

From the President and CEO

Realizing a sustainable world with tagging



Ryutaro Kotaki

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President and CEO

We start where our customers are

As the COVID-19 pandemic continues to loom in 2021, I offer my sincere condolences to the people suffering from the loss of loved ones or the effects of the disease. I also take this opportunity to thank all of you fighting hard to contain the spread of the virus and sustain our daily lives.

Throughout our 80-plus-year history, SATO Group has weathered global financial crises and many other difficulties, always working side by side with customers and face to face with their worksites. The relationships we developed and the knowledge we accumulated from these toils are an asset we prize today. Even as the pandemic prompts rapid changes in our business environment reshaping industry structures and advancing digital workstyles, SATO continues to work off of, and build on, its experience and know-how to play its part in creating a sustainable world.

FY 2021 is a start for us in terms of a new medium-term management plan and the change we envision. We renew our intent to concentrate more than ever on our core business and on sustainability.

Looking back at FY 2020

Last fiscal year began with a big drop in sales for the entire market due to the pandemic, but the second half of the year presented recovery trends in the Japan market. With customers facing new challenges in physical distancing and contactless operations, we focused on offering automation and RFID solutions, which started turning out figures in the second half. Outside Japan, many countries began recovering during the first half, and with a reorganized Sales Headquarters largely contributing to greater global collaboration, our koto-uri*¹ sales approach gained traction in our worldwide offices. These efforts led to highest-ever profits and successful results for our overseas business amid the pandemic.

Consolidated sales settled at ¥109.1 billion (down 6.3 percent year-on-year) and operating income at ¥5.8 billion (down 21.6 percent) for the full year.

*1 Sales approach of selling not just the product but combinations of products in the form of solutions that include hardware, consumables, maintenance services and software, demonstrating ROI and other value propositions for the customer.

Three years at the helm

Since becoming CEO in April 2018, I have focused our resources on SATO's core business of automatic identification solutions, with which we can demonstrate our strengths and find plenty of growth opportunities. At the root of this business is tagging, which is the act of physically attaching information to things and people. Tagging, as easy as it may sound, requires the expertise to choose the right technology to collect information that the customer needs, use the right label/tag to attach the information to different materials and shapes, and identify the optimal means of reading the label/tag data and the ideal timing to feed the data to IT systems. This expertise doesn't come in a day. It comes from all the trial and error we went through since our founding and the experience we have accumulated with our customers and business partners. Tagging is our strength that no other company could — or would even attempt to — imitate, and what allows us to keep honing our genbaryoku.*2

Tagging thus requires us to fully understand the customer's worksite, which naturally creates interaction and touch points with customers. Through our koto-uri approach of solving pain points, we get to interact even more with the customer, which heightens their trust in us, and goes back to creating other opportunities for further engagement. This is the very reason we tailor customer approaches by country, market and industry; this cycle of interaction is only possible when we understand customers deep into their business instead of merely generalizing them as "a customer."

Having been involved in the sales field in Japan for long, I am convinced that this ability to deliver auto-ID solutions "centered on the customer and shaped of tagging" is what fuels SATO's long-term growth. That's why I have committed myself in my role as CEO to foster this competency globally, and to make us into a corporate group with inimitable strength.

Looking back at these three years by business segment, I must first mention our Overseas sector that expanded its business by shifting its growth strategy from simply "selling the product" (printers and individual products) to "selling the solution," i.e., koto-uri. Koto-uri is far different from simply selling the product and is difficult to imitate, so its success depends on knowledge shared from the Japan team that has years of



**Tagging is our strength
that others cannot —
or would not — imitate**

accumulated experience. That was why we picked out employees in Japan with expertise on each market and industry and assigned them to assist each country. Together with the reorganization of Sales Headquarters in April 2020 to boost HQ support, collaboration stepped up between our global offices and HQ. These actions resulted in more business with industry giants, and as such success transposed to other regions as well, our global offices seem to have caught on with the koto-uri methodology. It did take longer than we had anticipated for local employees to change their mindset, but the apparent results prove that the shift has been successful.

The only challenge may be that some countries and regions are catching on slower than others. We are currently narrowing down on countries, markets, industries and applications to focus on, so that we can send in the right experts, or enhance our collaboration with the appropriate strategic partners.

In Japan, we have worked to innovate koto-uri, having our salespeople cooperate with market-specific teams of leading experts to provide customers solutions accurately directed to their pain points. While this effort has helped us develop new solutions for each industry and put us in more talks with potential customers, the greater complexity of customer pain points and higher levels of technologies applicable have made our solutions far more advanced than ever, prolonging the time needed for closing deals. We have countered this problem by changing the way we sell. Salespeople used to be fully responsible for every sales activity ranging from finding potential customers to closing out deals, but now we have our marketing department, call centers and market strategy divisions collaborate in the process. This teamwork now allows salespeople to concentrate on deals with higher win probability to close deals faster and, consequently, more.

While we continue to create customized solutions that meet industry-specific needs, we also work to identify elements within these customizations that we could standardize, so that the solution packages could reach more customers and reduce the burden customization poses on our production and logistics functions. It means optimizing our value chain.

In summarizing these three years, I must admit that we have not yet grown our business at the speed or scale we had planned. The fact that we had to restrict face-to-face sales activities due to COVID-19 distancing measures had no small impact on our company that boasts its competitive advantage in seeing the customer's pain points directly on site to propose the best fitting solutions. But as tough as the situation was, it made us rediscover that the essence of our genbaryoku is in our ability to understand the customer's worksites and to identify and solve their challenges, and that there are still many customers out there who seek that competency of ours. Our success in promptly delivering contactless and automation solutions that adapt to the new normal era, and in recording highest-ever profits in our Overseas business, has renewed our confidence for future growth.

*2 Our core competency of going to customer sites in an array of markets/industries to understand the essence of their pain points and offer solutions that improve or innovate their operations. It consists of three elements: industry expertise (versed in many industries), technical expertise (offering the best mix of products) and servicing (constantly improving operations at customer sites). (See Page 27)

Recognize change; innovate our business

We at SATO place high emphasis on recognizing how societal changes affect a country, market or industry and shape the pain points of customers at their front lines. It's about looking at the big picture to understand the essence of pain points, and to actually see with our own eyes how surrounding trends impact the customer's worksite rather than simply speculate and make generalizations. And that's how we come up with exclusive solutions that encapsulate our tagging expertise.

For example, the world today is facing digital transformation (DX), disruptions in industry supply chains, shifts in social norms linked to COVID-19, and greater sustainability challenges. Put these together, and we see that what customers really need now are solutions for supply chain visibility/stability and management of employee/visitor safety at the workplace. With customer interest also higher than ever on actions to reduce environmental burden, it makes sense that we put efforts as we do now into offering reassurance and enabling sustainable practices in the context of each market and industry to create and deliver tagging solutions geared toward operational efficiency, automation and traceability.

Throughout our history, we have always picked up on the changes of the times to provide tagging solutions that help solve real pain points on customer sites. We have innovated our business from hand labelers to barcode printers, and then to DCS & Labeling, expanding our value proposition all the while. Now, in response to the pandemic, we take that another step further, as I set "Tagging for Sustainability" as our next business model.

Our new Vision, and "Tagging for Sustainability"

As the pandemic quickened the societal changes we had been anticipating, I had to stop and rethink what SATO should aim and aspire to be. It resulted in my decision to change our Vision statement to, "To be the customer's most trusted partner for mutual growth, and always essential in an ever-changing world." It defines what SATO must be to grow sustainably in these times of rapid change: a company that collaborates with customers and other stakeholders to create new value.

I have also set a new phrase, "Tagging for Sustainability" to express the business model that we will be pursuing over the medium to long term in auto-ID solutions and for all stakeholders to know as our shared mindset. This involves steering our business forward in two dimensions (axes): coverage of supply chains in our target markets (horizontal axis) and the level of tagging technology for our solutions (vertical axis). (See figure below)

DCS & Labeling has been — and still is — our business model of giving things and people at a customer's site their own IDs to improve productivity, primarily in production, distribution and sale operations. It's what we have been doing since the late '90s when we began shifting to selling solutions: tagging identifier information with labels and converting it to digital data for customers to use on their systems to optimize operations.

As RFID, voice/image recognition and sensing technologies came about as new means of tagging beyond labels, IT infrastructure also made way for greater volumes of data to be collected, analyzed and used, allowing customers to expect not just improvement in their localized operations but also solutions to challenges spanning their entire supply chain. In order to meet these expectations, we needed to develop a business model that stands on the grounds of DCS & Labeling but is more advanced. That would be "Tagging for Sustainability."

Long-term business vision



* Those of/across production, distribution and sale

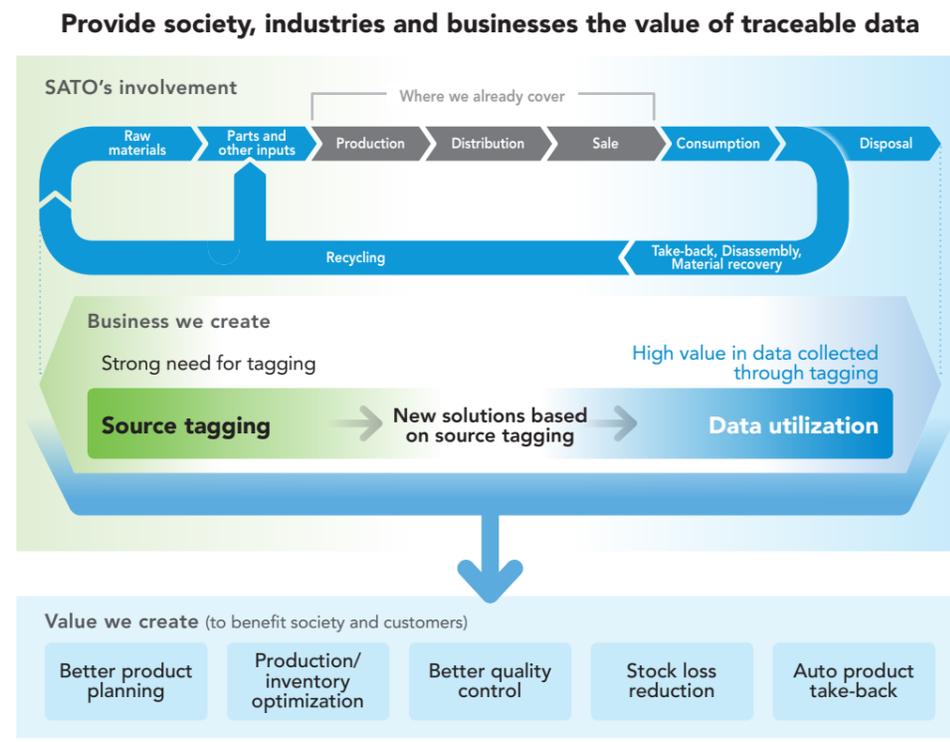
One example would be source tagging, the act of tagging at the very upstream of a supply chain using state-of-the-art tags. These tags would allow customers to not only track the ID of a product but also its status and use, while also tracing it across different supply chains as well. If a weight sensor tag were embedded in a medication bottle that would ultimately be handed to a patient, for example, it would be able to detect how many pills were consumed by the patient and when. The pharmacist or physician could use the data to provide the patient guidance on medication adherence, while the manufacturer could plan production or develop new products. Also, the tag could facilitate the sorting and collection of used bottles to make recycling much easier.

Source tagging this advanced will make individual items in a supply chain traceable from many different perspectives. And this will keep SATO involved over a far broader area of the chain covering both forward and reverse logistics, from when the item is manufactured and distributed to after it is used by a consumer and simply disposed of or collected back for disassembly and material recovery. It will mean more value for us to provide. (See figure below)

In a world that increasingly shifts toward a circular economy, we believe this concept of source tagging we envision will come to serve a greater purpose. And it can only happen when we play to, and hone, our unique strengths while collaborating with customers and stakeholders. We hope to establish ourselves as a company that a variety of stakeholders would want to partner with and find easy to partner with.

The way we would achieve this future is laid out in our new medium-term management plan put into effect from FY 2021.

Generating new business and value through tagging



The medium-term management plan

Fiscal years 2021 through 2023 that we set as the span of our new medium-term management plan will be time for us to see the results of our koto-uri efforts and to invest in growth strategies geared toward "Tagging for Sustainability." We expect to see effects of these investments materialize subsequent to this management plan, setting a milestone at FY 2025 when we would achieve a five-year CAGR (compound annual growth rate) of 6.0 percent for sales and operating income ratio of over 10 percent.

The three main strategies I have set to achieve these targets are: **1 enhance region/market strategies**, for us to expand business in supply chains by country/market/industry, **2 drive technological innovation**, to advance our tagging technologies and to support **1**, and **3 integrate environmental, social and corporate governance (ESG) ideals into our corporate model**.

You will see that **1** and **2** coincide with the horizontal and vertical axes in the figure on Page 9.

Where the medium-term management plan stands



Tagging for Sustainability

1 Enhance region/market strategies

Doing business in a circular economy means understanding how each individual 'thing' moves throughout a supply chain. That's why we continue to value our traditional approach of fully understanding our customer's worksites in each market and industry. In FY 2019, we defined the short-, medium- and long-term goals in our focal industries of retail, manufacturing, food, logistics and health care and the solutions we would provide. We will continue these market/industry strategies, taking into consideration the latest situation in each country/region and putting more emphasis on supply chains and the circular economy.

For Japan, we will boost profitability, enhancing our line of customer-centric products and solutions, optimizing our in-house value chain, and changing the way we sell. Our target will be to raise our 8.8 percent operating income ratio for FY 2019 by roughly two percentage points for FY 2025. Outside Japan, we will work on strengthening strategic partnerships, aiming to team with the best partner for both koto-uri and "selling the product" to promptly grasp growth opportunities that we see in abundance.

2 Drive technological innovation

“Tagging for Sustainability” cannot do without new developments and innovations in tagging technology, which is why we established the RFID Business Headquarters and an Innovation Lab earlier this fiscal year. The former integrated the product planning, production and business development functions related to RFID into a single organization to promptly pick up global RFID needs and deliver solutions to generate short- to medium-term results. Innovation Lab is an organization reporting directly to the CEO that engages in research and development on the aforementioned source tagging technology and other components of tagging that eye success in the medium- to long-term run. Our technological innovation does not assume that we invent everything by ourselves. We value open innovation, collaborating with partner companies to develop new tagging technologies flexibly and with speed.

We will also continue to develop and add competitive products and solutions to our core printer and label offerings, drawing on our advantage of knowing the customer’s worksites in each market and industry.

3 Integrate ESG into our corporate model

Our auto-ID solutions shaped of tagging can contribute to the circular economy, which is what we aim for in driving the above two strategies. This third strategy supports the two, and a particularly important element here is to build on human resources.

As tagging requires us to collaborate with customers in solving their pain points, people serve as the very source of this value creation. Providing a place for employees to nurture and bring out their best and to raise their motivation is absolutely necessary for us to proceed with “Tagging for Sustainability.” We have two primary means to make this happen. One is to create a culture of innovation. Here at SATO, we have “Ceaseless Creativity” (corporate motto) and “Rejoice in change” rooted as corporate culture that has been honed through our tradition of Teiho^{*3} that started 45 years ago. I hope to continue building on this culture to a point where all employees find it second nature to think and act on their own accord to innovate. The management will take the lead in setting up systems and environments that can inspire our diverse workforce to show initiative, inventiveness and passion in generating innovations.

And two is to drive digital transformation within the company. SATO has so many customer touch points ranging from sales and sales support to servicing, system engineers and contact centers. Our value chain, meanwhile, has many functions — R&D, production and logistics — all holding useful information that are not quite seamlessly integrated, causing some of our work to overlap between departments or communication with customers to work inefficiently. A new IT system integrating all this information would reduce overlapping work and raise productivity. We are also planning to equip this system with a feature that could suggest the best action for us to take from our contact history with a customer. It would allow, say, a service representative to put forward a new value proposition during a regular maintenance visit. With happier customers, employees would become more motivated knowing they can make a difference, leading to higher employee engagement, which would contribute to a positive cycle of value creation.

Corporate governance is a key pillar that supports our groupwide activities, which we

**People are the source of our value creation
We provide a place for employees to
nurture and bring out their best**



will reinforce from a global perspective in keeping with our business development. We will implement different governance controls that include identifying and managing local opportunities and risks particularly outside Japan to support our medium- to long-term business growth.

Lastly, in terms of sustainability, SATO takes part in the United Nations Global Compact (UNGC), a worldwide movement of companies that commit to adopting responsible business practices for a sustainable world. We will continue to prioritize and strengthen efforts to do business complying with UNGC principles concerning human rights, labor, environment and anti-corruption.

*3 Our unique insight sharing system through which employees regularly submit to the management “Reports on original ideas, innovations and proposals aimed to make the company better and on how to put them into action.” (See Page 26)



To our stakeholders

Considering the uncertainties in the business environment owing to the pandemic, we have decided to keep total dividend per share for FY 2020 at ¥70, same as the previous fiscal year, sharing the returns from our business with our four stakeholders as mentioned in our Credo. Our path ahead in “Tagging for Sustainability” may not necessarily be smooth, but we shall maintain firm ground on our corporate motto of “Ceaseless Creativity” and SATO Values as we take on new challenges to achieve sustainable growth and heighten our corporate value.

We stand by our customers in any business field amid any major change in environment and society, to deliver expansive value with tagging, which is a strength unique only to us. On behalf of the entire group, I ask for your unchanging support as SATO teams around the world work as one to pave our way through the times and exceed expectations of our customers and stakeholders.

From the CFO



Maximize our corporate value through financial and non-financial measures

Fusaaki Matsumoto
Executive Officer,
Chief Financial Officer (CFO)
and Chief Compliance Officer (CCO)

Taking up the role of CFO and CCO

As the new CFO and CCO effective April 2021, I hope to leverage my years of international CFO experience at multiple companies to help SATO Group grow globally.

At SATO, we manage cash flows to achieve a stable financial base, in line with our management policy of concentrating resources on our auto-ID solutions business to establish sustainable growth and stable profits. Our basic stance on cash flow control is to make investments within the limits of our cash flow from operating activities and maximize returns while maintaining positive free cash flow. Despite recent impacts from COVID-19, we have realized a business portfolio of sound profitability and disciplined financial management to keep our annual operating cash flow stable at above ¥8.7 billion on average over the past five years. Overall financial health is also our top priority as we aim to control financial leverage at no more than 2.0 to maintain balance with dividends and other shareholder returns. As the FY 2020 results show, our debt-to-equity ratio is stable at 26.5 percent. We also have a current ratio of 2.02, indicating the company's liquidity and ability to realize stable business activities and sustainable growth. While being adequately healthy in our financial position, we note the importance of having enough short-term liquidity and have signed a commitment line contract with our lenders (on top of existing overdraft agreements) to ensure we secure

financing to invest in business growth and deal with pandemics or other unforeseen circumstances.

Going by these business indicators, I can say with confidence that SATO's financial status is stable. While the company has come this far since its founding by keeping consistent focus on our core business backed by production and sales capabilities, we must now strive to maximize corporate value at the group level in order to continue growth into the future. This requires us to take certain risks to pursue the greatest possible returns from a medium- to long-term perspective. We established a Business Review Committee in April 2021 to help manage risks in a valid and prompt manner. This committee that I chair shall assess and analyze risks that SATO Group takes in conducting business, for example, when making investments and loans or acquiring and disposing of assets. It will help advance investment strategies and optimize our business portfolio over the medium to long term. Besides making investment decisions based on the WACC (weighted average cost of capital) benchmark of 8 percent, we will also work to strengthen corporate governance in terms of internal controls and compliance to lay a robust foundation for business management.

For now, the most important commitment to our stakeholders is to achieve our medium-term management plan for fiscal years 2021 through 2023.

Toward achieving our medium-term plan

Under SATO's medium-term plan, we aim to invest in growth strategies over a three-year span to see them materialize into results in subsequent years. By the end of the plan in FY 2023, we target sales of ¥130 billion, operating income ratio of 9.1 percent and ROIC (return on invested capital) of 10.3 percent. Underpinning this plan are three main growth strategies: (1) enhance region/market strategies, (2) drive technological innovation, and (3) integrate ESG into our corporate model. While I am responsible for implementing financial/capital strategies that aid the medium-term plan, I place particular emphasis on (3), given its importance in supporting the first two strategies. To this end, I will help strengthen governance for risk management and thorough internal controls. I will also address the social factor to create an environment for employees to engage in value-added work by enabling digital transformation and productivity improvements with a new in-house IT infrastructure.

In terms of capital allocation, we plan to strategically invest approximately ¥50 billion from cash reserves and cash generated over these three years in the aforementioned growth strategies, maintaining balance with shareholder returns and retained earnings. The efficiency of our invested capital will be measured against ROIC (the metric we now use in place of ROE), which depends largely on operating income ratio. In our Japan business, we will make investments aimed at creating new

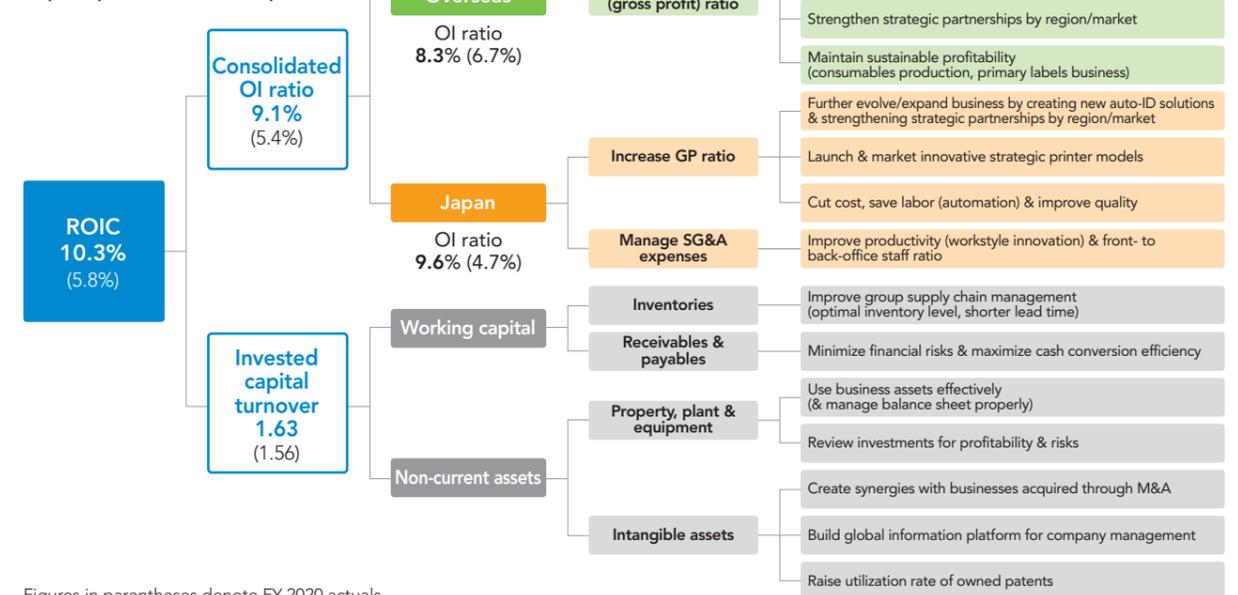
solutions and standardizing customized solution packages for select industries, so as to innovate our koto-uri sales approach for higher profitability. Outside Japan, we will invest in human resources and manufacturing facilities so that koto-uri can be further instilled to boost sales. As more investments become necessary for our business expansion plans, the Business Review Committee will review existing businesses and decide on new investments duly considering their risk-return profiles. We will also use business assets effectively and manage balance sheet items assiduously to improve our total asset turnover toward achieving optimal business and asset portfolios.

To raise ROIC to our target 10.3 percent, we must drive awareness across our business front lines, communicating to all employees the importance of the metric. This will be another responsibility of mine, holding active dialogues with employees to explain how ROIC is linked to their daily work and customer value creation.

At where we stand now, we want to shape a corporate management model that is capable of growing business in line with our strengths and delivering results gradually via a steady, reasonable process and timeline. Going forward, we aim to continue contributing to society with our business to become an indispensable part of society, because that's what we believe increases our corporate value on a sustainable basis. I ask for your continued support in our journey ahead.

ROIC tree for FY 2023

We now use ROIC to check our investment efficiency and business growth in each country and help us optimize our business portfolio



Figures in parentheses denote FY 2020 actuals.