February 1, 2019
Fuji Electric Co., Ltd.

Condensed Transcript of Q&A Session Regarding Financial Results Presentation for the Nine-Month Period Ended December 31, 2018

Date: February 1, 2019 (Friday) 10:00–11:00

General

Q. What were the reasons behind the downward revisions to the forecasts for business results in the Power and New Energy and the Electronic Devices segments and when were these reasons identified?

A.

・The downward revision to the forecast for the Power and New Energy segment was instituted in reflection of an increase in costs associated with a large-scale project that was identified during the third quarter of the fiscal year.

Everything was as planned with regard to the procurement of major equipment and the incurring of costs until it became apparent, in the third quarter, that we would need to purchase a larger volume of pipes and valves than had been initially expected and that installation costs were also going to increase. A loss was recorded in reflection of this development. Costs were translated to expenses for accounting purposes after careful assessment, and we do not expect any additional expenses to be incurred with regard to this project going forward.

・In the Electronic Devices segment, we decided to institute a downward revision to forecasts in January 2019 out of consideration for market conditions in the third quarter and beyond and performance thus far.

Q. When is the macroeconomic environment expected to improve?

A.

・It is difficult to formulate an outlook for the fiscal year ending March 31, 2020, and beyond due to the potential impacts of the trade friction between the United States and China and the issues surrounding the United Kingdom's decisions to withdraw from the European Union. The impacts on market conditions will vary by business, but we are hoping for an upturn around the midpoint of the fiscal year ending March 31, 2020.

Q. What businesses offer promising outlooks for the fiscal year ending March 31, 2020, and beyond?

A.

・We are currently in the process of formulating our plan for the fiscal year ending March 31, 2020. However, we can say that Fuji Electric's primary growth drivers are expected to be power electronics systems and power semiconductors. In regard to the former, we will focus on acquiring comprehensive electrical equipment solutions and system orders.

Power Electronics Systems

Q. How were trends in orders for low-voltage inverters?

A.

・Orders were strong in Japan during the nine-month period ended December 31, 2018, and this trend in continuing in the fourth quarter.
Orders in the third quarter were down by between 10% and 20% year on year, and we expect a similar level of orders in the fourth quarter.

Q. What is your outlook for the operating environment in major power electronics systems businesses?

A.

・In the energy management business, we project a large increase in orders on the back of higher system project demand in Asia. Based on our assessment of capital expenditure trends among domestic machine tool and semiconductor manufacturers, the power supply and facility systems business is expected to experience the prolongation of projects. The ED&C components business, meanwhile, is witnessing declines in sales of products to machine tool manufacturers contrasted by consistently robust sales of products to distribution panel manufacturers in Japan.

・The decline in demand for low-voltage inverters and servos in China is projected to continue throughout the first half of the fiscal year ending March 31, 2020. Conversely, we anticipate increased demand for low-voltage inverters in the United States and Taiwan. In factory automation systems, order trends for ship scrubbers have been favorable.

Q. What are your full-year forecasts for power electronics system components?

A.

・Looking at Fuji Electric's three major power electronics system product lines, we expect higher sales and income for low-voltage inverters. Factory automation components, however, will suffer year-on-year declines in overall sales and income as servos, which benefited from strong automation demand in the first half of the fiscal year, are being impacted by decreased demand from China in the second half. Industrial motors will see increased orders, predominately in Japan, leading to growth in both sales and income.

Q. What is the forecast for ship scrubber orders?

A.
・We expect to have an order backlog of more than 50 sets on March 31, 2019.

Q. Have there been any changes to the lineup, production systems, or order trends for ship scrubbers?

A.
・We currently offer scrubbers that can cover vessels up to the 16 MW class. Development is underway on scrubbers for large-scale 24 MW class vessels. We look to launch such scrubbers during the first half of the fiscal year ending March 31, 2020. In addition, we are examining the possibility of expanding our production system beyond the Chiba Factory, presently the only factory used, to include other factories. As for production capacity, we aim to achieve a capacity of six units a month within the fiscal year ending March 31, 2019, through capital expenditures in the Chiba Factory to generate annual sales of more than ¥10.0 billion. Turning to order trends, although orders were previously centered on newly built ships, we have recently been receiving orders for scrubbers to be used on existing vessels.

<u>Electronic Devices</u>

Q. Could you please breakdown the third-quarter performance and full-year forecasts for the Electronic Devices segment in terms of semiconductors and magnetic disks?

A.
・Third-quarter net sales amounted to ¥25.7 billion for semiconductors and ¥6.4 billon for magnetic disks. On a full-year basis, semiconductors are expected to generate net sales of approximately ¥110.0 billion while net sales from magnetic disks are anticipated to be around ¥24.0 billion.

・We have not disclosed such breakdowns for operating income.

Q. Is it possible to get a breakdown of the downward revision to the full-year forecast for operating income in the Electronic Devices segment by subsegment? Also, do the revised forecasts see the magnetic disk business maintaining profitability on the operating income level?

A.
・Of the ¥0.9 billion decrease in operating income, roughly half is attributable to semiconductors while the remaining half is associated with magnetic disks.

・Profitability is being maintained in the magnetic disk business.

Q. Sales in the Electronic Devices segment are projected to decline in the fourth quarter in comparison to third quarter while income increases. What are the reasons behind this outlook?

A.

・Net sales will decrease in fourth quarter as a result of foreign exchange influences as we assume an exchange rate of ¥105 to US$1.

Conversely, we anticipate a slight increase in operating income to result from a more favorable sales mix. The performance of industrial power semiconductors will be impacted by changes in the sales mix while automotive power semiconductors see performance improve.

Q. Why did operating income in the Electronic Devices segment decrease year on year in the third quarter and why is operating income in this segment projected to increase in the fourth quarter? Also, has there been any changes from the initial forecasts with regard to depreciation and leases paid?

A.

・The third-quarter decrease in operating income in the Electronic Devices segment was largely a result of foreign exchange influences. Year-on-year increases in R&D expenditures, depreciation, and leases paid were also factors. In the fourth quarter, we anticipate a slight increase in operating income as a result of changes in the sales mix.

・There have been no changes from the initial forecasts for depreciation and leases paid, and these items are projected to increase year on year.

Q. How were orders for power semiconductors in the third quarter and what is your outlook for orders in the fourth quarter?

A.

・In the third quarter, orders were down by between 10% and 20% year on year due in part to foreign exchange influences. This decrease in orders was primarily concentrated on products for the industrial field, with a large drop in orders for industrial modules and a slight decline in orders for discrete industrial devices. Orders for automotive power semiconductors were relatively unchanged year on year.

・In the third quarter of the fiscal year ended March 31, 2018, we recorded upfront orders. If the impacts of these upfront orders and of foreign exchange influences on orders in the third quarter of the fiscal year ending March 31, 2019, are excluded, the decrease in orders was in the single digits.

・Orders in the fourth quarter are expected to be around the same level as in the third quarter.

Q. What is your outlook for power semiconductor orders going forward?

A.

・It is currently unclear whether or not demand has dropped to its lowest point, and we expect flat growth in industrial power semiconductors through the first quarter of the fiscal year ending March 31, 2020. Orders for automotive power semiconductors are expected to grow in the fourth quarter of the fiscal year ending March 31, 2019, and on into the following fiscal year.

Q. What is the situation regarding capacity utilization and inventories for power semiconductors?

A.

・Front-end process capacity utilization is at more than 90%, nearly full capacity, centered on 8-inch wafers while back-end process capacity utilization is between 80% and 90% following the slight decline in orders for industrial power semiconductors. Inventories are at normal levels, and we do not feel that we are overstocked.

Q. Is it correct to assume that the sluggish orders for power semiconductors are a result of lower end demand rather than inventory adjustments at customers and distributors?

A.

・The sluggish orders for power semiconductors are a result of lower demand.

Q. What was the background for the decision to invest in increased production of power semiconductors ahead of schedule? Also, when will facilities begin operating at the increased capacity?

A.

・Demand for automotive power semiconductors is increasing at a rate that is exceeding our plans, prompting the decision to invest an additional ¥25.0 billion in production ahead of schedule. This amount is viewed as part of the announced amount of capital expenditure to be conducted leading up to the fiscal year ending March 31, 2024, and will be executed beginning in the second half of 2019 and continuing through 2020.

・The benefits of the ahead-of-schedule production capacity investments will start to appear in the second half of the fiscal year ending March 31, 2020, and the augmentations will be completed in the second half of the fiscal year ending March 31, 2021.

Q. What is the background behind the strong performance of automotive power semiconductors? Has Fuji Electric been siphoning shares away from competitors?

A.

・The strong performance of automotive power semiconductors is not exclusive to Fuji Electric, but is rather an industry-wide trend. However, Fuji Electric is the only company that is able to apply RC-IGBTs, which contribute to more compact equipment, to automotive applications, a factor that differentiates it from other companies.

Q. How long do you expect Fuji Electric to be able to maintain its technological edge with regard to RC-IGBTs?

A.

・Efforts to have proposed specifications accepted by customers with regard to automotive power semiconductors require five to six years to take root. We therefore expect to be able to maintain our technological edge for at least that long.

Q. Why is demand for IGBT modules increasing in comparison to SiC modules in regard to automotive power semiconductors?

A.

・At the moment, the price of SiC modules is rather high, which is why demand for IGBT modules increasing in comparison to SiC modules. For this reason, it is necessary to address environmental and fuel regulations with IGBT modules. However, there are limits to the performance that can be realized with silicon, the material used to make IGBT modules; SiC modules are required to accommodate high voltages such as 10,000 volts. With the exception of railroad applications, most automotive and standard industrial applications entail voltages of between 1,200 and 1,500 volts, meaning that silicon is sufficient.

Q. Has there been any changes to your plans to boost production of magnetic disks in light of the sluggish conditions in the data center and other markets?

A.

・Demand for products for data center applications is currently on the decline. Although we had planned to invest in increased production capacity for magnetic disks in the second quarter of the fiscal year ending March 31, 2019, these plans were revised in light of the low demand.

Q. Am I correct to assume that, although demand for magnetic disks was strong up until the third quarter, a rapid dip in demand was seen in the fourth quarter? Also, will this dip be temporary with demand growing over the medium term?

A.

・Demand began to fall below forecasts during the third quarter, and we expect demand to be substantially lower than anticipated during the fourth quarter.

・Magnetic disk demand is projected to increase from a long-term perspective.

Q. What portions of third-quarter magnetic disk sales are attributable to aluminum substrate disks and to glass substrate disks?

A.

・Aluminum substrate disks and glass substrate disks both accounted for roughly half of the third-quarter magnetic disk sales volume.

Food and Beverage Distribution

Q. Performance in the Food and Beverage Distribution segment has been low in comparison to previous fiscal years throughout the nine-month period ended December 31, 2018. Why, in contrast to this trend, has operating income begun to grow in the fourth quarter?

A.

・We have begun launching new products in the store distribution business, which are anticipated to contribute to higher net sales and operating income in the fourth quarter.