July 24, 2019
Canon Marketing Japan Inc.

Q&A at Second Quarter 2019 Results Presentation Meeting for Analysts

Date and time: July 24, 2019, 10:00-11:00
Venue: Hall S at the head office of Canon Marketing Japan Inc.
Answerers:

・Senior Vice President	Yoshiyuki Matsusaka
・Senior Vice President	Masachika Adachi
・Vice President	Shiro Hamada
・Vice President	Kunihiko Kubo

【Q1】
The IT solution business is allegedly doing well, but your competitors are also doing well thanks to subsidies for IT introduction and other effects. Please comment on future sustainability and the outlook, taking the scheduled consumption tax hike into account.

【A1】
The IT solution business is growing steadily, and although SI projects vary among industries, there has been numerous prospective business deals emerging, particularly for manufacturing and distribution systems. Our IT infrastructure business, which consists largely of data centers, has also been strong. While we hope that there will not be an impact of external factors such as the US-China relationship, we do not recognize any ongoing factors about which we should be particularly concerned.

【Q2】
With regard to the decline in sales of digital SLR cameras, what is your outlook for the timing of its bottoming out and the impact of the consumption tax hike? Do you expect that the Olympics models will be able to bolster sales?

【A2】
The Japanese market for digital interchangeable lens cameras was 1.06 million units last year, but it may fall below 0.9 million this year. The market is tough, particularly for SLR cameras among digital lens interchangeable cameras. The market for mirrorless cameras has been in line with our forecast at the beginning of the year. At this point, we are not

certain where sales will bottom out. In view of our history since the era of analog cameras, however, we expect the pace of the slowdown to gradually decrease. Considering the ongoing trend of a shift, particularly of digital SLR cameras to mirrorless models, the overall market will gradually shrink. As for the consumption tax hike, given that the increase this time will only be about 2% and that a range of measures have been taken, we do not expect a last-minute surge in demand and a reactionary fall as at the time of the previous consumption tax hike. We still expect some impact, however, and this year we brought forward promotions that are normally implemented in the fourth quarter to the third quarter. The weight of the third quarter will be greater than it is in ordinary years, and the weight of the fourth quarter is likely to decrease. In terms of whether the impact of the tax hike will be positive or negative, we expect that it will be neutral. Concerning the Olympics models, we hope that not only the cameras, but also the brand will be revitalized as we liven up the Olympics as one of the sponsors. We will view the Olympics positively, although the direct effect on camera sales may not be all that significant.

【Q3】

While sales of inkjet printers rose considerably by 8% in the second quarter, the full-year forecast for the number of units sold was revised downward. How should we interpret this?

【A3】

The reason for the 8% increase in the second quarter was growth in shipping due to sales to mass retailers after the release of models with the GIGA TANK in June. Meanwhile, the market for home-use inkjet printers continues to shrink. In addition, the number of New Year cards printed is expected to decrease again this year. Our result, however, indicates that net sales have increased in the first quarter and the overall first half of the fiscal year, despite the decrease in the number of units sold. The reason for this was an increase in unit prices from last year, and we will maintain profit while preventing net sales from decreasing as much as the fall in the number of units sold by continuing to increase unit prices, particularly those of relatively advanced models among the GIGA TANK models and home-use printers.

【Q4】

SG&A expenses reportedly decreased 2 billion yen in the first half of the fiscal year in the comparison before the rearrangement of the components. Do you have a plan or outlook for the full year or the second half of the fiscal year?

【A4】

We expect to spend on advertising and other expenses for new products to be released in the second half of the fiscal year. The result reflects our rather successful reduction of expenses in the first half, but we are currently posting expenses that correspond to net sales for the second half. We believe, however, that there is room for a reduction.

【Q5】

What is the situation in the second half of the current fiscal year compared to the last fiscal year?

【A5】

Expenses are likely to increase.

【Q6】

Is the increase in personnel expenses from the first half of the fiscal year attributable to the performance-linked bonuses?

【A6】

The largest part is the significant increase in retirement benefit expenses. Base salaries, welfare benefits, and other expenses related to personnel expenses are decreasing, largely due to personnel cuts. On the other hand, retirement benefit expenses have increased substantially this year in comparison to last year, partly due to the impact of the stock price at the end of last year. This situation will not change between the first and second halves of the fiscal year.

【Q7】

As in the first half of the fiscal year, will personnel expenses increase on a year-on-year basis in the second half?

【A7】

In terms of personnel expenses, we consider it inevitable.

【Q8】

Could personnel expenses grow in an effort to improve the sales force in the area segment and enterprise segment in particular?

【A8】

While we shift personnel as necessary, we do not plan to substantially change the personnel in specific segments.

【Q9】

Did the unprofitable projects in the IT solution segment just happen to occur in the second quarter? Is there any change in the overall level of unprofitable projects?

【A9】

We think that not having unprofitable projects is hard to achieve since we are working on new technologies and industries. If we look solely at the second quarter, some of the current projects are becoming unprofitable; in comparison to the previous year, however, we have been able to reduce the ratio of unprofitable projects to net sales. In addition, the target of system integrators is generally said to be less than 1%, and we have been able to keep the percentage of unprofitability within this range.

【Q10】

Does this mean that there will be a few unprofitable projects in the second half as well, but that the percentage will decrease?

【A10】

Yes, it does.

【Q11】

Growth in the sales of production printing has been sluggish. What are your future prospects?

【A11】

We are, in fact, taking time to install equipment and are releasing new products at present, and activities scheduled for the second quarter have been pushed forward to the third and fourth quarters. While the stock-based business is growing steadily and we expect to secure profit, we will see the sales results in the third and fourth quarters.

【Q12】

How is the market environment?

【A12】

It is not very active, and our customers are somewhat cautious about purchasing the products.

【Q13】

In the area segment, sales of software for operation efficiency are reportedly strong. Other companies are also focusing on solutions, and the service and solution businesses are growing. Regarding this, please explain whether good products have been developed as a result of that photocopier companies focused their efforts on such services or that the perceptions of customers have changed, or whether this is a result of labor shortages. If the situation has been improving, which side caused the improvement?

【A13】

We think that both sides contributed to the improvement. Work-style reforms, security improvements, etc. are the issues faced by the small- and medium-sized businesses which comprises the majority of the customers in the area segment, and demand for the use of IT to solve labor shortages has been growing. While we, including Canon S&S and our partners, have focused on photocopiers in the past, the support system of Canon ITS has now been developed, and we will build relationships with vendors and contractors that are able to cooperate with us. Furthermore, Canon products have been affiliated with cloud services, and solutions linked to work-style reforms are offered. We understand that we are currently becoming a company that is relied on by our customers operating small- and medium-sized businesses as a result of the synergy created by such developments.

【Q14】

Ricoh has recently been selling packages that are customized for each company by researching its customers' industries. Do you consider that it is necessity to see it as a factor for the competitive environment to worsen?

【A14】

We are not particularly concerned at this point. We are doing business with customers based on the relationships that we have already established in each area where we have strengths. Competitive relationships may develop if we go further from there, but we expect this situation to continue for a while.

【Q15】

Please explain whether there is currently any change or acceleration in the concentration of office MFPs. You stated in the past that you would focus on laser printers for specific industries. Has there been any change in this movement?

【A15】

Because the trend of replacing OA printers with multifunction printers in offices has been rising, the trend of using multifunction printers rather than laser printers in the same environment is increasing among customers. Customers operating businesses of certain sizes, however, place laser printers in departments that prefer single-function printers, rather than multifunction printers, in view of optimal placement. As for industry strategy, we are cooperating with vendors and approaching a range of business types including hospitals, public offices, schools, and manufacturers as an approach of printers customized for specific industries, and we are gradually seeing results for operational printers. This can be considered to be the result of relatively strong sales of laser printers in the area segment.

【Q16】

Is it appropriate to understand that there is no relationship between sales focusing particularly on solutions and the concentration of office MFPs?

【A16】

It is not that there is no relationship at all, but the relationship is not so strong.
