



Canon Inc.

Third Quarter 2017

Analyst Meeting

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Speech Summary (English Translation)

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Q3 2017 RESULTS

Key Message (Slide 3)

We made further progress in business structure transformation. As for existing businesses, an accelerated pace of recovery has led to all businesses achieving sales and profit growth. As for new businesses, we continued to post strong growth.

As a result, we were able to achieve a third consecutive quarter of overall sales and profit growth.

We also raised our full-year projection for net sales by 30 billion yen and operating profit by 20 billion yen, taking into consideration the progress we have made so far and the revisions we made to our exchange rate assumptions.

Q3 2017 (Slide 4)

As for the global economy, in the third quarter, the employment situation in major developed countries and regions, such as Japan, the United States, and Europe, continued to improve. In such emerging markets as China, we also saw gradual economic expansion.

Against this backdrop, our laser printer business remained on track with the strong recovery that started last year. We also posted solid sales of interchangeable-lens cameras, mainly driven by new models launched this year. On top of this, we significantly expanded sales of FPD lithography equipment and OLED vacuum deposition equipment, capturing rising demand for OLED panels.

In addition to the above, welcoming Toshiba Medical Systems Corporation (TMSC) to the Canon Group was another factor that contributed to a third consecutive quarter of overall sales and profit growth.

Transition in Sales and Op. Profit – Q3 2017 Actual v. Q3 2016 Actual (Slide 6)

Changes in exchange rates had a positive impact on net sales and operating profit as the yen declined in value against the U.S. dollar and euro.

As for changes in sales volume, together with the impact of the new consolidation, all business segments posted sales that exceeded those of last year. The Industry and Others segment, in particular, contributed significantly to overall sales and profit growth thanks to strong sales of lithography and OLED vacuum deposition equipment.

As for “Others,” the net impact was a negative 39.1 billion yen on operating profit. This reflects continuing efforts to limit price reduction, which was 3.9 billion yen in the quarter, as compared to 8.3 billion yen in the same period of last year. Additionally, cost reduction, which was 10.3 billion yen, shows ongoing positive effects of increased volumes as well as improved productivity.

Expenses, however, were 45.5 billion yen higher than last year. This was mainly due to the impact of new consolidation. Excluding this factor shows that expenses were in line with last year.

FY2017 PROJECTIONS

Exchange rate assumptions (Slide 7)

Considering the current situation, we reviewed our exchange rate assumptions for the fourth quarter. We now expect 112 yen to the U.S. dollar, which is the same as our previous projection. For the yen-euro, we revised our assumption from 125 yen to 132 yen.

Overview of Current Projection (Slide 8)

As for the global economy, despite a sense of uncertainty surrounding geopolitical and other risks, we expect such major countries and regions as Europe, Japan, and China to remain on a path of economic recovery led by the United States.

Against this backdrop, we will continue to put heavy focus on business structure transformation as we also work to achieve our target of growth in annual sales and profit for the first time in four years.

For existing businesses, which are sources of profit for the entire company, we expect our laser printer and camera businesses to turn to sales growth this year. We also expect to achieve significant growth in our lithography equipment business, capturing the strong demand. As a result, we expect all existing businesses to achieve sales and profit growth.

For new businesses, which are responsible for future growth, we expect significant sales increase, supported by a 70% increase in sales of industrial equipment of group subsidiaries, mainly driven by OLED vacuum deposition equipment and a 20% increase in network camera sales. Coupled with welcoming TMSC to the Canon Group, our new businesses are posting strong growth.

Against our previous projection, we are making steady improvement and exceeding our own expectations. Considering the progress we have made so far and the revisions we made to our exchange rate assumptions, we have raised our full-year projection for net sales by 30 billion yen, and operating profit by 20 billion yen.

FY 2017 Current Projection v. FY 2017 Previous Projection (Slide 10)

We adjusted our exchange rate assumptions for the fourth quarter to reflect the yen's declining value against the euro. This had a positive effect on projected net sales and operating profit.

As for changes in sales volume assumptions, the impact was negative on the Office segment. This reflects lower projected sales of low-end laser printers, a decision based on our established policy to prioritize profits. As for laser printer consumables, however, due to the steady shift towards high value-added hardware, sales remain strong. Additionally, for OLED vacuum deposition equipment, where we are working to enhance our production system, as we have made better than expected progress, we raised our projection for the Industry and Others segment.

As for "Others," the net impact was a positive 2.3 billion yen on operating profit. This reflects a further lowering of expected price reduction equivalent to 1.0 billion yen, which takes into account the progress we have made so far. As for cost reduction, against the backdrop of increasing production, we added an additional 2.0 billion yen for a full-year total of 32.0 billion yen.

As for expenses, we maintain our previous projection, which already called for significant reduction, as our results have been in line with our expectations.

DETAILS BY BUSINESS

Office – Q3 2017 Actual (Slide 11)

Amid the ongoing market shift to color copiers, we continue to post double-digit growth in color unit sales. This level of growth significantly exceeds that of the overall color market and mainly reflects expanded sales of models within our new next-generation lineup, which we completed in the first half of this year.

In addition to continued strong sales of our core iR ADVANCE C5500 series of mid- to high-speed models, other drivers of growth were the iR ADVANCE C3500 series, which targets small- and medium size offices, and the iR C3000, a series designed for emerging markets that offers competitive cost performance. Within this, the iR C3000 series is also contributing to the cultivation of new customers in emerging markets and a subsequent increase in overall market share.

The market for laser printer hardware continues to recover, recording a third consecutive quarter of year-on-year unit growth, thanks to economic expansion in emerging markets, especially China.

Against this backdrop, our hardware sales were below those of last year, but within the range of our expectations. This reflects the high level of sales in the third quarter of 2016 during which our hardware sales were going through a phase of recovery. Ultimately, we are making steady progress in shifting to high value-added products, evidenced by an increasing proportion of sales generated through new products, which will lead to stable consumable sales in the future.

For consumables, as per our plan, we significantly exceeded last year's sales. As a result, we posted a third consecutive quarter of year-on-year sales growth for our laser printer business.

Office – 2017 Full-year Projection (Slide 12)

As for color copiers, we are realizing growth that exceeds the market. With the completion of our next-generation color lineup in the first half of this year, we are now better equipped to propose enhanced customer solutions going forward. These models share common features that give them an advantage in the market, such as high image quality, improved operability via the adoption of a large touch panel, and reduced service maintenance costs. These models, in particular, offer decreased downtime, a feature that is earning high levels of trust from customers.

We will strive to expand our market share, continuing aggressive efforts to expand sales in the fourth quarter as well.

As for commercial printing, we expect sales to come in slightly below those of last year, reflecting a large deal achieved in 2016. Excluding this factor shows that we are maintaining strong sales of our color 100 page-per-minute model. For monochrome, we are also posting strong sales, particularly with educational institutions. As for wide-format printers, we are seeing progress with Océ's second-half launch of new products, strengthening our foothold in the expanding graphic arts arena.

As for the laser printer market, since the second half of 2016, we have been seeing a trend of recovery. And going forward, we expect the overall market to remain at its current level. Although we foresee weak demand in developed countries, we expect demand to increase in such emerging countries as China thanks to economic recovery and the shift to MFPs.

We have been steadily launching new models based on a redesigned platform that offers significant improvement in performance since 2015. In the first half of this year, we introduced new high-end models that achieve improved print speeds and lower running costs. Now armed with a full lineup, we will work to accelerate sales of these new products to stabilize sales of consumables even further.

Imaging System – Q3 2017 Actual (Slide 13)

For interchangeable-lens cameras, the rate of market contraction, primarily in developed countries, continue to slow down.

Against this backdrop, our sales, which were relatively high in the same period last year due to the earthquake, were down 5% to 1.31 million units, which was better than we expected.

In our lineup, we increased sales of the EOS 6D Mark II, a new competitively priced model within our range of interchangeable-lens cameras featuring full-frame sensors. This camera has been highly rated not only for significant improvement in such basic features as AF, but also for being able to offer this in a camera that is both compact and lightweight.

As for the compact camera market, which continues to recover from the earthquake, we posted strong sales of such premium models as the G9X Mark II, which offers excellent portability. Additionally, as our sales were at a low level due to the earthquake in the same quarter last year, our unit sales in the third quarter of this year showed an increase of 13% to 850 thousand.

Amid signs that the inkjet hardware market is stabilizing, our sales remained solid. In China in particular, by actively utilizing expanding e-commerce channels, we posted double-digit growth in hardware units, which drove overall performance.

By model, we continue to expand unit sales of printers incorporating large ink tanks. From a profit perspective, our strategically positioned TS-series has received high marks from users for their high-quality design and their selling prices remain stable even now, particularly in Japan, which is contributing to improved profitability.

Imaging System – 2017 Full-year Projection (Slide 14)

For the full-year, we raised our projection for interchangeable-lens cameras by 200 thousand units, as we posted better than expected results in the third quarter. We now expect sales to be down 3% to 5.5 million units.

One of the reasons for the revision was due to an increase in demand for high-quality images, particularly from smartphone users who use social media. Interchangeable-lens cameras, which are user-friendly and offer enhanced network capabilities that meet this demand, are leading to the acquisition of new users. As a result, our entry-class models have performed beyond our expectations. On top of this, sales of our new models that mainly target advanced-amateurs were also better than expected.

We also reflected this situation into our market projection, which is now projected it to be down 1% to 11.4 million units.

For compact cameras, as we are exceeding our expectations mainly with G-series models, we raised our projection and now expect our sales to be down 1% to 4 million units. As for the market, our outlook is for a 10% decline to 13.5 million units. As for inkjet printers, for the full-year, as our performance has been in line with our expectations, we maintain our projection for 2% unit sales growth.

In autumn of this year, we added a new product category to our lineup, introducing new models that employ the compact platform we adopted last year. The TR-series, a line of compact business models, targeting the home office segment, offers user advantages such as large display and rear paper feed functionality. Additionally, having revamped consumables, we are proceeding with the launch of our premium XK-series models, which offer such advantages as higher image quality for photos and lower running costs. Welcoming high value-added products into our lineup, we will stimulate demand during the year-end selling season, which will lead to improved profitability.

Medical System (Slide 15)

In the third quarter, sales were in line with our plan, driven by CT and ultrasound imaging systems. Among ultrasound systems, the Aplio i-series, which was launched in the first half of last year and has been highly rated by the industry for its leading-edge imaging technology, continued to perform well amid the expansion of market applicability from conventional use in radiology to use in cardiovascular medicine and obstetrics and gynecology.

As for our full-year outlook, we will work to improve profitability, enhancing cooperation with TMSC in an effort to reduce costs and improve expense efficiency, while also promoting sales of products that boast high precision.

Industry and Others – Q3 2017 Actual (Slide 16)

We are seeing a further increase in demand for OLED panels due to a strong shift towards their use in smartphones. Against this backdrop, we posted accelerated growth in sales of FPD lithography equipment, which were up more than 4 times that of last year to 29 units.

Additionally, for OLED vacuum deposition equipment, which offers overwhelming advantages in terms of both productivity and precision, we posted significant sales growth.

As for network cameras for which we continue to see market growth, by taking advantage of Canon and Axis's respective sales networks for products of both brands, we have been able to accelerate sales, posting 20% growth this quarter.

For reference, the sales composition of "Others," is approximately 35% for the industrial equipment businesses of Group subsidiaries and 25% for network cameras.

Industry and Others – 2017 Full-year Projection (Slide 17)

For IC lithography equipment, we expect our sales to increase by nine units to 73 units as we capture the increasing demand for such semiconductor devices as DRAM and NAND flash memory used in smartphones.

As for FPD lithography equipment, tools used in the production of small- and medium-sized panels have been a driver of growth. We expect this in the fourth quarter as well, driving unit sales that exceed those of last year and leading to sales growth for the full year.

Regarding OLED vacuum deposition equipment, in order to meet enduring demand, we are working to enhance our production system and we expect sales for the industrial equipment businesses of Group subsidiaries to be up 70% for the full year.

As for network cameras, we expect to maintain the strong performance we have shown so far, and for the year, post significant sales growth. In the first half of this year, we updated software used in video analytics, significantly expanding the number of compatible devices. We will continue to make these kinds of enhancements and strengthen our software going forward to expand our overall network camera business.

For reference, the sales composition of “Others” is projected to be approximately 35% for the industrial equipment businesses of Group subsidiaries and 25% for network cameras.

FINANCIAL SITUATION

Inventories (Slide 18)

The level of inventory at the end of September was within an appropriate range. Inventory turnover was 57 days, two days longer than it was at the end of June. The change represents a buildup of inventory of consumer related products in preparation for the year-end selling season.

Capital Expenditure / Free Cash Flow (Slide 19)

We raise our outlook for net income in relation to our previous projection, which links to an expected increase of 345 billion yen in free cash flow.

Going forward, we will preserve our financial health, maintaining efforts to keep capital expenditures below depreciation and our aim to ensure comprehensive cash flow management.

Cash on Hand (Slide 20)

As for cash on hand, due to a projected increase in free cash flow and other factors, we expect to hold 640 billion yen at the end of the year, which is 40 billion yen higher than our previous projection. This also reflect our expectation that we can maintain a level of cash on hand equivalent to approximately 2 months of net sales.

Dividend (Slide 21)

Our basic shareholder return policy is to provide a stable and active return, mainly in the form of a dividend, comprehensively taking into consideration medium-term profit forecasts, planned future investments, cash flow, and other factors.

This year, we passed a resolution to award a commemorative dividend, as we felt comfortable with the progress we are making in transforming the business structure.

Closing

Although the global economy seems to be on path of economic recovery, geopolitical risks and other uncertainties remain. Within this external environment, the Canon Group will work in a concerted effort to achieve its aim of sales and profit growth for the first time in four years, and make 2017 a break-through year that befits our 80th anniversary.