while maintaining high-quality levels of service. We believe that our service force represents a significant competitive advantage because it is continually trained on our products and its diagnostic equipment is state-of-the-art. We offer service 24 hours a day, 7 days a week, in major metropolitan areas around the world, providing a consistent and superior level of service worldwide.

## Manufacturing and Supply

Our manufacturing and distribution facilities are located around the world. The company's largest manufacturing site is in Webster, N.Y., where we make fusers, photoreceptors, Xerox iGen and Nuvera systems, components, consumables and other products. Additionally this year, updates were made at the EA Toner plant in Webster, N.Y. that was built in 2007 to give the plant the flexibility to meet demand for both first and second generations of EA Toner. This allows the plant to produce the new breakthrough Ultra Low-Melt EA Toner. Our remaining primary manufacturing operations are located in: Dundalk, Ireland for our high-end production products and consumables; and Wilsonville, Oregon for solid ink products, consumable supplies, and components for our Office segment products. We also have a major facility in Venray, Netherlands, that handles supplies manufacturing and supply chain management for the eastern hemisphere.

We are currently in the second year of a master supply agreement with Flextronics, a global electronics manufacturing services company, to outsource portions of manufacturing for our Office segment. The agreement has a three year term, with two additional one-year extension periods at our option. Our inventory purchases from Flextronics currently represent approximately 15% of our overall worldwide inventory procurement and production. Our pricing for inventory sourced through Flextronics is generally market based. We have agreed to purchase from Flextronics some products and consumables within specified product families although we do have the ability to source product from other suppliers without penalty to extent needed. Flextronics is required to acquire inventory based on our forecasted requirements and must maintain sufficient manufacturing capacity to satisfy these requirements. Under certain circumstances, we may become obligated to purchase inventory that remains unused for more than 180 days, becomes obsolete or remains unused on the termination of the supply agreement. If Flextronics were unable to continue to supply product, it would not result in a material disruption to our business because Flextronics primarily provides contract assembly labor and we continue to manage the inbound sourcing and supply chain management of raw materials and sub-assembly parts. In addition, we own the tooling and technology that Flextronics currently uses to produce our products; there are a number of alternative suppliers that could replace the contract assembly labor Flextronics provides and we have business resumption plans in place for Flextronics and other similar suppliers.

We acquire other office products from various third parties in order to increase the breadth of our product portfolio and meet channel requirements. We have arrangements with Fuji Xerox under which we purchase and sell products, some of which are the result of mutual research and development arrangements. Refer to Note 7 – Investments in Affiliates, at Equity in the Consolidated Financial Statements in our 2008 Annual Report for additional information regarding our relationship with Fuji Xerox.

## Fuji Xerox

Fuji Xerox is an unconsolidated entity in which we currently own a 25% interest and FUJIFILM Holdings Corporation ("FujiFilm") owns a 75% interest. Fuji Xerox develops, manufactures and distributes document processing products in Japan, China, Hong Kong, other areas of the Pacific Rim, Australia and New Zealand. We retain significant rights as a minority shareholder. Our technology licensing agreements with Fuji Xerox ensure that the two companies retain uninterrupted access to each other's portfolio of patents, technology and products.

# Our Business

## International Operations

We are incorporating by reference the financial measures by geographical area for 2008, 2007 and 2006 that are included in Note 2 – Segment Reporting in the Consolidated Financial Statements in our 2008 Annual Report. See also the risk factors entitled “Our business, results of operations and financial condition may be negatively impacted by economic conditions abroad, including fluctuating foreign currencies and shifting regulatory schemes.” in Part 1, Item 1A of this Form 10K.

## Backlog

We believe that backlog, or the value of unfilled orders, is not a meaningful indicator of future business prospects because of the significant proportion of our revenue that follows equipment installation, the large volume of products we deliver from shelf inventories and the shortening of product life cycles.

## Seasonality

Our revenues are affected by such factors as the introduction of new products, the length of the sales cycles and the seasonality of technology purchases. As a result, our operating results are difficult to predict. These factors have historically resulted in lower revenue in the first quarter than in the immediately preceding fourth quarter.

## Other Information

Xerox is a New York corporation, organized in 1906, and our principal executive offices are located at 45 Glover Avenue, P.O. Box 4505, Norwalk, Connecticut 06856-4505.

Our telephone number is (203) 968-3000.

On the Investor Information section of our Internet website, you will find our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to these reports. We make these documents available as soon as we can after we have filed them with, or furnished them to, the Securities and Exchange Commission.

Our Internet address is <http://www.xerox.com>