

First Quarter 2021 Results, Long-Term Management Objectives and Three-Year Management Plan:
Q&A at Presentation Meeting for Analysts

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Presenters:

- Masachika Adachi, President
- Hatsumi Hirukawa, Director and Vice President (in charge of group planning and group communications)
- Tsuyoshi Osato, Vice President (in charge of group accounting)

【Q1】

Your policy of strengthening IT solutions is not different from your traditional direction, but I feel that the details are a little bit different.

It sounded to me like you would more closely connect with Canon products, such as document solutions and the other added value they provide. Does this mean that some changes are taking place in the IT solutions business?

【A1】

As we have done before, we will continue to firmly strengthen the field called Edge Solutions and the service-based businesses. Edge Solutions is focused on the areas, industries and technologies in which we have an advantage.

While we are a system integrator, we have an advantage in dealing with a broad array of office equipment. We will add more Canon products to our IT solutions in a bid to take greater advantage of our strengths.

During the COVID-19 pandemic, there are increasing needs for the digitalization of documents. On this occasion, we stressed that we would step up document solutions.

【Q2】

You are ahead of other office equipment manufacturers in terms of system integration. However, your

document solutions do not appear to stand out. What will you change to bolster document solutions?

【A2】

We think we managed to provide large business customers with document solutions suited to their operations. However, we think that we failed to fully answer the needs of quasi-major and the larger medium-sized companies. I hope that you understand that we will improve our solutions for different types of customers.

【Q3】

Do you have a different perspective on the utilization of direct sales and agent sales channels for solutions for small and medium enterprises than you had in the past?

【A3】

We have large-scale talks with large companies about individual development involving system engineers. We deploy our full resources for them.

Meanwhile, we offer packaged solutions, rather than customized ones, to small and medium enterprises. We will transform the solutions we propose to quasi-major and the larger medium-sized companies into things like cloud services and market them to small and medium enterprises. Specifically, we think one option is utilizing the CaptureBrain AI OCR solution.

【Q4】

You explained specific strategies in the Three-Year Management Plan that made me look forward to your future achievements.

You are planning for a huge growth of your system integration services in the next three years. However, the past shows us that they did not grow at this high rate partly due to environmental changes. What is the difference from the past three years that supports this high expected growth rate? What specifically will thrive according to your forecast?

【A4】

Thank you for your positive expectations.

Regarding system integration services, it was common in the past to develop one system after another. Now, Canon IT Solutions is part of the Enterprise segment. It serves large companies together with the MA Division, which engages in direct sales to large customers, to produce synergy. For example, we are proposing a system that started with a non-life insurance company be used by other companies.

Although we have not yet developed it into a service-based item, we are beginning to create and propose SI core solutions. We will share these solutions with quasi-major and the larger medium-sized companies. We think the most important thing is to develop a service-based business model.

【Q5】

According to the plan, the security business will also grow over the three years. Until two or three years ago, it expanded rapidly. And then growth appeared to have stopped. What changes will take place over the next three years.

【A5】

Security is highly demanded by the market. The fastest growth is seen in security products and services for small and medium enterprises handled by the Area Business Unit. Canon System and Support plays a central role in providing a wide variety of security products and services. In the past, we proposed single items individually. In the future, we will propose comprehensive solutions that involve the coordination of a customer's overall security. We will speed up Makasete IT and other services in which we support comprehensive security.

Our growth plan is linked with the growth rate of the entire market. Our ambition is to grow faster than the market. However, we have formulated the plan assuming that we are attaining steady growth in line with the market.

【Q6】

Operating income for the first quarter showed a massive increase in the Consumer segment. What is the inkjet printer situation?

I would like to hear about your views on the trends in the sales volume of the main units and their unit prices. Will their prices fall in the future? Will high value-added models maintain their high percentage of total sales?

【A6】

In the inkjet printer market, relatively high-priced models are used by people working from home and SOHO users. However, we shipped a fairly large quantity last year, and we do not foresee considerable growth in the future. Given that working from home is becoming the new normal for large companies, ink demand will not fall significantly, even though it will not grow substantially.

【Q7】

A competitor sells low-priced models of monochrome LBPs. Are there any concerns about a fall of product prices or other negative effects arising from this?

【A7】

We also sell small-sized LBPs. The department dealing with mass retailers propose products that are suited to market needs.

We hope to run a business in which inkjet printers and LBPs do not compete for the same market. Some SOHO users do purchase LBPs. A majority of people working from home use inkjet printers. We will continue to closely watch market trends.

【Q8】

The IT solutions business marked sales declines for the first quarter in the Enterprise and Area segments.

According to your perception, how much did the market expand?

【A8】

In both Enterprise and Area, there was a huge plunge in sales of devices because of the discontinuation of support for Windows 7 last year. In Enterprise, there will be no impact from the reactionary drop in computer lots. In Area, the impact will gradually fade away.

【Q9】

Will you expand the solutions business for larger medium-sized businesses and small and medium enterprises?

I suppose that many of your transactions with small and medium enterprises are via agents. Will you train agents? I think that it is necessary to train agents to deepening their understanding after a product lineup is broadened.

Some competitors sell directly to larger medium-sized businesses and small and medium enterprises. What is the difference between you and them?

【A9】

We think that the greatest difference lies in security. For both direct sales and sales via partners, we have a team dedicated to support. It will provide solid support.

Canon System and Support and others will fully support small and medium enterprises. We will work

on support in the form of collaborations between our partners and Canon System and Support. Let us give one example. Partners have the resources to install computers and provide other services, but some may not have capacity to provide comprehensive IT solutions. We are able to supplement them to resolve the customer issues that are beyond our partners' capabilities.

【Q10】

Some competitors say that there is room to sell solutions to their existing small and medium enterprise customers. Do I understand that you also will conduct activities to increase penetration among your customers already using MFPs?

【A10】

As you say, you can understand that we will seek more sales from our customer base, specifically our MFP customers.

However, there are few small and medium enterprises managers interested in MFPs. We think many of them are wondering what to do for teleworking or for security. So, we are thinking of approaching companies that do not use our MFPs to propose products and services that respond to their issues so that we can later propose the introduction of MFPs.

【Q11】

How much scope for additional sales from MFP customers do you see?

【A11】

We have yet to publish the figure, but we perceive that there is still considerable scope for seeking extra sales.

【Q12】

Let me ask you about the Three-Year Management Plan. I think it is susceptible to being stretched. As president now, did you make the plan with a stance of stressing to officers in charge of different businesses and individual business department managers that its targets must definitely be met?

I appreciate that its operating income ratio and other figures are better balanced, but we are seeing dramatic changes in the economy today. I would like to know how thoroughly you thought out and how you set these figures.

【A12】

We set the Long-Term Management Objectives first, and then, we set target figures for the Three-Year Management Plan.

We have made efforts to cut SG&A expenses to obtain a lean structure. For existing businesses, we studied many different factors such as deepening internal digital transformation (DX), as well as our work processes and service productivity. We discussed our human resource structure and other aspects in collaboration with planning, marketing and operation teams to draw up the plan.

Uncertainties exist, but the figures were set by all members of management with a determination to attain them.

【Q13】

I think that incentives are important from the standpoint of operating departments. Since your company engages largely in sales activities, I imagine that you present some levels that you hope your workers will endeavor to achieve while giving instruction on a direction. Will you offer any incentive to the heads of operating departments if they meet their targets?

【A13】

A large proportion of remuneration for operating department managers and executive officers is performance-based. In this sense, they have a strong motivation to achieve the performance targets given to their departments as well as company-wide targets.

【Q14】

My question is about the earnings and expenses of data centers. You said that the data center business was growing, but in view of earnings and expenses as well as return on invested capital (ROIC), I do not think that it is sufficient. I hear that some U.S. companies are becoming more like real estate while others stopped value-added business to engage in a SaaS business. What do you think about earnings and expenses, targets and ROIC?

【A14】

With respect to our data centers, Building 1 reached full occupancy after a struggle. Building 2 is also heading towards full occupancy.

They have an aspect of real estate and an aspect of value-added services including operation. We focus on both.

At the moment, we are working to concentrate our servers. It takes time to increase occupancy. Large-scale cloud services are growing at high speed. We are studying what mix should be used to increase both profitability and efficiency. We will not put an emphasis on one and disregard the other.

【Q15】

You forecast that the data center business will break even. How long do you see it taking to reach profitability? For example, let us know roughly to what extent the earnings and expenses of the data center business are taken into account in the operating income in the Three-Year Management Plan.

【A15】

We have no information that we can disclose on this occasion. As you said, we will fully study how to boost its earnings capacity and put what we learn into action.

【Q16】

You have long been making considerable investments in your parent company. In the eyes of a shareholder, capital efficiency has not increased. Do you, as president, have any idea about ways of increasing capital efficiency, such as diverting money invested in Canon to return to shareholders?

【A16】

As I explained earlier today, our return to shareholders will center on dividend payments. We think that it is important to manage funds in a virtuous circle. We will gain earnings and reinvest them to increase earnings further. In this situation, we will pay dividends and make different investments. With regard to our financing to the parent company, we deposited some money with the parent company in consideration of interest rather than keeping it on hand because we were unable to make strategic investments. If we decide to invest, we can bring that money back at any time. We will make solid investment to run a virtuous circle of money and to provide returns to shareholders.

【Q17】

Will there be any change in your position in the Canon Group during the Three-Year Management Plan?

You have some positive achievements in IT solutions and other areas, but Canon's core business is the hardware business. Will it step up cooperation to spread successful methods to overseas? Or will it go further and reorganize you into a wholly owned subsidiary? What will occur in the future?

【A17】

Canon Marketing Japan is focused on IT solutions and is also striving to increase earnings from Canon products.

We are also executing a number of projects together with Canon Inc. They involve our system engineers. In an increasing number of cases, collaboration leads to a further increase in our value in the market.

We have yet to operate overseas. If the Canon Marketing Japan Group, especially Canon IT Solutions, attains major growth as a system integrator, we may possibly step into overseas markets. At the moment, there is no plan for a reorganization into a wholly owned subsidiary.

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Owing to various factors, actual results may differ materially from these projections.