



Canon Inc.

First Quarter 2016

Analyst Meeting

Tuesday, April 26, 2016

Speech Summary (English Translation)

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Q1 2016 RESULTS

Q1 2016 in Summary (Slide 3)

The global economy headed toward a gradual recovery thanks to steady consumer spending in developed countries such as the United States and those in Europe. Emerging market economies, however, remained weak due to such factors as the economic slowdown in China and the low price of oil.

As for exchange rates, delays in the expected U.S. interest rate hike and other factors caused the yen to appreciate.

As for our sales, Industry and Others business unit revenue increased significantly thanks to lithography equipment, the industrial equipment of Group subsidiaries, and the consolidation of Axis.

Laser printer revenue, however, substantially declined.

Additionally, for cameras, although unit sales of interchangeable lens cameras were at the same level as last year, compact camera unit sales continued to decline at a double-digit rate.

Overall, total net sales declined due to the aforementioned circumstances and the impact of the yen's appreciation.

We also recorded a significant decline in profits due to the yen's appreciation and the impact of lower laser printer consumable sales.

The negative impact of exchange rates on net sales and operating profit was 31.0 and 13.3 billion yen, respectively, compared with the same period of last year.

Transition in Sales and Op. Profit – Q1 2016 Actual v. Q1 2015 Actual (Slide 5)

As for “Changes in Sales Volumes,” we recorded a significant increase in Industry and Others business unit revenue. In addition to strong sales of lithography and OLED display manufacturing equipment that was supported by market growth, this reflects the effects of consolidating Axis from the second quarter of last year.

Conversely, we recorded a significant decrease in laser printer hardware and consumable unit sales, mainly due to continued economic weakness in emerging markets. A decline in compact camera unit sales was also a factor for revenue decline.

As for “Others,” price reduction was 4.8 billion yen, an even lower level than last year for mainly cameras. Cost reduction was 6.4 billion yen, exceeding the level of last year, thanks to efforts to improve productivity through such measures as reducing fixed costs amid lower production volumes. As for expenses, although 10 billion yen in mainly advertising expenses were cut, total expenses were basically flat, reflecting the consolidation of Axis.

FY2016 PROJECTIONS

Exchange Rate Assumptions (Slide 6)

Concerns about a global economic slowdown and the decline in oil prices are having an effect on U.S. plans to raise interest rates, which caused the yen to strengthen from the beginning of this year.

Taking the current situation into account, we revised our exchange rate assumptions for the remaining months of this year. (Changed from 120 to 110 yen to the U.S. dollar and from 130 to 120 yen to the euro)

Overview of Latest Projections (Slide 7)

Although we expect the global economy to continue on a path of gradual recovery, we now expect the pace of recovery to be slower than we originally assumed. This view takes into consideration the economic slowdown in China, the decline in oil prices, the worsening financial environment and the IMF's recent decision to lower their projection for world output in 2016, from 3.4% which it had projected at the beginning of the year, to 3.2%.

As for our sales, we lowered our unit sales projection for laser printers, mainly for monochrome SFPs. Accordingly, we lowered our projection for consumables. As for other businesses such as copiers and cameras, we basically did not change our projections as our performance in the first quarter was essentially in line with our expectations, when excluding the impact of exchange rates.

The negative impact of revised exchange rate assumptions on net sales and operating profit were 158.1 and 61.2 billion yen, respectively, compared with our previous projection.

With these changes, we lowered our full-year projections for net sales and operating profit by 250.0 billion yen, and 60.0 billion yen, respectively, and we now expect sales and profits to be below those of last year.

Transition in Sales and Op. Profit – FY 2016 Current Projection v. FY 2016 Previous Projection (Slide 9)

As for “Changes in Sales Volumes,” within our Office business unit, we lowered our projection for laser printer hardware and consumables, which led us to lowering our previous projection for both sales and profits.

As for “Others,” we expect price reduction to be 49.0 billion yen, which is basically in line with our previous projection. For cost reduction, we expect 34.0 billion yen, which is also similar to our previous projection. Regarding expenses, we will work for thorough reduction over the full year. As we did in the first quarter, we will focus on reducing advertising expenses. As for R&D expenses, we will take measures to improve development efficiency. Through these measures, we included an additional reduction of 30.0 billion yen for the full-year.

DETAILS BY BUSINESS

Office - Q1 2016 Actual (Slide 10)

Starting with copiers, despite the bearish monochrome copier segment, the overall market was basically flat thanks to growth in color.

Within the color copier segment, we are growing faster than the market, posting a double-digit increase in unit sales, thanks to the continued strong performance of our new strategic products. As for monochrome copiers, although we posted lower unit sales, new products targeting emerging markets showed a positive trend, contributing to growth in some regions.

As for commercial printing equipment, we have expanded sales of such new products as high-speed inkjet cut-sheet printers, and high-end wide-format printers for graphics.

Laser Printer - Market trend and sales strategy (Slide 11)

Due to conveniences created through technological advancement and cost reduction, market demand for laser printers has increased, particularly within the small-office segment.

Although the market has experienced periods of negative growth due to its strong correlation with economic slowdowns, as a mid- to long-term trend, the shift towards color and multifunction machines has led to steady market expansion at a pace that has exceeded global economic growth.

Laser printers have gained acceptance, particularly in emerging markets, for their low price and easy maintenance. And as central office machines, sales have been expanding in line with economic growth in each emerging market country.

Since the middle of 2014, however, the market has been contracting, impacted by economic slowdown in China and the low price of natural resources.

In the latter half of 2015, prolonged economic weakness became a growing concern, which led to a strengthening sense that emerging markets would further decelerate. In the market for low-end laser printers, where prices had fallen, momentum was lost due to low profitability. This situation also caused the market to shrink in developed countries.

We sense there are several factors, apart from macroeconomics that could explain this worsened market environment:

1. Intensifying price competition: Since the yen started to depreciate from the latter half of 2012, prices continued to decline, which led to deteriorating profitability, mainly for low-end models, which in turn caused the market to shrink.
2. Enhanced lineup of business inkjet printers: There is a possibility that this may be a contributing factor for the slowdown, particularly in emerging markets.
3. Consumables: Possible growing shift towards third-party solutions.

We have succeeded in proactively expanding this business. At the same time we have taken counter-measures in case of these structural market changes, to maintain profitability and growth in a

mature market, developing high-value-added products that will lead to an efficient increase in consumable sales.

As part of this, last year, we started introducing products based on a renewed platform. These new products offer enhanced user conveniences through such features as reduced power consumption via low-melt toner technology, faster First Print Out Time (FPOT) and space-saving designs.

The first of these color model products were launched in the spring of last year, and has already exceeded the sales results of replacing models, giving us confidence about the performance of our new products. As toner has been renewed as well, we expect genuine consumable sales to grow. Moving forward, we will continue replacing our lineup with new models to increase consumables.

In a market characterized by severe competition, we will control sales of existing low-end products in order to avoid aimless expansion, and put our focus heavily on profitability.

Due to the sluggish market environment and our efforts to control sales of low-end models, we recorded a significant decline in first-quarter unit sales compared with the same period of last year. Associated with this, we also made efforts to control shipments of consumables, mainly for existing products. These factors led to an overall decline in laser printer revenue.

As for the laser printer market, according to a market research firm, it is projected to bottom out and return to positive growth in the second half of 2016. The pace of recovery, however, is projected to be modest. For the full year, unit sales are projected to decline 1% this year and grow 1% next year. The laser printer market in emerging markets is also expected to return to positive year-on-year growth in the second half of 2016 from its dramatic drop in the middle of 2015. In driving growth, underlying support is expect to come from MFPs, color models in developed countries, and monochrome models in emerging markets. We expect market growth to be basically flat over the mid-term, which is essentially in line with this market research.

Though we feel more time is needed before we see a real recovery, we will promote the spread of new products that pursue user convenience, steadily replacing our install base. Thus we will expand sales of consumables leveraging the switchover to new products. There is a time lag for hardware sales to link with consumable sales. However, in line with the progress we are making in switching to new hardware, we expect consumable sales to gradually increase.

Furthermore, we expect the MPS market to expand. As the market moves toward saturation, the key to supporting growth is to offer comprehensive services. Going forward, we will further strengthen cooperation with our OEM partner, developing products that respond to changing market needs. At the same time, we will take steps to thoroughly reduce cost of sales, promoting automation as we have with cameras.

From a long-term perspective, we expect gradual growth to continue, supported by potential demand. At the same time, however, we expect the current harsh market environment to persist for the time being. Additionally, as we expect shipment adjustments to continue throughout the first half for both hardware and consumables, we lowered our 2016 projection for sales, accordingly.

Office - FY2016 Projection (Slide 12)

For color copiers, we expect new products to remain core for us to outpace this market segment with double-digit unit sales growth.

For monochrome copiers, we will expand the roll out of emerging market models globally and also focus on high-end devices, thus we expect to grow at a rate that outpaces the market, similar to color copiers.

For solutions, in addition to MDS, by strengthening our outsourcing services, we expect double-digit growth.

Regarding commercial printing systems, in addition to new products, we will focus energy on expanding sales of our enhanced lineup of continuous-feed systems to facilitate the expansion of consumable sales.

Imaging System - Q1 2016 Actual (Slide 13)

The interchangeable lens camera market has been on a trend of gradual recovery in developed countries. In the United States and Western Europe, the market remained firm. In Asia, however, the trend of year-on-year market contraction continued. Within this market, our unit sales were 1.02 million, the same level as last year, as we expanded mirrorless camera unit sales, mainly in Asia.

The compact camera market continued to contract in all regions. And our unit sales declined 22% to 1.06 million compared to the same period of last year. Within this market, sales of our expanded line of premium digital compact cameras remained firm, leading to an improvement in our overall market share.

The inkjet printer market continued to contract, particularly in Asia and other regions within emerging markets.

Within this market, we grew unit sales by expanding sales of new products in developed countries. Even in emerging markets, where economic conditions remain weak, we were able to steadily grow unit sales of refillable ink tank models for high volume printing that we launched last year. As a result, our total unit sales of inkjet printers were at the same level as last year. Revenue, however, declined due to the impact of exchange rates.

Imaging System - FY 2016 Projection (Slide 14)

For interchangeable lens cameras, we left our projections for both the market and our own unit sales unchanged. (Market: 11.5 million units, Canon: 5.2 million units)

We announced new high-end models, starting with the flagship EOS-1D X Mark II. The new models have not only improved performance in areas such as subject tracking and image quality, but also offers enhanced features that address the strong need for video and improved networking features.

In addition, by expanding our lineup of mirrorless cameras, we have succeeded in capturing new users, including women and young individuals. Together with entry-level DSLRs, we will work to stimulate market demand and expand our market share.

We left our compact camera projections for the market and our own unit sales unchanged as well. (Market: 20.0 million units, Canon: 5.0 million units)

At the end of April, we will launch the PowerShot G7 X Mark II, our first camera to be equipped

with our latest image processor. As we work to further raise our market share, we will also take steps to improve profitability, reducing costs through the standardization of parts and other measures.

As for the inkjet printer market, although we expect the trend of contraction to continue, we left our projection for our full-year unit sales to be at the same level as last year.

We will continue efforts to expand sales of refillable ink tank models for high volume printing in emerging markets. Furthermore, we will strengthen our B2B offerings. In addition to MAXIFY, our range of business inkjet printers for SOHO customers, and our large-format printers, we are enhancing our lineup of high-value-added offerings by launching such products as our professional-model A2 inkjet printer, which we released last fall.

Industry and Others - Q1 2016 Actual (Slide 15)

For semiconductor lithography equipment, while the spread of IoT demand for communication and other related devices is rising, demand to reduce production costs is gaining traction. In this market, demand for i-line and KrF tools have been stable and we maintained unit sales at the same level as last year.

For FPD lithography equipment, we expanded sales of systems mainly used in the manufacturing of large panels.

As for network cameras, we grew sales significantly, reflecting, among other, a large contribution from the consolidation of Axis. As for the industrial equipment of Group subsidiaries, thanks to a significant increase in sales of Canon Tokki, which benefitted from strong demand for their OLED display manufacturing equipment, overall sales of industrial equipment of Group subsidiaries, which includes Canon Anelva and Canon Machinery, grew roughly 80%.

For reference, “network cameras” and “industrial equipment of Group subsidiaries” account for about 25% and 15%, respectively, within the “Others” segment of the Industry and Others business unit.

Industry and Others - FY 2016 Projection (Slide 16)

In the semiconductor lithography equipment market, we saw signs of manufacturers adjusting their production of smartphones. In response to this, customers are delaying a portion of their capital expenditure until next year. As a result, we lowered our full-year sales projection.

As for FPD lithography equipment, amid a growing trend to incorporate OLED panels into mobile devices, manufacturers have been actively investing in capital expenditure. Thus, we raised our full-year sales projection. At the same time, we also raised our projection for Canon Tokki. As a result, overall sales of industrial equipment of Group subsidiaries are projected to increase by roughly 50%.

As for network cameras, in addition to Axis’s full-year contribution to our results this year, with efforts to strengthen Canon branded high-value-added products, we expect total network camera sales to increase by roughly 40%.

For reference, network cameras and the industrial equipment of Group subsidiaries both make up about 25%, of “Others” revenue.

FINANCIAL SITUATION

Inventories (Slide 17)

Inventory at the end of March was 52 days or 5 days longer than the end of December 2015.

Merchandise inventory increased by 3 days due to the launch of new products, mainly cameras. Work-in-process increased by 2 days, reflecting, among others, preparations to install semiconductor production equipment.

Compared with the end of March 2015, however, inventory was 2 days shorter due to reduction in work-in-process of Canon Tokki's OLED display manufacturing equipment. As a result, work-in-process declined from 17 days to 15 days.

Capital Expenditure / Free Cash Flow (Slide 18)

We expect free-cash-flow to be negative 420 billion yen for the full year. This is related to the acquisition of Toshiba Medical Systems Corporation.

For the acquisition, we raised funds through bank loans, which stood at 660 billion yen at the end of March.

Although we raised a considerable amount of funds in this way, our basic policy concerning shareholder return has not changed.

For dividends in particular, while our projection for this year's dividend remains undetermined, we will continue our focus to provide a stable and active profit return which has been and remains our management policy.

Cash on Hand (Slide 19)

Cash-on-hand at the end of the year is projected to be 690 billion yen, as funds for the aforementioned acquisition have been secured through bank loans.

Closing

Due to the severe external environment, characterized by such factors as the yen's appreciation since the beginning of the year, we revised our projections and now expect full-year net sales and profits to be below that of last year.

Canon will focus efforts on its major strategies of Phase V of the Excellent Global Corporation Plan, for instance, expanding future growth driving businesses, such as commercial printing and network cameras, and thoroughly working to improve profitability of its existing businesses such as laser printers and cameras, which are and will be stable earning bases.