

# Letter to the Shareholders



> **Dr. Wolfgang Ziebart**  
President and CEO of Infineon Technologies AG

Dear ladies and gentlemen,

Last year we made substantial progress in realigning our company and setting the course to profitable growth, to which a number of facts bear witness. We completed the transition of our Memory Products segment into a legally independent entity as of May 1, 2006; it was listed on the New York Stock Exchange on August 9, 2006. We distinctly improved the consolidated earnings before interest and taxes to negative €15 million from negative €183 million (without charges: positive €181 million from negative €79 million). In the reporting period, our share performed significantly better than the trend registered in the industry, achieving a distinct price increase of 14 percent. The price trend was clearly above that of the SOX Semiconductor Index (negative 4 percent) and Dow Jones US Semiconductor Index (negative 4 percent). In the coming year we will continue to rigorously pursue the path to profitable growth, primarily focusing on processors for mobile phones within the wireless business. We are confident that we will successfully accomplish this task in the current financial year. I would like to go into further detail below on what we have achieved over the last year and what we intend to do in the future to reach our goal of profitable growth.

A significant step in realigning our Group was the carve-out of the Memory Products business to form the independent company Qimonda. This profound step for the company was completed on May 1, 2006, having been performed smoothly two months ahead of schedule. It was immediately followed by preparation and execution of the IPO (Initial Public Offering). Qimonda shares were listed on the New York Stock Exchange for the first time on August 9, 2006. We expect the carve-out and listing of Qimonda to yield a number of strategic advantages. Qimonda and our remaining businesses will benefit from both

companies now being able to make decisions faster and with a view solely to the necessities posed by their own operations. In addition, investors are now offered more differentiation in investing in Qimonda on the one hand and in the remaining Infineon segments on the other. A further aspect for Qimonda is that separate capital market access is not only a competitive factor, but also opens up wider strategic options. We see the share price increase of 45 percent between initial listing and the end of November 2006 as an extremely positive sign. Qimonda's results also make us confident. Qimonda earnings before interest and taxes improved in the course of the 2006 financial year from negative €123 million in the 2005 December quarter to positive €215 million in the 2006 September quarter. In the 2006 September quarter, Qimonda upheld its position as second-largest DRAM supplier in the global market having first reached that position in the 2006 March quarter. By introducing the 75-nanometer technology in the third calendar quarter of 2006, Qimonda has closed the ranks to the technology leader and manifested the company's technological capabilities. In the long term, we continue to aim at holding a minority interest in Qimonda. One use for the proceeds resulting from the reduction of our interest in Qimonda will be a selective strengthening of the remaining Infineon businesses. Furthermore, we will also consider buying back shares and intend to obtain the authorization to do so at our Shareholders' General Meeting.

We made good progress also in our core business excluding Qimonda in the last financial year. Over half of our activities in this segment presently generate considerable growth, with clearly positive earnings before interest and taxes. Besides solid profits before interest and taxes we have continuously gained market share in all these businesses. Today, we are the global market leader for power semiconductors, radio-frequency ICs for mobile phones and wireline access chips. In the area of semiconductors for automotive applications we are the market leader in Europe and number two worldwide. Substantial parts of Infineon's businesses today have already achieved our goal of profitable growth.

A small number of areas still need our special attention, however. In the course of our strategic realignment we decided to continue some of these activities. We believe that we can generate more value through a turnaround of those activities than by closure or sale. Here again, we have a number of positive developments to report. Compared to the previous year's figures, we have distinctly reduced our losses in the chip card ICs sector and achieved a positive result before interest and taxes in the last quarter of the past financial year – one quarter earlier than planned. We are committed to stabilizing this trend in the current year and establishing the basis for improved profitability by introducing a bundle of newly developed products. In the wireline communications sector we returned to the profit zone already at the end of the 2005 financial year and posted a profit before interest and taxes, accompanied by an increase in market share. We again expect to see a positive contribution for the current financial year. The figures for discrete semiconductors, tuners or radio-frequency power semiconductors have also moved out of negative into positive earnings territory before interest and taxes.

In the last financial year we were also highly successful in gaining new customers for processors used in mobile phones. In mid-2006 we secured LG Electronics of Korea as a new customer for our EDGE system solutions. With Panasonic of Japan, we won a leading customer for our 3G solutions. We also received orders and commitments from further significant customers for joint developments in our ultra-low-cost, EDGE and 3G products. The insolvency and loss of our former main customer, BenQ Mobile's German subsidiary, has therefore struck us especially hard. Despite the remarkable success with new customers, we have still not yet achieved the diversification in our customer base necessary to compensate for this loss without putting any countermeasures in place. We have therefore streamlined our internal structures further and reduced the fixed costs. In this way we cut development expenditures without jeopardizing the sales potential created in the last year. This potential flows from a number of contracts already awarded and from further projects with renowned customers. These projects are at an advanced stage and we are confident that they will lead to firm orders. Together with the orders already in hand, the earnings position of the wireless communications business should see constant improvement during the 2007 financial year. We anticipate break-even earnings before interest and taxes in the wireless communications business by the end of the 2007 calendar year.

Beyond individual measures taken in specific areas, we have launched a company-wide program to simplify workflows and thereby reduce costs: ICoRe, the Infineon Complexity Reduction Program. Within this program we systematically analyze the distribution of tasks and the process structures throughout the company. We will simplify processes and resolve overlap. The planning is expected to be concluded in the 2006 calendar year and ensuing action will be taken within this financial year, resulting in annualized savings of at least €50 million starting in the second half of the 2007 financial year.

We expect further positive effects within the framework of our strategic realignment from our new strategy for manufacturing and development. As far as manufacturing is concerned, we will no longer invest in our own production capacities for 65-nanometer components and below. This means a significant drop in investment volume as compared with in-house manufacturing. In addition, we are pursuing a co-operation scheme in the area of process development for these components. It delivers us leading-edge solutions at significantly lower cost than if developed in-house. In the last financial year, for instance, we announced the availability of development facilities for the 45-nanometer process together with our development partners Chartered Semiconductor, IBM and Samsung. In contrast, we will maintain our own process development and production facilities for power semiconductors, because in this case the production technology used and production quality attained is an important factor setting our products apart from competition and supporting their competitiveness. Our new facility for power semiconductors in Kulim, Malaysia, which started production far earlier than planned in September 2006, illustrates our manufacturing and development strategy for power semiconductors. We expect this facility to make a

positive contribution to earnings from the end of the 2007 financial year. Overall, this approach reduces capital expenditure while maintaining the competitiveness of our production environment. It thus creates the potential for improved cash flows in the company.

In the last financial year we gained good ground with our realignment. We are satisfied with the progress made, but not with the level reached. I can assure you, our shareholders, that together with my colleagues in the Management Board I will do my utmost to ensure that 2007 will be a year of further improvements in the Infineon Group.

Finally, I would like to express my thanks and appreciation to our employees, personally and on behalf of the entire Management Board, for the excellent work they have done in the last financial year. In a time in which the company has faced serious changes and exceptionally complex issues, we have been able to build on our employees' competence, commitment and dedication, and by doing so, to achieve remarkable success. This experience reinforces my optimism for the future.

Neubiberg, December 2006

Yours sincerely



Dr. Wolfgang Ziebart  
President and CEO