Summary Translation of Question & Answer Session at
FY 2018 Third Quarter Financial Results Briefing for Analysts

Date: January 31, 2019
Location: Fujitsu Headquarters, Tokyo
Presenters: Hidehiro Tsukano, SEVP, CFO

<u>Questioner A</u>

Q1: *With regard to the business model transformation expenses you explained today, when will the resource-shift at the plant actually happen, and what is the timing for reduction of fixed costs? Also, what other sorts of business model transformations do you envision in the future, and how significant will they be in financial terms?*

A1: We have now made some provisions related to the Augsburg plant staff, but there will be a period of time before we see the impact on cash flow, or before the effects become apparent. The reason for this is that there will be a transition period for our manufacturing capabilities, and the resource shift will proceed in stages. The reality is that there will be no significant impact during fiscal 2019. We plan to fully close the plant in September 2020, so the full-scale effects will be apparent thereafter.

We spoke about a number of initiatives beyond the Augsburg plant during the Management Direction progress review, but we are still working out the specifics, so we would like to provide an explanation at the stage when the details have been fixed.

Q2: *Could you tell us about the progress with the resource shift of the 5,000 employees in Japan?*

A2: The resource shift is primarily moving people from indirect units to customer-facing units that need strengthening. For example, we are moving as many people as possible to consulting, to roles where people will get involved in customer processes and propose a variety of improvements, or to BPO related roles – so that they don't incur costs, but instead create profits. We have a severe lack of that sort of personnel, and we would like to increase our numbers as much as possible. Right now, we are looking at each individual's suitability, whether they would fit that sort of role. We have not yet determined how many of those 5,000 employees will fit that role well, so I cannot give specific numbers at the moment. We would like to take some more time on this.

<u>Questioner B</u>

Q1: *You have not changed your full-year forecasts, but you are forecasting about 110.0 billion yen in profits for Services in the fourth quarter, for example. Can you really achieve this? Please tell us about your progress up to now and your outlook, including the other segments as well.*

A1: We are aiming for an operating profit from regular business activities of 140.0 billion yen in our full-year forecast. In doing the math, certainly the fourth quarter forecast seems difficult to achieve, but as I explained earlier, orders and sales are at record levels, and most of that will accumulate in the fourth quarter. The inspection and acceptance for major business deals are planned for March, so we can include that. On top of that, we still have room to cut expenses in the fourth quarter, so we believe that if we can reliably perform on that front, we can make significant inroads.

Q2: *With regard to the business model transformation expenses, were the expenses recorded in the third quarter moved forward from the fourth quarter? Also, will you see some beneficial effects in fiscal 2019?*

A2: The expenses recorded in the third quarter were largely according to plan. In the fourth quarter, we are considering recording expenses for the measures for multiple countries that were announced in October, but the regulations and environment of each country are different, so there is a race against time in how much we can get done. There are some transformation expenses that can be recouped as soon as they are recorded, but there are also some for which it will take time to have an effect. The expenses recorded in the third quarter are ones that will take some time to have an effect, with the full-scale effects coming in the second half of fiscal 2020. We are still in the process of calculating the final numbers, so I cannot give you a sense of the scale at this moment, but I think we will be able to enjoy a fairly significant effect.

Q3: *What are the specific details of the business model transformation expenses recorded this quarter?*

A3: We have about 1,500 employees in our Augsburg plant, and other employees based nearby as well, so overall we have about 1,800 employees in the area. A portion of those employees will be leaving the company as part of the plant closure, so the expenses are for that process.

Q4: *Do you mean that the majority of the expenses are for a premium severance pay provision?*

A4: Yes. At the moment, however, we must continue to produce products, so we will be gradually reducing our production capacity. As a result, the process has become structured such that the effects will be delayed.

Q5: *Is the 36.0 billion yen in expenses for the 1,800 people?*

A5: No. The total number is 1,800 people, but the number of people retiring is only a portion of that.

Questioner C

Q1: *With regard to unprofitable projects, we got the impression that they amounted to about 5.0 billion yen in Japan and about 3.0 billion yen outside Japan in the third quarter of fiscal 2017, but could you tell us how that compares to this year?*

A1: Speaking very broadly, we have limited those losses to about half of what they were in the third quarter of fiscal 2017. In fiscal 2017 they got somewhat out of hand. For fiscal 2018, we have kept them more or less in line.

Q2: *Profits from services rose by 8.8 billion yen on a regular business activities basis this quarter, so if you limited losses from unprofitable projects by about 4.0 billion yen, then should we understand that your regular business activities improved by about 5.0 billion yen?*

A2: Yes. We would like you to understand that our Services business is trending toward higher profits.

<u>Questioner D</u>
Q1: *I understand that your operating profit forecast for this fiscal year is on a basis that excludes one-off factors. I recognize that this is predicated on about 100.0 billion yen in profits from those one-off factors, which will almost entirely be consumed by expenses. Is there a possibility that you will use up all this 100.0 billion yen in expenses? Or is there also a possibility that you will record even more expenses that significantly exceed the 100.0 billion yen in profits?*

A1: The operating profit forecast of 140.0 billion yen we have committed to for the market is predicated on achieving that level from our regular business activities. At the same time, we have about 100.0 billion yen in one-time profits from the sale of businesses, and from changes to our retirement plan. While the truth is that we cannot know how things will turn out in the end until we get there, our current stance is that we will do everything we can to control expenses within that 100.0 billion yen, while pursuing the measures we need to take.

Q2: *If you are able to achieve everything you are currently considering, is there a possibility that you will undertake even more significant transformations for which the expenses would exceed 100.0 billion yen?*

A2: This is somewhat difficult to answer, but essentially our assumption is that we will be able to hold things to about that level. The alternative, or, in other words, expenses not going according to our assumptions, is entirely possible. We finally cleared the first significant hurdle in this third quarter, but there are still projects ahead of us, and we will not be able to give clear numbers until the situation becomes more fully visible. Our intention is to control expenses within that 100.0 billion yen estimate.

Q3: *In the telecommunications field, there has been a trend toward restricting technology made in China, but do you foresee this effecting your company as a result of this trend?*

A3: We recognize that the current environment provides a very strong tailwind for our telecommunications business. At the same time, with 5G, for example, our current assumption is that actual full-scale business will begin in 2020 and beyond. If there is no further standardization or an established ecosystem before then, we will have difficulty expanding our market. Our assumption is that the market itself will be larger, and extend for a longer period of time, than the 4G/LTE era, but I think it is still not yet clear what will happen, when, and where. There is clearly a tailwind blowing in the current environment, but we cannot yet tell where and how this will have an impact on the state of the business.

Q4: *It seems your Technology Solution business is doing extremely well in Japan, but your competitors have also produced good results, so could you tell us about your sense of market conditions?*

A4: In Japan, revenue from customers in the manufacturing field is up 13% for the third quarter, and projected to rise 8% for the year as a whole. Retailing and distribution is up 13% for the third quarter, and projected to rise 5% for the year as a whole. Financial services is up 14% for the third quarter, but projected to fall 3% for the year as a whole. Social infrastructure, which includes our telecommunications business, is down 15% for the third quarter, and projected to fall 13% for the year as a whole. The public sector is up 9% for the third quarter, and projected to rise 6% for the year as a whole. Overall, we are up 7% for the third quarter, and projected to rise 2% for the year as a whole. To touch on the macro level first, I think that while IT was previously thought of as more of a cost, it is now being thought of more as an investment. The departments that are investing in IT have changed from just the so-called CIO departments to the main business lines. For example, we are now beginning to get direct requests from marketing, finance, and sales departments for specific types of applications, and I think that is now becoming more significant. I think that is being thought of as an investment for that company. I think it is clear from the numbers I gave earlier, particularly with manufacturing, as well as with retailing and distribution, while previously 5% was considered significant growth, we are now hitting double digits, so things are going pretty well. We also expect to see this same trend continue in the future.

<u>Questioner E</u>
Q1: *Regarding the business model transformation expenses, for the 36.0 billion yen relating to the Augsburg closing, could you give us a few more details?*

A1: We assume that the majority of the 36.0 billion yen will be expenses relating to personnel. There will also be a portion of the expenses relating to the assets. We expect that personnel-related expenses will be at a level that is roughly equivalent to similar cases we have experienced in the past.

Q2: *Regarding the resource shift in Japan, will you decide during this fiscal year how large the expenses will be?*

A2: Yes, all of the expenses will be determined within this fiscal year.

Q3: *In the past, there have been several cases in which, when you received an inflow of cash from some kind of special item, a certain amount was returned to shareholders. I believe there will be a further unwinding of cross-shareholdings, and I would like to confirm what your thoughts are about share buybacks in these cases.*

A3: When we think about overall shareholder returns, our basic position is that we would like to raise dividends, but we have not ruled out the possibility of share buybacks. I would like you to understand that, if our overall rate of shareholder returns is not sufficient, we will also undertake share buybacks. Until about three years ago, we would not undertake share buybacks, so we declared that essentially all shareholder return would be from dividends only, but we have changed our position, and now we will also consider share buybacks as part of overall shareholder return.

Q4: *Does that mean that, when you have a significant inflow of cash, you can consider undertaking share buybacks? Or, as in this case, when you have significant cash outflows because you are recording expenses while you change your business structure, does it mean that you cannot consider share buybacks?*

A4: I just want to explain the way we approach this issue. Just because there may be a large inflow of cash, we do not think that we need to strengthen shareholder returns based on that cash inflow. Our thought is to raise the level of shareholder returns as much as we can, and we want to think about the overall rate of shareholder returns in terms of dividends plus alpha. In other words, we do not want to raise returns temporarily, and then, if there are no large inflows of cash the next year, simply terminate any more share buybacks.

<u>Questioner F</u>
Q1: *You mentioned that your business outside Japan is going through a somewhat tough time, and I remember that, previously, you had said that you had gone too far in shifting your business mix all at once from Managed Infrastructure Services, to Business Application Services, and that you wanted to engineer a soft landing by going back and capturing some of your previous Managed Infrastructure Services business. Is that strategy going well, or is business weak because of macroeconomic conditions? Please give us further background information on your results.*

A1: We actually succeeded in shifting more of our resources focused on Managed Infrastructure Services to Business Application Services, but we were not able to succeed in capturing enough Business Application Services business relative to the resources we had shifted. The result was that our Managed Infrastructure Services business fell, but we were not able to increase our Business Application Services business, so our overall earnings declined. Furthermore, we are taking on the challenge of digital services, an important target area for Fujitsu. Right now, the size of the average order is very small, so we need to capture a dozen or several dozen times the number of orders for it to become a significant source of earnings, but we have not yet been able to capture that volume yet, so we continue to face difficulties. By the way, we have decided to go back to grouping Managed Infrastructure Services and Business Application Services together. We decided to change our approach and make it one segment because both areas of business are coming from the same customers. On the other hand, our digital business is a different segment.

Q2: *In explaining the relatively strong performance of your System Products business, you mentioned that sales of servers and software, in particular, have been increasing both inside and outside Japan, but is this because the investment environment is improving, or is it because your market share is improving? Please also tell us your views about the sustainability of these increases.*

A2: Regarding servers, the main servers here are known as x86 servers, and we believe our market share has risen a bit both inside and outside Japan. In terms of the value of this business, even if unit volumes decline, the price per server is trending up because, for example, it comes with more memory, or the storage capacity is higher. Multiplying the price by the volume to get our revenue, we think it is still increasing. In addition, considering all that is happening in the current environment, we think the fact that we mainly focus our product development, design, and manufacturing operations in Japan is something that our customers in Japan truly appreciate.

<u>Questioner G</u>

Q1: *Please tell us your current way of thinking on Shinko Electric and Fujitsu General. I think you previously said that you did not want to sell them, because the stock prices were going down, but what are your current thoughts?*

A1: There has been no change to our policy with regard to non-core businesses of proceeding to spin them off as independent businesses, without exception, at some point in time. I think, however, there is a difference in whether that timing is within a year or something longer.

Q2: *Then, am I correct in understanding that there has been no change in your previous stance, and that you are not now in a rush to sell?*

A2: We are not doing anything in behind the scenes and then hiding it.