

FY2018 Full-Year Financial Results Presentation

Q&A

Overall

Q: What is the thinking behind the share repurchase that you announced?

A: We have had a high level of capital expenditure over the past several years. Although this trend will continue in the 2019 fiscal year, we anticipate a lower level of capital spending in the 2020 and subsequent fiscal years. As for free cash flows, the collection of cash was somewhat delayed in 2018 fiscal year, but we plan to recover them in the 2019 fiscal year.

Epson seeks to transform office printing by accelerating the replacement of laser printers with inkjet printers. We decided to repurchase Seiko Epson shares after taking into account the current share price compared to the future increase in corporate value that this growth strategy will yield.

Q: The consolidated number of employees has increased by about 10,000 people over the past three years. What factors contributed to this increase?

A: The number of people employed by our overseas manufacturing companies has increased. The new factories in Indonesia and the Philippines were supposed to be highly automated, but automation has not kept pace with the increase in production. This is the main reason for the increase in employee headcount.

The key to greater efficiency is the automation of logistics and inspection processes. Inspection processes, in particular, will be thoroughly automated over the next three years.

Printing Solutions

Q: Can you explain the nature of the accounting change involving printheads?
What effect will this change have on business profit?

A: Epson formerly allocated printhead inventory to the product lines where Epson intended to finally use them, and the net realizable values of the inventories were calculated by product line after allocation, resulting in the recording of inventory devaluations for the inventory allocated to ink cartridge model product lines.

In recent years, Epson has shifted toward an emphasis on high-capacity ink tank printers rather than ink cartridge printers. This shift has resulted in improved inkjet printer unit profitability. Meanwhile, it has become more difficult to identify product lines at the printhead manufacturing stage due to the expansion of external printhead sales and the emergence of a more diverse range of printhead applications. Epson therefore changed the method used to calculate the net realizable value of printheads to better reflect the current business reality. As a result, inventory devaluations are not recorded for printhead inventory, so compared to the former method, the cost of sales decreased by ¥5.4 billion and business profit increased by the same amount.

This accounting change will primarily affect the printer business, in addition to a much smaller impact on the professional printing business.

Q: Will this accounting change alleviate fluctuations in quarterly financial results caused by fluctuations in ink cartridge printer model production volume and the balance of profits between the first half and second half?

A: This change only alleviated the portion associated with printheads. Ink cartridge printer units will still be subject to devaluations moving forward.

As a result, the impact of production volume fluctuations on financial results will not be entirely dispelled. However, the size of fluctuations will be reduced by the amount associated with printhead devaluation.

Q: How was the sales situation for high-capacity ink tank printers?

A: In the 2018 fiscal year, sales trended downward in Latin America, particularly from the second half. Sales were affected by a slowdown in economic activity and by competition.

In the fourth quarter, there was instability in some regions, including political instability in Mexico and a steep drop in the value of the Argentine peso, among other things. However, signs of a rebound in sales were seen in places such as Brazil as we stepped up our sales efforts and increased promotions for high-capacity ink tank printers.

Inventory adjustments by dealers/distributors in China in the third quarter slowed sales, but strong growth returned in the fourth quarter once inventories were normalized. Additionally, we also were able to meet online demand in the fourth quarter, compared to third quarter where we misread such demand.

Sales continued to grow in developed economies such as North America, Western Europe, and Japan, and the unit sales of Epson's high-capacity ink tank printers in these markets accounted for more than of 10% of total high-capacity ink tank printer sales.

Q : Major office printer manufacturers also launched linehead inkjet printers. What do you think of this move?

A: The important thing for Epson is the extent to which inkjet printers replace laser printers. The challenge is getting customers to understand the advantages of inkjets. So having a large number of players launch and advertise new inkjet models is a good thing in terms of Epson's strategy.

Sales of Epson's high-speed linehead inkjet multifunction printers have not yet expanded to the point where they boost Epson's financial results, but our promotion efforts to date are putting us in a position to win major contracts in Japan and to environmentally conscious customers in Europe.

Sales to medical and education institutions are picking up as they come to appreciate certain features of inkjet printers, including low print costs, low energy consumption, low waste, and low dust emissions. Moving forward, we are looking to build a new business model by combining these printers with our PaperLab dry-process office papermaking system.

Q: You have forecast a decrease in profit in printing solutions for the 2019 fiscal year. What factors do you see contributing to this decrease?

Also, how are you going to use sales promotion expenses in the printer business?

A: In the long-term, we will spend as needed to further increase our presence in the printer market in order to replace laser printers with inkjet printers. Short-term, spending may outpace sales, but the profit structure should remain unchanged. In the 2019 fiscal year, we plan to spend as needed while expanding sales of high-capacity ink tank printers to 10.2 million units.

Q: What products will fuel revenue growth in the professional printing business in the 2019 fiscal year?

A: Sales of large format photo printers in existing markets have been on a downward trend for the past several years. We anticipate halting this trend but do not expect significant growth in this category. Large-format printers used for signage and business applications will be the primary revenue drivers. In addition to these, we will grow revenue from external sales of printheads.

Q: Printing solutions inventory increased at the end of the 2018 fiscal year, but what type of product inventory was involved?

A: Sales of high-capacity ink tank printers were impacted by sluggish economic conditions and political instability in Latin America. Inventory increased because we fell short of our internal plan in the first half of the fourth quarter.

We also underachieved on our ink cartridge printer sales plan, but inventory stayed at an appropriate level because we simultaneously reduced production.