Summary Translation of Question & Answer Session at Briefing on Initiatives to Strengthen the Solutions and Services Organization in Japan for Media, Securities Analysts and Institutional Investors

Date:	February 25, 2021
Location:	Live-streamed from Fujitsu Headquarters, Tokyo
Presenters:	Hidenori Furuta, COO & CTO
Q&A Participants:	Masaki Kubota, Head of Japan Region
	Katsuhiro Uramoto, Head of Japan Global Gateway

Questioner A

Q1: *I do not think you will succeed in generating benefits from your reforms just by changing your organization or its form. What is your plan for generating concrete results? In addition, in implementing your reforms in stages since last year, please tell us about any issues you have uncovered.*

A1 (Furuta): We are pressing a switch and changing the formation of our organization, but that is to accelerate our plans, which are to enhance the strengths of our products and offerings in our solutions business. Specifically, there are overlaps in the products of our group companies. For example, for our suite of products in the area of security, or in the products we develop for cross-industry customers, we will make value-added products that are stronger and more attractive. Another issue is that, up until now, there were cases in which Fujitsu or Fujitsu Japan would use one of our system integration (SI) companies, which would, in turn, use a partner company, creating a delivery structure with multiple layers of management, but now we can eliminate that extra layer by using the Japan Global Gateway. We are moving to a structure that enables each individual to play an active role in delivering high-quality services. So, the second point would be that we are raising the capabilities of individuals.

In addition, there have been changes before to our system engineering companies, and those changes produced benefits. The most recent case was in 2017, when we integrated three companies in a major merger that brought together Fujitsu Systems East Limited, Fujitsu Systems West Limited, and Fujitsu Mission Critical Systems Limited. The resulting cost efficiencies, improvements in the strengths of our products, and improvements in the quality and cost of delivery have been making a large contribution to the results and profit figures of our system integration business in Japan for the past several years. Therefore, we expect the current reorganization of our 15 SI group companies to further accelerate those benefits.

Questioner B

Q1: *For the improvement to earnings from such measures as eliminating overlapping investments and costs, roughly what year do you expect them to appear, and how large do you expect them to be? In addition, as the aim of this reorganization, when do you expect to create the representative services that you can provide uniformly around the world, and roughly how many do you expect to create? If you have any targets, please tell us.*

A1 (Furuta): Regarding the impact on costs, we are aiming for the combination of the three measures (reorganization of the 15 SI group companies, establishment of Japan Global Gateway, and full launch of Fujitsu Japan) to generate roughly 20 billion yen in cost efficiencies in fiscal 2022. It is not just cost efficiencies–we are also aiming for top-line growth, although I cannot provide you with specific figure at the moment.

We already have many globally standardized services. The initiative to establish global offerings is something that we are promoting worldwide. In total we have eight services, such as in our partner business, primarily with SAP and Microsoft, for such industries as manufacturing, automobiles, and retail, in which Fujitsu provides value-added services. In addition to individual system integration projects in Japan, we also want to deliver those types of offerings globally, including in Japan, and we aim for that expansion in fiscal 2021 and beyond. Specific figures are still under consideration.

Q2: *In integrating the system integration companies into Fujitsu Limited or Fujitsu Japan, how will that change your personnel expenses? Will it entail a change in headcount or a change in HR policies?*

A2 (Furuta): As of April 1, the treatment of personnel expenses and HR policies for the 15 companies will continue as is with the integration into Fujitsu Limited and Fujitsu Japan. We want to make shifts in an optimal way in fiscal 2021. There will be job-based compensation, primarily for senior staff at Fujitsu and Fujitsu Japan, so compensation and other policies will be in accordance with their jobs. Currently, because each of the 15 SI group companies has its own history, there is considerable variability in compensation and other policies, so after April 1 we want to take a year to consider how best to adjust them for Fujitsu and Fujitsu Japan.

Questioner C

Q1: *I have two questions about your business activities in Japan, including Fujitsu Japan. The first is that, with this series of reforms, I think that the role of the business producers, who will be the core point of contact with customers, is very significant, and my understanding is that, rather than simply a name change from "sales," that value they are expected to provide is also changing. In terms of acquiring a new set of skills for that purpose, how much progress has been made in the past year?*

The second question is about your business with channel partners. Earlier you explained that you are switching from selling things to providing system integration services and solutions, but please tell us a bit more about the specific forms these collaboration arrangements will take. You also used the expression "development-type collaboration," but please tell us a bit more about the form of these business arrangements and how you will share the earnings as you expand them.

A1 (Furuta): In reforming front-line sales, establishing business producers is not a measure that just applies to Fujitsu Japan. It is also being implemented at Fujitsu Limited. Domestically, here in Japan we are reforming the front-line point of contact with customers, including what we used to call sales and also including system engineers.

Regarding your second point about channel partners, a variety of partners have supported Fujitsu in our growth to date. As Fujitsu's own business portfolio is changing, we are carefully explaining to partners that our relationship with them also must change, and we will work together.

(Kubota): I would like to add some information about how we are training business producers. Within the Fujitsu Group as a whole, we are changing the designation of approximately 8,000 salespeople to business producers, and since last year we have been providing training to all 8,000 salespeople. Nearly 3,000 employees have finished the first phase of training. With everyone teleworking because of COVID-19, most sales activities are by video conferencing. Regardless, there is a need to dig more deeply into customer needs and work together to identify issues that need to be addressed. I think this is an issue that applies to all of Japan, but because, up until now, we had been building systems that were individually optimized, not for each industry but for each individual customer, that prevents standardization, and is a structure that makes it difficult to generate new business. Therefore, we are transcending an industry-specific approach to adopt a cross-industry approach. My understanding is that the employees who will implement this approach as business producers are steadily changing.

Regarding your second question about partners, up until now our focus was on hardware products, but now we are making a major shift to solutions. This is not just our desire, but that of our partners too, so with their understanding we will work to expand our business together.

Q2: *In the shift to solutions, does that mean that partners will work with you to create solutions?*

A2 (Kubota): There will be cases in which solutions created by one partner will be sold by a different partner on Fujitsu's cloud, and there will also be cases in which Fujitsu creates new SaaS models. I think there will be a variety of different patterns.

<u>Questioner D</u>
Q1: *What is the approximate profit margin that you are targeting for Fujitsu Japan? For Fujitsu as a whole, you have set an operating profit margin target of 10% for Technology Solutions in fiscal 2022, and considering that Fujitsu Japan will be positioned as a core part of that, I would presume that you would need to set it higher than 10%, but if you have decided on a specific target, please tell us what it is.*

A1 (Furuta): We have set the operating profit margin target of Fujitsu Japan at 10% for fiscal 2022. As you know, there is considerable variability in the operating profit margin of each of Fujitsu's business segments. Because our overall target of Technology Solutions is 10%, we have set the operating profit margin target for Fujitsu Japan at 10%, but when we think about the Solutions/Services sub-segment, we are aiming for a profit margin that is much higher than 10%.

Questioner E

***Q1:** Regarding your ERP solutions business for small and medium-sized enterprises (SMEs), I think your core product is Glovia, but please tell us the current scale of your revenues and market share for ERP solutions for SMEs. In addition, in seeking to capture a dominant position in Japan, what is your potential for expanding your share in the SME market or raising your profitability, and what plans do you have to achieve these objectives?*

A1 (Furuta): Fujitsu Japan is not just responsible for the private sector SME market in industries like manufacturing and distribution. The functions responsible for markets like local government, healthcare, and education will also be integrated into Fujitsu Japan. Within that, packaged solutions and ERP solutions for local governments and the healthcare sector are overwhelmingly strong with a market share of over 20%. On the other hand, unfortunately, for private sector SMEs, the share of Glovia is not at that high. We are now trying to think about that situation from scratch. For example, in the accounting area, we think the same solutions used for local governments can also be used for the private sector as well. We are thinking that, if we standardize a strong solutions platform, we could make it so that it could be used for the private sector, for local governments, and for healthcare. In other words, for solutions that were created in different forms because the industries were different, we could standardize them where they can be standardized for integrated offerings. From the ground-up, we are thinking to create value-added offerings to expand our market share.

(Kubota): According to our own in-house research, our current market share is 22% in local governments, 33% in healthcare institutions, and 20% in educational institutions. Our objective is to increase this to 40%. Because of COVID-19, obviously the healthcare sector, but also the area of private sector SMEs have been struggling this fiscal year. Amid these conditions, we increased our cloud revenues by 30%. We first want to promote a shift to the cloud, and then, using that as a base, promote a variety of SaaS offerings to expand our business.

Questioner F

***Q1:** What is the current scale of your revenue from cloud-related business, and what is your target for fiscal 2022?*

A1 (Furuta): That's a very difficult question. It depends on how you define cloud, and how you include infrastructure areas such as IaaS, PaaS areas, and also the SaaS areas that are built on top of them. In terms of Fujitsu Japan, with regard to new applications for local governments, healthcare institutions, and SMEs, they are all essentially cloud-based by default, so the majority of that business could be said to be cloud business. For Fujitsu as a whole, last year we announced the systematization of hybrid IT services, and revenue in that category for fiscal 2019 was about 520 billion yen.

To add a bit more supplemental information about the cloud, while we offer the proprietary Fujitsu Cloud IaaS within Japan, the PaaS services and applications that run on that cloud do not exclusively run on Fujitsu Cloud. They also run on our cloud services offered by our partners, including Microsoft's Azure and AWS. I would like you to understand that the numbers change depending on how you handle all of these categories. The default, however, including for

Fujitsu Japan, is for all fundamental products and services to be cloud-based, excluding individualized SI.

Q2: *When selling partner solutions, I think there is a possibility of ending up with a whole crowd of various products and packages, so how do you organize that?*

A2 (Furuta): With regard to partner solutions, as you pointed out, I think there is a need to organize them going forward, including the lineup of Fujitsu's application packages. As we touched on in our presentation, we will be cleaning up our packaged solutions lineup starting this April. We will be rethinking Fujitsu's unique offerings from scratch, including the possibility of completely changing the current lineups, with a set of application packages for small and medium-sized private enterprises and sets of packages for three areas in the public sector.

With regard to the solutions offered by our partners, Fujitsu and Fujitsu Japan will be offering them in the form of managed services centered on Fujitsu's infrastructure services, with application packages from our partners on top of that in lineups centered on their areas of expertise. Because there is a possibility that the functions of some packages may overlap, however, depending on the market, we would like to systematize this going forward as we think about our partner strategy and product lineup, systematizing both Fujitsu's proprietary packages as well as the solutions offered by our partners at the same time.

<u>Questioner G</u>

Q1: *In 2017, you integrated three SE subsidiaries, Fujitsu Systems East Limited, Fujitsu Systems West Limited, and Fujitsu Mission Critical Systems Limited, and there was an explanation that this had an effect. Could you tell us where that actually improved efficiency and give us a sense of the scale of the results? This time you have said it will have an effect of 20 billion yen, but is that something you can actually achieve? In addition, could you give us an explanation of how you arrived at that 20 billion yen figure, such as whether there is a possibility of exceeding that number, or if there are any variable factors, or if you feel you are being conservative?*

A1 (Furuta): We integrated those three subsidiaries in 2017, and the effect was seen in 2019. It had the effect of improving the cost of sales ratio for system integration by a little over 1%. If we think about an improvement in the cost of sales ratio in Japan, where we have revenues for system integration of 700-800 billion yen, 1% is quite significant. Naturally, there are other variable factors as well, such as unprofitable projects, but a 1% impact was fairly large. The 15 SI group companies we will be integrating this time, however, are not as large as the companies we integrated in 2017. In terms of the scale of effect of integrating these 15 SI group companies, if we assume that the reduction in the cost ratio will be 1%, we expect that to be about 6 billion yen, about one third of the 20 billion yen. This is neither a conservative estimate nor an overconfident estimate, but is based on past experience. Any number of measures contributed to the 1% improvement in the cost of sales ratio. I referred to the issue of overlapping layers of management earlier, and there are many elements to that, such as the fact that many tasks that were being done twice due to having separate companies, including reviews of various projects and business deals, will be eliminated, while non-customer-facing staff responsible for quality assurance can be consolidated, and the rate of occurrence of unprofitable projects will be reduced through quality, cost, delivery, or 'QCD'. Due to these factors, from past experience we can say that there has been an effect of more than 1%, and we expect to achieve that this time as well. To expand a bit more, we have said that the total impact of the organizational restructuring will be 20 billion yen, but the impact of integrating the 15 SI group companies will be 6 billion yen. We expect measures taken due to the establishment of the Japan Global Gateway to have an impact of over 6 billion yen, while the effect of integrating Fujitsu Japan will be close to 7 billion. In other words, these measures each make up about one third of the total impact. What I am looking forward to is the Japan Global Gateway. By utilizing our offshore locations, called GDCs, we will not only reduce unit prices for engineering work, but also increase standardization, efficiency, and productivity, which is why Mr. Uramoto, here with me today, has even higher internal targets. These, however, are internal targets, while as an organization, we are expecting effects of over 6 billion yen. For Fujitsu Japan, internally we are talking about an operating profit margin target of 10% by fiscal 2022, but because we are in the midst of assiduous discussions of the effects of integrating front-end functions as well, and to what extent we can grow the top line, we will be keeping a close eye on profit margins for Fujitsu Japan.

Q2: *Could we have a comment from Mr. Uramoto about the Japan Global Gateway?*

A2: (Uramoto): We have also been working on standardization for many years. What we would now like to aim for with the Japan Global Gateway is for the level of standardization to advance to an even more refined point. Specifically, we would like to reach a level of standardization where we can refine an individual task to the point where it can be managed in a week or two. We are aiming for global resource utilization that overcomes the boundaries of individual skill dependency and language. If we can do that, I believe we can shift from an individual project-based structure to a service structure for each solution, which can then move from project to project, continually contributing to increased quality and productivity.

Questioner H

Q1: *I would like to ask about your SE and Sales structure. I believe that at Fujitsu, you have a history of repeatedly unifying and then separating your SE and Sales organizations. I understand that now you are unifying the organizations, but are things going well? If they are, what is behind that? In addition, is there a possibility that while you are changing your Group structure now, this might change again in the medium term?*

A1 (Furuta): To look back at the history for a moment, in 2004 we intended to unify our Sales and SE organizations as part of Solution Business Restructuring, abbreviated SBR. This was undone in 2009, but looking back on that time, even though we said "unify," in the end they were simply part of the same business group or head office, while the Sales organization and the SE organization were still separated internally, so they were never truly combined. Their functionalities were also still separated into Sales functions and SE functions, so, to sum up, while the organizations were combined, internally they were separated. Once again, Fujitsu's business portfolio has largely shifted to solutions and services, so we need to change our previous sales style, as what we are selling has shifted from hardware to solutions and services. Since we began thinking of providing solutions and services to customers as a form of consulting, account-based SE and sales have become fundamentally the same sort of job, so we have not simply changed their name to business producers, we are also working on reskilling, as we explained. This current unification of Sales and SE has already begun to be implemented in the business group that handles the automotive industry, and we are positioning our staff as business producers regardless of whether they come from the SE side or the Sales side. As of April 1, we will be doing this for the business groups for all industries, including Fujitsu Japan. At that point, we will clarify the role of business producers, functionally speaking, and assign people to that role. Because they are not being functionally divided within the organization but instead fully unified, we expect that this is where the effects will come from. Roles will focus more on SE or more on Sales depending on the industry, but we will be offering full-fledged guidance from April 1 to proceed toward unification while utilizing the varying unique characteristics.

Questioner I

Q1: *In your cloud business, you have said that there are some areas where you will collaborate with your partners, but on the other hand, what is the solution strategy that Fujitsu will pursue on its own?*

A1 (Furuta): The basic idea is combination. I think this is not an era when we can offer customers solutions composed of only our own products, and even within our proprietary products, there are some that include open source elements, so I would like you to understand that this is the era we are in now. I think that combinations will change simply based on how much quality assurance Fujitsu does. In addition, strategies will also naturally change based on the industry. For example, in the case of Fujitsu Cloud, we are using another company's platform, but we are doing quality assurance. In addition, while I would say that if there are customers who are fine with other companies' public clouds, including their quality, we will offer that to them, and for the applications that will run on that cloud, we would install Fujitsu's proprietary applications. We are thinking of the application field, the PaaS field, and the IaaS field separately, and our strategy will therefore change for each industry based on that assumption.

(Kubota): I think the case of the government cloud is the easiest example to understand. The selection will of course vary based on the degree to which the vendor can guarantee the quality of the data and applications in that cloud. This is something we are fully discussing with customers when making these selections.