

## Interview with the President & COO



We take on  
the challenge of creating  
future innovation.

**Toshiaki Higashihara**  
President & COO

### **What is your opinion about the progress of the 2015 Mid-term Management Plan?**

The Hitachi Group is recording steady gains in earning power, and we have achieved record-high operating income for two consecutive years. We are currently targeting an overseas revenue ratio of more than 50%, and this is within our reach. Also, regarding the Hitachi Smart Transformation Project, a cost structure reform project, the cumulative cost reduction benefits from this project for five years are expected to exceed our target of ¥400.0 billion.

As a result, I have had a profound sense that the Hitachi Group has started to see results from its reform initiatives. On the other hand, the issues we face in recording additional growth have also become clear. First, we must achieve further improvement in our earning power. Single-digit profit margins will not be sufficient for the Hitachi Group to succeed in competition, record growth, and thereby increase its corporate value. The 2015 Mid-term Management Plan is a milestone on the path to future growth. We will enhance the earning power of the Hitachi Group by implementing aggressive initiatives on a global basis and by steadily advancing reforms during ordinary times, such as rigorous structural reforms for certain businesses for which growth is not expected.

Another urgent issue is the bolstering of our ability to generate cash. Since October 2014, we have been working to further deepen and enhance the Hitachi Smart Transformation Project and implement initiatives focused on cash generation. Accordingly, we are reevaluating business processes from demand forecasting to service provision from an end-to-end perspective. We are also promoting reforms in supply chain management to increase overall operational efficiency. At the same time, we are taking steps to visualize our overall cash flow and to optimize collection and payment periods for accounts receivable and accounts payable as well as inventory levels. In these ways, we will improve the cash conversion cycle. By further raising our earning power and strengthening our ability to generate cash that is the source of growth, we will accelerate Hitachi's growth trajectory.

## Hitachi is focusing on the Social Innovation Business. Specifically, could you describe what types of businesses are involved in this field?

Even on a worldwide basis, Hitachi is a unique company because we have both IT and social infrastructure businesses. The Social Innovation Business resolves issues faced by society and customers through innovation that combines both IT and social infrastructure, thereby contributing to improvements in people's quality of life.

For example, we are providing packages that combine rolling stock and maintenance services for a railway project in the U.K., which is a good example of the integration of the IT and social infrastructure businesses. Through the collection and analysis of big data from the hundreds of sensors that are installed on each train set, we can offer advanced maintenance services, such as predictive diagnostics that can help prevent breakdowns. In this way, stable operations and

reductions in operating costs are realized. In 2009, we supplied the U.K. with Class 395 high-speed trains, which have sustained stable operations since that time. This rolling stock significantly reduces the amount of time passengers spend on trains. As a result, we have received favorable feedback from many customers. One grateful commuter said, "I am now able to spend more time enjoying breakfast with my family thanks to substantial reduction in commuting time."

In these ways, the Social Innovation Business simultaneously realizes both economic value and social value by resolving problems faced by society and customers. In addition, it is a business that can ultimately contribute to improving the quality of life for individuals who are the customers of our customers.

## To enhance and expand the Social Innovation Business, the Company will strengthen three functional layers: front-line function; analytics and control function, which form a common platform; and product, software, and service function (hereafter, product function). Would you describe the background to this approach and the specific initiatives that will be implemented in the future?

### Strengthening front-line capabilities

Previously, Hitachi was a "product-out" type of company that made high-quality products and then, subsequently, sold them to customers. However, to resolve the issues faced by customers and society, it is essential that we take a "market-in" approach, where we first identify what customers need and which direction we should take, and then create solutions through a process of collaborative creation. Front-line functions play the lead role in these initiatives and, accordingly, we are strengthening these functions in each industry and region.

Applying this approach to business sectors, we have integrated our various front-line functions and established new in-house companies in the fields of healthcare and energy. Also, for IT services in fields such as finance, public & government and social infrastructure, we have consolidated the front-line functions including sales, engineering, and consulting units, which had previously been distributed throughout the Hitachi Group. Through these initiatives, we have reinforced our ability to address challenges.

We are also using this approach with regard to global management. On April 1, 2015, I appointed Chief Executives to serve as representatives of the Hitachi Group in four regions: the Americas, China, Asia-Pacific, and EMEA-CIS. We are accelerating the establishment of a system for *Autonomous Decentralized Global Management*, under which each regional Chief Executive autonomously takes the lead in

business activities. The Chief Executives are implementing projects with the authority to make investments and the responsibility for profit and loss. In regard to R&D, project finance, procurement, and other areas, we will maximize utilization of the Hitachi Group's shared resources on a global basis.

We have also reorganized the R&D structure to reflect a "market-in" approach. The Global Center for Social Innovation, which has been established in Tokyo, North America, China, and Europe, is not a place for technical development but rather a place to work together with customers on the front-line in order to identify issues and find solutions. We will promote collaborative creation with customers by utilizing a variety of means and tools. These include "Kizashi," by which we can forecast future social trends and search for new business areas, based on political, economic, social, and technological factors in a region, and "Cyber PoC\*," a simulation tool for verifying total return on investment, such as the capital expenditures and operating costs necessary for solutions.

\* POC: Proof of Concept

### Strengthening analytics and control capabilities

We are moving ahead with establishing and strengthening common platforms, such as those for big data analytics and control, which are the source of competitiveness for the solutions we provide on the front-line.

Regarding the analytics function, in May 2015, we acquired Pentaho Corporation, a big data analytics software company in the U.S. Moving forward, we will increase the value of our solutions by applying Pentaho's common platform for big data utilization to a variety of industries, such as healthcare and energy.

In the control function, Hitachi has the technologies and know-how to create autonomous decentralized systems. These systems can continue to operate even if a portion of a system breaks down, and they can also be expanded in a phased manner. Hitachi has already achieved strong results with these systems in a variety of fields. These include East Japan Railway Company's Autonomous Decentralized Transport Operation Control System (ATOS), in which I was previously involved, as well as systems for the steel industry. In the future, we will work to generate more sustained, efficient solutions through "symbiotic autonomous decentralized" systems, where systems in different fields, such as railways, energy, and water, are connected in stages and work together on an overall basis.

### **Strengthening product capabilities**

If a business has products that can succeed on a global basis, then the competitiveness of solutions that utilize those strong products will all be enhanced.

With this in mind, in May 2015, we established the Industrial Products Company, which incorporates the medium-scale and large-scale industrial equipment businesses that had previously been spread throughout the Hitachi Group. Products include motors, inverters, substation control devices, compressors, and pumps, which are the core components of infrastructure systems.

In addition to promoting product businesses that have a comparatively short cash conversion cycle, we will create optimal combinations of these businesses and social infrastructure businesses, which have a long cash conversion cycle. This approach will contribute to the stable generation of cash over the medium-to-long term.

## **What is the Hitachi Group's approach to the optimal business portfolio?**

Business portfolio reevaluation is a never-ending process. Can we increase value through combinations with IT? And by doing so, can we resolve the issues faced by society and customers and contribute to improvements in people's quality of life? We are continually reevaluating our business portfolio to further strengthen our front-line function, analytics and control function, and product function, all with these questions in mind.

In product businesses, in addition to taking steps to enhance our own competitiveness, we have the option of collaborating with partners or utilizing joint ventures. For example, in the railway business, the Hitachi Group provides a comprehensive range of services, including rolling stock, signals, operational management, maintenance, IC tickets, and seat reservation systems. In these types of businesses, we will

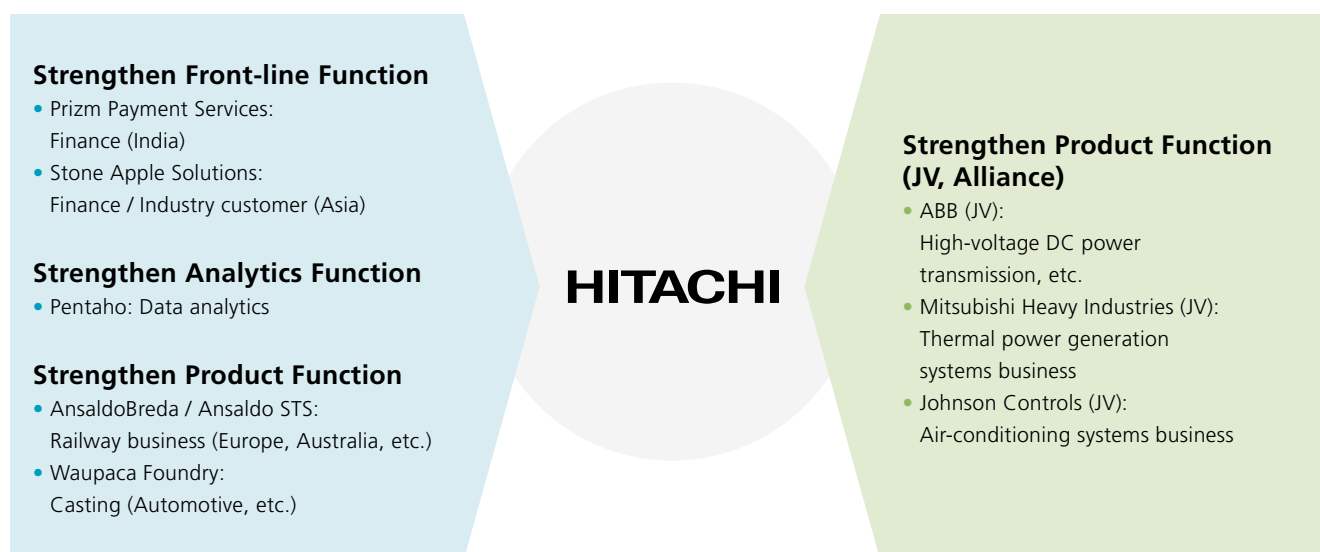
take steps to increase the competitiveness of our product businesses while working aggressively to incorporate external resources, such the acquisition of Italian companies that manufacture rolling stock and signaling systems.

On the other hand, in regard to businesses where a certain scale is needed on a global basis, we will aggressively advance partnerships with companies that are global leaders. For example, we have established a joint venture with Mitsubishi Heavy Industries, Ltd., in the thermal power generation systems business and will establish another joint venture with Johnson Controls, Inc. of the U.S. in the air-conditioning systems business. In addition to raising the competitiveness of the products themselves, we will increase the value of the total solutions that utilize those products.

In this way, with an ongoing focus on businesses that we need to strengthen on our own and businesses for which we will increase competitiveness through partnerships, we will move forward with business portfolio reforms that are more transparent to external stakeholders.



## Acquire necessary resources (customer base, sales channel, technologies) for growth, optimize business portfolios and increase revenue



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

Hitachi adopted a committee system in 2003 and, since that time, we have worked continuously to strengthen corporate governance. Outside directors have been a majority of the Board of Directors since June 2012 and, currently, 8 of the 12 directors are outside directors. Moreover, four of the outside directors are non-Japanese. The outside directors have extensive knowledge, including management experience at global companies. They offer frank opinions, ranging from corporate strategy to issues of each business and product such as growth scenarios for the Hitachi Group, cash flow, and market positioning. As a result, other Company executives and I have become aware of a wide range of issues, and we have been able to utilize these findings in management initiatives. The executive officers, who fulfill the business execution function, and the outside directors, who fulfill the management oversight function, conduct deliberations together in an

open manner, and the opinions of the outside directors are actively reflected in management, without being restricted to the status quo.

In regard to shareholder return, in fiscal 2014, against a backdrop of steady gains in earning power, we raised the annual dividend ¥1.5 per share, to ¥12.0. Moving forward, we will strive to improve our profitability and strengthen our financial position. Our policy will be to target sustained growth through continued investment and to provide stable returns to shareholders. We will respond appropriately to the Corporate Governance Code that was applied in Japan in June 2015, and we will implement management with a greater awareness of ROE and other indicators of capital efficiency. In these ways, we will strive to strengthen corporate governance in an ongoing manner and to increase shareholder value.