

October 24, 2017  
Canon Marketing Japan Inc.

## Q&A at Third Quarter 2017 Results Presentation Meeting for Analysts

Date and time: October 24, 2017, 10:00-11:00

Venue: Hall S at the head office of Canon Marketing Japan Inc.

Answerers:

- Senior Vice President Koichi Yagi (President of Imaging System Company)
- Senior Vice President Akihisa Kamimori (President of ITS Company, President & CEO of Canon IT Solutions Inc.)
- Senior Vice President Yoshiyuki Matsusaka (in charge of Corporate Planning Headquarters and Brand Communications Headquarters)
- Senior Vice President Masachika Adachi (President of Business Solutions Company)
- Vice President Shiro Hamada (Group Executive of Accounting Headquarters)

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[Q1]

Please tell us about the prospects for digital cameras and inkjet printers during the year-end shopping season.

[A1]

The market of digital interchangeable lens cameras is generally maintaining stable performance, but that of SLR cameras is sluggish. The market of mirrorless cameras has grown from a year earlier, and our EOS M100 that was released this October is selling well. As described here, despite the sluggish trend of the SLR camera market, the mirrorless camera market is growing and our new products are selling, and we will actively promote them to younger customers with a promotion campaign to sell more. For inkjet printers, although the market is sluggish, our products released last year remain strong, and not only our market share but also the average unit price are increasing remarkably. Regarding 4Q, however, because the unit sales price already increased significantly last year, we do not expect the unit price to go up at as high a rate as those of 1Q to 3Q. For cartridges, although we will implement promotion measures on printing from now on, we anticipate that the prospects of the market trend are weak.

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[Q2]

In the market of office equipment, considering the situation of our competitors, I think that Canon Marketing Japan is receiving a tailwind. Please explain the actual business environment.

[A2]

We do not know any more about our competitors' situation than the published information, and we do not feel that we are specifically receiving a favorable wind in the market. However, we recognize that we certainly did what we should do, such as protecting our machines and replacing competitors' machines with our machines.

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[Q3]

Since the market is mature and even shrinking, I believe that this is an opportunity for Canon Marketing Japan to show off. That is, based on Canon's product strength, you can enter into a mode where you receive survivors' benefits. Please tell us the trend of unit sales prices for consumer products and office equipment by comparing them to the previous year to the extent possible.

[A3]

With regard to consumer products, in 3Q, average unit prices increased by 7% for SLR cameras, 15% for mirrorless cameras, 13% for compact cameras, and 13% for inkjet printers. In terms of the annual forecasts, we expect increases of 1% for SLR cameras, 13% for mirrorless cameras, 10% for compact cameras and 10% for inkjet printers.

Our understanding is that the office equipment business has not reached a situation of attaining survivors' benefits. We believe that our MFPs are strong in SMEs as well as being sufficiently competitive to match in large companies. But we consider the middle-tier market to be the area where we have an opportunity to grow in the future. That is, rather than mentioning survivors' benefits, we are still steadily expanding in the fields where we can grow. LBPs are going to be integrated into MFP, as we have explained before, but we will firmly expand them for the specific industries where our competitors are still strong.

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[Q4]

For semiconductor manufacturers, industrial equipment is strong in Q3, and its plan for 4Q is also aggressive. I would like to know what types of business are strong and how the prospects for the next year look.

[A4]

We expect that the market conditions related to semiconductors will be good until about the end of next year. We deal in a variety of overseas semiconductor manufacturing production equipment, and each of them is expanding. Among them, Mattson's lamp annealing apparatus, etc. is expanding, in particular.

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[Q5]

IT Solutions has improved its profit in this 3Q. I can also see profit improvements in associated companies' results. Please explain the reasons.

[A5]

Currently, the SI service business is enjoying excellent performance. In particular, for the financial industry, we are in a situation where it has broken past records several times on a monthly basis. With regard to the IT Infrastructure and Service business, IT Infrastructure is negative because our clients' orders happened to reach a bottom, but IT Services is gaining datacenter occupants earlier, and a result is becoming evident. With regard to the embedded business, we have been intentionally shifting our target market drastically to the automobile industry, for instance automobile equipment manufacturers and automobile parts manufacturers. We are currently in a transition, and our sales are lower than they were last year, but profit is hitting the bottom to some degree. For the product business, key products that we are dealing in intensively are selling very well. Outcomes like these are becoming apparent in 3Q. We understand that the SI business and product business, in particular, have expanded significantly.

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[Q6]

I understand that the reason why SI is good is thanks to deals in the financial industry. Will this continue for a while?

[A6]

The financial market has major integration projects, but they are going to finish. However, we expect that the good performance will continue for the financial industry until sometime in the next year. On the other hand, an area where major new demand is emerging is the industrial field. We expect that it will rise at a considerably large scale. Accordingly, looking to the future, we believe that we will be able to operate the SI service business stably as well.

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[Q7]

In terms of profit, because sales and profit dropped in 3Q of last year, it could look like an increase in profit this 3Q due to the reaction.

[A7]

We can now earn profit more easily than before; one reason is because we have bigger projects this year compared to last year, and another reason is because we have transformed ourselves into a leaner business structure.

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[Q8]

Overall sales of IT Solutions and Security appear to be slowing down in terms of growth rate. What do you expect the growth rate to be in the next year and beyond?

[A8]

In the security field, there are many areas such as network security, web content security, and control system security. For our Canon Marketing Japan Group, terminal-related security is particularly large. In addition, network security products etc. represented by UTM got on the group's channel, and they are expanding. Right now, in the group, we are considering selling these products as a whole group. We expect that they will significantly extend in the future accordingly.

Another business opportunity is that when building customer systems aligned with customers' intentions, we integrate and propose new solutions. We are gradually gaining strength in this business, and Canon IT Solutions is also carrying out the business.

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[Q9]

Looking at the 4Q plan for Business Solutions, you appear to have created a bullish plan on the whole. Did you create it on the basis of actual projects to some extent?

[A9]

Generally, yes. However, we revised it downward a little for network cameras and production printing. That is because we reflected the progress in 3Q. In particular, for production printing, products were delayed and it is difficult to complete acceptance inspections within the year for large and expensive continuous feed equipment, for which acceptance inspections take hours. We revised it downward, taking those prospects into account. Except for these factors, we expect that we can manage as planned.

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[Q10]

It sounds to me as if the maintenance service is weak from 1Q until 3Q. How can the minus 1% in 3Q be broken down, separating unit price and quantity?

[A10]

Beginning with the conclusion, the minus 1% in 3Q is as originally planned. The trend of unit prices is continuing to decline, but we have managed to prevent a drastic drop. That is the reason why it is not a large minus.

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[Q11]

How could you explain it when separating the print volume and the unit price?

[A11]

The print volume changes when the number of business days is one day longer or shorter than the previous year. Even if the unit price is constant, when the print volume decreases slightly compared to the previous year, sales decrease. On average, however, we believe that it is gradually increasing.

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[Q12]

I understand that you have focused on LBPs for specific industries for some time, and that the performance is improving. This field is where your competitors are strong. I would like to know whether changes in their sales approach have worked to the advantage of Canon Marketing Japan's sales. In addition, you mentioned that the volume of toner for specific industries is five times. Has it changed? Furthermore, what proportions do the specific industries account for in MIF? Please tell me even if you cannot provide the numeric data.

[A12]

With regard to the medical section, which is one of the specific industries, we are not only selling directly, but are also selling through system integrators. We have numerous cases of the latter too. Concerning this area, we will collaborate steadily with system integrators, but as a prerequisite, our equipment needs to become their recommended machines after their evaluation is combined with the system integrators' applications. Currently, our machines are recommended by many system integrators, and we are taking actions in accordance with the timing of replacement in hospitals (next year or later). Other than these, we are promoting them in both direct sales and indirect sales. In terms of the proportion of the

specific industries in MIF, we cannot disclose it. If you ask about the proportions between general offices and specific industries, general offices automation still accounts for the majority. While we are replacing LBPs with MFPs for general offices automation, we are expanding LBPs for specific industries.

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[Q13]

You have mentioned that the plan for network cameras has been aggressive for some time, but you lowered the bar this time after all. What is the reason from among the following; big projects shifted to another quarter, the plan was too high in the first place, or it is due to market factors?

[A13]

For 4Q, we see some projects dealt in by the unit of lot. Because Axis cameras have been expanding in terms of both direct sales and indirect sales since around 3Q, we created an aggressive plan for 4Q. However, it is true that we specified a high objective in the first place because it is a growing business. Because we cannot increase sales by spiritualism alone, we revised it downward by taking into account the trend in 3Q and the forecast in 4Q.

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[Q14]

You made a comment a while ago stating that IT Solutions had achieved a lean business structure. When aiming for operating profit of 3.5% in 2018 and operating profit of 4.1% in 2019, I would like to ask whether you can achieve them if the current market environment continues and you continue the current actions.

[A14]

Our understanding is that the industry as a whole is on a long path to growth. As a background, new technologies are getting on new platforms, and many companies are investing in them to differentiate themselves from other companies. Accordingly, we want to join the trend and do business. To do that, we want to transform ourselves into a different business style, proposing new methods based on the cloud, in addition to the traditional consignment development business. For this, engineers are required to understand everything. We are just about to establish a dedicated team of those engineers and ask them to create a variety of things, separate from their various irrelevant duties.

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[Q15]

I would like to ask what you will do to increase profit in the imaging system section in the next year and beyond.

[A15]

We cannot reduce SG&A expenses forever. We therefore need to increase net sales and earn a profit. We can see that the SLR cameras market will be in a difficult situation in the future among digital interchangeable lens cameras. Accordingly, we want to expand mirrorless cameras considering the growth potential of the market and the share of our products. With regard to printers, we expect that home printers will experience a difficult situation, but we can still extend business printers more, which is an area in which we can grow.