

## President Sakuta Discusses Omron's Future

### "Downsizing for Success" and our Motto, "Change! Challenge! Create!"



Hisao Sakuta,  
President and CEO

**Q** Please explain the "operating income of positive zero" objective for fiscal 2009.

#### "Operating Income of Positive Zero" is "Downsizing for Success"

We have been aiming to achieve an operating income margin of 10% as a validation of a solid profit structure. We saw our income margin peak at 9.9% in fiscal 2005; however, we only expect to maintain a breakeven margin in fiscal 2009.

We have opted to refer to it as "positive zero" rather than simply "zero" profit. The reason behind this is that instead of becoming apathetic and randomly cutting costs and investments to strike a balance between income and expenses, we will maintain certain costs and continue investing in what is necessary for the Company's future and to nurture our competitive merits. In other words, we strongly believe we must forge

ahead with "downsizing for success." Another aspect of this approach is to be humble yet with a positive frame of mind for "starting fresh from zero."

FY2008 Actual and FY2009 Plan

(Billions of yen)

	FY2008 Actual	FY2009 Plan
Net sales	627.2	510.0
Gross profit	218.5	175.0
SG&A expenses	164.3	135.0
R&D expenses	48.9	40.0
Operating income	5.3	0
Non-operating loss, net	-44.4	-3.5
Net loss before taxes	-39.1	-3.5
Net loss	-29.2	-2.0

**Q** What are the key emergency measures for achieving operating income of "positive zero?"

#### Cutting Fixed Costs by ¥55 Billion and Variable Costs by ¥5 Billion

We are implementing emergency measures to cut approximately ¥60 billion in costs in fiscal 2009. We also plan to reorganize both our business domains and management structure as part of an extensive reform of our operating structures, with the aim of lowering manufacturing fixed costs and variable cost ratios and setting the foundation for fortifying our earnings base for the medium and long term. Specific measures will include cutting labor costs by rescinding a portion of director compensation and management salaries, setting up performance-based salary systems, and restricting overtime work. Since the Company is essentially in crisis mode, we will strictly limit spending, including even R&D expenses, and restrain capital investment for the future unless there is specific objective and a clear schedule for producing return. Advertising

costs, overhead costs, and other peripheral outflows will also be limited to the bare essentials.

Also, steps taken in fiscal 2008 to lower goodwill and property, plant and equipment are beginning to produce results, including reducing depreciation costs. We estimate that these measures will put us on track to cut approximately ¥55 billion in fixed costs. Additionally, we plan to lower variable costs by approx-

FY2009: Items for Improvements in Profit & Loss Structure

	Target value (approx.)
Reduce fixed costs	¥55 bn
• Labor costs, overhead costs	
• Depreciation (restraints on investment)	
• Depreciation (impairment of fixed assets)	
Reduce variable costs	¥5 bn
• Raw material costs and others	

imately ¥5 billion by reducing spending on raw materials and other items.

We are also preparing to consolidate our large-scale liquid-crystal backlight operations and have made the decision to shut down six domestic and overseas

**Emergency Measures**  
(Generate profit in FY2009 through cost cuts)

**Profit Generation**

[1] **Cost cutting**  
Advertising, R&D, indirect costs, etc.

[2] **Withdrawal from underperforming businesses**  
Four businesses in Japan/abroad (ECB, AEC)

[3] **Reduction of other fixed costs**  
Return of part of directors', executive officers', and managers' compensation, ban on overtime work, etc.

**Cash Flow Creation**

- Freeze on large-scale investments
- Reduction in ordinary investments

production sites of semiconductor products, automotive components, and other products. The effects of these measures should begin appearing in fiscal 2009 and contribute to further lowering fixed costs and other expenses.

**Structural Reform**  
(Strengthen profit base over the medium term)

**1. Business Domain Reform**  
Restructure 3 control-based businesses: IAB, ECB, and AEC

- IAB: Strengthen front line and profit base
- ECB: Re-strengthen mechanical components business
- AEC: Implement thorough efforts to improve profitability

**2. Operational Structure Reform**  
(1) Elimination and consolidation of production bases, (2) variable cost structure reform, (3) IT structure reform, (4) head office function reform

## Q How will you reorganize the Company's business domain?

### Restructuring Core Segments (IAB, ECB, and AEC) to Consolidate Strengths

We have redefined our business domains as industry, society, and lifestyle and will accordingly realign the business structures of the three core segments—IAB (Industrial Automation Business), ECB (Electronic Components Business), and AEC (Automotive Electronics Business)—, which in fiscal 2008 contributed approximately 75% of Omron's total sales.

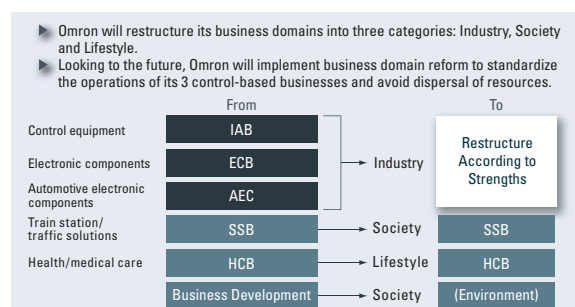
Our aim is to enhance the usage efficiency of management resources and fortify the individual business strengths of each segment by reorganizing the three core segments in the industry domain. Specifically, we will strengthen the marketing capabilities of IAB, fortify the production and development operations of ECB, and spin off AEC segment operations to enable each business to develop to full strength.

Omron is a collection of diverse strengths and weaknesses. While we are fully aware of our many weaknesses, rather than seeking to shore up our weak points, we are restructuring with a focus on making our strengths even stronger. We are seeking to strengthen IAB's marketing capabilities, using distri-

bution channels for general-purpose products and to enhance our global production and technical capabilities for control devices used in mechanical components (relays, switches, connectors, and other electronic components used in machinery), which are fundamental to all three main control-based businesses.

We anticipate growing demand for mechanical components in the BRICs and other emerging economies. However, the market environment is changing and competition is intensifying, particularly from Chinese companies. We are therefore taking steps to fortify our leading position now to ensure our continuing competitiveness in the future.

### Business Domain Reform



## Q What other specific steps will be taken to consolidate strengths?

### Strengthening IAB Marketing Capabilities and Fortifying ECB Production and Development

We have extensively discussed whether the best marketing strategy for IAB would be to conduct direct sales or use distributor sales channels. We believe a distributor-based sales structure is the most effective for broadening sales of general-purpose products like mechanical components to a large number of users. Moreover, IAB uses this sales structure very effectively and has become the industry's top supplier of

mechanical components on a global scale. IAB is also very strong in Quality, Cost, and Delivery (QCD), which is essential to remaining a leading competitor in mechanical components field.

From this perspective, consolidating our strengths means shifting human resources to augment IAB's domestic sales and marketing capabilities and developing more deeply integrated operations with distributors. We plan to fortify IAB operations primarily by adding approximately 300 people, representing

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a roughly 50% increase in staff, and creating stronger alliances with domestic distributors. We also plan to integrate the sales and marketing functions of ECB's distribution channels into IAB.

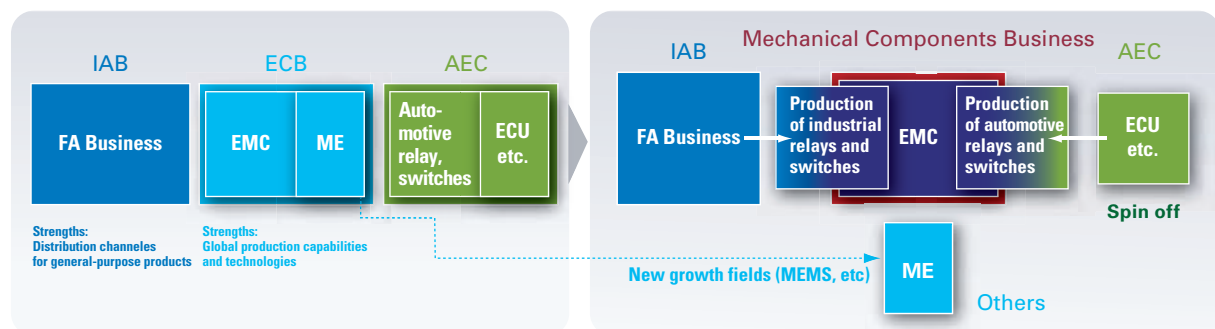
Omron's share of the domestic market for control equipment remains solid at roughly 40%, according to Nippon Electric Control Equipment Industries Association standards, but it has slipped by five percentage points over the past 10 years. Our performance objective is to regain market share of 45% over the short term.

We have decided to have ECB focus its expertise on mechanical components and rename the segment the Electronic and Mechanical Components (EMC) Business Company, with the new name taking effect in September 2009. EMC will take over the develop-

ment and manufacturing of mechanical components currently conducted in each of the IAB, ECB, and AEC segments to provide integrated development and manufacture of industrial, consumer electronics, telecommunication, and automotive relays, switches, and connectors.

With ECB focusing on mechanical components, micro electronic (ME) components operations will be shifted from ECB to the Others segment. Micro electronic components encompass liquid-crystal backlights and micro electro mechanical systems (MEMS), to which Omron has dedicated significant effort to date. ME is rapidly developing into a new growth field and will be under my direct supervision as we aggressively develop and expand our ME operations.

Consolidating strengths of the three main control-based businesses



FA: Factory Automation EMC: Electronic and Mechanical Components (Electronic mechanical components, such as relays, switches, connectors, etc.) ME: Micro Electronic components (Electronic components, MEMS, and other electronic components such as liquid-crystal backlights, etc.) ECU: Electronic Control Units (Automotive electronic control units)

**Q** The three main control-based businesses remain susceptible to economic fluctuations. What steps have been taken to address this issue?

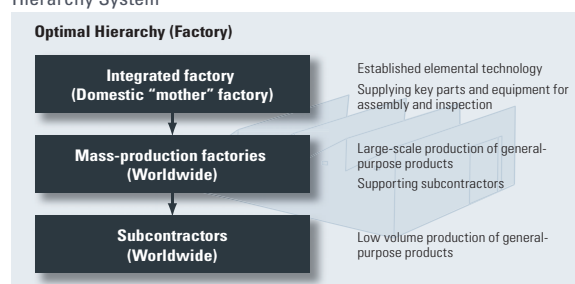
### Building a Production Structure Resilient to Fluctuations in Demand

The industrial sector is the main market for IAB, ECB, and AEC and, for that reason, their results are inevitably prone to fluctuate with the economy. We can, however, take steps to make them more adaptable to changes in the business climate by dispersing operations geographically and diversifying business content. Nevertheless, the global recession has made this susceptibility glaringly apparent. While acknowledging that an impact is inevitable during periods of growing economic uncertainty, we must urgently increase their resilience to fluctuations in demand.

One step, which we will take while concurrently ramping up production capacity for EMC, will be to create an optimized, hierarchical manufacturing system. We are gathering our specialized technologies in materials, processing, metal molds, and other areas into our integrated "mother" plant in Japan. These technologies form the nucleus from which arises the unmatched strength of Omron's products. From this

centralized factory, we will then supply products, assembly equipment, and inspection equipment to mass-production plants and subcontractors around the world. We will also retool our second-tier mass-production factories around the world for mass production of general-purpose products and continue supporting our subcontractors in other regions by commissioning small-scale production of general-purpose products. This three-tier hierarchy of manufacturing operations will further raise QCD while remaining resilient to fluctuations in demand.

Efficient And Strengthened Production Capabilities by Three-tiered Hierarchy System



## Q How will AEC be transformed in light of the huge impact the global recession has had on the automotive industry?

### **AEC to be Spun Off to Leverage Autonomous Management and Collaborative R&D, and Operations Catered to the Automotive Industry**

Worldwide automobile production has been rapidly declining since reaching a peak in 2007. The industry has been simultaneously undergoing a major transition, bringing rapid growth in demand for compact cars and eco cars along with an increasing need for electronic components. From a long-term perspective, this shift presents a business opportunity for AEC. However, since increasing sales is meaningless if the business still produces a loss, going forward AEC must stress the distinct strengths of its automotive products.

We are therefore reorganizing AEC by shifting the mechanical components operation to ECB and focusing AEC resources on developing its distinct strengths in electronic control units (ECUs) and other automotive electronics. AEC will continue developing ECUs on Omron's sensing and control technology with a focus on electronic equipment for auto bodies that will contribute to the realization of comfortable and easy-to-use automobiles. The primary focus will be power window switches and keyless entry systems along with next-generation automotive systems, such as

passive entry and engine push-start systems (please see page 37 for details). Our strategy is to raise profitability by focusing on specific technologies with worldwide applications.

In addition, automotive electronics are being used in a wider range of applications as the industry rapidly advances development of hybrid vehicles, electric cars, and other environmentally friendly automobiles. As the applications become more diverse, the technology is becoming increasingly sophisticated and complex, raising the importance of vigorous and flexible collaborative R&D and operations with other companies.

The changes in the automobile industry have made it vital that we modify our previous approach of some Omron Group companies supplying automotive parts to all clients on an equal basis. To this end, we plan to promote the transformation of AEC into a highly specialized company that specializes in electronic equipment for auto bodies by spinning it off in April 2010 to leverage the benefits of autonomous management, the ability to concentrate on core clients, and greater latitude for collaborations with other companies for product concept generation and business realization.

## Q What operational reforms will be implemented as part of Omron's structural reform?

### **Four Areas of Management Reform**

Management reform will be carried out in four categories. First, we will consolidate our 49 domestic and overseas production sites and reduce the number of sites by one-third. Six production sites are now being shut down, including the Minakuchi Factory (semiconductor manufacturing operations were shifted to the larger Yasu Factory) and the automotive electronic components manufacturing facility in England (we are continuing to meet demand in Europe through exports from other factories). We will keep implementing management reforms as necessary.

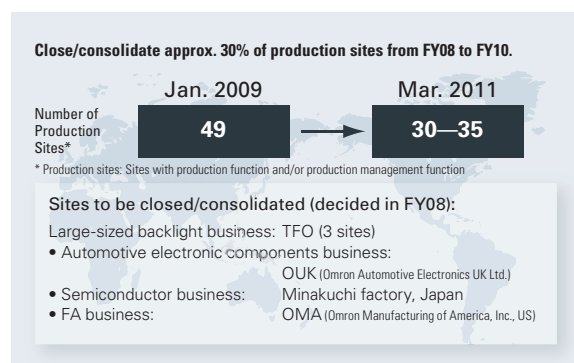
The second operational reform will be to revise the variable costs structure. We will continue to develop common product formats and to progress with standardization. At the same time, we will reduce the number of parts that must be purchased, conduct bulk purchases to lower materials costs, and decrease the number of man-hours necessary for inspection of components, quality assurance, and final product inspection. Through these measures, we are aiming to lower the variable cost ratio by 2.5 percentage points by fiscal 2011 in comparison to fiscal 2008.

Third is reform of our IT structure. We began reforming the Group's IT structure in fiscal 2007 with the aims of improving our administrative efficiency

and establishing an infrastructure for information sharing throughout our worldwide manufacturing, sales, development, and finance operations. We have budgeted ¥10 billion for investment over a four-year period and expect to have a new IT infrastructure in full operation in fiscal 2010.

The fourth operational reform concerns the functions of the head offices. We will take a scalpel to the swelling administrative expenses incurred at the head offices as our global operations expanded. The head office staff activities will be divided into support and strategic functions and strictly evaluated for necessity and value to trim any and all excess.

#### Closure/Consolidation of Sites



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### Q Is the Company advancing any growth strategies in new areas?

#### Activating Omron Group Synergies for Full-fledged Entry to the Environmental Business

We believe the Omron Group has unique capabilities to help tackle pressing environmental issues. Responding to global warming and other environmental issues is critical for the future of humanity, and it has been estimated that by the year 2050 we must reduce total global emissions of greenhouse gases (CO<sub>2</sub>), by half of the year 2000 level. Achieving this presents a major challenge that will require groundbreaking new technology and ideas. From our point of view, this is the type of challenge that is perfectly suited for developing new businesses for our environmental business.

In March 2009, we established and commenced full-fledged operations of the Environmental Solutions Business Headquarters, which is under my direct supervision. The headquarters is focusing on providing CO<sub>2</sub> emission reduction solutions for retail stores, factories, distribution operations, offices, schools, and

various other sites and developing total environmental solutions to help clients realize their environmental management objectives.

The Omron Group had previously been developing environmental businesses for CO<sub>2</sub> emission reduction through each of its business segments. The Environmental Solutions Business Headquarters works laterally with IAB, ECB, and other business segments to integrate components used in each segment's environmental solutions operations. It also develops solutions by identifying areas to monitor and provides specific control solutions to further reduce CO<sub>2</sub> emission volumes.

Environmental business is a new direction that will leverage the synergies of the Omron Group. We are aiming for the environmental business, including the contribution from the Environmental Solutions Business Headquarters, to generate ¥50 billion in sales in fiscal 2013.

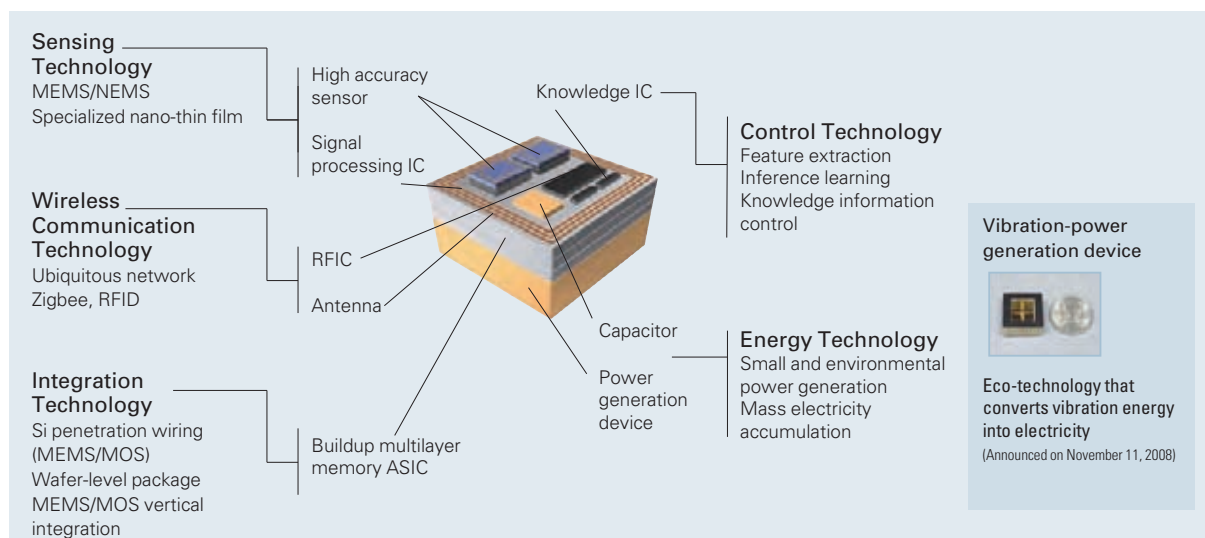
### Q What other growth fields are you focusing on in addition to the environmental business?

#### Actively Developing Sensor Networks, MEMS, and Vision Sensing

Advances in sensing technology are increasing the range of potential applications and generating a shift in needs from basic sensing and control functions to information management functions aimed at fulfilling specific objectives. Sensors are playing an increasingly central role for supporting administrative functions related to safety, product quality, equipment lifecycles, work environment, and the health and behavior of people at manufacturing sites as well as across the broader spectrum of industry, society, and lifestyle. This is evident in the intense interest that has been generated in our face recognition systems (see page 25 for details).

I am speaking in futuristic terms, but we are conducting research in several areas to expand and advance sensor applications, such as further integrating our MEMS technology into sensor networks (intercommunicating sensors) and autonomous sensors required for household electric power generation devices. I also believe we are moving closer to realizing vibration sensors that can sense the changes in vibrational activity that occur as structures age and can be used in bridges or buildings for safety and prevention against structural collapse. These sensors could also be paired with permanent sensor systems that can generate electricity from extremely subtle vibrational movement.

Technology Driving Future Growth: Progress in Sensing



## Q What are the Company's policies regarding capital, such as its shareholder return and financial policies?

### Reinforcing Our Defense with Loans and Improving Cash Flow

Omron's policy on the distribution of profits is to provide the maximum amount possible to shareholders from the Company's surplus cash account after determining that sufficient funds are maintained for internal reserves for essential R&D, capital investment, and other business growth-related investment, and in consideration of the current level of free cash flow. Our policy is to maintain a minimum 20% dividend payout ratio and to target 2% dividend on equity (DOE) ratio.

In fiscal 2008, taking into consideration the result of a ¥29.2 billion net loss, we distributed ordinary dividends of ¥25 per share, representing a ¥17 decrease from the previous fiscal year and a DOE ratio of 1.7%. We have not yet set the dividend rate for fiscal 2009 as we feel it is prudent to wait until we have a better idea of how business conditions will develop and how the Company is progressing toward its forecast targets in this environment.

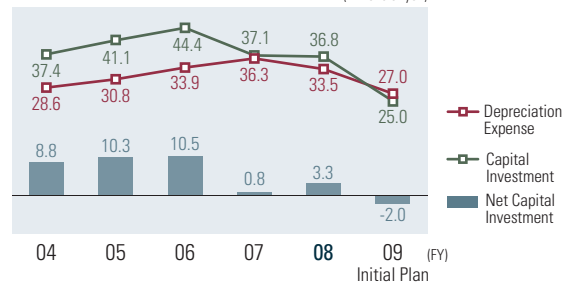
Our financial policy at present is to preserve our cash holdings to ensure we are fully prepared for unanticipated contingencies. In fiscal 2008, we secured approximately ¥20 billion in long-term loans for this purpose. In fiscal 2009, we plan to improve total cash flow by approximately ¥25 billion by lowering inventories (¥15 billion) and reducing capital investment (¥10 billion). In accordance with the anticipated ongoing decline in sales in fiscal 2009, we plan to reduce



R&D expenses by ¥8.9 billion and reduce the proportion of R&D expenses to sales down to 7.8%.

Investment in R&D is directly related to investment in business growth and is not usually an area where we would want to economize. Given the current economic environment, however, we are concentrating R&D spending on fortifying our competitiveness in mechanical components and in specific fields with strong growth potential, particularly MEMS and environmental businesses.

Depreciation Expense and Capital Investment (Billions of yen)



## Q How will Omron be changed when it emerges from this difficult period?

### Operating Income of ¥100 Billion when Sales Recover to ¥750 Billion

When we reached our high point for operating income—¥65.3 billion in fiscal 2007—the Company had been in business for 75 years. For fiscal 2009, a mere two years later, we are challenging ourselves to attain positive zero operating income. Nevertheless, as we discussed earlier, we are approaching this as “positive zero” because it will represent a significant structural reform achievement.

We plan to steadily reinforce our profit structure and substantially lower our breakeven sales point as foundational steps for the Company's future. Our specific goal is to reform and improve our profit structure so that when we raise sales back to the ¥750 billion level achieved in fiscal 2007, our profit structure will yield operating income not of ¥65.3 billion but surpassing ¥100 billion.

The Omron Group is not content to bow our heads and wait for the storm to blow over. We are forging ahead with our heads held high as we put into practice our motto— “Change! Challenge! Create!”

### Strengthen Profit Base in the Medium Term

