Financial strategy to achieve the long-term vision

Nabtesco has been working to increase its capital efficiency by implementing "Measures to improve our financial performance" as part of its management materiality. In the medium-term management plan, we uphold the improvement of ROIC as one of our management targets. To achieve this target, we are making efforts as described in the following.

Atsushi Habe
Representative Director
Managing Executive Officer
Corporate Planning, Accounting & Finance, Information Systems and Corporate Communication

We will build the optimal business portfolio for increasing our corporate value on a medium- to long-term basis.

Financial situation

For the fiscal year ended December 31, 2022, our consolidated net sales hit a record high of ¥308.7 billion, being driven by the continued brisk demand for precision reduction gears used in industrial robots as well as by the impact of the weaker yen, and despite demand for hydraulic equipment used in construction machines dropping sharply in the Chinese market. On the other hand, operating income came to ¥18.1 billion, affected by decreased sales and profit in the hydraulic equipment business, sharp rises in materials prices in the Component Solutions Segment, a shortage of electronic components in the Accessibility Solutions Segment, and increased costs in the overseas platform screen door project.

For the fiscal year ending December 31, 2023, demand will continue to be brisk for precision reduction gears and marine vessel equipment. Also, in the automatic door business, demand for our products will expand for use in large commercial buildings in Japan, and demand will recover on a full scale for aircraft equipment in both the civil and national defense sectors. Accordingly, we expect that net sales will increase by 9.8% year on year to ¥339 billion. Operating income will also rise by 44.8% year on year to ¥26.2 billion thanks to increased sales as well as to the offsetting of rises in materials prices by the raising of our own prices and the recovery of production volumes due to the resolution of the shortage of electronic components.

Introduction of business portfolio management

Nabtesco formulated a medium-term management plan for three years from 2022 (hereinafter, "the MTMP"), upholding "ROIC: 10% or over" as one of the management targets with an eye to fostering optimal portfolio management for profitable growth, in addition to promoting capital efficiency-oriented management.

To this end, we set the Basic Policy on the Business Portfolio at the Board of Directors meeting held at the end of 2022. The policy requires us to carry out financial evaluation and business potential evaluation for each business unit to visualize the position of the unit within the business portfolio. We have been managing our business portfolio based on this policy since FY2023.

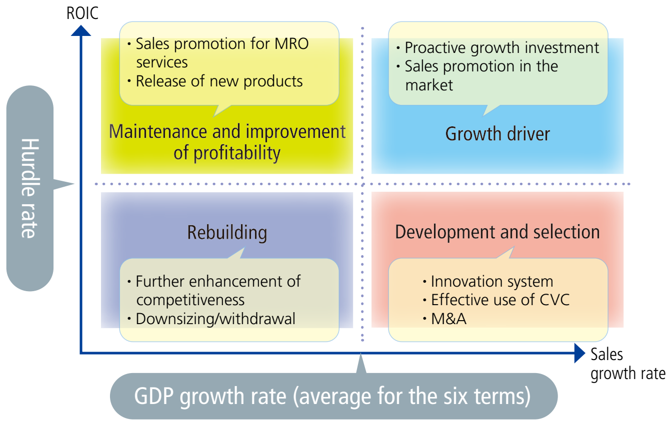
In financial evaluation, we evaluate whether or not each business has generated returns beyond the cost of capital and has achieved sustainable growth. For the evaluation, we classify each of our in-house companies and the group businesses into business units and map the units in a matrix comprising four quadrants, with the vertical axis showing ROIC and the horizontal axis the sales growth rate. We also show the average Economic Value Added (EVA) for the six terms by business unit to visualize the status of the unit.

According to the matrix showing ROIC and the sales growth rate, Nabtesco is lacking in business units categorized as belonging in the "Development and selection" quadrant, and we thus need to increase the number of such units, for which we should take both intangible and tangible measures. Accordingly, we have already been implementing intangible measures to optimize our human capital and create intellectual property, while establishing the intrapreneurship program "Light" and the in-house company innovation system in 2022 as tangible measures. We will also foster the use of the CVC fund and examine M&A to increase the number of business units included in the "Development and selection" quadrant.

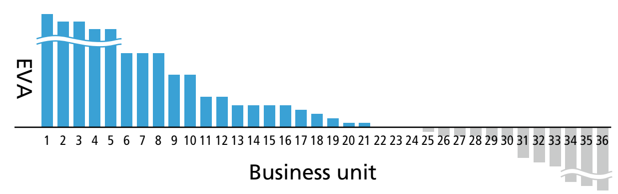
Financial evaluation

- Categorize all of the businesses into 36 business units
- Evaluate whether or not each of the units has generated returns beyond the cost of capital and has achieved sustainable growth
- Speed up the actions to increase the number of business units included in the "Development and selection" quadrant

● Matrix showing ROIC and the sales growth rate



● Distribution of EVA by business unit



In the business potential evaluation, we evaluate whether or not each of the business units has objective market potential and possibilities that cannot be identified through financial evaluation as well as the ESG-related risks and opportunities posed to the business unit. Based on the results of the financial evaluation and business potential evaluation as described above, we will engage in deeper discussions on the direction of our business portfolio at Board meetings. We will then conduct examinations to set an action plan for each business unit so that we can proactively make growth investments and promptly take necessary actions, including the downsizing of or withdrawal from a business, toward building a business portfolio that is optimal for Nabtesco.

Business potential evaluation

- Evaluate whether or not each of the business units has objective market potential and possibilities that cannot be identified through financial evaluation
- Evaluate ESG-related risks and opportunities posed to the business unit

Industry attractiveness	• Market size • Growth potential • Attractiveness of the industry
Strength of the Company	• Market share, competitive advantage • Inimitability • Brand value • Synergies with other businesses
ESG-related risks	• Environment (Amount of CO_2 emissions and others)
	• Social (Occupational accidents and others)
	• Governance (Frequency of product defect-related incidents and others)
ESG-related opportunities	• Initiatives implemented to solve social challenges through business

Approach to capital allocation

In the MTMP, we attribute importance to financial discipline for long-term growth. We sold part of our shares in Harmonic Drive Systems in 2021 and the remainder in 2022. As for the allocation of capital including the cash gained through the sale of the shares, we prioritize the use of funds for growth investment toward the achievement of the long-term vision. For capital investment, we are making a large investment in FY2023 in the new plant to be completed in Hamamatsu city to increase our production of precision reduction gears. We will also make proactive R&D investment for the electrification and systemization of our products.

For shareholders' return, we uphold the policy of keeping our consolidated dividend payout ratio at 35% or over. We purchased our own treasury stocks in the amount of ¥20 billion in 2021 while paying dividends in line with the policy.

Due to the deposit related to the sale of our shares in Harmonic Drive Systems, we now have cash on hand at a level higher than usual, whereas we make it a rule to secure cash on hand at the amount equivalent to our average sales for two months. Also, for flexible borrowing, we will maintain our "A" rating from credit rating organizations, for which we will keep our equity ratio at around 50%.