



Axis AB  
Annual Report 2003

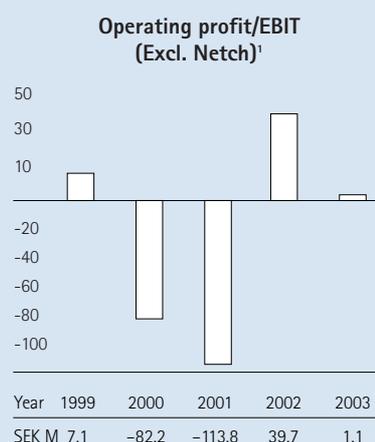
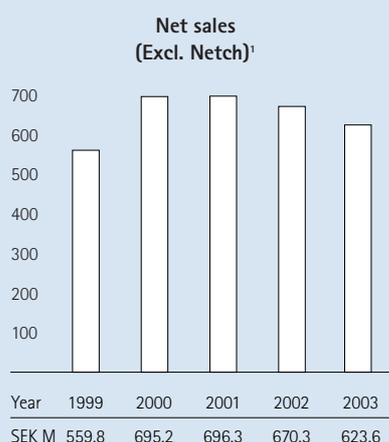


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## The year in brief

- **Video product area increasingly strong** with growth of 18 percent despite negative currency effects.
- **Net sales declined** by SEK 46 M to SEK 624 M. Currency effects impacted sales negatively by SEK 71 M.
- **Operating profit of SEK 1 M (40)**. Profit for the year was affected by restrained gross margins as a result of currency trends and some decline in prices.
- **Aggressive investments in technology and product development.** In addition to several successful product launches, the technical platform for Axis' new generation of video products was completed. These products will be launched successively during 2004.
- **Strategic acquisition of software company.** With the purchase of Attento, Axis' investment in software applications was strengthened, thus enabling the company to offer complete solutions for surveillance systems.



<sup>1</sup> Axis implemented a restructuring process during the second quarter of 2001, including divestment of the 59-percent holding in Netch Technologies.

## FINANCIAL INFORMATION 2004

Three-month report	April 15, 2004
Annual General Meeting	May 13, 2004
Six-month report	July 9, 2004
Nine-month report	October 15, 2004
Year-end report for 2004	February 2005
Annual Report 2004	March 2005

Axis' financial information in Swedish and English is available on the Axis Web site [www.axis.com/corporate/investor/](http://www.axis.com/corporate/investor/).

Reports may also be ordered from Axis AB, Emdalavägen 14, SE-223 69 Lund, Sweden tel +46-46 27218 00, fax +46-46 13 61 30, e-mail [ir@axis.com](mailto:ir@axis.com)

## Key data

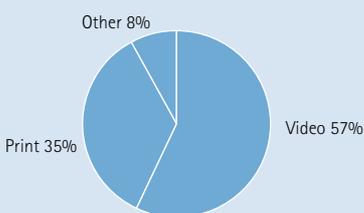
SEK M	2003	2002
<b>Group</b>		
Net sales	623.6	670.3
Operating profit	1.1	39.7
Earnings after net financial items	8.3	51.4
Liquid funds at end of period	103.0	130.0

## This is Axis

Axis increases the value of network solutions. The company is an innovative market leader in network video and print servers. Axis' products and solutions are focused on applications such as security surveillance, remote monitoring and document management. The products are based on in-house developed chip technology, which is also sold to third parties. Axis was founded in 1984 and is listed on the Stockholmsbörsen's O-list. Axis operates globally with offices in 14 countries and in cooperation with distributors, systems integrators and OEM partners in 70 countries. Markets outside Sweden account for more than 95 percent of sales.

### MARKET CHANNELS

Sales by product area



#### PRODUCTS & SYSTEM SOLUTIONS

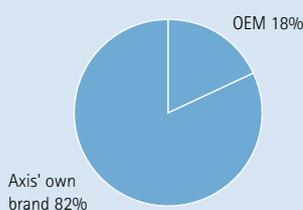
Products & System Solutions includes Axis' sales under its own brand. Axis focuses primarily on two product areas, Video and Print.

**Video.** Network cameras and video servers in systems that are primarily used for security surveillance and remote monitoring applications.

**Print.** Print servers for flexible print management.

**Other.** Scan, Store & Access – Solutions for efficient document management and data storage plus access points for wireless connection to local networks.

OEM – Proportion of sales



#### PLATFORMS & CUSTOMIZED PRODUCTS

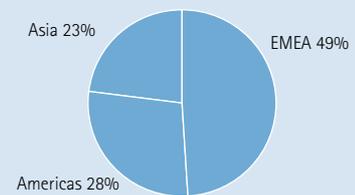
Platforms & Customized Products includes custom-tailored products that are sold under other brands through OEM licensing, as well as hardware and development platforms that are sold directly to third-party developers. OEM customers are primarily large, global manufacturers of printers/copiers and video products.



## MARKETS AND SALES

Axis operates globally, with sales in more than 70 countries. The company's 14 subsidiaries conduct marketing work and have customer responsibility. Products and solutions reach the end customers through a well-developed network of distributors, OEM partners, systems integrators and resellers. The geographic distribution of sales between Asia, the Americas and EMEA contributes to an effective spread of risks.

Invoicing by regions



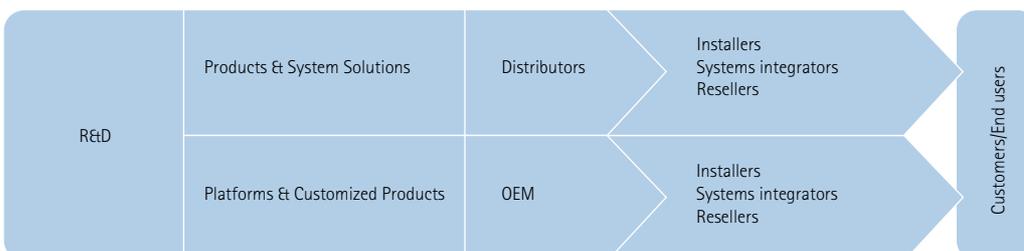
## CUSTOMER SEGMENTS

Axis prioritizes six main customer segments for its own branded products.

<b>Education.</b> Universities, schools, educational institutions, etc.	<b>Bank &amp; Finance.</b> Banks, post office, insurance companies, etc.	<b>Retail.</b> Stores, gas stations, superstores, etc.	<b>Transportation.</b> Airports, railways, ports, traffic monitoring, waterways, toll booths, etc.	<b>Government.</b> Government authorities, police, military, medical services, prisons, museums, casinos, etc.	<b>Industrial.</b> Process industries, engineering and construction, pharmaceutical companies, energy and mining companies, etc.
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## LEADING TECHNOLOGY

Since Axis was founded in 1984, the company's solutions have been based on proprietary hardware and software that enable the company to offer leading products at attractive prices. At the core of Axis' products is ETRAX, a chip for network connectivity. In addition, Axis has developed ARTPEC, a chip for network cameras and video servers. Combined with Axis' software, these chips create a common technology platform.



## Continued video growth despite currency effects

The very positive trend for Axis' largest product area, Video, continues. Despite negative currency effects, network video solutions showed a sales growth of 18 percent for the full year. A weaker U.S. dollar and a restrained IT market, however, affected consolidated sales and earnings during 2003.

As the newly appointed president of Axis, it is naturally a disappointment to note that operating profit for the year amounted to a modest SEK 1 M.

The drastic weakening in the U.S. dollar had a significantly greater impact on sales growth than we had anticipated at the beginning of the year. This, together with the global uncertainty and a restrained IT market, made increases in both sales and profit margins impossible. Sales, which amounted to SEK 624 M, declined by 7 percent, compared with the preceding year.

The gross margin, which amounted to 51.6 percent, was affected during the year by reduced revenues from customer-specific development projects, but also to some extent by declining prices in certain products and markets.

The balance sheet remains strong with an equity/assets ratio of 69 percent and liquid funds totaling SEK 103 M.

### FOCUS ON PROFITABILITY

As in the preceding year, there was a strong focus on profitability. To offset the continued weak investment climate in the IT market and ensure stable and positive development for Axis over the long term, a number of cost-saving measures were implemented during the year. These included personnel reductions in the

Swedish organization. The savings effect of these measures amounts to approximately SEK 15 M annually and takes full effect from January 2004.

At the same time, it is pleasing to note that the year was characterized by several positive signals. The company can report a continued highly positive trend for network video solutions, which despite a weak market climate and negative currency effects, showed sales growth of 18 percent for the full year. The growth, measured in local currencies, was more than 30 percent in both EMEA and the U.S. This is a trend that strengthens our conviction that the growth potential in the Video product area remains significant.

Several factors also confirm a clear breakthrough for the technology shift from analog to network-based surveillance solutions. Apart from a steadily increasing interest in security and surveillance, we were able to note increased activity in all customer segments with several significant orders as a result. At the same time, several global IT players, such as IBM, Cisco and Ingram Micro, announced that they would intensify their efforts in IP-based video solutions. Further proof of the shift in technology is the increasing competition that has emerged in keeping with the growth during the year. Several of the major players in traditional analog CCTV\* now have network-based products in their portfolio.

### NUMEROUS PRODUCT LAUNCHES

Axis has therefore, continued its aggressive investments in technology and product development during the period. This has resulted in several successful product launches, as well as the completion of the ARTPEC-2 technology platform for the new generation of video products to be introduced in 2004.

In December, we also strengthened our development efforts in software applications through the acquisition of Attento. This was a strategically important

\*Closed Circuit Television



step in ensuring that our products will continue to be competitive components in total solutions. It also provides Axis with a better opportunity to supply our Application Development Partners (ADPs) with components that further simplify integration with Axis' products.

The development of sales channels also proceeded according to plan. This resulted in a large number of new reseller and systems integration partners in both the IT and security sectors. In addition, new strategic distribution agreements were signed with such partners as Anixter.

Our strategic focus remains firm going into 2004. Axis is active in a dynamic growth market with its network video solutions, as well as in a more mature market for print and document management products. Our product and market activities will continue to prioritize the fast-growing video product area with a renewal of the product portfolio during 2004. The new generation of Axis video products offers better performance and enhanced functionalities. Examples of higher performance are superior image quality, high quality video streams and the ability to handle large volumes of data. An example of a new functionality is MPEG-4. Our overall ambition is to strengthen Axis' position as the market leader in network video solutions, while continuing to defend our position as the second-largest player in the market for print servers. We will also continue to leverage the company's core competence in networked solutions for OEM and technology customers in the area that we call Platforms & Customized Products.

#### **FUTURE OUTLOOK**

Although the economic trend remains difficult to predict, we have a positive outlook for Axis. During the year, players in the security market began in earnest to make the transition from analog to digital video solutions. With our strong market position and the extensive renewal of the product portfolio that Axis is now initiating, the growth potential in this product area is very good. At the same time, we must naturally remain aware of the increasing competition that is emerging in keeping with the shift in technology. However, we cannot expect the same growth opportunities in print servers, which is a significantly more mature product area. In addition, some uncertainty continues to prevail as to whether the investment climate in the IT market will really improve during 2004.

Given our leading technology, strong market position, clearly focused strategy and stable financial base, I am optimistic. All the prerequisites are in place to achieve profitable growth during 2004.

The past year presented many challenges, and I would like to close by thanking all Axis employees for their excellent efforts during 2003.

Lund, February 2004

*Ray Mauritsson*



## Business concept, goals and strategy

### BUSINESS CONCEPT

Axis' business concept is to offer the market intelligent network products and solutions. The company is focused on two main areas: network video and print servers. Axis' in-house developed products are primarily used in applications for security surveillance, remote monitoring and document management. These solutions aim to provide maximum customer value through less administration, reduced costs and expanded areas of application.

### OVERALL GOALS

Axis' overall goal is to maintain satisfactory profitability while further strengthening and enhancing its position as the market-leading supplier of IP-based solutions in the Video product area and to retain the corresponding position within the Print product area. By so doing, long-term growth in value is also created for shareholders.

### FINANCIAL GOALS

Axis' long-term goals are to achieve the following no later than 2005:

- Annual sales growth of 30 percent. This goal was established based on the long-term growth trend for digital video solutions in combination with Axis' leading position in this segment, as well as a stable trend within print servers. As a comparison, Axis' video sales increased by 50 percent between 2001 and 2003.
- A profit margin before tax of 10 to 15 percent. The profit target was established on the bases of an anticipated improvement in the gross margin resulting from the potential of Axis' new product generation in Video and that the video offering can be supplemented by a broader range of proprietary applications that result in a higher degree of refinement.

- An equity/assets ratio of at least 50 percent. This goal was established on the basis of the anticipated growth and the financial resources that may be required during the period.

### STRATEGY

#### Technology and products

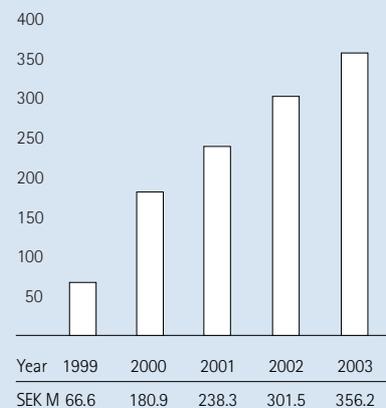
- Continuously developing, strengthening and broadening the company's offering. During 2004, virtually the entire product portfolio in Video will be renewed. The new generation of video products offers higher performance and enhanced functionalities. At the same time, the video offering will be supplemented with proprietary software, thus enabling Axis to offer customers complete, scalable and flexible solutions for security surveillance and remote monitoring applications. Part of the implementation of this strategy was the acquisition of the Danish software company Attento in December 2003.
- Further refine the portfolio and increase the number of solutions within each customer segment through greater knowledge of customer requirements.
- Retain a technologically leading position by continuing to increase knowledge in the areas of network and video technology and new intelligent network products and solutions that contribute to future growth. Over the coming years, additional software, integrated chips, products and total solutions will be introduced to create future sales under the Axis brand, to OEM partners and to third-party developers.



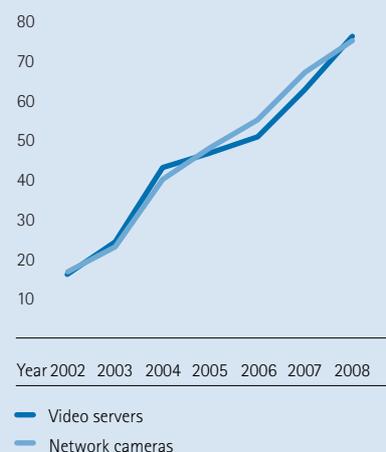
### Market and sales

- Continue the strong investments in marketing and market education that have been started while strengthening market presence through additional contracts with strategic partners. Axis products and solutions reach end users through a global network of distributors, resellers and systems integrators.
- Continue to develop the vertical market focus that was initiated in 2003 by actively working up six prioritized customer segments.
- Retain the market position with respect to print servers through increased efforts in sales and marketing together with existing sales partners.
- Continue to expand partnerships with new OEM partners who require solutions for networked video products while continuing to focus on existing partners.
- Supplementing organic developments with acquisitions as necessary. The objective should be to strengthen Axis both in terms of products and markets, as well as geographically, particularly in the Video product area.

Axis Video sales trend



IMS Research's growth forecast for network cameras and video servers (EMEA)



Sales in EUR M at manufacturing level, according to IMS Research's report titled "The EMEA market for CCTV and Video Surveillance Equipment."



#### **Australian wine merchant saves 250,000 dollars**

The leading wine and spirits merchant in Queensland, Australia is the Grape Group. When the company was looking for a solution to reduce losses in stores, one requirement was that the surveillance system should be easy to operate for wine enthusiasts who were not technically skilled. It also had to be possible to administer the system locally in each store and from the head office in Fortitude Valley. Axis was selected, and nearly 80 network cameras were installed in 30 stores. The company already knew that most thefts occurred when staff were fully occupied. The monitors were

therefore installed by the cash register so that employees could see if anyone tried to pilfer a bottle. In addition, thieves who try to break into the store at night and disable the video system were also outwitted. One camera in each store is connected via broadband to the head office and continues to function. Since the system was installed, loss has been reduced by AUD 250,000 on an annual basis. The system also allows better inventory control, since images from the cameras can be compared with cash reports.

## **Products & System Solutions**

Axis' sales of products under its own brand accounts for 82 percent of total sales. The fastest growing product area is Video, which during 2003 accounted for 57 percent of sales.

### **Video**

The market for network video solutions continued to develop very rapidly. During 2003, the Video product area increased the installed base by nearly 50 percent to about 300,000 units. A new generation of network cameras and video servers is expected to result in a continued favorable growth during 2004 and should further strengthen Axis' position as the world's leading supplier in this product area.

Since 1996, when Axis launched the first network camera that could be connected to a data network, the company has been the market leader in network video solutions. Axis currently offers a broad range of network cameras and video servers for a large number of applications, of which the most prominent are systems for security surveillance, remote monitoring and broadcasting.

Network video offers users new possibilities and increased flexibility. One advantage is that security and surveillance equipment can use existing network infrastructure, which simplifies the applications and reduces costs for both installation and operation.

Unlike analog CCTV (Closed Circuit Television), network cameras do not require their own infrastructure in the form of separate cabling and special monitoring stations. Network cameras are connected directly to IP networks and provide fast and easy access to video in real time, regardless of where in the world the user is located.

Axis video servers digitize images from analog cameras, thus making it possible to transfer images and sound over an IP network. Video servers offer a cost-efficient bridge to existing CCTV systems where the analog information is digitized and can be processed in the same manner as information from digital network cameras.

#### **CUSTOMER BENEFITS WITH NETWORK VIDEO**

- Lower installation cost.
- Easier to store and distribute images.
- Image processing and analysis are easier.
- Accessible over the Internet and wireless networks.
- Lower operational costs and ease of use.

#### **THE YEAR IN BRIEF**

During 2003, Axis signed several strategic contracts with such partners as Lenel and Anixter that constitute a clear recognition of Axis' technology, as well as the increased importance of IP-based video solutions for security surveillance and remote monitoring. A large number of orders were received in all customer segments, ranging from the school segment in the U.S. to industrial monitoring in Asia.



#### **Better protection against car break-ins with images on hard disk**

Vandalism and theft are an increasingly serious problem in parking lots. Owners of parking facilities are therefore investing greater sums in surveillance. In December 2002, a digital system based on Axis network solutions was implemented by the German company Ruhr-Park Parkhausbetriebsgesellschaft in Essen. The system uses the existing data network and is easy to use. Costs can therefore be kept down. Images from entrances and exits, payment stations, fences and other locations on the facility are recorded and simultaneously displayed

on a number of monitors in a monitoring center. In these respects, the system is no different from older analog systems. However, the IP-based system, which was developed by DSS, Datensicherheit & Service, has many more advantages than an analog system can deliver.

Images can be stored on a hard disk and quickly retrieved for analysis. Alarms can be sent by e-mail, SMS and even via MMS, the new standard for images being used in modern mobile phones with a built-in camera.

Axis also strengthened and broadened its offering with a number of new products during 2003. The product that generated the greatest interest internationally was the AXIS 205, the world's smallest network camera, which was launched during the autumn. This product primarily targets small and medium-sized companies, as well as demanding home users.

Three months after the launch, the new camera had already exceeded sales expectations by a wide margin and also received several international awards. Axis also introduced its most advanced camera to date, the AXIS 230, an MPEG-2 camera that offers advanced functionality including DVD-quality video (30 frames per second on NTSC or 25 frames per second on PAL) and synchronized sound over an IP network. In addition, AXIS 230 can operate with both day light and infrared light, which means that it can also be used at night.

Axis' software offerings were strengthened through the strategically important acquisition of the Danish software company Attento in December. Axis thus supplements its video offering and is able to provide complete, scalable and flexible solutions for security surveillance and remote monitoring.

#### **PARTNER PROGRAM STRENGTHENS AXIS**

An important component in Axis' continued expansion of its product range and its focus on the professional market is the successful ADP (Application Development Partner) program. This is an initiative that ties external product developers closer to Axis while ensuring a broad range of applications for the company's products.

In addition, the ADP program broadens Axis' presence in both new market segments and new language areas. Currently the program comprises just over 140 companies in 29 countries and includes such key players as Honeywell, Lenel, Nice and ABB.

#### **MARKET TRENDS**

Axis is the leader in a market that is undergoing a transition from analog systems to IP-based video systems. This creates opportunities for new solutions in the security sector, but also opens the door to completely new application areas. Surveillance has primarily been associated with security applications but will increasingly be used in other applications in such customer segments as Industry and Retail.

An important driving force in the sale of Axis solutions is that IT and security departments are rapidly being integrated with each other in many companies. This is an advantage for Axis, since IT departments already have in-depth knowledge of IP networks.

In keeping with the increase in the number of IP-based solutions, competition has become tougher. All major manufacturers of analog surveillance cameras have begun producing network video products. These include Panasonic, Sony, Sanyo and Pelco. In addition, a number of local suppliers, primarily in Asia, have begun to develop and market network cameras and video servers.

Axis is currently competing successfully against both large and small competitors. The company has built up extensive expertise in both R&D and sales, which provides synergies with respect to availability and service. Axis can also offer the market's broadest product range in combination with extensive experience and established technology.

Axis prioritizes the professional segment where the demand for sophisticated systems is growing rapidly. At the same time, the company has developed a very competitive alternative in the entry-level market with the launch of the AXIS 205 Network Camera.

### Network cameras increase security and lower costs

Increased security in schools is high on the wish list of many American parents. Security costs money, however, and Canton High School in Mississippi therefore sought a solution that would not exhaust the school's budget. The final choice was a system from Camera WATCH, which installed 24 cameras that were linked to the Internet via Axis video servers. Fights and crime were quickly eliminated when the system was installed. The Internet connection meant that the principal,

teachers and security personnel could see what was happening from any Internet-connected PC, both in and outside the school. If something serious occurred, school personnel could send images via e-mail to the police so that they would know who to look for.

A positive side effect is that the school's costs for security are now lower than previously, since security personnel are not needed around the clock, thus reducing salary costs.



### FAST-GROWING MARKET

Internet-based solutions still account for less than five percent of the total sales of surveillance systems. This means that the replacement market for analog systems presents a very great potential for Axis products. The CCTV market is estimated at about USD five billion annually.

Over the past two years, the move toward network cameras has been relatively rapid, and the trend is expected to continue. The market for digital monitoring systems is expected to grow by about 15 percent annually at a global level through 2007, according to security analyst JP Freeman in a 2002 report. In 2001, Frost & Sullivan valued the global market for network cameras and video servers at USD 791 M in 2005.

### SURVEYS CONFIRM AXIS' POSITION

In a 2003 report titled "The EMEA market for CCTV and video surveillance equipment," IMS Research predicted continued strong growth for IP-based network video products in the region. The average market growth over the coming five years is expected to amount to 28.4 percent for network cameras and 30.3 percent for video servers. IMS Research estimated in the report that the EMEA market for network cameras and video servers would amount to EUR 151.1 M in 2008. Axis is positioned as the undisputed market leader in network video products in the region. The survey shows that Axis has a market share of 59.8 percent for network cameras. In the video server segment, Axis is also the leader with a market share of 35.4 percent, which is far ahead of the nearest competitor.

## Scan, Store & Access

In addition to Axis' two main product areas, Video and Print, systems for document management and wireless access are sold in the Scan, Store and Access product area.

Axis' document servers simplify the management of paper documents in a cost-efficient manner. By connecting a scanner and/or a digital copier to the network via a document server, it is very easy to digitize paper documents and forward them directly. With an Axis CD/DVD server, everyone in a workplace can retrieve information simultaneously from the same CD and DVD discs, regardless of whether they are working in a Windows, Macintosh or UNIX environment.

Axis' access points are based on the Bluetooth communication standard and allow users to connect wirelessly to the Internet and the local network.

### MARKET TRENDS

Scan, Store & Access offers user-friendly and effective products that complement the larger Video and Print product areas and make it possible to deliver to those users who desire more extensive network solutions. As a result of continued weak demand and tough competition in both document management and access points, sales in this area declined during 2003.

### More efficient printer administration at Föreningsparbanken

Printing problems are a major source of irritation in many companies. In several surveys, the Gartner Group has shown that computer problems in companies also result in substantial costs in the form of lost working time and lower productivity. Employees spend many working hours solving problems with computers and printers. The U.S. industry analyst calls these hidden IT costs.

When Föreningsparbanken decided to update large portions of its IT system, one of the most

important requirements was to obtain a uniform administration of printers so that it would be easier to identify any printing problems.

Föreningsparbanken chose print servers from Axis to obtain a uniform, future-proof and cost-effective solution. The goal was to create an IT environment with the highest possible customer value.



## Print

Axis is one of the world's leading manufacturers of print servers, which enable the implementation of cost-efficient and user-friendly printing functions regardless of the network environment and printing equipment. With the market's largest range of external print servers, Axis can meet the demands of large companies and organizations, as well as small customers.

Print servers allow a printer to be shared by many users connected to a network. Axis servers are independent of printer model and manufacturer and can be accessed from many different computers, including PCs, Macs, UNIX and IBM mainframes. Integrated administrative tools allow IT administrators to monitor and control the printing system simply from a single computer using a standard Web browser.

### THE YEAR IN BRIEF

Axis is the world's second largest brand in print servers, a position it has held for several years, and has an installed base of more than two million units worldwide.

The past year was characterized by a weak IT market and negative currency effects. Sales in the product area declined by 21 percent during the period.

Despite a restrained market, Axis consolidated its position as number two in the global print server market through a broader product offering and several important contracts.

During the year, five new print servers with a USB (Universal Serial Bus) connection were introduced, of which two are designed for IBM mainframes. USB enables peripherals to be easily connected to a computer.

### MARKET TRENDS

The market for print servers is mature and thus more affected by business cycles than more pronounced growth markets. Against this background, Axis prioritizes investments in sales and marketing together with existing sales partners.

Although market trends in this product area are highly influenced by general trends in IT investments, there are other driving forces that favor the product area.

One of these is the transition to USB, which is expected to shape trends over time. This is a significant technology shift for external print servers since demanding requirements are placed on the market players' ability to change their product offering.

Axis adapted to this trend at an early stage and can offer a broad range of products with a USB interface. Another driving force is the trend towards wireless networks where Axis also has products at the forefront of development.

By strengthening its sales efforts through its extensive distribution network and leveraging its strength as a technology leader, Axis will be able to maintain its position and even to take market share in the print server market.



## Platforms & Customized Products

In addition to products sold under its own brand, Axis' technology is used in a large number of contexts by other players.

OEM sales account for the major share of Axis' technology sales. Customers are global manufacturers of printers and copiers, as well as companies that develop video products. Customers include such major players as Canon, Sony, Toshiba and Konica Minolta. Axis currently supplies customized network solutions to these customers. The major share of sales consists of printer solutions, although video solutions account for a growing share of OEM sales.

Central to the OEM offering is the proprietary chip ETRAX, which together with Axis' software, makes it possible to develop networked applications quickly and cost-efficiently.

In addition to OEM licensing, Axis sells hardware and development platforms to third-party developers, who create proprietary solutions based on Axis' technology. Axis' development platforms are very flexible, which makes them attractive for a broad market. There is currently a need for networked solutions in most industries, and Axis' technology is therefore offered to a large number of third-party developers. Volume sales to this group, as with OEM licenses, are often preceded by a long design and development phase

### THE YEAR IN BRIEF

During 2003, Axis further strengthened its position as the internationally leading OEM supplier of customized solutions in Video and Print, and as a supplier of network technology to third-party developers. Several existing partnerships were expanded and new ones established. Several volume orders were signed with third-party developers.

A partnership was also established with PI Vision in the U.K. This company is the world leader in large video systems for the security industry. PI Vision's Universal Video Management System can be fitted to include 5,000 video channels and can be used with

variants of the AXIS 2400+ and AXIS 250S video servers for both video and audio.

An OEM contract for Axis' video server technology was signed with the Chinese manufacturer YAAN. This company is a leading player in the Chinese market for surveillance cameras.

One example of how Axis' network technology can be used in other contexts is the contract with the Swedish security experts Rosengrens regarding SafePay, a system for cash handling. Axis' ETRAX chip is integrated with SafePay to create an intelligent network connection.

### MARKET TRENDS

Through well-functioning relationships with the major global equipment manufacturers, Axis has developed a strong position, and its proprietary technology is recognized as the leader in several application areas.

Axis has a stable revenue base in OEM and third-party sales, which has accounted for nearly one fourth of the company's sales in recent years. During 2003, however, the OEM share declined to 18 percent as a result of both the negative currency effects and continued restraint in the IT market, which affected printer manufacturers among others.

The international trend is that manufacturing companies are focusing on their core business and are thus increasingly predisposed to purchasing basic technology and solutions from such suppliers as Axis.

A driving force for OEM sales is the transition from analog to digital, network video solutions. Axis' position as a global leader and its broad product portfolio in this area mean that most of the future growth in OEM sales will come from companies that require video solutions.



**AXIS**  
COMMUNICATIONS  
**ARTPEC—2™**  
19054  
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G 0331  
WJF31933  
KOREA

## Research & Development

Axis' development work is focused on hardware and software for networked solutions, primarily in Video and Print. In these areas, the company has an R&D staff of 120 people with world-class expertise. Operations are centralized in Lund, Sweden. Since its founding in 1984, Axis has been able to offer world-leading products at attractive prices.

During 2003, 18 percent of Axis' total sales was invested in research and development in hardware and software, as well as customer-specific development.

The core of Axis' products is ETRAX, an application-specific integrated circuit (ASIC) for connection to fixed and wireless networks. This chip is included in all products and, together with Axis' software platforms, constitutes a very flexible technology base on which world-leading products can be developed quickly and cost-efficiently.

### DEVELOPMENT OF INTEGRATED CHIPS

Axis has two families of proprietary chips, ETRAX and ARTPEC.

ETRAX handles calculation, memory management and all communication. The chip gives Axis many advantage since it is both less expensive and contains more functions than corresponding solutions available on the market. In addition, the chip is small and uses relatively little power, making it possible to build small but intelligent products.

The chip includes a number of features such as processor and network functionality. During 2003, an advanced version was launched that also includes a memory module in which the Linux operating system can be stored. ETRAX thus became a single-chip Linux computer, which opens the door to new applications that have generated interest among Axis' OEM customers.

ARTPEC is used in network cameras and video servers where it performs image analysis and compression. During 2003, a second-generation chip was developed called ARTPEC-2. Enhancements include significantly faster image compression, support for MPEG-4, superior image quality and the ability to connect various types of image sensors. The chip also provides an open interface for advanced image processing.

### DEVELOPMENT OF PROPRIETARY PRODUCTS

A majority of the employees in R&D work with the development of Axis' own products, which are sold under the Axis brand and include network cameras, and video and print servers. A significant portion of this work is devoted to software platforms and applications. During 2003, a new software platform was developed that provides the foundation for the next generation of video products.

### CUSTOMER-SPECIFIC DEVELOPMENT

Axis' R&D department also conducts customer-specific development on behalf of the company's OEM customers. This development work is based on Axis' ETRAX and ARTPEC chips around which functions and products are developed according to customer specifications.

The chips launched in 2003 and those scheduled for launch in 2004 provide significantly greater opportunities for developing new, customized solutions and have therefore attracted considerable interest among both existing customers and other companies that sell networked solutions.

### PATENTS AND PARTNERSHIPS

An active patent strategy is pursued to protect Axis' investments in core technology and intellectual capital. During the year, 14 new patents were granted, of which most were in Video. Axis has been awarded 33 patents over the years.

Lund University is an important partner in research that relates to chip architecture and image analysis.



#### More cars with less stress in Chinese plant

In May 2000, Volkswagen began manufacturing its mid-range car Passat in the Chinese city of Anting, 50 km outside of Shanghai. As in most auto manufacturing plants, a barcode is attached to each car as it moves along the assembly line. The barcode follows the car throughout the manufacturing process and is read with a scanner so that the right parts are automatically supplied to each assembly station. However, like food items in a supermarket cash line, not all barcodes can be read. A human

must then intervene, which often delays production. In Anting, such a case triggers an alarm, which then directs an Axis network camera to take a photo of the illegible barcode and forward the image to a PC. A window then automatically opens on a computer screen to display an image of the barcode sticker. This allows the car to be quickly identified and the problem corrected, resulting in a higher production rate. This system was created by SeeTec and Industrielle Automatisierungssysteme.

## Global Axis

Axis, with its head office in Lund, Sweden, is represented globally through its own subsidiaries in 14 countries and through partners in 70 additional countries. These partners are distributors, resellers, systems integrators and OEM partners. More than 95 percent of sales take place outside Sweden.

Since the company was founded, a conscious effort has been made to continuously increase its internationalization and to develop a network of business partners in all regions. Extensive international experience, in-depth knowledge of local conditions and an increasingly strong partner network are a few of Axis' most important success factors.

This consistent focus on indirect distribution has created a strong trust between Axis and its business partners. Sales take place via distributors, systems integrators and suppliers of security systems. This indirect sales model has become one of Axis' strengths as the company in this manner attains greater geographic scope and reaches a greater number of users than would be possible through direct sales to end customers.

To simultaneously establish a channel to end users, the company has created the Axis Channel Partner Program, which is intended to create close relationships with value-added resellers (VARs) and systems integrators. These partners are closest to end customers in the professional segment where advanced network video solutions are expected to show rapid growth. Axis has now recruited more than 1,000 qualified partners to the company's Channel Partner Program. The increase in the number of partners constitutes a clear recognition both of Axis' technology and the importance of IP-based video systems for such applications as security surveillance and remote monitoring.

During 2003, Axis also signed a number of strategic agreements with such customers as Lenel and Anixter, which are both active globally. During the autumn, Ingram Micro, IBM and Cisco all announced that greater effort would be devoted to security products, which further strengthens the perception of a growing market potential for digital security solutions.

#### SALES TRENDS IN 2003

Axis has a leading international position in network video products. The trend over the preceding year continued to be extremely positive in all regions, despite weak economic conditions. Overall, the Video product area reported a growth of 18 percent, compared with 26 percent during the preceding year. Growth, measured in local currencies, was significantly higher and constituted more than 30 percent in the U.S. and Europe. Other product areas that are more sensitive to business conditions, however, were affected by a general restraint with respect to IT investments.

As in the preceding year, EMEA (Europe, Middle East and Africa) accounted for more than half of the company's sales. In EMEA, as in other regions, Axis is the market leader in Video, with a 59.8 percent share for network cameras and a 35.4 percent share for video servers.

The Americas accounted for 28 percent of sales in 2003, compared with 27 percent in the preceding year. During 2003, the U.S. economy stabilized and showed increasingly strong signs of recovery toward the end of the year. Although the IT market remained weak, the security market continued to grow. This contributed to a strong growth in Video, which during the year accounted for the major share of Axis' sales in the U.S.

During the year, the U.S. sales organization focused on educating the market regarding the advantages of network video and recruited more than 600 resellers and systems integrators with good geographic dispersion throughout the country. The customer segment that showed the strongest growth during 2003 was Education, with installations in hundreds of schools



### 30 courts in New York City build joint network

New York with its 7.4 million inhabitants devotes substantial resources to security. An important step towards increased security in the city's court system was taken with a surveillance solution purchased by the New York State Unified Court System. All courts can be monitored in real time from a central location. In addition, those responsible for the courts can connect to the system via their office computers. They can thus see what is happening on their own screens.

The joint network, which is called CourtNet, was built using network cameras, video servers and audio modules from Axis. Audio modules are used to transfer speech over the network.

and universities. Asia accounted for 23 percent of total sales. Development in the region was strongly affected during the spring by the outbreak of SARS and the war in Iraq. The significant exception for Axis was the ASEAN region (Singapore, Malaysia, Indonesia and Thailand), where sales increased, compared with the preceding year.

Asia is more severely affected than other markets by price competition from companies that have introduced network cameras. The newly launched AXIS 205, however, is a very competitive alternative to these products. At the same time, Axis has strengthened its position as the leading supplier in the professional segment, which places high demands on quality.

A significant share of Axis' sales in Asia derives from Japan, where the economy has been characterized by recession for more than a decade. Some stabilization was noted in 2003, and the number of tender requests for video systems increased. During the year, Japan continued the almost explosive deployment of broadband following a late start. The development of this infrastructure and the fact that Japan is the world's

second largest exporter mean that the country receives a high priority in Axis' global strategy. Axis has OEM contracts with several of the largest electronics companies.

### OUTLOOK

Growth in the U.S. economy and a more stable global economy are naturally positive for a continued strong growth in Axis' Video product area.

An equally important trend is the continued transition from analog to digital video systems. In this context, Axis' sales organization plays an important role in educating partners so that they understand the significant advantages of network video solutions.

In keeping with increasing demand, greater competition on a global basis can be expected, above all, from Japanese companies.

The print server market is significantly more sensitive to business cycles. Axis is working to offset these effects with aggressive marketing through existing channels and customers.





## Human resources

Axis is an innovative company whose success builds on the knowledge, experience and commitment of its employees. To maintain its leading position in the market, the company therefore invests continuously in developing the skills of its employees.

Over a long period of time, Axis has systematically built a strong company culture. Together with employees, management works with a number of values and guidelines that in combination with the overall business objectives lay the foundation for an appealing working environment and create requisites for profitable growth. The common guidelines encourage creative and innovative thinking among all employees. At the same time, the values should create respect for individual differences and contribute to a positive development in which everyone is encouraged to ask questions, take initiatives and responsibility, to strive to stay ahead and to always deliver results on time.

Diversity is a part of Axis' business culture and fosters both creativity and understanding of global customers' challenges and opportunities. People with a background in some 20 nationalities work at the head office in Lund.

In February, Axis was awarded a prize as Sweden's best workplace in the category, exemplary work for diversity. Sponsors of the award were the Swedish business weekly *Veckans Affärer*, Oxford Research

and Great Place to Work Institute. The award was part of an EU initiative to recognize the 100 best workplaces in Europe.

### HOW COMPETENCE LEVELS ARE ENSURED

Axis strives to be an attractive employer and offers its employees continuous training. In order to retain key employees, Axis invests in such programs as leadership development and special career ladders for engineers.

To also ensure a high level of competence in future recruitment and to be an attractive choice for new graduates, Axis has worked in collaboration with Lund Technical University for many years. Axis provides advisors for about 10 undergraduate theses each year. Axis employees teach certain university courses, and the company each year presents the coveted Axis Award for the best undergraduate engineering thesis.

As part of its efforts to offer an attractive workplace, Axis works actively to promote gender equality and has clear guidelines for improving the working environment.

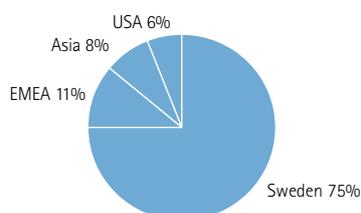
### LOW ABSENTEEISM

Axis places great emphasis on keeping fit, in part by providing access to training facilities and subsidizing fitness activities. During the year, absence due to illness amounted to 1.08 percent, with 1.23 percent for women and 1.04 percent for men. The figure was 0.61 percent for the age group 0-29 years, 1.19 percent for ages 30-49 and 1.42 percent for ages 50-65.

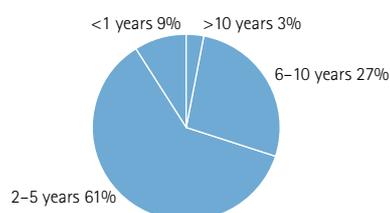
Personnel turnover as of December 31, 2003 amounted to 6.4 percent (6.6).

The average age of employees was 35.5 years.

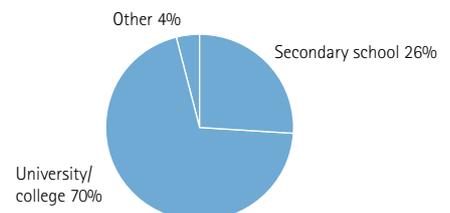
Employees by regions



Length of employment



Education level





## Environmental policy

Axis' environmental goal is to provide products and solutions that are sensible throughout their life cycles in an environmentally responsible manner.

All operations shall be conducted in such a manner as to be energy efficient, enable recycling and cause the least possible environmental impact while complying with legal, regulatory and other requirements.

### INVOLVEMENT AND COMMUNICATION

Axis will create an environmental responsibility among its employees and ensure that they are trained and motivated to apply Axis' environmental policy in their daily work. Environmental aspects should be an integrated element in each new project.

Axis will provide clear environmental information about products, services and operations to customers, suppliers, shareholders, employees, government departments and the public.

Axis will promote and support customers' and partners' choice of environmental friendly products.

### SUPPLIERS

Axis shall maintain a continuous and constructive dialogue with suppliers and subcontractors in order to reduce or eliminate negative impact on the environment during the manufacturing process and the choice of materials. Axis will require that suppliers and subcontractors are knowledgeable of environmental legislation and applicable regulations, and provide evidence of compliance with such regulation. Axis will also require that suppliers identify raw material content of products supplied to Axis and recommended end-of-life treatment for such products.

### ENVIRONMENTAL WORK IN 2003

During the year, Axis worked with the following Environmental measures:

- Axis was approved as a Sony OEM Green Partner. This means that the company works to reduce and eliminate substances that impact the environment. Sony only purchases components and materials from suppliers who are Green Partners.
- Axis is a member of the industry association El-kretsen, which was established in Sweden to resolve the issue of producer responsibility for electrical waste. As of July 2001, there is a law requiring producers to take responsibility for electrical and electronic products.
- Projects were conducted to eliminate such environmentally hazardous substances as cadmium and lead from products.
- All packaging is gradually being replaced by more environmentally compatible alternatives.
- Transports are the part of the logistics chain with the greatest environmental impact. Axis strives to use environmentally certified transporters to the greatest extent possible.



## Opportunities and risks

### OPPORTUNITIES

Axis' growth potential is in large part linked to the shift from analog surveillance systems to IP-based video solutions. To this are added the opportunities relating to new application areas and new customer segments in Video, such as the education, retail and manufacturing sectors.

As an established leader in network video solutions, Axis is well positioned to take advantage of the growth opportunities that are created both by the shift in technology and in new application areas.

### RISKS

In addition to the operational risks associated with macroeconomic trends, Axis is exposed to risks linked to the technology shift and Axis' position in a relatively early-stage market. The expected growth, primarily in networked video, will result in increased competition from financially strong companies in CCTV that are becoming more determined to establish themselves in this area. Among these are major electronic companies, such as Bosch, JVC, Panasonic, Sony and Sanyo.

### STRENGTHS

Axis' primary strength is the company's technology and market leadership in network solutions and products within Video. The combination of long experiences with proprietary network technology and a global network of distributors and strategic partners gives Axis a strong foundation on which to continue growing.

To retain and strengthen its leading position, Axis works constantly to develop technology, cultivate new customer segments and expand into new markets.

### RISK MANAGEMENT

#### Operational risks

The commercial risks to which operations are exposed consist of credit risks for sales, political risks, delivery risks and property and damage risks. Credit risks for operative flows are managed at the local level. The Group's credit policy provides a framework for how these risks should be managed. Political risks are primarily associated with local regulations for camera surveillance. Today there are no known changes regarding legal restrictions in this area. Risks in the legal area are handled by Axis' specialists in cooperation with external lawyers and legal advisors.

#### Intellectual property risks

Exposure to intellectual property risks in the areas of patents, IT and human resources are handled by Axis' specialists in cooperation with external lawyers and legal advisors. To date, a small number of disputes regarding patent infringement have been discussed, but none have resulted in any sanctions against Axis.

#### FINANCIAL RISKS

Axis' financial policy specifies how responsibility for financing operations should be delegated within the Group, which financial risks the Group is prepared to take and guidelines for how these should be limited.

#### CURRENCY RISK

Axis' strong international character means that both sales and profits are dependent on the relation between the Swedish kronor and other currencies.

Exchange-rate changes affect the company's results in a number of ways, including when sales and purchasing take place in different currencies, when financial results in the regions are translated to SEK and when assets and liabilities are valued in different currencies.

The flow of foreign currencies is hedged on business prerequisites and may not be speculative in nature. Some 70 percent of expected sales after deduction of costs are hedged. It is the Axis Group's



total currency exposure, and not that of individual companies or regions, that is hedged.

If at least a 5-percent change of an exchange rate in relation to SEK risks affecting earnings by more than SEK 0.5 M, a currency hedge must be used. The most important currencies for the Group are USD, EUR and JPY.

Exchange-rate trends during 2003 were characterized by a stronger SEK against the USD. This was reflected in the sales trend, since direct currency effects had a negative impact of SEK 71 M on sales. A strengthening of the SEK against the USD also characterized 2002. The total negative effect on consolidated sales during that year was SEK 26 M.

#### LIQUIDITY AND BORROWING

As of December 31, 2003, Axis has SEK 103 M in liquid funds and unutilized credit facilities of SEK 80 M. Available credit guarantees relate primarily to financing of operations. Axis' financial capacity is measured as the liquidity reserve and unutilized credit guarantees. The goal is that the two should not be less than 10 percent of average annual sales.

Axis' financial policy allows the Group to invest liquid funds in financial instruments with a term of at most two years.

The company employs derivative instruments to limit financial risks. These instruments are not used for speculative purposes.

#### SENSITIVITY ANALYSIS

The table below provides an indication of the effect of the most important factors on Axis' earnings for the 2003 fiscal year. Apart from currency risks, the factors considered to have the greatest effect on earnings are purchase prices and salaries.

	Change, %	Effect on earnings, SEK M
Exchange rate, SEK/EUR	+/-5	+/-5
Exchange rate, SEK/USD	+/-5	+/-6
Purchase prices	+/-5	+/-10
Salaries	+/-5	+/-10



## The Axis share

Axis was listed on the O list of Stockholmsbörsen (Stockholm Exchange) on June 27, 2000 and was included on the Exchange's O list last year. A round lot consists of 500 shares. During 2003, 13,896,368 Axis shares were traded, corresponding to an average trading of 55,809 shares per market day. Trading in the share took place on all market days. The turnover rate was 21 percent, compared with 125 percent for the exchange average.

The last paid price on December 30, 2003 was SEK 17.00. The highest price was SEK 19.80 on January 10, 2003. The year's lowest price, SEK 11.00, was noted on May 30, 2003. During the year, the share fell from SEK 19.00 to SEK 17.00, corresponding to a decline of 10.5 percent. During the same period, the SAX-ALL Share Index rose by 29.8 percent. The Affärsvärlden IT index rose by 73.8 percent.

### MARKET CAPITALIZATION

On December 30, 2003, Axis' market value was SEK 1,171 M, which corresponded to a decline of 7.6 percent during the year.

### SHARE CAPITAL

The share capital amounted to SEK 689,000, divided among 68,900,000 shares, each with a par value of SEK 0.01.

#### Development of share capital

Year	No. of shares	Par value (SEK)	Share capital (SEK)
1984	500	100.00	50,000
1985	5,040	100.00	504,000
1987	5,640	100.00	564,000
1997	564,000	1.00	564,000
1999	56,400,000	0.01	564,000
2000	68,900,000	0.01	689,000
2001	68,900,000	0.01	689,000
2002	68,900,000	0.01	689,000
2003	68,900,000	0.01	689,000

### OWNERSHIP

At year end, the number of shareholders was 9,803 (9,245). The proportion of foreign shareholders was 2.7 percent.

The table below shows Axis' ownership structure as of December 30, 2003.

Owner	No. of shares	Share of capital and votes, %
Mikael Karlsson, privately and through company (LMK Industri AB)	18,445,764	26.7
G. Kallstrom Et Co AB (part of Skanditek Group)	13,539,765	19.7
Martin Gren, through company (Grenspecialisten AB)	7,557,471	11.0
Fourth AP Pension Fund	3,320,700	4.8
Livförsäkringsaktiebolaget Skandia	3,125,000	4.5
Other	22,911,300	33.3
<b>Total</b>	<b>68,900,000</b>	<b>100.0</b>

#### Ownership structure 2003-12-30

Size classes	Number of owners	Number of shares	Percentage of shares	Percentage of votes	Market value SEK 000s
1-500	6,182	1,465,180	2.13	2.13	24,908
501-1,000	1,790	1,622,447	2.35	2.35	27,582
1,001-10,000	1,691	5,273,260	7.65	7.65	89,645
10,001-50,000	97	2,037,593	2.96	2.96	34,639
50,001-100,000	14	1,050,566	1.52	1.52	17,860
100,001-	29	57,450,954	83.38	83.38	976,666
<b>Total</b>	<b>9,803</b>	<b>68,900,000</b>	<b>100</b>	<b>100</b>	<b>1,171,300</b>

#### Per-share data

	2003	2002
Profit after financial items, SEK per share	0.12	0.75
Cash-flow, SEK per share	-0.39	-0.74
Equity, SEK per share	4.36	4.53
Share price on closing date, SEK	17.00	18.40
Share price/equity, % per share	390	406
Dividend	0.15	-
P/E ratio	neg.	35
P/S ratio	1.9	1.9
Number of outstanding shares, (000s)	68,900	68,900
Average number of shares, (000s)	68,900	68,900

### DIVIDEND AND DIVIDEND POLICY

Axis' dividend policy is to pay a dividend amounting to about one-third of the profit for the year after-tax, with consideration to the company's equity/assets goal. Given this policy and the results for the year, the Board of Directors and the President propose that no dividend be paid for 2003.

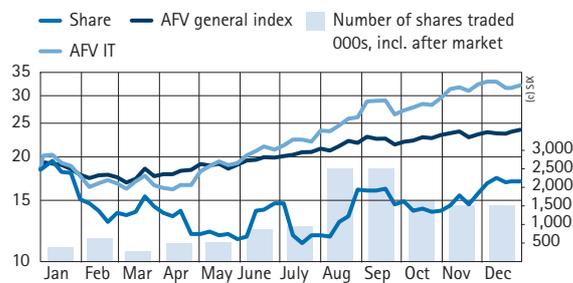


## WARRANTS

Since 1999, Axis has had an outstanding warrants program open to all employees. It is intended to encourage a long-term commitment to ensure a profitable business. The terms, number of warrants and the dilution that would result from full exercise of the warrants are shown in the table below. See also Note 23 on page 36 for further information.

Recipient	Maturity date	Exercise price	No. of warrants	No. of shares	Dilution
Personnel in Europe and Asia	04-10-01	19.50	430,000	430,000	0.60
Personnel in Europe and Asia	05-09-30	54.00	1,128,000	1,128,000	1.60
Personnel in Europe and Asia	05-09-30	63.00	172,250	172,250	0.30
Personnel in Europe and Asia	06-10-02	18.00	221,600	221,600	0.30
Personnel in Europe and Asia	07-10-02	26.00	104,200	104,200	0.15
Personnel in U.S.	04-10-01	19.50	140,000	140,000	0.20
Personnel in U.S.	10-09-30	48.00	172,250	172,250	0.30
Personnel in U.S.	06-10-02	18.00	89,000	89,000	0.10
Personnel in U.S.	07-10-02	26.00	64,000	64,000	0.09
<b>Total</b>			<b>2,521,300</b>	<b>2,521,300</b>	<b>3.64</b>

## Share price trend



## Analysts who regularly follow Axis

Company	Name
Danske Equities	Lars Horslund
Enskilda Securities	Lars Sveder
Handelsbanken Capital Markets	Jonas Eixmann
Kaupthing Bank	Mikael Laséen
Nordea Securities	Greger Johansson
REDEYE	Urban Ekelund
E. Öhman J:or Fondkommission	