Summary Translation of Question & Answer Session at Management Direction FY2020 Progress Review and FY 2020 Financial Results Briefing for Analysts

Date: April 28, 2021
Location: Live-streamed from Fujitsu Headquarters, Tokyo
Presenters: Takahito Tokita, CEO & CDXO
Takeshi Isobe, CFO

Questioner A

Q1: *Regarding your growth investments, you mentioned that, in fiscal 2021, you plan to spend an additional 50.0 billion yen in operating expenses beyond what you spent this past fiscal year, but please tell us more about the content of these investments. In which segments do you plan to record the most investments? Also, please give us an idea of the negative effects on costs in fiscal 2021 versus the benefits in fiscal 2022 and beyond by segment.*

A1 (Isobe): Regarding the content of our growth investments, naturally the biggest portions will be in Solutions and Services, as well as shared investments for Technology Solutions. In Services-related investments, the investments will mainly be for the Japan Global Gateway and investments in our global offerings. In terms of our offerings, we want to decide on our focus areas across the entire globe and roll them out, and our investments are mainly for that. For the Japan Global Gateway, the investments will be to put our organization in order to achieve greater delivery efficiencies. For the shared investments in Technology Solutions, we are upgrading our ERP system to promote data-driven management. In conjunction with that there will be investments in assets and expense-related investments. In addition, one big initiative we are planning for fiscal 2021 is investments in rethinking our office spaces for our Work Life Shift initiative. We expect to make fairly large investments in renewing and converting our offices. These last two areas are expected to generate across-the-board benefits. We think the first areas of investments will, in our domestic solutions business, have a big impact on expanding our digital transformation business and increasing its profitability, and the investments in global offerings will create a strong tailwind for our international regions that, we hope, will also contribute to top-line growth.

Q2: *For the additional 50.0 billion yen you will invest on top of the amounts you invested in fiscal 2020, will it have a bigger impact in the first half or the second half?*

A2 (Isobe): We expect it will be similar levels in the first and second halves, but if I had to compare them, the second half should be bigger.

Q3: *Your plan is for 12% growth in the sales of Solutions and Services in fiscal 2021, but on an industry segment basis, what areas will increase? In addition, how are you viewing things in terms of timing? Will growth be high in the first half, for which comparisons with fiscal 2020 present a low hurdle, or the second half?*

A3 (Isobe): We are hoping for some growth in sales in the first half, but it is really from the second half that we expect a strong recovery. There was a lot of damage to our revenue in the first half of last year, and therefore, in terms of prior year comparisons, we are envisioning a recovery to some degree in the first half, but we expect the overall upturn, including an increase in demand for digitalization, will in the second half. In addition, in terms of the growth rate in sales of Solutions and Services, we expect growth across all industry segments. However, what I would like you to pay attention to is that we think sales are expected to be a bit higher because of the impact of Fujitsu Japan Limited. When hardware products are sold through Fujitsu Japan Limited, we will record sales in both the Solutions and Services subsegment as well as hardware products related segments/subsegments. Without such a special impact, we would not reach double-digit growth.

Q4: *Does that mean that, across a wide range of industries, you are expecting high single digit percentage point increase?*

A4 (Isobe): Yes.

Questioner B

Q1: *In Technology Solutions, you are projecting an increase in profitability will result in an increase in operating income of around 50.0 billion yen, please tell us what will contribute to that.*

A1 (Isobe): In broad terms, there are two things contributing to it. The first is an improvement in gross margin. As measures to achieve that, we will increase the proportion of offshored work from Japan utilizing the Japan Global Gateway. Our Services business has nearly 2 trillion yen in sales, so raising our gross margin on that business by 1% will have the biggest impact. Aside from that, there is the increase in productivity we expect from remote work and a reduction in unprofitable business, but of the 50.0 billion yen, about two-thirds is expected to come from an improvement in gross margin. In addition, while we are accelerating growth investments, we expect over a 10.0 billion yen contraction in expenses from the effect of consolidating existing investments and greater efficiencies in development. Please understand that it is the combined effect of these factors that we expect to amount to 50.0 billion yen.

Q2: *In network products, you are anticipating an increase in revenue of around 25.0 billion yen from fiscal 2020 to fiscal 2021, is this because the impact of higher sales of 5G base stations is expected to be large?*

A2 (Isobe): It will mainly be 5G base stations, but we also expect an increase in backbone network products. Regarding base stations, demand for base stations from Dish Network in North America is increasing. In North America, our mobile systems business has traditionally not been very large, but for fiscal 2021, we are expecting it to reach double-digit billions of yen.

Questioner C

Q1: *On page 31 of your briefing materials, there is a dash mark for growth investments in fiscal 2022, but does that mean that the 50.0 billion yen in growth investment this fiscal year will be repeated in fiscal 2022?*

A1 (Isobe): Your understanding is correct. We will have additional 50.0 billion yen in growth investments in fiscal 2021, and that level will continue.

Q2: *In conjunction with an increase in revenue of 300.0 billion yen from fiscal 2021 to fiscal 2022, you are planning for an increase in operating income of 60.0 billion yen, representing a profit margin of 20%. Please tell us the reasons for this.*

A2 (Isobe): I think that the point of your questions is that, comparing to the prior fiscal year, the contribution of increase in revenue to operating profit in fiscal 2022 is fairly low. The first point is that we want the scale of the revenue increase in fiscal 2022 to be on the same scale as the revenue increase in fiscal 2021. On top of that, to the extent that revenue declined in fiscal 2020 because of the impact of COVID-19, we want to increase revenue another step by the same level. By increasing the speed of growth of DX revenue, we expect that volume to be on the scale of 150.0 billion yen in revenue. To put it another way, if revenue increases by 300.0 billion yen, while it may be optimistic, we expect to generate 90-100 billion yen in gross margin, but our first aim is to strongly increase our top line, while, at the same time, targeting conservative amounts for profits. We think the key to success depends on how quickly we can increase our top-line results. In terms of increases in profitability, for both fiscal 2021 and 2022, we are projecting 50.0 billion yen, and if we can thoroughly control expenses, those are amounts that we should be able to fully achieve. The biggest hurdle to achieving our financial targets is the speed at which we can increase our top line, and that is where we need to concentrate our efforts. If we can, to some extent, achieve that, we think there is no reason why we should not be able to meet our medium-term targets for fiscal 2022.

Q3: *Does that mean that, by tracking the revenue trend in first and second quarters, we should be able to confirm your progress toward meeting your medium-term targets?*

A3 (Isobe): Your understanding is correct.

Questioner D

Q1: *In your forecast for higher revenue in Technology Solutions on page 31 of your announcement materials, what sort of presumptions about your legacy business are you including? In the global market, I think IBM and HP, which have a similar business model to Fujitsu, struggle under the weight of legacy hardware, and find it structurally difficult to grow. In light of that structure, how will you increase revenue?*

A1 (Isobe): I will answer with the understanding that, when you say legacy, you are referring to hardware. Hardware largely falls into the areas that we are categorizing as "For Stability," and for those areas, we are expecting a certain amount of revenue growth for at least fiscal

2021. One point is that we will be properly restarting projects that had been put on hold. In addition, we are planning to become comprehensively stronger in the Japanese market, which is also one of the reasons for creating Fujitsu Japan Limited. If we can make steady progress, including in capturing private demand in regional areas, we think that we will be able to secure a certain amount of growth in "For Stability" areas as well. There is no change, however, in where we are aiming for significant revenue growth, which is in our "For Growth" areas, including DX.

<u>Questioner E</u>

Q1: *If we take your target of an operating profit margin of 10% as the first phase, and if in the second phase you were aiming for 12-15%, in line with some competitors or the industry as a whole, what sorts of hurdles would you have to overcome?*

A1 (Isobe): I do not think there would be any particular hurdles. We feel that, at the current point, the most difficult hurdle we face is really whether or not we can significantly increase revenue in DX and other "For Growth" areas. I think 10% is a challenging hurdle, but I definitely feel it is a level we ought to be able to achieve, and I think we could reach an even higher level. To achieve that, the biggest challenge will be to change the way we have been moving forward with the DX business, and pick up the pace of growth a bit.

Q2: *Could looking at Ridgelinez's financial results be a leading indicator of this?*

A2 (Isobe): Ridgelinez might also serve as a key performance indicator, but Ridgelinez by itself does not have the energy to boost overall volume. In addition to growth in "For Growth" areas overall, we would like to further organize and clarify the seven key focus areas CEO Tokita mentioned earlier, and show you numbers for those areas in a traceable way.

<u>Questioner F</u>

Q1: *For fiscal 2021, you are forecasting 12% growth for revenue in Solutions & Services, but looking at the status of incoming orders for fiscal 2020, I think that forecast may be a bit strong. How much has your current order backlog grown compared to the previous year?*

A1 (Isobe): Excluding the special impact of Fujitsu Japan Limited, we expect revenue growth in Solutions & Services in the high single digits, and while that might still seems to be a bit strong as a forecast, our overall order backlog in Japan as of the end of fiscal 2020 has grown by more than 10% from the end of fiscal 2019.

Q2: *Do you think it is realistic that you can achieve revenue growth in high single digits, in percentage terms, with your current order backlog?*

A2 (Isobe): I cannot say anything quite that definitive. We will need to continue to secure new orders and restore normality to our pipeline, but we have a sense that our order balance will increase to some degree.

Q3: *Are your forecasts for Device Solutions and Ubiquitous Solutions for fiscal 2021, excluding special factors, not rather low for the current state of the businesses?*

A3 (Isobe): Please understand that, when it comes to Ubiquitous Solutions, with the end of the GIGA school PC demand and a relaxation of demand for remote work, volume will drop significantly, and we expect that price competition will also become more severe as a result. As for Device Solutions, results will continue at about the same level as in fiscal 2020, particularly for Shinko Electric. We are taking a somewhat conservative view in our foreign exchange assumptions, but we are assuming that profit levels will continue at their current high levels.

<u>Questioner G</u>

Q1: *You spoke about global offerings and the Japan Global Gateway as contributing to improved profit margins in fiscal 2021, but am I correct in understanding that those improvements will continue into fiscal 2022 and beyond? Or should we think that there is still some amount of room for improvement?*

A1 (Isobe): We are not thinking of fiscal 2022 as the final goal, but if we are able to reach about the halfway point in fiscal 2021, then I think we will be able to push on to that next level. The use of offshoring in Japan is starting from an extremely low level, but using the Japan Global Gateway, we will be able to further standardize processes and raise our offshore usage level. At the same time, by continuing to standardize, we will also improve quality. This will not be sudden, however. We view this as moving from stage to stage, expanding the effects as we go.

<u>Questioner H</u>

Q1: *With regard to the status of incoming orders as given in the presentation material, could you give us a bit more of a breakdown by industry? In terms of market sentiment in the enterprise IT field, please tell us your sense of the current feeling, whether there are further downside risks, or whether things will continue to recover. Also, the growth rate for incoming orders increased significantly in the fourth quarter for the Japan Region, so could you tell us the reason for that?*

A1 (Isobe): For enterprise, we feel that things are beginning to recover. There was a declaration of a state of emergency due to the spread of COVID-19 in the fourth quarter, and we are still in a somewhat unstable situation, but demand is returning. I would like you to understand that our sense is that demand will return strongly due to the reopening of delayed projects or due to DX, and that these are areas where we will be able to increase our business, or where we ought to increase our business. For the Japan Region, demand returned particularly strongly in the fourth quarter in February and March. For customers in local government and healthcare, particularly in the first half of fiscal 2020 and carrying on into the second half, they were swamped with work responding to issues on the ground, and many of them were not in a position to think about DX or even IT. At the same time, it is certainly the case that these are areas where DX is extremely necessary. Please understand the demand that emerged in the second half of the fiscal year as customers that had put things off reached the point where they had to be addressed. Please understand that customers in healthcare, which were in difficult circumstances in which, even though there was strong demand for digital technology, they did not have the energy to spend on implementing it, have now reached a point where they have no choice but to restart investment in this area, what we are calling a "For Stability" area, in order to maintain their businesses. The true recovery in demand may take a bit more time to arrive.

End