March 2, 2020

Bucephalus Research Partnership Limited
15C Casey Building
38 Lok Ku Road
Central
Hong Kong

Attn: Mr. Alexander Robert Medd

Dear Mr. Medd,

I am writing to you in response to a video clip you published on YouTube titled "Lenovo #4: Starting to look like fraud" on February 26, 2020.

We appreciate your interest in our company. However, we are deeply troubled that you published this video without first contacting us to check the facts. Therefore, we would like to highlight that your video included a number of allegations regarding Lenovo that are, indeed, factually incorrect – for the reasons set forth below. In addition, in an apparent attempt to build interest in your video before its release, you used the word "fraud" to describe the company. We take absolute exception to this characterization, and believe your use of such word was both unprofessional and irresponsible.

As a global company operating in over 180 markets around the world, Lenovo commits to the highest standards of transparency and integrity in our financial reporting. As such, we want to take this opportunity to highlight several inaccuracies in your commentary that require an understanding of the relevant facts:

Re: <u>Invoice pattern trending towards quarter-end, channel health and year-on-year increase of account receivables</u>

First, our sales did indeed skew late in the previous quarter. As discussed in our webcast, this was due to a shortage of a key component which was well known in the industry. While the supplier de-committed its volume and delivery schedule, a disproportionate portion of our supply arrived late in the quarter. Nonetheless, with Lenovo's exceptional supply chain operational excellence, we managed to utilise all available supply and deliver our products to customers towards the end of the quarter. This resulted in more revenue than usual being booked just before quarter-end. This was also reflected in our accounts receivable (AR) ageing, with the 0-30-days AR bracket showing the largest year-over-year increase. We have never engaged in so-called "evergreen invoicing", and your assertion to this effect is absurd.

We maintain a prudent operational policy to facilitate channel inventory control. We do not allow sell-in to the channel if a customer's inventory exceeds a certain level. Moreover, our policy would not recognise such sale in our financial statement even if it had taken place. As such, there is no incentive for us to "stuff channel" as you inaccurately claimed in your video.

Second, the increase of our trade receivables and notes receivables was mainly due to less AR factored during the quarter. The factoring service provider that had supported Lenovo AR since we acquired IBM's PC division exited the business in 2019. In 1QFY19/20, when we first experienced a notable increase in our AR balance, we discussed the details including the need to replace our factoring partner during our investor webcast.

Our new financing partner set up a new vehicle to take over the factoring service operation. Operational issues naturally need to be resolved before we can return to the efficiency level achieved with our previous service provider, including more than doubling the number of countries covered under the existing service scope. Another issue is a 3-5 day gap in invoice processing speed from our previous factoring program, although we were able to improve the cadence of processing from twice a month to once a week.

As a result of these temporary dynamics, our factoring volume has dropped significantly year-over-year and our AR balance has risen. Your allegation that our rising AR reflected aggressive sell-in to the channel, and even the use of “evergreen” invoices, is completely without merit.

Re: Finance cost

Of course we incurred costs in the course of transitioning to a new factoring partner and ramping up new operations. This included additional short-term operation and financing loans, which led to higher finance costs. However, we are starting to see positive impact from our continuous efforts to improve the efficiency of our new factoring vehicle. As a result, our 3QFY19/20 finance costs and factoring costs were reduced by $28.6M and $25.6M quarter-over-quarter, respectively. Your claim that our higher factoring costs suggested deteriorating quality of debt is, therefore, unfounded.

Re: Bad debt provisions

Your assertion that our bad debt provisions “are falling” is also incorrect because it fails to consider AR ageing composition. We review our provision policy every two years, and we have not changed our bad debt provisioning policy in that period. The policy requires a higher provision rate on older AR meaning, for example, that AR in the 0-30-days bracket would command a lower provision rate than those in the over-90-days bracket. Therefore, assessing the bad debt provision as a percentage of total AR alone does not provide the full picture. The profile of our AR mix is actually better than a year before with more AR now in the 0-30-days bracket. Consistent with Lenovo’s financial disclosures and contrary to your analysis, our provision dollar **increased** double-digit in 3QFY19/20 as compared to 1QFY19/20 and 3QFY18/19.

Re: Independent directors

We are particularly dismayed about your comments regarding our independent directors. Your claim that they would not challenge our company just because they have been serving on our board for a long time is far from the truth. According to our readily-available filings with the HK Exchange, two of our independent directors have served on our board for less than 4 years, three (including one re-designated from non-independent to independent) between 6-8 years and the remaining two 9-11 years. No independent director has served in this position for more than 12 years. We believe this mix of independent directors assures a depth of experience with Lenovo as well as clear accountability, and it is consistent with industry best practices in corporate governance, ethics and compliance.

Re: Legend, our largest shareholder

You also assert that Legend's cash demands are driving Lenovo's decision-making. While we cannot comment on how Legend runs its business, we can assure you that our leadership is focused on what is best for Lenovo and our full range of investors. Your speculation to the contrary is misguided.

Re: Increase of our trade payables and other payables

We have identified our payment terms, which are currently less favourable than the market average, as an area for improvement. For instance, we are taking appropriate action to lengthen our payables days in order to continuously improve cashflow management. As noted in your video this initiative has indeed improved our cashflow management – but you attributed this improvement to "delaying payments to suppliers" and "desperately trying to preserve cash", which is patently untrue.

Meanwhile, you may not be aware that we operate a hybrid model in our supply chain, i.e., a mix of both in-house manufacturing and subcontractors. Our non-trade payables actually **decreased** year-over-year mainly due to higher in-house manufacturing – reflecting our investments for greater efficiency and operational excellence. The reference in your video to an **increase** in non-trade payables is not accurate.

Re: Dividend

Lenovo has a consistent dividend policy of paying 30-40% of our pre-tax profit. We strive to maintain this dividend level even at times when fundamental changes affect our business. The company's cashflow is typically sufficient to generate these dividend payments, with rare exceptions. Your charge that we resorted to additional borrowing to fund dividends is baseless.

Likewise, your argument that we declared a dividend simply because our largest shareholder demanded it is just wrong. Our investors and analysts who have taken time to understand our dividend policy know otherwise.

Re: Growth from acquisition

All of Lenovo's growth over the last twelve months was organic. In addition, it was driven on a global basis and not by a single location. Your accusation that our growth derived from acquisition is inaccurate. In 3QFY19/20, our PC shipments increased 12-30% year-on-year in APAC ex-China, EMEA, LA and North America, again, reflecting strong organic growth.

As to your remarks about our China business, we believe you would have concluded differently had you studied the overall PRC market environment. Our Personal Computer & Smart Device business performance was in line with the market while our Data Center business grew significantly during the quarter. As for our mobile business, we have communicated consistently that our focus is on strategic geographies such as Latin America and the US – and it was careless of you to comment without understanding the company's strategic intent.

I hope my clarifications are helpful to your analysis of the company. I ask that, in the future, you kindly contact our Investor Relations team with any questions concerning Lenovo's published financial data before expressing your views publicly, to avoid misstatements that can potentially confuse or mislead market investors. To this end I am happy to share the contact details of our Investor Relations team below. We are committed to providing transparent, quality public information vital to the accurate assessment of Lenovo.

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Yours faithfully,

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