
Interview with the President & CEO



Toshiaki Higashihara
President & CEO

i Social Innovation



**Hitachi aims to further advance
the Social Innovation Business and become
“An Innovation Partner for the IoT Era.”**

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How do you evaluate the 2015 Mid-term Management Plan?

Under the 2015 Mid-term Management Plan, we were able to achieve a certain degree of results. For example, we reached our target for revenues of ¥10,000 billion and significantly strengthened our cash-generating capability. Over the past three years, we recorded a stable adjusted operating income ratio at a 6% level and steadily improved our earnings. However, as with the EBIT ratio, we did not reach our target for a stable adjusted operating income ratio of more than 7%. This was primarily attributable to unprofitable projects in the overseas plant business, centered on the Middle East, and to our slow response to market changes in the telecommunications and storage businesses.

Despite slowing growth in China and in natural resource and oil-producing countries, it is likely we would have been able to achieve our targets if we had rigorously implemented project management and structural reforms. Moving forward, it will be my duty as CEO to carry out thorough measures to address these issues and place Hitachi on a stable growth track in the advanced Social Innovation Business, which will leverage the use of digital technologies.

Hitachi is aiming to be “An Innovation Partner for the IoT Era.” Would you describe the background and how to achieve this?

By leveraging IT and operational technology (OT), such as control and operation technology, Hitachi is rolling out the Social Innovation Business globally, where the Company provides advanced social infrastructure systems.

With IoT and digitalization making ongoing progress, people’s preferences and values are changing from products to outcomes, from owning to sharing, and from closed to open environments. Against the background of these changes, there are new developments in the business world. Companies need to transit from a “product-out” approach, where they supply the products that they have developed, to a “market-in” approach, where they work together with their customers to understand these customers’ issues in order to create solutions and new value.

Hitachi accurately anticipated this trend through the Social Innovation Business. Moving forward, we will maximize the leveraging of IT and OT as our strengths and lead the IoT Era through our advanced Social Innovation Business, which will draw on the latest digital technologies such as artificial intelligence (AI) and big data analytics. In this way, we will strive to contribute to improvements in people’s quality of life.

The key to these initiatives will be Lumada, the IoT platform that we launched in May 2016. We will collect larger amounts of data through the IoT, and Lumada offers a common platform for more rapidly converting this data into high-value digital solutions while promoting collaborative creation with a larger number of customers and partners. Distinctive features of Lumada include its ability to provide multiple solutions on a single platform and its open architecture, which means that Lumada can be connected to customer systems easily and extended in stages. Furthermore, Lumada utilizes secure, high-reliability technologies that have a proven track record in the Social Innovation Business.

In April 2016, we launched a new business structure that is more market-driven. Under this new structure, the front, which consists primarily of 12 business units, works to resolve customer issues and provides solutions in four focused business domains. The front will utilize Lumada to create a wide range of digital solutions, and by sharing use cases through Lumada, we will steadily develop our advanced Social Innovation Business on a global basis.

What is Hitachi’s approach to the optimal business portfolio?

In fiscal 2016, we will examine our low-profitability businesses and clarify which businesses we will reinforce and which we will dissolve. In addition, under the 2018 Mid-term Management Plan, we will focus on the Social Innovation Business, which will leverage the use of digital technologies toward the next growth stage. For example, through investments and M&A we will continue to build up businesses that have synergies with digital technologies such as AI and big data analytics that can generate

added value. On the other hand, in businesses that require a certain operational scale in global markets, we will move forward with business restructuring initiatives, including partnerships with other companies. Our transfers of portions of our shares in Hitachi Transport System and Hitachi Capital were examples of this approach. Going forward, we will continue to accelerate reform of the business portfolio as we work to strengthen the Social Innovation Business.

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Please explain the positioning of the 2018 Mid-term Management Plan and its targets.

The 2018 Mid-term Management Plan is positioned as a milestone for Hitachi's move up to the next stage, and on that basis we will implement management strategies with a focus on cash and profits. The plan includes ROA and operating cash flow margin as new target indicators. We will increase asset efficiency by examining low-profitability businesses and accelerating business portfolio reforms. In addition, through improvements in earnings and working capital, we will generate cash as the source of investment and link these initiatives to future growth.

Our starting point for fiscal 2016 revenues is ¥9,000 billion, primarily because Hitachi Transport System and Hitachi Capital have become equity-method affiliates. In fiscal 2018, we will aim for revenues of ¥10,000 billion through accumulated orders, such as the railway business in Europe and M&A initiatives. Moreover, we will strengthen the front, which will be a driver of our growth.

Over the next three years, we will increase the front workforce by 20,000 people, and through special training programs we will strive to develop human capital who can work together with customers to identify and resolve their issues. In this way, we will aim to have the front contribute 40% of revenues in fiscal 2018. With regard to our cost structure, our SG&A expense ratio will increase slightly due to the strengthening of our front workforce and increasing R&D expenses. Nonetheless, we will take steps to improve the gross margin by promoting cost reduction centered on products, carefully examining low-profitability businesses, and expanding service businesses by bolstering the front. In fiscal 2018, we will aim for adjusted operating income and EBIT ratios of more than 8% each and net income attributable to Hitachi, Ltd. stockholders of more than ¥400.0 billion.

Would you describe cash-generation initiatives and Hitachi's approach to investment?

Under the 2015 Mid-term Management Plan, we further enhanced and expanded the Hitachi Smart Transformation Project, a cost structure reform project, and worked to reinforce our cash-generating capability. Consequently, our operating cash flow margin* improved from 5.7% in fiscal 2012, to 8.6% in fiscal 2015. We have also instituted improvement targets for the cash conversion cycle (CCC)* at each in-house company, and we had significant achievement. We largely reduced the CCC by 10.2 days from fiscal 2014 to fiscal 2015. Moving forward, we will reevaluate cost structures and make further progress in optimization of accounts receivable collection periods, accounts payable payment periods, and inventory levels. Through these initiatives, we will strive to achieve an operating cash flow margin of more than 9%* in fiscal 2018.

In addition to increasing the operating cash flow margin, we will restructure the business portfolio and sell assets to secure cash for investment. For capital expenditure, we will carefully

select growth businesses. In M&A, we will conduct more rigorous evaluations of such factors as business synergies, investment returns, and risk, and after acquisitions we will implement thorough monitoring of investment effectiveness. In these ways, we will boost investment returns. Over the next three years, we are planning a cumulative total of ¥1,000 billion in investment, of which about 60% will be allocated to the front and platform, and about 40% to products. First, by investing in competitive products, where the CCC is relatively short, we will accelerate our cash-generating capability over a shorter time period. The cash obtained will subsequently be used to invest in the front and platform areas, which will lead to increased earnings growth over the medium-to-long term. We will implement cash management to achieve an optimal mix by carefully combining short-term and medium-to-long-term revenue sources.

* Manufacturing, Services and Others

Finally, what is Hitachi's approach to strengthening corporate governance, and what is the shareholder return policy?

Since we adopted the committee system in 2003, we have taken steps to continually strengthen the oversight function. In addition, we have worked to establish a framework for reflecting a global, diverse viewpoint in management. Since June 2012, outside directors have been a majority of the Company's Board of Directors, and in June 2016, the number of non-Japanese outside directors was increased by one. Currently, 9 of the 13 directors are outside directors. Moreover, 5 of the outside directors are non-Japanese.

Hitachi's Board of Directors is composed of professionals who are active in various fields with experience at the CEO level. Meetings of the Board of Directors include vigorous exchanges of opinions on such matters as the strategies that Hitachi should implement and points of differentiation from competitors, as well as advice based on the directors' philosophies as management leaders and on their past experience. In these ways, the meetings foster enhanced awareness and motivation. The courses of action that are shared at meetings of the Board of Directors are aggressively reflected in management's subsequent actions.

Going forward, we will continue taking steps to strengthen corporate governance, such as complying with all the principles for companies under the Corporate Governance Code that took effect in Japan in June 2015.

Regarding the shareholder return policy, we are now in a phase of investing for future growth, and we need to continue to implement aggressive investments to succeed in global competition. We will strive to achieve stable growth in dividends by increasing net income attributable to Hitachi, Ltd. stockholders and cash flow.

In addition, we have introduced stock options as stock-based compensation, thereby having management leaders share the benefits and risks of stock price fluctuations with shareholders. In doing so, we aim to advance management based on a medium-to-long-term perspective and achieve sustainable improvements in corporate value.

