

Message from the CEO

Overcoming the COVID Crisis Through Selection and Decentralization Management Based on the OMRON Principles to Survive and Thrive in the New Normal Era

September 2020
President and CEO

Yoshihito Yamada

In 2020, 12 years after the global financial crisis of 2008, the world was suddenly beset by a new threat in the form of the novel coronavirus, COVID-19. President and CEO Yoshihito Yamada believes that OMRON will continue to survive and thrive in the new normal era, when the unforeseen has become the norm.

Mr. Yamada has heralded a new concept, Selection and Decentralization for a unique OMRON style of management based on the OMRON Principles. We spoke to him about his resolve to open the way to the future.

(Interviewer: Integrated Report Production Team)

What is Needed to Overcome this Unprecedented Crisis

— **Editor: The global COVID-19 pandemic has dealt a more devastating blow to the global economy than the 2008 global financial crisis. What is your view of the situation?**

When the spread of the novel coronavirus reached global pandemic proportions, demand fell around the world, and this has cast a shadow over all industries. I am prepared for the likelihood that the damage to the global economy will be further intensified going forward. Employment will become unstable and personal consumption will be adversely affected. Businesses may also be plunged into even more dire straits. We have truly entered an age of the “survival of the fittest.” On the other hand, the crisis has also resulted in major leaps forward. Take healthcare, for example. Progress in telehealth had previously been hampered by various regulations, but it has now advanced considerably on a global scale. In production settings, there are growing needs for new kinds of labor-saving through collaboration between human workers and robots, to ensure social distancing and protect the health of workers. In this way, we are seeing two changes occurring simultaneously—a decline in total demand and a stirring of new demand. OMRON will address these changes head-on and continue to survive and thrive in this age of survival of the fittest.

— **Most of us have heard of the term, “selection and concentration,” but you recently signaled an interesting new concept of “selection and decentralization.” What meanings and aims are embedded in this concept?**

This concept of selection and decentralization is something that OMRON has been pursuing for some time. For OMRON, *selection* refers to choosing those business areas in which we can leverage our core technologies, based on the OMRON Principles. In the course of that selection, we clearly distinguish domains in which OMRON itself will engage and areas in which OMRON seeks to work together with collaborators and partners. *Decentralization*, on the other hand, means to establish multiple “pillar businesses,” instead of relying on a single particular business, customer, or country. In today’s highly uncertain environment, dependence on just one particular business, customer, or country increases risk. With multiple pillar businesses that are independent of each other, we can diversify risk, and, by connecting these pillar businesses organically, we can create a more resilient organization. Ordinarily, the global deployment of multiple businesses would adversely affect efficiency. However, OMRON has the OMRON Principles,

which are our common values, so even with the individual organizations acting independently, they can still create synergy. Decentralization also includes the concept of diversity. What to select, how to decentralize, and how to incorporate diversity. These questions are constantly on our minds as we work to bring resilience to our business portfolio.

In fiscal 2019, OMRON made the significant decision to sell off its Automotive Electronic Components Business. This was the result of *selecting*, as our engines for future growth, our Industrial Automation Business (IAB), Healthcare Business (HCB), and Social Systems, Solutions and Service Business (SSB), as well as the Electronic and Mechanical Components Business (EMC), which supports these three businesses. The vision we are aiming for is to make firm profits with these four (3+1) pillar businesses. Our vision is not one of a core business being leant on by other businesses. That is not what we are striving for. Having *selected* our business areas, we are now *decentralizing* our pillar businesses. Should one of our businesses face adversity, the other businesses will be able to compensate for the impact of that adversity and hold the entire company steady.

[Refer to Selection and Decentralization table on p.13 →](#)

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— **Amidst this crisis of the COVID-19 pandemic, how has OMRON been able to protect its employees and achieve the continuation of its business? Has the selection and decentralization concept worked in this situation as well?**

Of course, it functioned very effectively. At OMRON, the protection of our employees’ health is our top priority. In late January, when the pandemic was in its early stages, we established a framework for gathering information from various locations around the world in real time and in an integrated manner. At the same time, we issued directions for flexible responses in each area, including temporary shutting down factories and shifting to work-from-home, instead of having people come into the office. Our mission was to protect employees’ health while maintaining business operations, to fulfill our supply responsibilities. This act of balancing these two missions, more than anything, is the responsibility of executive management.

OMRON has diversified its risk by establishing a tri-polar framework for our supply chain between Japan, China, and Southeast Asia, in which each pole complements the others organically. In the early stages of the pandemic, production in China was shut down but, thanks to back-up from production centers in Japan and southeast Asia, we were able to overcome the crisis without disrupting the flow of supply. What made this possible was our groundwork in decentralizing and organically linking independent organizations. Specifically, it

was the result of smooth transition of production and sharing of production technology based on a framework of independent complementarity. In this way, selection and decentralization is achieved by independent organizations connecting with each other and having the ability to back each other up.

[P17 Responses to COVID-19 Pandemic](#) →

OMRON Principles Unleash the Passion of Our Employees

— **We understand that, even in this time of crisis, the OMRON Principles were put into practice in various locations in the world. Could you give us some specific examples?**

Many challenges were pursued in various parts of the world. What made me particularly happy was that the employees took the initiative to think about what they could do themselves and pursued these challenges voluntarily.

For example, our engineers in the Industrial Automation Business in Europe voluntarily participated in an external project for the development of ventilators, and in the United States and Asia, our people worked with partners to develop unmanned sanitizing robots equipped with UV. At the height of the pandemic, our production centers in the Healthcare Business in China and Italy responded to requests from governments to manufacture critical products for treatment of COVID-19, such as thermometers, nebulizers, and medical suction equipment. There are many other examples of local employees showing initiative and putting the OMRON

Principles into practice.

The term “instilling” in an organization is often used in terms of corporate principles, but I take a different view. My image is of “unleashing,” or “releasing” employees’ will to implement those principles, not instilling them. If they are able to take personal ownership of innovation driven by social needs, as stated in the OMRON Principles, our employees will think and act of their own volition. The implementation of the OMRON Principles by employees will resonate with their colleagues around them, generating a great movement to change the world. Each and every employee will take a step forward to realize a better society. It is my belief that management based on the OMRON Principles is what will unleash our employees’ passion.

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Fiscal 2019 Review and Fiscal 2020 Outlook

— **In fiscal 2019, we were rocked greatly by the intensifying confrontation between the United States and China and the COVID-19 pandemic. What is your view of our business results in fiscal 2019?**

It was a harsh year. We were unexpectedly beset by the COVID crisis in the fourth quarter of this year, but even before then, the geopolitical risk from the trade friction between the United States and China had been weighing heavily on the company. With the Industrial Automation Business significantly affected by the negative spiral in trade

Selection and Decentralization Approaches

Approaches	Outcomes	Opportunities
Business Domains	<ul style="list-style-type: none"> Establishment of three domains + one business positioned in growth areas Establishment of IAB, HCB, and SSB, as well as EMC, which supports those three businesses, as focus businesses Building ROIC mechanisms into management to enable the automatic review of areas of focus 	<ul style="list-style-type: none"> Create new businesses as future pillars Expand profit from service business
Business Centers	<ul style="list-style-type: none"> Establishment of global management framework through Overseas Headquarters (six locations) Localization of managerial positions overseas (70% of positions localized in FY2019 against FY2020 target of 66%) Transfer of overseas HR function to Singapore 	<ul style="list-style-type: none"> Strengthen functions of Overseas Headquarters Strengthen governance function to respond to bloc economy trend and geopolitical risk
Technology	<ul style="list-style-type: none"> Development of technologies with Sensing & Control + Think Acceleration of initiatives for creating innovation with external partners by OSX* Acquisition of technology through investment in external ventures by OVC* 	<ul style="list-style-type: none"> Implement advanced technologies in society
Production Frameworks	<ul style="list-style-type: none"> Establishment of global tri-polar production framework between Japan, China, and Southeast Asia (IAB: Japan (Kusatsu/Ayabe), China (Shanghai), Indonesia) (HCB: Japan (Matsusaka), China (Dalian), Vietnam) 	<ul style="list-style-type: none"> Decentralize production centers in line with local production/local consumption strategy (Europe, US, etc.) Further reinforce individual production centers’ alternative production functions
Purchasing function	<ul style="list-style-type: none"> Ensured outstanding QCD based on group purchase volumes through central purchasing Realized stable procurement during pandemic 	<ul style="list-style-type: none"> Reinforce product competitiveness through adoption of advanced materials Reduce procurement costs through optimization of logistics
Diversity	<ul style="list-style-type: none"> Recruitment of mid-career personnel (99 in FY2019, alongside 174 new-graduate recruits) Recruitment of people with different skills through a job scheme 	<ul style="list-style-type: none"> Strengthen personnel mobility and rebuild HR systems Increase percentage of female managers in Japan Diversity in the Board of Directors (foreign nationals)

* OSX: OMRON SINIC X Corporation * OVC: OMRON Ventures Co., Ltd.

and capital expenditures, our whole-company results fell sharply by ¥54.6 billion compared with the previous year. While sales were significantly down, we were able to minimize the decline in our profit.

This is the result of being able to improve our gross profit (GP) margin (gross profit on net sales), which indicates our capacity to earn profits. Generally, a decline in sales leads to a decline in GP margin, but at OMRON, our GP margin rose by 0.4 percentage points over the previous year to 44.8%, our highest on record. We achieved this through our ongoing ROIC Management efforts, such as a shift to solution sales and the introduction of competitive new products.

This increase in GP margin could be described as evidence that our earning ability is not hindered by change. We are also seeing a definite strengthening of our financial position. This is clear from a comparison of the figures for fiscal 2008, the year of the global financial crisis, with the figures for fiscal 2019, when the COVID crisis struck. Our GP margin in fiscal 2019 was 10 percentage points higher than fiscal 2008's 34.8%. Cash and deposits, borrowings, and shareholders' equity ratio have all also improved substantially.

On the other hand, in terms of growth power, which is the ability to withstand trials in business conditions and push up sales, challenges still remain. From the viewpoint of establishing a self-driven growth structure, we are still lacking strength. Going forward, we will band together across the entire company to strive for "ambidextrous management"* as a way to build up the power to achieve self-driven growth. Ambidexterity in management means companies striving to achieve perpetual growth by

simultaneously exploiting existing businesses and exploring and establishing new businesses in a well-balanced manner. The growth of our existing businesses alone will not be enough to achieve dramatic growth in sales. We will strive to create new business areas through OMRON's mission, that is, innovation driven by social needs.

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* From *Lead and Disrupt: How to Solve the Innovator's Dilemma* (2016), O'Reilly, Charles A., III, and Tushman, Michael L.

— With further adversity anticipated, how will OMRON survive fiscal 2020? What is your outlook for fiscal 2020 based on the first-quarter results?

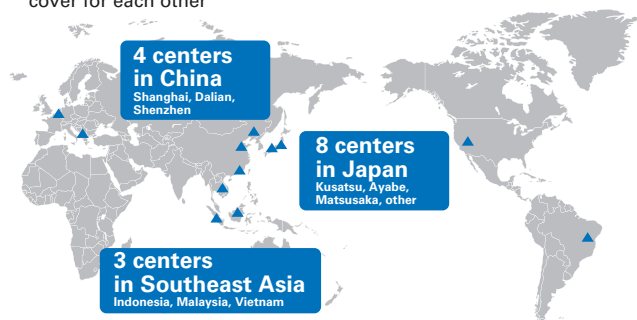
I do not believe that the catastrophe wreaked by COVID-19 will end in a year. The decline in final demand will continue to weigh heavily. Our highest priority will be to endure this era of the survival of the fittest.

Thanks to our responsiveness to change, even in this unprecedented crisis brought about by COVID-19, our first-quarter results showed a significant increase in profit compared with the previous year, despite a decline in net sales. There were three main reasons for this result.

Firstly, we were able to curb the extent of the sales decline from our initial projections by firmly capturing unforeseen demand that emerged from the pandemic, such as a sharp rise in demand in digital industries, increased demand for production of personal protective equipment such as masks, and increased demand for thermometers. Secondly, we further improved our gross profit margin by continuing to engage in various initiatives such as strengthening our product lineup, reducing variable costs, and implementing structural reforms. Thirdly,

BCP Framework in Supply Chain (Major Production Centers)

Operations based on a tri-polar production framework, building a production framework in which production centers are able to cover for each other



Changes in Financial Position (Billions of yen)

	FY2008	FY2019	Difference
GP margin	34.8%	44.8%	+ 10.0%pt
Cash and deposits	46.6	185.5	398.0%
Borrowings	54.4	1.7	3.1%
Shareholders' equity ratio	55.4%	70.0%	+ 14.6%pt

FY 2019 Results (Billions of yen)

	FY2019 Results	Y/Y
Net Sales	678.0	- 7.5%
Gross Profit	303.7	- 6.7%
Operating Income	54.8	- 18.6%
Net Income*	74.9	+ 37.9%
Gross Profit Margin	44.8%	+ 0.4%pt

* Net income includes net income from discontinued business (Automotive Electronic Components Business) (including profit from sale).

Q1 FY2020 Results (Billions of yen)

	FY2019 Q1 Result	FY 2020 Q1 Result	YOY change
Net Sales	160.0	146.5	- 8.5%
Gross Profit (Gross profit margin)	71.5 (44.7%)	66.4 (45.3%)	- 7.2% (+ 0.6pt)
Operating Income (Operating income margin)	10.0 (6.3%)	12.5 (8.5%)	+ 24.2% (+ 2.2pt)
Net Income in Quarterly Period	8.5*	9.7	+ 13.5%

* Includes quarterly net income from discontinued business (Automotive Electronic Components Business).

there was a curbing of fixed costs, through the progress made as planned in the cuts decided at the beginning of the fiscal year, and through the restriction of business activities due to COVID-19. We achieved better results than expected for the first quarter, but with the pandemic showing signs of prolonging, we anticipate that the market environment will remain uncertain. Therefore, on the premise that the harsh business conditions will continue at least until the end of the fiscal year, we have selected a conservative scenario that eliminates factors of high uncertainty as much as possible, and set a full-fiscal-year forecast of falls in sales and profit. Of course, we do not believe that this is all we need to do. We will continue to seize business opportunities firmly and aim to enhance our performance. The business environment is uncertain, but we will continue to make investments that will be essential for future growth in the post-COVID era.

[P25 Table: FY2020 Plan →](#)

— The two years of fiscal 2020 and 2021 have been designated as a period of preparation and transformation in anticipation of the post-COVID era.

I expect the with-COVID era to continue for some time. The impact of the pandemic is also bound to have a significant impact on future society. Accordingly, we have designated those two years as our critical response period, in which we will place top priority on responding to the crisis to ensure the continuation of our business and secure profits. At the same time, we will proceed with preparations and reforms for the post-COVID era and work on developing our next long-term vision. The next long-term vision will commence in fiscal 2022, after that two-year period. Although the COVID crisis has been a tremendous trial, it has also given OMRON a clearer outline of the innovation driven by the social needs of the near future that we should seek to achieve. People's values, business models, and the image of society are all on the verge of enormous change. Over those two years, OMRON will seize those changes and accelerate our transformation, so we can continue to be a pioneer in creating inspired solutions to future social needs.

Demonstrating OMRON's Raison d'Être in an Era of Major Transformation

— As the major transformation of society proceeds, how will OMRON transform its business and demonstrate its own raison d'être in the next long-term vision?

Basically, our plan to make the Industrial Automation, Healthcare, and Social Systems, Solutions and Service businesses, and the Electronic and Mechanical Components Business

that support these three businesses, our engines for future growth will not change. However, we will work on the following three challenges within that plan.

The first is the deepening of existing businesses in response to new needs. This includes, for example, businesses that deal with telehealth, and Industrial Automation Business such as robots for further labor saving. In the post-COVID society, there will be more and more progress in automation. It is vital that we address this potential firmly.

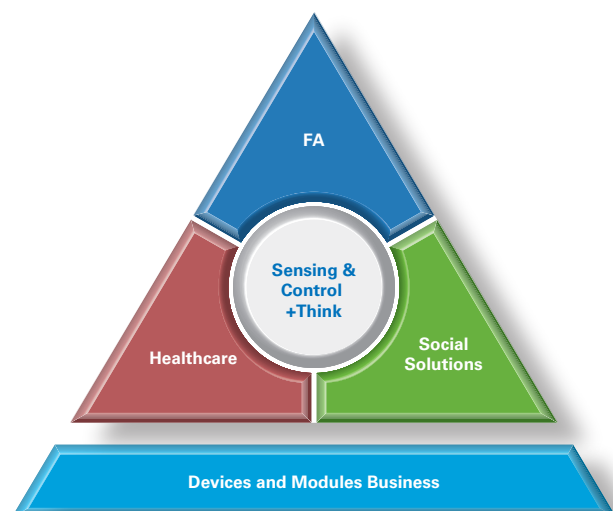
The second is to establish new businesses.

Examples include service-based businesses and recurring businesses, in line with the significant trend away from goods toward services. In the IAB, we will leverage the knowledge and data we have acquired to date to realize the ultimate in production lines that will generate no defective products. We will establish service-based and recurring businesses by leveraging our proprietary technologies, such as the world's first AI-equipped controller and industry's first image processing system that uses AI technology to detect flaws and defects without the need to learn enormous volumes of data.

In the HCB, we have launched telehealth services in the United States with the aim of achieving Zero Events of cardiac infarction and cerebral stroke. Our target for this service is to have 100,000 users and a business scale of ¥5 billion or more over the next five years.

The third challenge, the overhaul of operations and digitalization, is one that underpins the entirety of OMRON's business. For the past several years, we have been pursuing a project to introduce a new main information system. In order to establish new businesses and to realize service-based and recurring businesses, this new main system must be well suited to these businesses. Further, we will address reforms of our HR systems to enable us to assign the most appropriate people from around the world to projects that will find solutions to new social issues, thus allowing our people to reach

■ OMRON Focus Domains



their full potential. These three challenges represent OMRON's challenge for its own self-transformation.

P33 Business1 →

— In the future, the world may enter an age of frequent risks, with different crises, such as epidemics of unknown infectious diseases, large-scale natural disasters, and increased geopolitical risks, occurring simultaneously. Under such circumstances, how will OMRON grow on the global stage while solving social issues?

When the unforeseen becomes the norm. That is the very definition of the "new normal" era. Besides infectious diseases and natural disasters, there is also likely to be disruptive technological innovations. That is why our only option is to manage our business on the assumption of uncertainty and sudden change. So, how do we achieve that? I believe that our only option is management based on the OMRON Principles. This entails first understanding the essence of our own raison d'être and of the value that we should offer to society. Then, so that we can respond flexibly according to the circumstances closer to the front line, our management must collaborate with the people supporting the front line and make swift decisions. If things do not go according to plan, we should then correct our course immediately and try again. This cycle of actions should be repeated at high speed. This is the only style of management that will allow us to respond to change. Therefore, to ensure that everyone is moving forward in the same direction, it is important to have something that can be shared, something that will resonate. For OMRON, that something is the OMRON Principles. In terms of overcoming the trials of the COVID crisis, I believe now is when management based on the OMRON Principles and management that resonates will demonstrate their full strength.

— In response to the COVID crisis, one after the other, international organizations and institutional investors released statements in which they called on industry to implement serious ESG management. OMRON possesses many non-financial intangible assets, such as intellectual property, human resources, environment, and governance. How will you link those assets to future corporate value and accelerate management based on the OMRON Principles?

Various social issues raised in the SDGs (Sustainable Development Goals), such as poverty and climate change, already existed before COVID-19. Far from being resolved, these issues are only getting worse. What can companies do under such circumstances? How should they manage their business? All stakeholders, not only

investors, are casting an increasingly severe eye on companies, and companies' level of commitment is being called into question. In response to these expectations from society, OMRON will set specific sustainability challenges, shed light on them, and bring in external parties to help solve them, and repeat those actions in a constant cycle. These efforts will resonate out and attract excellent people to OMRON. Together with those people, we will solve social issues through business, which will lead to the expansion and regeneration of our business.

Besides our sustainability initiatives, OMRON has the OMRON Principles, our core technologies cultivated over many years, effective governance, and most important of all, employees who are passionate about solving social issues. Combining the power of all these things, we will engage forthrightly in our mission to solve social issues through business. That is because such an endeavor means, no more and no less, putting OMRON Principles into practice.

P31 Sustainability Initiatives: Progress →

— Could you tell us your own intentions and resolve, as president, toward the new normal era?

The COVID-19 pandemic is not yet over. Firstly, we need to survive and thrive in this era of the survival of the fittest. The key to achieving this will lie in how, while continuing our business with the health of our employees remaining our top priority, we can sow seeds for future growth in the post-COVID era. Looking back, OMRON successfully sowed the seeds for future growth during the global Financial crisis, when OMRON's financial position was even weaker than it is today. Those seeds have since blossomed into business models such as the Industrial Automation Business's "innovative-Automation" and have become the driving force for growth today. Our actions in times of adversity are what will determine our future.

In that respect, M&As and alliances are also forms of seeding that are necessary for future growth, and the current adverse conditions represent an opportunity in this regard. By combining our own strengths with new capabilities from outside the company, including M&As and alliances, we will steadily advance our preparations for a major leap toward the next era.

Our goal is to become a corporate group that people can always depend on, and an organization that continues to live up to the high expectations of people from all over the world. In the new normal era, we will continue to contribute to a better society and realize sustainable growth.