



Professor Dr Gerd Litfin
Founder of LINOS AG
and Chief Executive Officer (front)
Volker Brockmeyer
Chief Financial Officer
Dr Holger Schmidt
Chief Technical Officer
Dr Hans-Joachim Richter
Chief Operating Officer
(from left to right)

*Dear Shareholders, Employees
and Friends of LINOS AG,*

Let us put it bluntly: last year was disappointing. Demand for our photonics products fell short of our expectations for the second year in a row. We ended the year with revenue of EUR 69.8 million and generated consolidated EBIT of minus EUR 9.2 million. Although we can handle this, we are not satisfied. This result is attributable essentially to the decrease of 29 per cent in total performance to EUR 66.4 million, which was compensated for by a corresponding reduction in the costs of purchased materials but was offset by a disproportionately small cut in personnel expenses. Like shares in other technology companies, the price of the LINOS AG share remained very low throughout the year because of the difficult situation on the Neuer Markt and company profitability.

In view of the poor development in earnings, we started to implement an ambitious reorganisation programme as early as the second quarter. We had two aims in doing this. It was necessary at short notice, first of all, to cut

costs and to reduce personnel and production capacities, which we had needed to increase when our sales markets were growing at double-digit rates. We also restructured our procedures and production processes, secondly, in order to become leaner and faster. The relocation of production operations to our Polish plant is a good example of these activities, which will be taking effect in the medium and long term. We have invested in equipment, measurement technology and the training of our staff there. We will be able to manufacture high-quality products inexpensively at the Warsaw location in future as a result.

We implemented most of our reorganisation programme by the end of the year. We have reached our objectives on the cost side to a large extent. We have succeeded in reducing our inventories substantially and in increasing cash flow. These assignments have therefore been completed. I would like to take this opportunity to express my thanks for the commitment our staff have demonstrated in this context.

It goes without saying that we had to make considerable efforts to stabilise revenue last year - with impressive success, as the increase in quarterly order intake for the fifth time consecutively shows. The individual market segments on which we focus in our Information Technology & Communications, Health Care & Life Sciences and Industrial Manufacturing business divisions developed very differently, however. Demand for photonics components in telecommunications, for example, remained extremely low. The semiconductor industry appears to have bottomed out now and a return to a normal if not inspiring demand level is becoming apparent at the moment. The Health Care & Life Sciences business division developed extremely steadily; the reduction here was comparatively small. We were particularly successful in the defense market segment, where we develop passive security systems.

The strategy chosen has to be reviewed particularly closely too in such a difficult year as 2002. Do we need to rethink fundamentally? Does our business model with its industry and business division strategy have the potential to produce sustained success? Our industry strategy is based on the concept of us being a single integrated source for all the major development and production operations along the photonics added value chain. This puts us in a position to implement our business division strategy and to develop high-end optical systems for many different applications. This strategy has helped to stabilise our revenue considerably, while creating good growth prospects at the same time. Our comprehensive know-how distinguishes us clearly from the competition. LINOS is the right company to contact no matter what optical problem needs to be solved - that is the reputation we have developed which many of our competitors envy us for. So there is not any doubt that our strategic focus is correct.

Our growth path has been interrupted all the same. We are therefore planning to give higher priority to strategic partnerships in future, with the help of which we will be increasing our market share. We intend to play a more

important role on the US market in this way. We are also concentrating on making further improvements in our sales activities. One major step here is the planned establishment of our sales company in France.

This takes us on to the outlook for the future. Although we do not anticipate a strong upswing in the short term, there are definitely signs of a recovery in individual market segments, e.g. in the laser technology field. It is not, however, possible to make sound forecasts for all the business divisions at the present time due to the global economic and political uncertainty. We are therefore devoting our attention primarily to returning LINOS AG to profit in a difficult market environment. To my way of thinking, it is still absolutely undeniable that photonics is a growth market with tremendous long-term potential and that LINOS holds an excellent position on this market.

I would like to thank you, our shareholders, for the confidence you have placed in us.

Göttingen, February 2003



Professor Dr Gerd Litfin
Chief Executive Officer of LINOS AG