

Q&A Summary

Event Name: 1H FY2023 Financial Results Presentation

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Speaker: Seiji Izumisawa, Member of the Board, President, and CEO

Hisato Kozawa, Member of the Board, Executive Vice President, and CFO

Questioner 1

Q: Regarding the one-time expenses from the PW1100G-JM Engine Program in Aero Engines, other companies have explained that they have recognized these expenses based on an assumption of \$7 billion in total losses for the program as a whole as disclosed by RTX and in accordance with their participation share. How much has MHI incurred in expenses on a JPY basis?

Furthermore, regarding the profit bridge, you explained that the "Variance in one-time expenses in Thermal Power and other businesses" amounting to -¥10 billion was the difference between the one-time expenses from the PW1100G-JM Engine and the organizational transformation expenses for European operations which incurred in 1H FY2022. Please let me know the breakdown of this figure.

Kozawa: Regarding the one-time expenses from the PW1100G-JM Engine, we booked future estimated expenses as a lump sum of less than ¥20 billion based on our participation share in the program. There are slight differences in accounting methods between companies, but our basic approach is the same as other companies, and we calculated based on our participation share (2.3%).

Regarding the "Variance in one-time expenses in Thermal Power and other businesses," because this fiscal year included no organizational transformation expenses for European operations (less than ¥10 billion) which were booked in 1H FY2022, the figure here is total of this upside and the one-time expenses from the PW1100G-JM Engine, i.e., -¥10 billion. Moreover, IGCC incurred some expenses this fiscal year, but, as in FY2022, we did not include this in the "Variance in one-time expenses in Thermal Power and other businesses."

Q: Is it correct to understand that Integrated coal Gasification Combined Cycle (IGCC) incurred some expenses this fiscal year, but this was not a large amount?

Kozawa: That is correct.

Q: You did not revise the full-year business profit forecast of ¥300.0 billion. At the beginning of the fiscal year, the impact of foreign exchange effects was expected to be ¥11.0 billion, and the impact of rising personnel, energy costs, and others was expected to be ¥15.0

billion. The effect of price optimization was expected to contribute to an increase in profit. Do you expect any change in the breakdown of these factors in 2H FY2023?

Kozawa: With regard to foreign exchange rates, the situation is much more positive than the initial forecast because of further depreciation of the yen. Moreover, the effects of price optimization to offset materials cost inflation are similarly positive. While business profit was expected to increase due to these two factors, the less than ¥20 billion in one-time expenses from the PW1100G-JM Engine were not factored in at the beginning of the fiscal year. The general idea is that we have maintained the ¥300.0 billion business profit target, because the positive and negative factors I just mentioned will offset each other. We revised the initial Corporate & Eliminations (C&E) business profit forecast from ¥0 to -¥20 billion. I cannot deny that the initial forecast was slightly high, and as the negative YoY impact of gains on asset sales and an increase in R&D and other investments mainly in growth areas is increasing, we revised the forecast to reflect progress made in 1H FY2023.

Q: Defense booked around ¥270 billion in order intake in Q2 alone. Could you let us know which products you booked?

Kozawa: Among the Defense equipment orders booked in Q2, a large vertical launch system (VLS) project accounted for more than ¥100 billion.

Q: You increased the order intake forecast for Aircraft, Defense & Space (ADS) by ¥800.0, but was this increase all in Defense? Did the order intake forecast in Defense & Space increase from the initial ¥850.0 billion to around ¥1.6 trillion?

Kozawa: The Commercial Aviation Aero Structures business performed slightly better than our initial forecast due to foreign exchange effects, but a large part of the ¥800.0 billion increase was in Defense. Therefore, please understand that the order intake target for Defense & Space is around ¥1.5 trillion to ¥1.6 trillion.

Q: What is your outlook for Defense order intake volume in the next fiscal year and thereafter? MHI's previous view was that it would be difficult to maintain order intake at the ¥1 trillion level in the next fiscal year, but have you changed your view, concluding that order intake will indeed continue to exceed ¥1 trillion in the long term? What is your view of Defense in both the short and medium term?

Kozawa: Defense order intake will probably decrease in the next fiscal year. Normalized order intake was around ¥500 billion in the past, and I expect it to be a little more than ¥1 trillion in the future. However, the annual order intake figures will depend on Japan's defense budget, so we do not know exactly how large they will be. As for this fiscal year,

many projects have fallen within our purview, including orders for missile systems booked in Q1.

Questioner 2

Q: Although you have maintained your business profit forecast at ¥300.0 billion, and considering the adjustments made between segments, my understanding is that Energy Systems (Energy) has used the ¥20 billion buffer for the PW1100G-JM Engine one-time expenses. I also understand that there was upside in Logistics, Thermal & Drive Systems (LT&D) and ADS from the impact of the depreciation of the yen and the effect of price optimization. However, this upside was offset by a decrease in gains on asset sales in C&E. Does your having used the buffer included in the Energy numbers mean that you do not expect any expenses in IGCC going forward? Based on the progress in 1H FY2023, please explain how you feel about the situation.

Kozawa: The buffer that we had set aside for risk at the beginning of the fiscal year was not used for the PW1100G-JM Engine one-time expenses. The losses in Aero Engines were offset by the upside in foreign exchange effects and price optimization. Additionally, C&E includes a slight adjustment between segments, but this was not a significant change.

Q: On the whole, your results are on track to exceed the plan. Does the apparent increase in expenses in C&E come from, for example, pushing out of some gains on asset sales into the next fiscal year in order to distribute the upside from this year and stabilize profit in each fiscal year? You say you have not used the risk buffer yet, but please let me know if there is any change in your view on IGCC in 2H and thereafter.

Kozawa: At the beginning of the fiscal year, the risk buffer was not necessarily specific to IGCC, but was rather set aside to cover unexpected events in our plant projects. It was not used for the PW1100G-JM Engine one-time expenses. There is no change in the situation at IGCC, and corrective work is proceeding as planned.

As regards C&E, gains on asset sales tend to get the most attention, but the initial forecast for each segment was somewhat conservative, while the initial target for C&E was a little high. We have made a corrective adjustment in the revised forecast.

Q: During the 2024 Medium-Term Business Plan (MTBP) period, you will seek to strengthen profitability and achieve growth at the same time, but are you expecting to increase revenue? You also said that new business opportunities are emerging in Nuclear Power and Defense, but could you explain your approach to these opportunities?

Izumisawa: The 2024 MTBP will seek to strengthen profitability in the same way as the 2021 MTBP did. We are currently in the phase of drafting the 2024 MTBP. In addition to new

opportunities in Nuclear Power and Defense, we are currently working to grow our services businesses, and we will aim to increase total revenue.

Q: I imagine that opportunities and topline expansion will include Defense, Nuclear Power, the Energy Transition, energy conservation and automation. At the same time, you said that you will continue to optimize your business portfolio. Does this mean that businesses in segments other than Energy and ADS will be targets for another round of optimization?

Izumisawa: I believe it is necessary to optimize the business portfolio in order to shift resources to our growth areas. On the other hand, any one of our businesses could be necessary when expanding into new areas, depending on how they are used together. We are currently considering these possibilities with each segment and strategic business unit (SBU).

Questioner 3

Q: Although order intake results and progress versus the plan in Gas Turbine Combined Cycle (GTCC) have been steady, comparing the 1H FY2023 results with the 2H FY2023 forecast suggests that there may be a little weakness in Energy in 2H, mainly in GTCC. Could there be any upside to the current order intake or inquiries forecast in GTCC?

Kozawa: We received orders for a large project in 1H FY2023, which contributed to the strong order intake results. However, comparing the results in 1H with the forecast for 2H, there is absolutely no weakness in GTCC, and we expect the situation will remain positive. Order intake in Steam Power is expected to be lower than last year, but order intake from other businesses will compensate for this.

Q: I believe that you booked some one-time expenses related to the closure of Mitsubishi Logisnext's Swedish plant. Is it safe to say that this was included in this year's business profit forecast, so there will be no impact from this during the next fiscal year?

Kozawa: We revised the business profit forecast for LT&D considering one-time expenses. My understanding is that the expenses related to that issue are in the single-digit billion yen range.

Q: You mentioned that MHI will provide one-stop total energy solutions under the 2024 MTBP. During your considerations regarding the 2024 MTBP, what do you see as your shortcomings, and what do you want to expand on? Also, MHI will participate in two hydrogen projects in the US. The scale of hydrogen projects in the US as a whole is large, and I do not know the extent of your participation, but can we expect these projects to contribute to revenue?

Izumisawa: As for Energy Transition-related projects, I believe that CO2 capture and hydrogen projects will progress from feasibility studies (FS) to front-end engineering (FEED), but it is not yet clear to what extent they will reach final investment decisions (FID) during the 2024 MTBP period and become a reality. I think we can expect a certain amount of revenue when these projects actually begin to move forward. In terms of our shortcomings, the Energy Transition requires a connection between upstream and downstream processes, or between demand and supply; otherwise, projects cannot get off the ground. Furthermore, it is necessary to pay attention to whether prices including subsidies will allow for projects to be feasible. MHI is also working with ExxonMobil, which definitely has great potential.

Questioner 4

Q: Please elaborate on the background of GTCC's strong performance in FY2022 and FY2023. Is use of gas turbines as a backup for alternative power sources increasing, or are these systems being used for base load power? Have some projects started up again because of expectations for hydrogen co-firing? In addition to your having secured a high market share similar to last year's, I think that strong long-term service agreement (LTSA) orders may be one of the reasons GTCC is performing well.

Kozawa: I think our market share has been a big factor in this. MHI had the top market share from January to June this year. The high reliability of our latest main model of gas turbine, the J Series, especially the JAC line, has allowed us to attain the top market share. In addition to high performance evaluations, from the perspective of readiness for conversion to hydrogen fuel, we have a demonstration plant at our Takasago Hydrogen Park, and we also have high reliability ratings.

In terms of individual projects, the prevailing opinion had been that there would be demand for small-size gas turbines in order to compensate for the variable output of renewable energy, but there has been demand for our large frame gas turbines as well. Recently, we have received inquiries for simple cycle projects, which do not include the heat recovery boiler or steam turbine present in a combined cycle plant. During negotiations for these projects, customers have been telling us that they highly rate the performance and reliability of the J Series.

Q: What are your thoughts regarding profit margins in the Defense business? I do not think it will be easy to increase profit margins because of the R&D involved, but could you provide management's view on profit margins in the future when the current order backlog is translated into revenue?

Kozawa: While some media reports have mentioned 15% margins, due to the cost escalation factors involved, our understanding is that around 10% may be a more realistic

figure. It is hard to say whether we will be able to win orders with 10% margins, as this will depend on customer evaluations. That said, we have received orders with margins close to 10% recently, and we hope that the Defense business will be able to achieve a 10% margin in a few years.

Q: The 2024 MTBP will seek to increase both business profit margins and revenue, but I would like to confirm whether there is a commitment to achieve a 10% business profit margin. The weight of a number changes when it reaches double digits, but you also have to balance profitability with growth, so is there not necessarily a preference for double digits?

Izumisawa: Although it is difficult to provide a clear answer, I am dedicated to achieving a double-digit margin. In order for MHI to develop sustainably, we want to secure profit margins that will rival our competitors'. However, I cannot commit to reaching 10% right away. Please understand that we are at the stage of considering how to set realistic goals.

Questioner 5

Q: The effect of price optimization was +¥24 billion in 1H FY2023. Because the initial full-year forecast for this was +20 billion, you increased the LT&D business profit guidance by ¥10 billion. However, considering the +¥5 billion impact from the depreciation of the yen and one-time expenses related to the factory in Sweden in the single-digit billion yen range, the upside from price optimization should be around ¥10 billion. Please let me know the background of the higher-than-expected price optimization effects.

Kozawa: Part of the reason for the higher-than-expected price optimization effects is that, although there has been some impact from inflation, we have succeeded in limiting cost increases. As for the full-year forecast, I think the magnitude of YoY upside to business profit will become smaller in 2H FY2023, because we experienced a lot of positive impact in 2H FY2022.

Q: How much of an increase to business profit is expected in the current fiscal year versus the initial plan of +¥20 billion? Can we expect to see continued positive impact to business profit in the next fiscal year?

Kozawa: The outlook for the next fiscal year will depend on inflation. The reason why price optimization effects have been so significant this fiscal year is because of the low profitability we had in the past. Starting with the normalization of the relationship between price and cost taking place now, we will aim to pass through cost increases to customer prices as needed going forward. As such, I do not expect that we will see significant contributions from this item in the future. Going forward, we need to make sure that price increases do not fall behind cost inflation.

Q: Revenue progress in Turbochargers during 1H FY2023 was slow compared to the initial plan, and I believe that profitability is not good. Can we expect profit margins to recover in the next fiscal year?

Kozawa: Unfortunately, Turbochargers has been slow to recover, and while it is definitely struggling, I do not think this business will be much further behind the initial full-year forecast. In the next fiscal year and beyond, we plan to make some improvements to this business with a variety of approaches.

Q: I think there are many opinions on the transition to electric vehicles (EVs), but what are the possible scenarios for MHI's Turbochargers business in the medium to long term? Are you going to continue with this business, or are there scenarios where you might choose other options?

Izumisawa: The Turbochargers business is in a difficult situation, and we must do something about it. However, although the market for EVs will grow, demand remains strong for internal combustion engine vehicles, including plug-in hybrids, so we expect that the turbochargers market will be flattish.

Questioner 6

Q: In terms of upside in 2H FY2023, other than the IGCC buffer, price optimization benefits, and foreign exchange effects, is there anything that you have accounted for conservatively in the guidance? Also, I do not think there has been any improvement in the situation in Europe or China, so is there any risk of downside including in LT&D?

Kozawa: The ¥20 billion risk buffer is not specifically for IGCC but was set aside for risk in plant projects. While I would not consider this to be a very conservative estimate, if these risks can be successfully managed, this will be an upside factor. Regarding foreign exchange rates, the average rate for revenue recognition in 1H FY2023 was around ¥140/USD, so I do not think there will be too much upside. No risk factors are accounted for conservatively in the guidance.

That said, again on the risk side, while LT&D is showing good progress on the whole, there seems to be some slowdown in Europe. Although the US has performed well so far, considering the recent interest rate trends, an end to favorable conditions could be near at hand. We are monitoring the situation closely to prevent a dip in performance caused by an economic downturn.

Q: While the ROE target was 12% under the 2021 MTBP, the plan for this fiscal year is 11%. I think the business profit margin is in line with the plan, but is 11% ROE realistic considering asset turnover and financial leverage? Please let me know if you are particular about 12% ROE.

Kozawa: Profits are trending in line with expectations, but there are some factors that have increased equity due to a widening gap between market and book value caused by the rising stock price, together with foreign currency translation effects. When these factors are removed from the equation, I think that we will reach 12% ROE. Although I cannot share with you the specific ROE target under the 2024 MTBP, we would like to be able to achieve stable double-digit percentages.

Q: Under the 2021 MTBP, the revenue target for new businesses during FY2023 is ¥100 billion, and the target for FY2030 is ¥1 trillion. What is the revenue target under the 2024 MTBP? Based on the results of the 2021 MTBP, I would like to know how much you plan to increase revenue in which growth businesses and which businesses you are confident in.

Izumisawa: I expect the Energy Transition will take longer than originally envisioned. In particular, hydrogen and ammonia will not become a reality unless the supply and demand sides are properly connected, and although there are some hydrogen projects in the US, they will take longer than initially expected. However, there are many FSs including those in the inquiry phase, and we are also working on many CO2 capture projects. While closely monitoring when and in what form these projects will take shape, we will make plans including potentially shifting our focus to the US.

On the other hand, I think the data center business will get off the ground sooner than expected. Demand for data center-related systems such as those supporting 5G and generative AI is growing, especially in the US.

Logistics is an area that we want to steadily grow. I believe that the automation of logistics will rapidly spread, including as a means of addressing the expected shortage of truck drivers in Japan in 2024. Therefore, I would like to set forth a plan for our organizational approach to this area in the 2024 MTBP.

Questioner 7

Q: At what pace do you expect Defense revenue to grow in the future?

Kozawa: Until now, annual revenues were less than ¥500 billion, but I expect this to reach around ¥1 trillion from FY2026 to FY2027. From now until then, revenue will gradually increase.

Q: Is the general idea that revenue will increase by ¥100 billion per year in FY24 and FY25, then by ¥200 billion in FY2026?

Kozawa: There may be slight variations from year to year, but that is basically correct.

Q: Your operating environment has changed significantly since the 2021 MTBP was originally announced, but how will the initiatives taken during the 2021 MTBP – including new businesses and expanded services related to logistics – be incorporated into the 2024 MTBP? Please let me know if there are any current initiatives or future topics you can look forward to.

Izumisawa: On the topic of services, we are developing remote repair support solutions using augmented reality (AR) in our Paper Converting Machinery business, and we are also working to develop the same service for other products. Revenue from these efforts is gradually increasing.

As for the automation of logistics, our system has begun to be applied to factory logistics, and the groundwork we have laid is gradually becoming a reality. The outlook for the volume this business may reach will likely be included in the 2024 MTBP.

I think the major change in the situation from when we originally drafted the 2021 MTBP is in the Energy Transition. At that time, there was a strong shift to renewable energy, and the Energy Transition was only likely to involve CO2 capture. However, the market for gas turbines has grown, and now the biggest challenge for the Energy Transition is how to realistically create a roadmap to decarbonization. Under these circumstances, I believe that the preparations we have been making including technology development, are being connected to real opportunities in a variety of ways. I believe that we will either see significant growth during the 2024 MTBP period, or we will prepare groundwork for a major increase in results in the following MTBP.

Q: It seems like it will not be difficult to achieve a 10% business profit margin in the future. What do you think?

Izumisawa: During the 2021 MTBP, we have made a lot of progress in streamlining the business as well as improving management efficiency, including productivity, so I believe we are in a position where this is well within reach. It will take one or two more big pushes, but I do not think it is an impossible goal.

Kozawa: From a financial point of view, everyone's attention tends to focus on the P&L and profit margins, which of course I view as important. However, how to manage ROIC is also important, and considering the product mix, I do not think it will be that easy.

Note regarding forward looking statements:

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