Today’s Agenda

Current Status Recap

Targeted outcomes and specific action plans

Numerical targets

Transforming Shiseido into a company that insists on winning by facing realities

December 17, 2014

Masahiko Uotani
Representative Director, President & CEO
Shiseido Company, Limited

December 17, 2014

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Representative Director, President & CEO
Shiseido Company, Limited
Favorability Rating of Company Is Decoupled from Domestic Market Share

Favorability rating and market share to 2002 are based on Shiseido survey. Market share for April 2003 to March 2009 is based on INTAGE Inc. SLI - Diary data. For April 2009 to March 2013, market share is based on INTAGE Inc. SLI- web purchase comparison data (value basis) for general cosmetics (defined by Shiseido; comprising cosmetics, haircare, body care and others).

Operating Profitability Far Below Competitors

Favorability rating and market share to 2002 are based on Shiseido survey. Market share for April 2003 to March 2009 is based on INTAGE Inc. SLI - Diary data. For April 2009 to March 2013, market share is based on INTAGE Inc. SLI- web purchase comparison data (value basis) for general cosmetics (defined by Shiseido; comprising cosmetics, haircare, body care and others).
Decline in Marketing Investment

### Japan

- **Billions of yen**
  - 2006: 34.9
  - 2013: 21.4

- **Selling expenses**
  - 2006: 83.9
  - 2013: 53.7

- **Advertising expenses**
  - 2006: 117.5
  - 2013: 92.0

- **Ratio to net sales**
  - 2006: 23.6%
  - 2013: 22.3%

*Sample, rebate and promotional expenses

### China

- **Composition of marketing investment**
  - **2006**
    - Selling expenses: 72.3%
    - Advertising expenses: 27.7%
  - **2013**
    - Selling expenses: 75.1%
    - Advertising expenses: 24.9%

Figures for Japan are based on publicly disclosed data. Figures for China are based on actual results of two sales companies in China.

Decline in R&D Investment

### R&D Expenses as a Percentage of Net Sales

- **2003**
  - Shiseido: 2.8%
  - Company A: 1.8%
  - Company B: 2.4%
  - Company C: 3.5%

- **2013**
  - Shiseido: 1.8%
  - Company A: 2.4%
  - Company B: 3.5%
  - Company C: 3.7%

### Comparison with Other Companies

- Shiseido: 1.8%
- Company A: 2.4%
- Company B: 3.5%
- Company C: 3.7%

Figures for Japan are based on publicly disclosed data. Figures for China are based on actual results of two sales companies in China.
Fundamental Issues

**Brands That Aren’t Growing**
- Poor customer orientation
- Too many brands
- Confusing brand portfolio
- Declining investment in marketing and R&D

**Inefficient Organization**
- Delayed decision-making and response to market changes
- Japan-centric organizational structure
- Barriers between head office and front-line sales
- Unclear allocation of responsibility
- Personnel system that lacks competition and does not nurture young employees
- High ratio of selling, administrative and personnel expenses

“There’s an attitude that the head office is on top and the sales company is the underling. We’re both in the same group, aren’t we? I feel a real barrier between us.”

“No one takes responsibility when we don’t get results, including senior management. We don’t even get an explanation.”

“Now that I’m over 40, at last I’m in a managerial position. Everything up until now has been the waiting period of the seniority system.”

Shiseido’s Potential and Strengths

- Long history, contribution to culture
- Spirit of omotenashi
- Safe, reliable, high-quality products
- Human resources and loyalty
- Global operations
- R&D and technological capabilities

The Shiseido Group corporate philosophy
Our Mission, Values and Way

Our Mission
Our Values
Our Way
Today’s Agenda

Targeted Outcomes and Specific Action Plans

- Numerical targets
- Current status recap

Mega Trends Changing Consumers’ Lives

- Globalization
  Values and tastes are diversifying as people explore new territories

- Urbanization
  Social scenes and lifestyles have diversified

- Information
  Advances in information technology allow for easy access to information

Active Consumer

Connected through various networks, enjoy diversified roles, make their own choices
The Five Paradigm Shifts

Shiseido-oriented View  
(Shiseido shall…)

Ideal  
(present a uniform ideal)

Aspire  
(create an image of being the authority on beauty to be aspired to)

All  
(possess almighty power)

Fixed  
/respond to general/average situations)

By  
(be in a position to give instructions)

Consumer-oriented View  
(Consumers expect us to…)

Individual  
(support the pursuit of unique beauty)

Inspire  
(foster mutual trust based on honesty)

Role  
( fulfill the required role)

Mixed  
(support flexibility for different situations)

With  
(maintain an equal relationship)

Desired Outcomes and Roadmap

2015-2017  
Restructure the Business Foundation  
Enhance brands  
Increase marketing and R&D investment  
Organizational/personnel system reform  
Strengthen China, Asia, TR* and EC businesses  
 ¥30-40 billion Groupwide structural reform

2018-2020  
New Strategy to Accelerate Growth  
New brands/M&A  
Continue investment/Achieve returns  
Build global system  
Establish business in emerging countries/new areas  
Review and revise business models

2020  
“We create beauty, we create wellness”

Become a company that is full of energy for growth
Become a company that is a topic of conversation around the world
Become a company that young people adore
Become a company that is brimming with youthfulness

• Operating income over ¥100 billion
• ROE of 12% or more

* Travel Retail

[Image of the page]
Strategic Directions in Each Region

Europe
- Unify European marketing
- Integrate back office operations
- Restructure business operations in low-profit countries

Asia

Japan

Americas
- Accelerate growth of makeup brands/lines
- Integrate back office operations
- Normalize ADC* operations

Improve profitability
- Increase customer-driven investment
- Localize functions and authority
- Establish independent electronic commerce (EC) business

Restructure business

Restore market share
- Increase customer-driven investment
- Prioritize enhancement of prestige and cosmetics brands
- Focus on bolstering selected brands in personal care category

Expand growth potential
- Expand prestige brand market share
- Establish foundation for cosmetics brands
- Enhance TR and emerging country operations

Toward Brand Enhancement

Integrated customer-driven marketing
Marketing X Innovation
Product development based on innovative core technologies

Human resources and organization with strong ability to execute
- Regional, front-line focus
- Flat organization
- Speed
- Accountability

*Shiseido Americas Distribution Center
New Organizational Matrix with Brand and Region Vectors

**Brand Vector**
(4 brand businesses)

**Region Vector**
(6 regions)

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**New Organizational Matrix Concept (From April 2015)**

**Regions**
- Japan
- China
- Asia
- Americas
- Europe
- TR

**Brands**
- Prestige
- Cosmetics
- Personal care
- Professional

**Corporate/shared functions**

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**Think Global, Act Local in Action**

**Local Subsidiary Functions**
The front line responsible for expanding business by meeting the needs of local customers

**Regional Headquarters (RHQ) Functions**
Strategic hubs that support locally rooted brand development

**HQ Functions**
Strategic support team for the Shiseido Group

CEO
Japan: Unify Head Office and Sales Company Functions

Current

After Domestic Organizational Restructuring (From April 2015)

Prestige
- Brands
- Channel planning
- Sales/BC*

Cosmetics
- Brands
- Channel planning
- Sales/BC*

Personal care
- Brands
- Sales

Digital
- watashi+
- Internet/Mail-order business

Wholesalers and distributors

Department stores and cosmetic specialty stores
Drugstores/General merchandise stores/Home centers/Supermarkets/Convenience stores

BC: Beauty Consultant(s)

A Personnel System That Stimulates and Rejuvenates the Organization

- Global mobility
- External personnel
- Revise the design and working environment for Japan-centric posts
- Active roles for women

- Promote competent (young) personnel
- Selective education
- Evaluation and position/compensation based on abilities and achievements
- Work rule design
- Competency
- Culture of responsibility for commitments

Diversity

Principles of competition

Roles & responsibilities
Personnel System Reform in Japan and China: Motivating Beauty Consultants (BC)

- Transform into a group of beauty professionals
- Encourage recruiting of and promotion to regular employees
- Switch to an evaluation and position/compensation system that is linked to store sales
- Increase roles for young employees
- Expand scope of work and assign people to the jobs they are suited for
- System for career changes

Fundamental Strategy for Prestige Business

- Focus on building the global brand SHISEIDO and the bareMinerals, CPB* and NARS brands
- Expand share in Japan, Americas and Europe through steady growth
- Drive growth in the high-growth markets of TR, China and Asia

* CPB: clé de peau BEAUTE
Fundamental Strategy for Cosmetics Business

• Premium
  Mid-to-high price/high-value-added category:
  Introduce new ELIXIR line for China and Asia in 2016

• Entry
  Low-price/youth category:
  Aggressively build Za brand mainly in Asia

Create Strong Brands by Expanding and Changing the Nature of Marketing Investment

Select and focus on brands for investment
Shift to investment that focuses on customers
Expand marketing investment by a cumulative total of more than ¥100 billion over three years
Build brand value & loyalty

Marketing Investment

Cumulative increase of more than ¥100 billion
Expand investment

2014 15 16 17 2020
(Forecast)
Expand Core Brands/Lines and Achieve over ¥1 Trillion in Sales through Brand Investment

- Eliminate and consolidate small, unprofitable brands/lines (decrease of 28 brands)
- Redeploy brands/lines according to customer segmentation
- Strengthen product lifecycle management
- Brand M&A

Achieve over ¥1 trillion in sales

Expand R&D Investment to Innovate

- Establish a globally based research organization
- Increase research facility personnel worldwide from 1,000 to 1,500*
- Strengthen basic research
- Establish a Global Innovation Center
- Increase R&D expenses from 1.8% to 2.5% of net sales*

* Forecast for 2020
Invest in Categories That Are Essential for Growth

Aggressively expand in the TR category, which is highly profitable and offers excellent growth potential

- Develop exclusive products
- Expand investment in sales counters
- Establish an independent organization to strengthen operations in Asia

Strengthen electronic commerce (EC)/digital category to reach young consumers

- Establish independent organizations for each region
- HQ to plan strategy
- Expand IT and marketing investment

Restructure the China Business

Issues in China

- Slow response to market changes
- Overemphasis on sell in/increase in inventories
- Complex organization and processes
- Poor management of BC organization
- High cost structure
- Increasingly competitive environment

Business structure reform

- Reduce costs
- Restructure and increase investment in brand portfolio
- Unify activities to increase store sales
- Localize authority/ Promote local employees
- Establish independent EC business to become #1 digital company
- Restructure and reinvigorate BC organization
Ceaseless Structural Reform

- Find new suppliers and enhance collaboration
- Reform the cost planning process
- Shift to area-based shared services
- Review and optimize IT investment
- Revise evaluation and position/compensation system
- Control the number of employees
- Revise personnel expenses and productivity
- Source promotional items more efficiently
- Scrutinize return on investment
- Revise the demand forecasting and planning process
- Aggressively utilize new suppliers
- Control the number of employees
- Find new suppliers and enhance collaboration
- Reform the cost planning process
- Shift to area-based shared services
- Review and optimize IT investment

Raise Structural Reform to the Next Level

Until Now

- Began by reducing and streamlining
- Generated effects with a focus on Japan
- Made issues visible through reduction initiatives
- Directed cost improvements from the head office
- Optimized inventories and increase store sales by unifying activities in Japan

From Now

- Reform that addresses core issues
- Global rollout in all categories (leverage economies of scale globally)
- Organizational and process reform (change the way of working)
- Reengineer the China business
- Corporate officers commit to results and make decisions on a weekly and monthly basis.
Generate Investment Resources to Build a Foundation for Growth

Billions of yen
Europe: 2.5-5.0
China: 6.0-8.0
Japan: 15.0-18.0
Asia: 0.5-1.0
Americas: 6.0-8.0

Generate ¥30-40 billion over three years, by 2017

Expand investment in consumer marketing and R&D

Today’s Agenda

Numerical Targets

Current status recap
Targeted outcomes and specific action plans
### Toward Net Sales of Over ¥1 Trillion

**Net Sales**
Billions of yen

- **2014 (Forecast):** ¥770 (CAGR 3-5%)
- **2017:**
- **2020:** ¥1,000+ (CAGR 5-7%)

### Expand Earnings by Reengineering Businesses

**Ratio to net sales (%)**

<table>
<thead>
<tr>
<th>S&amp;A expenses</th>
<th>Phase 1</th>
<th>Phase 2</th>
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<tbody>
<tr>
<td>Cost of sales</td>
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<td>24.0 to 24.5</td>
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<td>Marketing costs*</td>
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<td>R&amp;D</td>
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<td>Personnel expenses*</td>
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<td>Other expenses</td>
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<tr>
<td>Operating income</td>
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<td>6.5 to 7.0</td>
</tr>
</tbody>
</table>

*Counter depreciation expenses and costs of BC who are hired by distributors and retailers previously included in other expenses have been reclassified as marketing costs and personnel expenses, respectively.*
**Shiseido’s Key Performance Indicators (KPI)**

**Sustained growth**
- Invest in brands
- Increase brand equity
- Grow net sales
- Increase operating income
- Increase corporate value

**ROE(%)**

- Strengthen management of CF and BS
- Emphasize FCF\(^1\) and CCC\(^2\)

Increase management efficiency

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1. Free cash flow  
2. Cash conversion cycle
Allocate the Value Created to Investments for Growth and Shareholder Returns

- **Investments for growth:** Strengthen marketing, R&D and M&A investment
- **Dividends:** Target a 40% payout ratio, and pay stable, sustained dividends
- **Share repurchases:** Execute when free cash flow and market conditions are appropriate

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Signs of Change at Shiseido: ICHIGAN Project

**YoY Store Sales (10-day periods)**

- Chart showing YoY store sales trends from July to November 2014, with a notable increase in November.
Total Commitment of Management

Reform and strengthen management
Accountability
Commitment to structural reform

Leadership that emphasizes operating realities

Rejuvenate Shiseido

Excerpt from January 2015 issue of GOETHE, Gentosha
Article by Toru Uesaka Photograph by Tadayuki Aritaka
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