Management's Discussion and Analysis

Overview

During fiscal 2018, the year ended March 31, 2019, the overseas operating environment for Fuji Electric saw a trend toward investment restraint in the Chinese market in the second half of the fiscal year due to factors including the trade friction between the United States and China.

In Japan, despite a sense of slowing down in some sectors, there was firm demand resulted from increases in the replacement of aged equipment and investments in automation, labor saving, and energy saving for production facilities aimed at improving productivity.

In this environment, we sought to complete the measures put forth in the FY2018 Medium-Term Management Plan, Renovation 2018, which concluded with the fiscal year ended March 31, 2019. In addition to strengthening the power electronics systems business and promoting proactive investments with a view to expanding the power semiconductor business, we further enhanced manufacturing capabilities, and pursued improved profitability by reenergizing the Companywide Pro-7 Activities designed to enhance business quality.

Financial Performance

Net Sales

Net sales in fiscal 2018 increased by 2.4% year on year, to ¥914,915 million, as a result of strong demand.

In the Power Electronics Systems—Energy Solutions, Power Electronics Systems—Industry Solutions, Power and New Energy and Electronic Devices segments, sales increased year on year. However, sales in Food and Beverage Distribution segment decreased year on year. Domestic sales increased by 1.1%, to ¥682,503 million. Overseas sales increased by 6.3%, to ¥232,412 million.

The ratio of overseas sales increased by 0.9 percentage point, to 25.4% year on year.

Cost of Sales, Selling, General and Administrative Expenses and Operating Income

The cost of sales increased by 2.7% year on year, to ¥679,877 million, and the ratio of cost of sales to net sales increased by 0.2 percentage point, to 74.3%.

Selling, general and administrative expenses decreased by 0.3% year on year, to ¥175,066 million. The ratio of selling, general and administrative expenses to net sales decreased by 0.6 percentage point, to 19.1%.

Operating income increased by ¥4,010 million year on year, to a record high of ¥59,972 million, due to higher net sales and production volumes as well as the benefits of cost reductions. The operating margin increased by 0.3 percentage point, to 6.6% year on year.

Non-Operating Income (Expenses) and Ordinary Income

Non-operating income (net) was ¥3,507 million, a ¥3,422 million increase from ¥85 million in the previous fiscal year. This increase was mainly due to a ¥2,169 million increase in foreign exchange gains (losses), a ¥610 million increase in dividends income and a ¥446 million increase in equity in earnings of affiliates.

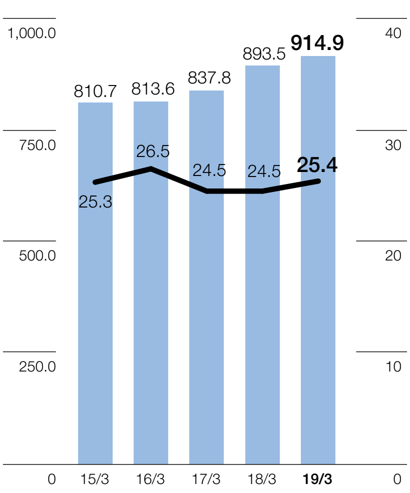
As a result, ordinary income grew ¥7,432 million year on year, reaching a new record high of ¥63,479 million.

Extraordinary Income (Loss), Income before Income Taxes and Non-Controlling Interests

Extraordinary income totaled ¥2,451 million and included a gain on sales of noncurrent assets, a gain on sales of investment securities and foreign currency translation adjustments reversal gains. This represented a ¥551 million year-on-year increase due to an increase in foreign currency translation adjustments reversal gains,which were offset by a reduction in gain on sales of investment securities.

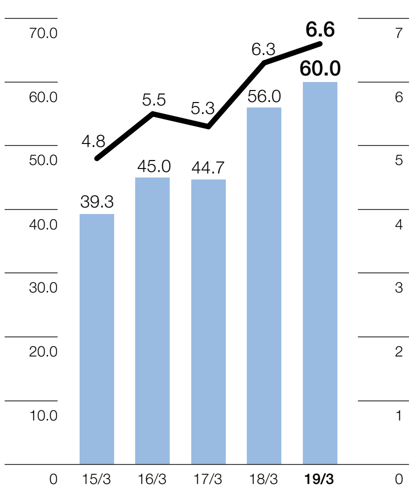
Extraordinary loss totaled ¥3,643 million and included a loss on disposal of noncurrent assets, a loss on devaluation of investment securities and the impairment loss. This represented a ¥2,501 million year-on-year increase primarily due to the impairment loss recorded in this fiscal year.

Net Sales / Ratio of Overseas Sales to Net Sales



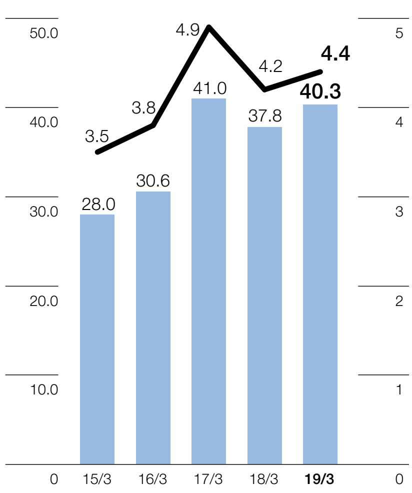
■ Net Sales (left)
— Ratio of Overseas Sales to Net Sales (right)

Operating Income / Ratio of Operating Income to Net Sales



■ Operating Income (left)
— Ratio of Operating Income to Net Sales (right)

Net Income Attributable to Owners of Parent / Ratio of Net Income Attributable to Owners of Parent to Net Sales



■ Net Income Attributable to Owners of Parent (left)
— Ratio of Net Income Attributable to Owners of Parent to Net Sales (right)

Net Income

Income before income taxes increased by ¥5,482 million year on year, to ¥66,287 million. After subtracting ¥17,217 million in income taxes (the net of income taxes-current and income taxes-deferred) and ¥4,803 million in net income attributable to non-controlling interests, net income attributable to owners of parent increased by ¥2,504 million from the previous fiscal year, to ¥40,267 million.

Results by Business Segment

Power Electronics Systems—Energy Solutions

Net sales: ¥224,787 million (an increase of 3.3% year on year)
Operating income: ¥16,854 million (an increase of ¥2,839 million year on year)

Net sales and operating income increased year on year. Solid performance in the facility / power source system business and the ED&C components business supported.

- In the energy management business, net sales decreased year on year primarily due to the impact of large-scale orders from overseas in the previous year and weak demand for smart meter. However, operating income increased year on year due to the benefits of cost reduction efforts.
- In the facility / power source system business, net sales and operating income increased year on year due to increases in large-scale orders in Japan.
- In the ED&C components business, net sales and operating income increased year on year as a result of strong demand from power distribution manufacturers.

Orders received in fiscal 2018 (Power Electronics Systems—Energy Solutions segment of Fuji Electric Co., Ltd., non-consolidated-basis) totaled ¥141.4 billion.

Power Electronics Systems—Industry Solutions

Net sales: ¥321,942 million (an increase of 0.3% year on year)
Operating income: ¥19,393 million (an increase of ¥473 million year on year)

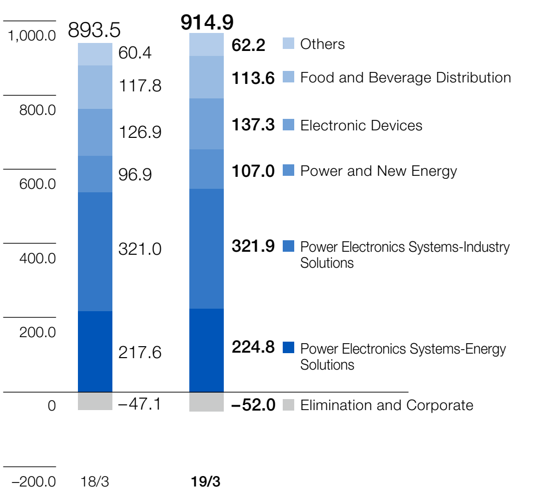
Net sales and operating income increased year on year. Performance was driven by the factory automation business, the equipment construction business and the IT solutions business.

- In the factory automation business, net sales and operating income increased year on year as a result of strong demand mainly for inverters, motors and FA System in Japan partially offset by weak overseas business result in the second half.
- In the process automation business, net sales and operating income decreased year on year due to the impact of large-scale orders in the previous year.
- In the social solutions business, net sales and operating income decreased year on year primarily due to weak demand for electrical equipment for railcars.
- In the equipment construction business, net sales and operating income increased year on year due to increases in orders from the electricity equipment construction including the plant power distribution equipment.
- In the IT solutions business, net sales and operating income increased year on year due to increases in orders from the academic sector and the public sector.

Orders received in fiscal 2018 (Power Electronics Systems—Industry Solutions segment of Fuji Electric Co., Ltd., non-consolidated-basis) totaled ¥154.1 billion.

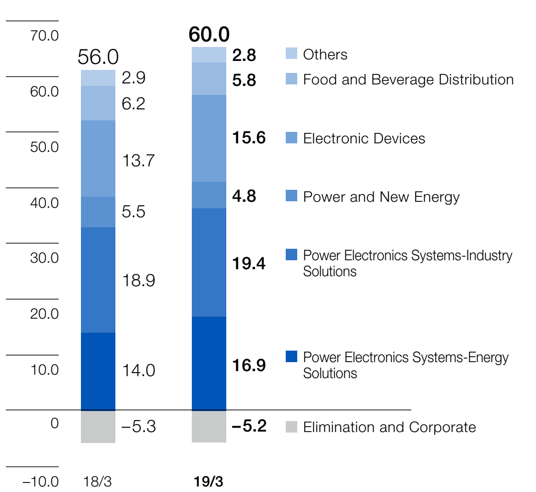
Net Sales by Segment

(Billions of yen)



Operating Income (Loss) by Segment

(Billions of yen)



Power and New Energy

Net sales: ¥107,012 million (an increase of 10.5% year on year)
Operating income: ¥4,750 million (a decrease of ¥771 million year on year)

- In the power generation business, net sales increased year on year due to increases in orders from the solar power generation systems. However, operating income decreased year on year as a result of cost increases in large-scale orders.

Orders received in fiscal 2018 (Power and New Energy segment of Fuji Electric Co., Ltd., non-consolidated-basis) totaled ¥80.0 billion.

Electronic Devices

Net sales: ¥137,334 million (an increase of 8.2% year on year)
Operating income: ¥15,623 million (an increase of ¥1,924 million year on year)

- In the electronic devices business, net sales and operating income increased year on year as a result of strong demand from the automotive field and the magnetic disks partially offset by weak demand for power semiconductors in Japan from the industrial field in the second half.

Orders received in fiscal 2018 (Electronic Devices segment of Fuji Electric Co., Ltd., non-consolidated-basis) totaled ¥91.4 billion.

Food and Beverage Distribution

Net sales: ¥113,606 million (a decrease of 3.5% year on year)
Operating income: ¥5,756 million (a decrease of ¥478 million year on year)

- In the vending machine business, net sales and operating income increased year on year primarily due to strong demand from customers in the Japanese market.
- In the store distribution business, net sales and operating income decreased year on year due to weak demand for store equipment for use in convenience stores.

Orders received in fiscal 2018 (Food and Beverage Distribution segment of Fuji Electric Co., Ltd., non-consolidated-basis) totaled ¥101.8 billion.

Others

Net sales: ¥62,231 million (an increase of 3.0% year on year)
Operating income: ¥2,766 million (a decrease of ¥95 million year on year)

R&D Investment and Plant and Equipment Investment

R&D

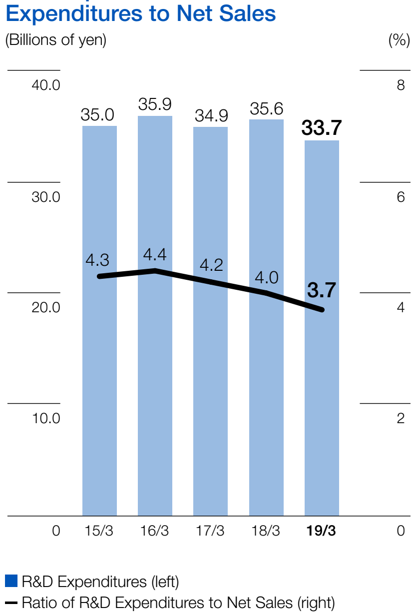
Fuji Electric focused on research and development activities for creating competitive components and systems centered on power electronics technologies and, power semiconductor technologies, and activities for developing solutions that produce value for customers by combining fundamental technologies.

The Company has re-organized its R&D structure to accelerate R&D activities. Product development functions are delegated to the respective business groups. The corporate R&D group is responsible for technology marketing, advanced research, and basic research.

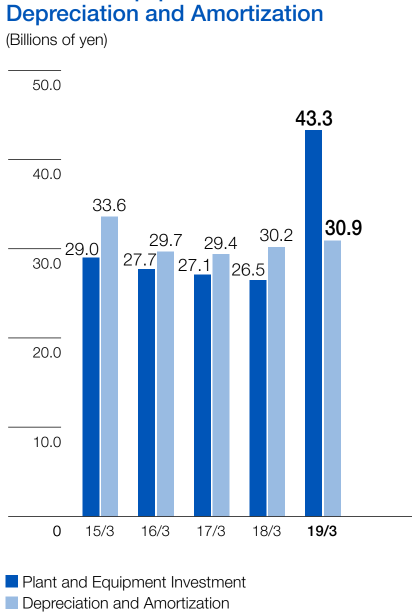
The Company's R&D expenditures in fiscal 2018 totaled ¥33,669 million.

As of March 31, 2019, the number of industrial property rights which were registered in Japan and overseas and held by Fuji Electric stood at 12,574.

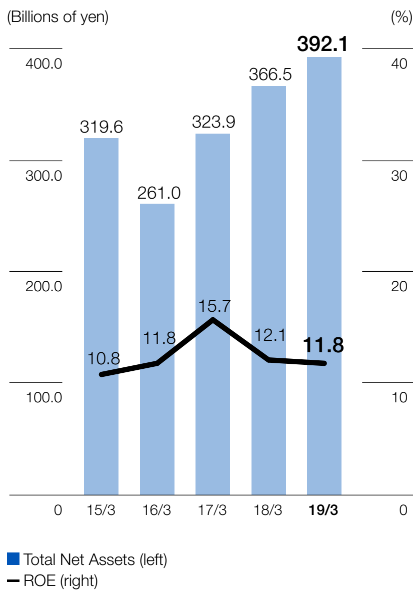
R&D Expenditures / Ratio of R&D Expenditures to Net Sales



Plant and Equipment Investment / Depreciation and Amortization



Total Net Assets / ROE



Plant and Equipment Investment

Plant and equipment investment, including leases, amounted to ¥43.3 billion in fiscal 2018. These expenditures were primarily directed toward electronic devices and power electronics and included new semiconductor product startups and production capacity expansions for automotive applications, as well as increasing sales of systems products and automation of production lines.

Major investments were as follows.

The Electronic Devices segment conducted large-scale investments in front-end processes to increase production capacity of power semiconductor chips mainly for automotive applications at the Yamanashi Factory.

In back-end processes, capital expenditures for production equipment to increase production of intelligent power modules (semiconductors element used in power generation) were conducted at domestic and overseas bases, and investment in launching the production line for new automotive products was carried out at factories in Japan.

In the Power Electronics Systems—Energy Solutions segment, investments were conducted in earthquake countermeasures at the Chiba Factory, and in beginning construction of a factory in Thailand for the purpose of bolstering sales of system products.

The Power Electronics Systems—Industry Solutions segment conducted capital expenditures for expanding mass-production of printed boards in Thailand. Meanwhile, we made capital expenditures at the Suzuka Factory with the aim of reducing the cost of rotary machine models.

In the Food and Beverage Distribution segment, investments were conducted in new servo presses to reduce the cost of vending machine models.

Financial Position

Total Assets

Total assets on March 31, 2019, stood at ¥952,659 million, an increase of ¥37,915 million from the end of the previous fiscal year.

Current Assets and Current Liabilities

Total current assets increased ¥54,625 million from the previous fiscal year-end, to ¥573,096 million. This increase is mainly due to increases of ¥27,215 million in inventories and ¥21,747 million in trade receivables.

Total current liabilities stood at ¥425,894 million on March 31, 2019, an increase of ¥21,153 million year on year. This increase is mainly because the decrease of ¥2,490 million in short-term debt partially offset by increases of ¥12,693 million in trade payables, ¥4,921 million in current portion of long-term debt, and ¥2,599 million in income taxes payable.

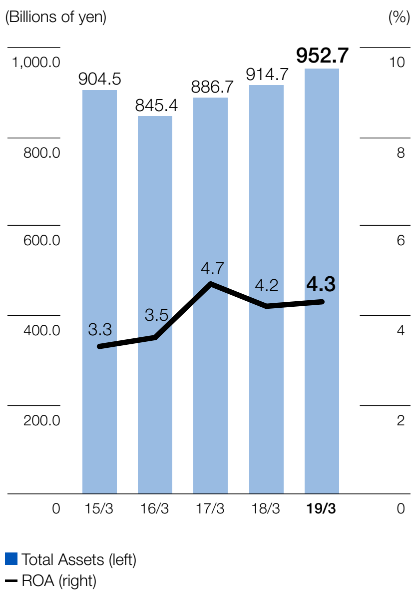
Noncurrent Assets

Total noncurrent assets decreased by ¥16,710 million year on year, to ¥379,563 million on March 31, 2019. Net property, plant and equipment were ¥182,124 million, an increase of ¥7,524 million year on year. Total investments and other assets amounted to ¥197,439 million, a decrease of ¥24,234 million year on year. This decrease is mainly due to a ¥23,727 million decrease in net defined benefit asset.

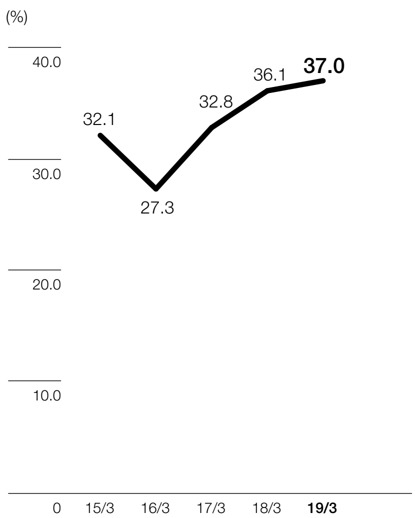
Long-term Liabilities

Total long-term liabilities decreased by ¥8,753 million from the previous fiscal year-end, to ¥134,704 million. Net defined benefit liability and lease obligations increased by ¥3,275 million and ¥2,095 million, respectively, but these increases were partially offset by a ¥13,887 million decrease in long-term debt.

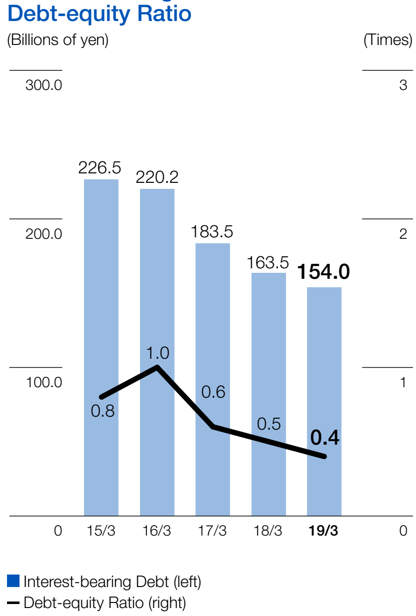
Total Assets / ROA



Equity Ratio



Interest-bearing Debt / Debt-equity Ratio



Net Assets
Net assets as of March 31, 2019, totaled ¥392,061 million, an increase of ¥25,515 million from the previous fiscal year-end. This increase was mainly attributable to an increase of ¥28,423 million in retained earnings.

As a result, the equity ratio stood at 37.0%, an increase of 0.9 percentage points year on year.

Debt
Interest-bearing debt as of the fiscal year-end totaled ¥153,985 million, a decrease of ¥9,522 million year on year. The ratio of interest-bearing debt to total assets was 16.2%, representing a 1.7 percentage-point decrease from the previous fiscal year-end.

Cash Flow
Consolidated free cash flow (net cash provided by (used in) operating activities + net cash provided by (used in) investing activities) was a positive ¥33,501 million, a ¥5,095 million decrease from the previous fiscal year's positive free cash flow of ¥38,596 million.

Cash Flows from Operating Activities
Net cash provided by operating activities was ¥54,949 million, compared with ¥53,146 million in the previous fiscal year. Major factors of cash increase included income before income taxes and an increase in trade payables.

Major factors of cash decrease included an increase in inventories and an increase in trade receivables. Cash flows from operating activities increased by ¥1,803 million year on year.

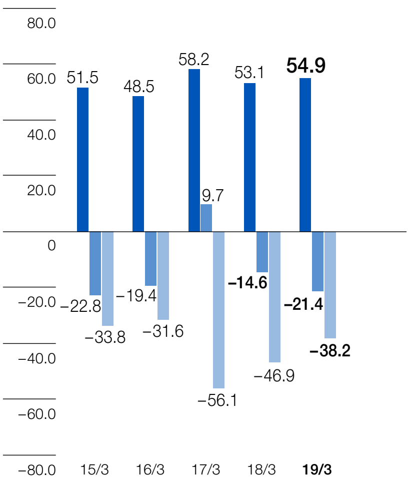
Cash Flows from Investing Activities
Net cash used in investing activities was ¥21,448 million, compared with net cash used in investing activities of ¥14,550 million, in the previous fiscal year. This was primarily a result of the purchase of property, plant and equipment.

Net cash used in investing activities increased by ¥6,898 million year on year.

Cash Flows from Financing Activities
Net cash used in financing activities was ¥38,172 million, compared with ¥46,887 million in the previous fiscal year. This was principally due to the redemption of bonds and the repayment of lease obligations.

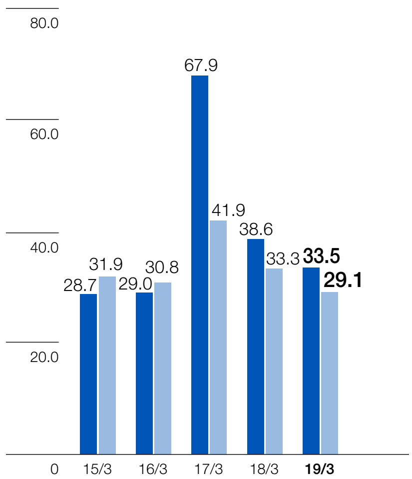
Net cash used in financing activities decreased by ¥8,715 million year on year.

Cash Flows
(Billions of yen)



■ Cash Flows from Operating Activities
■ Cash Flows from (Used in) Investing Activities
■ Cash Flows from (Used in) Financing Activities

Free Cash Flow / Cash and Cash Equivalents
(Billions of yen)



■ Free Cash Flow
■ Cash and Cash Equivalents

Risk Factors

Fuji Electric works to mitigate business risk and other risks in a systematic and methodical manner. However, there are various risks, such as those listed below, which could have a negative effect on the operating results and financial position of Fuji Electric.

As of March 31, 2019, the following factors were judged to have a potential future effect on the operations of Fuji Electric.

(1) Risks Related to Changes in the Operating Environment

(a) In addition to increasing raw material and components prices against the background of a weak yen, such changes as the drastically increasing demand in emerging nations may result in tightened supply and demand as regards materials and raw materials. Consequently, although Fuji Electric strives to lessen the risk of rising raw material prices through commodity swap transactions, significant increases in these prices could have a negative effect on the operating results of Fuji Electric.

(b) Fuji Electric is developing operations actively in overseas markets, focusing particularly on expanding sales in China and other Asian markets. In addition, economic trends in Japan, such as private sector capital investment and public investment affect the Company significantly. In order to minimize the effect on operating results of overseas and domestic market trends, the Company is implementing overall cost and expense reductions. However, a deterioration of the business climate or a change of economic policy in China, a dramatic change in product supply and demand or intensified competition in the market, or a steep decrease in price levels as a result of such factors could affect Fuji Electric's operating results.

(c) Based on an established set of management criteria, Fuji Electric systematically employs forward-exchange contracts to minimize the risk of exchange rate fluctuations on its operating results. However, the forward-exchange contract policy is not capable of entirely mitigating exchange rate risk. Consequently, fluctuations in exchange rates, primarily between the yen and the U.S. dollar, could have a negative effect on the operating results and financial position of the Company.

(d) Fuji Electric's interest-bearing debt totaled ¥153,985 million as of March 31, 2019. A higher-than-anticipated increase in interest rates could lead to a significant additional interest payment burden, which could have a negative effect on the operating results of the Company.

(e) Trends in the financial markets or deterioration in Fuji Electric's financial indicators could impact on Fuji Electric's fund procurement or interest payments, for example by prompting early repayment due to infringement on financial covenants relating to certain loans. Such an event could affect Fuji Electric's operating results and financial position.

(2) Risks Related to Product Quality

Fuji Electric has put in place a quality assurance system designed to ensure the highest level of quality for all of the products that it manufactures and sells. Although the Company has taken precautions in the form of product liability insurance to provide compensation for product liability claims, in the event that major defects are found in any Fuji Electric products due to unforeseen factors, there could be a negative effect on the Company's operating results and financial position.

(3) Risks Related to Investments

Fuji Electric concentrates its management resources on quickly identifying potential business growth areas and conducts investment in facilities and R&D with the objective of expanding and developing the Company's business. The large-scale investment necessary and short product cycles in the semiconductors and magnetic disks fields, in particular, as well as shifts in product demand and intensifying competition increase the possibility that the Company might not be able to recoup its investments. Such events could thereby have a negative effect on the Company's operating results.

(4) Risks Related to Technology Development

Fuji Electric makes a concerted effort to develop technology that matches the needs of the market. However, there is a possibility that competing companies will gain an advantage through faster development, or that the Company will be unable to bring products to market in a timely manner should development not progress according to plan. Such events could thereby have a negative effect on the Company's operating results.

(5) Risks Related to Overseas Business Activities

Fuji Electric is seeking to expand its overseas presence, with a particular focus on Asia, including China. Consequently, the Company is exposed to the following risks, which could have a negative effect on the Company's operating results and financial position:

- Unforeseen changes in laws and regulations as well as tax systems that could have a detrimental effect on the Company
- Disadvantages arising from political conditions
- Social turmoil related to terrorist incidents, war, and other events

(6) Risks Related to Intellectual Property

Fuji Electric effectively manages its intellectual property rights and develops new products and technologies in a manner that does not infringe on third-party patent rights. However, since the pace of technological innovation is accelerating and the Company's operations are becoming more global, the possibility of disputes over intellectual property rights is increasing. A dispute of this nature could have a negative effect on the Company's operating results and financial position.

(7) Risks Related to Business Alliances

Fuji Electric actively collaborates with third-party entities in joint ventures, tie-ups, and other forms of alliances with the objective of enhancing competitiveness in each of its fields of business. Cooperative relations are essential to the success of such collaborations.

However, differences in business systems, corporate cultures, or other aspects could impede the smooth integration of business strategies, technologies, products, personnel, or other elements necessary for a successful collaboration. Such circumstances could thereby have a negative effect on the Company's operating results.

(8) Risks Related to Human Resources

The business activities of Fuji Electric depend heavily on its human resources. Retaining and training superior personnel in such fields as technology, production, sales, and administration is essential to the growth of the Company. Should the Company be unable to retain and/or train such necessary human resources, this could have a negative effect on the Company's operating results.

(9) Risks Related to the Leakage of Personal Information

As a part of its business activities, Fuji Electric handles personal information about numerous individuals, including customers, suppliers, and employees. Fuji Electric has formulated and strictly enforces thorough internal regulations regarding the gathering, use, and management of personal information. However, the Company cannot entirely rule out the possibility that such information could be leaked due to unforeseen circumstances. Any leak of this kind could damage trust in Fuji Electric and thereby have a negative effect on the Company's operating results.

(10) Risks Related to Major Natural Disasters

Fuji Electric has a network of bases throughout the world. In the event of a major natural disaster, production facilities could be damaged, operations at manufacturing facilities could be halted, shipments of products could be delayed, and other related problems could occur. These events could thereby have a negative effect on the operating results and financial position of the Company.

(11) Risks Related to Soil Contamination

Based on the international standard for environmental protection systems, the Company works to prevent, measure, and monitor soil contamination at its operating sites. Prior to selling any land, the Company carries out soil surveys and takes other appropriate steps in accordance with relevant laws and regulations. However, as a result of these measurements and surveys, the Company may incur costs for soil remediation measures, which could have a negative effect on the operating results of the Company.

(12) Risks Related to Retirement Benefit Liabilities

Fuji Electric has a lump-sum payment plan and a corporate pension plan for its employees when they retire. Retirement benefit costs and liabilities are calculated on the assumption that they are accepted as reasonable on the basis of actuarial calculations. Fuji Electric and certain domestic consolidated subsidiaries have also entrusted listed marketable securities to employee retirement benefit trusts. Consequently, changes in the discount rate, the expected rate of return on pension assets and stock prices that are used as the basis of computing pension benefit obligations, differences between these expectations and actual performance, changes in the prices of entrusted listed marketable securities, and other items could have a negative effect on the operating results and financial position of Fuji Electric.

(13) Risks Related to Compliance

Fuji Electric conducts business in a variety of fields and regions throughout the world, and as such is subject to the laws and regulations of numerous countries. The Company has put in place an appropriate internal control system to ensure compliance, but the possibility of legal violations cannot be discounted entirely. Should such a violation occur, this could have a negative effect on the Company's social credibility and/or operating results.

(14) Risks Related to Lawsuits and Other Legal Proceedings

Fuji Electric, in the course of its business, could become the subject of a lawsuit or other legal proceeding, and could as a result unexpectedly become liable for the payment of large amounts of compensation. Depending on the content of such a decision, this could have a negative effect on the Company's operating results.