A Message from the CFO

Basic Approach to Financial Strategy

MHI Group has a unique standard of financial stability called Triple One Proportion, or TOP, which refers to an ideal 1:1:1 balance among revenue, total assets, and market value. In terms of the relationship between turnover and total assets, we view achievement of TOP to be a total asset turnover ratio of 1, which we see as one of the main financial barometers of the manufacturing industry. Regarding the relationship between total assets and net profit, given that share price mainly trends together with profitability, we believe a return on assets (ROA) above 6% is necessary, although this depends on the valuation method and general thinking around share price.

Comparing our FY2021 results against these targets, our total asset turnover ratio was only 0.75, and ROA was 2.3%. Therefore, there remains much room for improvement.

We continue to take steps to improve return on invested capital (ROIC) in each of our businesses, for example, by shortening the cash conversion cycle (CCC) and raising productivity. As CFO, one of my missions is to improve asset efficiency throughout the Company. In order to achieve this, I am working to manage assets by replacing those with inferior profitability with assets expected to contribute to future earnings. In terms of scope, this involves not only real estate holdings and past investments, but optimizing the business portfolio as well.

I fully understand that investors and shareholders focus on return on equity (ROE). In addition to pursuing higher profitability, today we maintain a conservative capital structure with a high level of equity. That said, I believe that as profitability and the asset portfolio improve going forward, we will have the option of gradually increasing leverage.

2021 Medium-Term Business Plan Progress

The 2021 MTBP, which began in April 2021, has two overarching goals, developing growth areas and strengthening profitability. We are focusing on three financial measures: business profit margin and ROE on the P&L side and interest-bearing debt on the BS side. In FY2023, the final year of the Plan, we are targeting a business profit margin of 7%, ROE of 12%, and interest-bearing debt of 0.9 trillion yen. To achieve these targets, as we indicated in our capital allocation plan for the three-year period of the 2021 MTBP, we seek to decrease interest-bearing debt and strengthen financial stability by improving profitability, increasing regular operating cash flow, and investing those funds into growth areas.

In FY2021, the first year of the 2021 MTBP, we exceeded our initial projections for orders received, revenue, and business profit. Business profit margin was approximately 4.2%, and ROE around 7.7%. Free cash flow reached a record 301.8 billion yen, the result of increased operating cash flow and substantial growth in investing cash flow, enabled by asset sales, including those of strategic shareholdings. In response to these results, we issued

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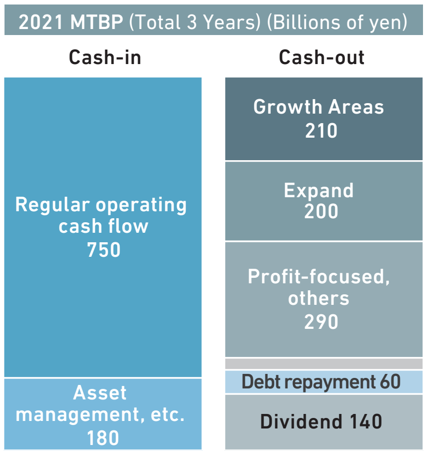
Financial Indicators Over Time

	FY2018	FY2020	FY2023
Revenue	¥4.1 trillion	¥3.7 trillion	¥4.0 trillion
Business profit margin	5%	1.5%	7%
ROE	7%	3.1%	12%
Total assets	¥5.1 trillion	¥4.8 trillion	¥4.5 trillion
Interest-bearing debt	¥0.67 trillion	¥0.9 trillion	¥0.9 trillion
Equity	¥1.7 trillion	¥1.4 trillion	¥1.5 trillion
Debt/Equity ratio	0.4	0.6	0.6
Equity ratio	34%	28%	33%
Dividend per share	¥150	¥75	¥160



* Adjusted from previously disclosed materials for the portion realized in advance in FY2020.

an annual dividend of 100 yen per share, exceeding our projection at the start of the term.

Turning to the balance sheet, as of the end of FY2021, total assets increased by around 300 billion yen year-on-year. This increase was largely due to three factors: inventory build-up in preparation for supply chain disruptions, increased yen valuation of foreign currency-denominated assets associated with the devaluation of the yen near the end of the fiscal year, and holding of excess cash on hand. While this increase in total assets did occur at the same time as efforts to curb assets in the lead up to TOP achievement, it was fully within our allowed range. In FY2022, effectively maintaining control of inventory levels and lead times amid supply chain instability in order to improve CCC has been a challenge, and we are implementing measures to address this. As of the end of FY2021, gross interest-bearing debt finished near 735 billion yen, down roughly 170 billion yen year-on-year. Net interest-bearing debt, which excludes cash and cash equivalents, reached approximately 420 billion yen, down some 240 billion yen compared to the end of FY2020.

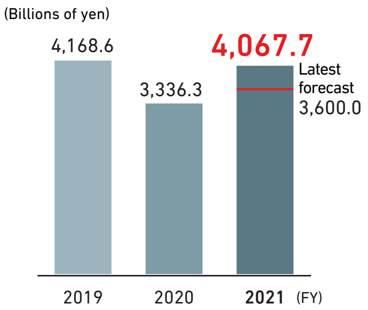
In light of the business profit margin, ROE, and interest-bearing debt figures I have just cited, overall I believe the first year of the 2021 MTBP showed acceptable results. That said, in order to achieve our targets for FY2023, especially a 7% business profit margin and 12% ROE, we will need to raise our profitability by one or two steps to meet the market's expectations.

Risk Management

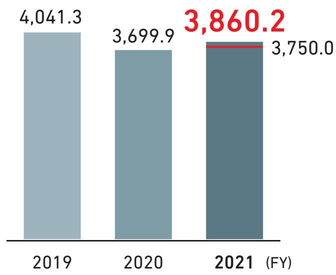
A major risk factor for the foreseeable future will be ongoing supply chain disruptions. The adversities that impacted global markets in 2021–semiconductor chip shortages, soaring material prices, and rising logistics costs–are likely to continue affecting MHI Group's earnings going forward. However, these are common challenges shared by all companies, and we hope to gain our customers' understanding as we request that they assume a fair share of increasing costs.

FY2021 Financial Results

Orders Received



Revenue



EBITDA

¥292.4 billion

(+¥99.0 billion YoY)

EBITDA margin

7.6%

(+2.4% YoY)

Free Cash Flow

¥301.8 billion

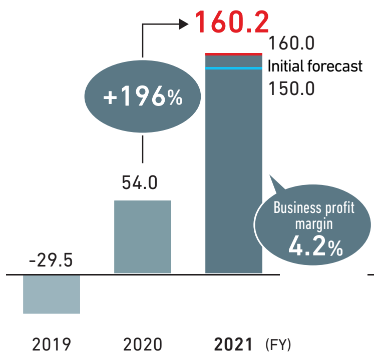
(+¥579.0 billion YoY)

Operating Cash Flow

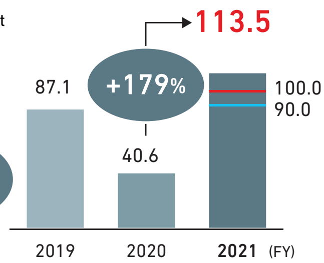
¥285.5 billion

(+¥380.5 billion YoY)

Profit from Business Activities



Profit Attributable to Owners of Parent



Interest-Bearing Debt

¥734.9 billion

(-¥170.6 billion YoY)

Net Interest-Bearing Debt

¥420.6 billion

(-¥239.5 billion YoY)

ROE

7.7%

(+4.6% YoY)

Dividends

¥100/share

(+¥25/share YoY)

At the same time, we will continue taking internal steps to curb costs. We see cost structure reform as an ongoing issue, and during the three years of the 2021 MTBP, we are targeting a 20% reduction in SG&A ratio. To that end, we are continuing with function sharing and consolidated purchasing while also pursuing organizational and human resource optimization through improvements in administrative processes and IT systems. For example, we are working to cut process operating costs by integrating finance and accounting systems at our Group companies worldwide and also by standardizing and sharing not only the systems themselves but also the tasks associated with them. We anticipate results beginning in FY2023.

To manage financial risk in general, we are consolidating funds at financial subsidiaries Groupwide and building a mechanism to lend surplus funds to Group companies when needed. This will not only enable us to optimize borrowing and reduce capital procurement costs for MHI Group as a whole, but it will also allow us to understand the flow of funds to and from each Group company, which should help us mitigate various risks.

Insofar as foreign exchange risk is concerned, an increase in the ratio of production outside of Japan and other factors have reduced overall impact from exchange fluctuations compared to previous periods. However, as we transition to handling more currencies, the impact from exchange fluctuations of currencies other than the U.S. dollar and euro has increased in relative terms. With respect to interest levels, policy changes are gradually underway to move away from the financial relaxation seen globally since the start of the COVID-19 pandemic. Since the markets are outside of our control, we are taking steps to minimize risk with diverse hedging methods while recognizing that a certain amount of market fluctuation is inevitable.

A Message from the CFO

Approach to Growth Investments, Capital Policy and Shareholder Return

MHI has defined the Energy Transition and Smart Infrastructure as two growth areas in which we are actively investing during the 2021 MTBP period. Both of these efforts will contribute to realizing Carbon Neutrality. Specifically, we intend to make in-house investments in plants and equipment as well as R&D. Externally, we anticipate M&A as well as investment in start-ups. For the time being, we plan to make roughly 200 billion yen in annual growth investments, with total investments to reach approximately 300 billion yen per year.

We expect the capital to fund these investments to come mainly from operating cash flow and asset sales, including those of strategic shareholdings. We also have debt borrowing capacity as our financial structure has improved through interest-bearing debt reductions. As a result, we plan to rely primarily on internal funds and debt. At present we are not planning to resort to equity financing. That said, depending on financial market trends and our capital needs, we may need to use appropriate fund-raising methods, including equity financing. So, we are continuing investigation and research in preparation for any possibility.

Concerning shareholder return, we are currently aiming for a payout ratio of around 30%. In order to respond to the medium to long-range expectations of our shareholders and investors, we believe that both dividend levels and stability are important. In the future, I believe that defining shareholder return using dividends on equity (DOE), which calculates dividends as a ratio of equity, is another possible approach.

As a short-term method of shareholder return, share buyback offers another possibility. However, in light of MHI's long business development span, I believe that combining long-term growth investments with stable dividends would likely be more acceptable to shareholders and investors. Therefore, we first plan to raise our dividend levels by improving our normalized profitability, after which we will consider other shareholder return methods as a next step.

Our Approach to Business Portfolio Management

At MHI Group, we continuously evaluate the performance of our business units, known as Strategic Business Units (SBU), using an in-house evaluation method called the Strategic Business Assessment System. Applying the results of these ongoing evaluations, we recalibrate and optimize our business portfolio through the strategic allocation of management resources. Specifically, we allocate internal equity and debt to each SBU based on our evaluation of their growth and earning potential. Management puts a lot of thought into the allocation of resources to individual SBUs. Decisions relating to allocation are reached through discussions among members of the management team taking into account each SBU's current performance as well as its future growth potential. Resources are taken away from businesses designated for scale reduction, whereas businesses we wish to grow receive ample fund allocations.

During the 2021 MTBP period, we have divested some businesses and locations with issues. For example, we divested our Machine Tools business and part of Koyagi Shipyard to other companies. At the same time, we acquired Mitsui E&S's Naval and Governmental Ships business.

When considering which areas of MHI Group's business portfolio should be expanded, I look at each business from two perspectives. The first is whether or not a given business can expect market growth. I have to be cautious, however, how to define the market being considered. It is meaningless to assume a business has growth potential if there are areas of the market that we cannot access. I have to ascertain a realistic picture of the situation based on the actual ability to access the market, MHI Group's positioning versus competitors, and other factors. The second perspective is whether MHI is the best owner or not. This is based on the idea that MHI Group should acquire businesses whose value we are capable of increasing to a level unachievable by other companies. Conversely, we should release our businesses if the opposite is true. Making a comprehensive evaluation – based not only on the Company's technological strengths but also on considerations such as MHI Group's presence in the given market, and how skilled our management is in that industry–and coming to a level-headed determination of who–MHI or another company–would be more capable of growing said business and raising its value, is a perspective I believe is vital to business portfolio management.

Enhancing Corporate Value through Dialogue with Shareholders and Investors

Throughout the years, we have continued to respond to society's evolving needs and provide the world with products and technologies supporting residential and industrial infrastructure. We have followed this path in line with Our Principles, our philosophy which is rooted in the Three Principles of Mitsubishi Group.

In accordance with the 2021 MTBP, we are seeking to achieve Carbon Neutrality, a challenge of global scale. We are addressing two areas in particular, the Energy Transition and Smart Infrastructure. In order to finance these efforts, we have raised a portion of the needed funds with two Green Bonds and FY2022's Transition Bond. I hope these bonds will be widely understood to reflect our stance and actions being taken toward realizing Carbon Neutrality.

In the past, the focus of discussions with shareholders and investors was our finances and short-term results. Recently, however, I sense a growing shift toward interest in topics relating to sustainability, such as ESG. I would like to convey precisely to investors how our management is aligned with the U.N.'s Social Development Goals (SDGs) by making appropriate disclosures not only of financial information but also of non-financial information as well. Although opportunities to meet directly with shareholders and investors and to discuss such matters decreased during the COVID-19 pandemic, going forward I hope to have more direct meetings so that we may engage in communication on a deeper level.

Looking ahead, I will continue to work hard to explain our yearly initiatives in detail to shareholders and investors as well as to share the results of the 2021 MTBP with you. I sincerely ask for your continued understanding and support.