Dear Investors

We published our financial results for FY2016 on February 10th, 2017.

This material summarized selected questions & answers on them.

Agenda

・Management analysis

・Selected questions & answers

Management Discussion and Analysis

FY2016 marked a milestone for full integration with DMG MORI AG (European group entity, hereafter AG). FY2017 will be of significant importance in that external parties can evaluate our performance in comparable basis without complicated accounting treatments associated with business integration.

We started cooperation with AG in March 2009 by holding a 5% stake of each other. In 2011, we increased the stake in AG to more than 20%, and as a result, AG became a company accounted for using the equity method. Following that, in April 2015, we further increased the stake in AG to 52.54% and consolidated the company for accounting purpose. In April 2016, we increased the stake in AG to 76.04%, and, in August same year, the Domination Profit and Loss Transfer Agreement (hereafter DA) came into effect. At that point, the full integration with AG, both in operation and in financial purposes, was completed after approximately 8 years of time.

In FY2016, we made adjustments in the overlapping resources and non-core businesses which arose during the integration with AG. The cash outlay to purchase additional shares in AG and associated debt balance had peaked out, and the debt balance began to decrease. In accounting aspects, the deduction of shareholders' equity occurred, which arose due to the acquisition of additional shares in AG (after consolidation) and recognition of liability to purchase shares in AG following the Domination Agreement. On the other hand, we strengthened the equity with perpetual subordinated loan and bond. Such complicated accounting treatments will no longer happen after FY2016.

For FY2017, such complicated factors as mentioned above will be removed. We, therefore acknowledge that this year is of significant importance, because external stakeholders can evaluate our performance on a comparable basis. We will strive to achieve the announced forecast.

＜Review of FY 2016 result (Jan to Dec 2016)＞

The highlights in FY2016 are as follows; 1) we made JPY 14.3bn as one-off expenses to adjust the overlapping resources with AG and non-core businesses. Following this, we expect cost savings of JPY 6.5bn in FY2017. 2) We strengthened our competitive position as Machining Solution Provider. We tightened partnership with our major peripherals' makers to expand the types of peripherals which can be equipped to our machine and improve the quality of peripherals. We also expanded our Technology Cycles lineup to 28, which comprise of Cutting Cycles, Handling Cycles, Measurement Cycles and Monitoring Cycles. These Technology Cycles contribute to enhance production efficiency and to provide solutions to our users. 3) As for the new product lineup, we enlarged the product lineup by adding DMU 210 second generations, which are suitable for heavy cutting, and 4th generation of the DMU duo BLOCK series, which possess particularly high precision and are suitable to be customized. In September, we launched the CMX series as global standard model in the volume-zone products. The model is well accepted by the market and we saw a steady increase in order intakes. CMX series offer 290 types of standard options (which have been selected as a result of the problem-solving with customers in the past), and an extensibility for future customer needs such as IoT adoption, because they are equipped with our cutting-edge Human Machine Interface CELOS. 4) As for financial part, we spent JPY 61.5bn to acquire the additional stake in AG. Yet, we maintained the net cash inflow of JPY 8.1bn, which is calculated by deducting cash flows in investments from cash flow from operation, and proceeded to the path to net debt reduction.

＜Prospects for FY 2017 (Jan to Dec 2017)＞

We recognize that FY2017 (Jan to Dec 2017 period) will be the important year to demonstrate our capabilities after full-integration with AG. Assuming that the demand will be on the same level as in the previous year, we plan to make operating profit of JPY 22bn (+ 69% in normal basis) and net profit attributable to our shareholders in the amount of JPY 11bn. We expect that our investments as Total Solution Provider in the last years will begin to yield fruits this year. In 2016, around 45% of our machines were equipped with our qualified peripheral goods (DMQP: DMG MORI Qualified Peripherals/ Products) , this ratio will further be increased in this year. Likewise, already more than 30% of our newly sold machines are equipped with Technology Cycles, which shows the customers' acceptance of the software. These solution providing measures are delivering added value to our customers, which in turn will contribute to the improvement in our financial performance through increased sales revenue. Other than that, the cost savings from adjustments of overlapping resources and non-core business in 2016 and the turnaround of the US subsidiary will contribute to our group's profit this year. We expect that we can generate Free Cash Flows of around JPY 15bn to 20bn because, in addition to improved net profit, our capital expenditure had already peaked out. We will reduce the net debt balance with those Free Cash Flows to strengthen our financial position. We also plan to raise the annual dividend per share to JPY 30.0 (2016：JPY 26.0/ share).

Figure 1: Summary of financial performances

Jan - Dec (100 Million JPY)	2015 Pro Forma	2016 Actual	Change (%)	2017 Forecast	Change (%)
Sales revenue	4,284	**3,766**	-12.1%	**3,800**	+0.9%
Operating profit (before one-off items)	360	**130**	-63.9%	**220**	+69.2%
(%)	8.4%	3.5%		5.8%	
One-off expenses/ gain	+51	**-110**		**-**	
Operating profit	411	**20**	-95.1%	**220**	
(%)	9.6%	0.5%		5.8%	
Finance cost	**-21**	**-32**		**-40**	
(thereof, economic compensation from DA)		**(-7)**		**(-20)**	
Net profit	**358**	**-57**	-	**120**	
Attributable to shareholders	324	**-78**		**110**	
Attributable to non-controlling interest	34	**21**		**10**	
Dividends per share (JPY)	26.0	26.0		30.0	
D&A	146	170		170	
Capex	266	152		100	
(Exchange rate) USD/JPY	121.1	108.9		110.0	
EUR/JPY	134.3	120.3		120.0	

(*)FY2015 was irregular with 9 month period due to the change of financial year from the period of April -March to the period of January - December. In this documentation, we present Jan to Dec 2015 results, fully including the financial results of AG, in order to facilitate year-on-year comparison.

As for one-off items, there are such items as a gain from step acquisition in Jan – Dec 2015 or expenses from adjustments of overlapping resources and exit from non-core businesses, respectively a gain from sale of marketable securities etc. in 2016.

Net profit attributable to shareholders are calculated on the proportional basis of to the stake in AG.

Selected questions & answers

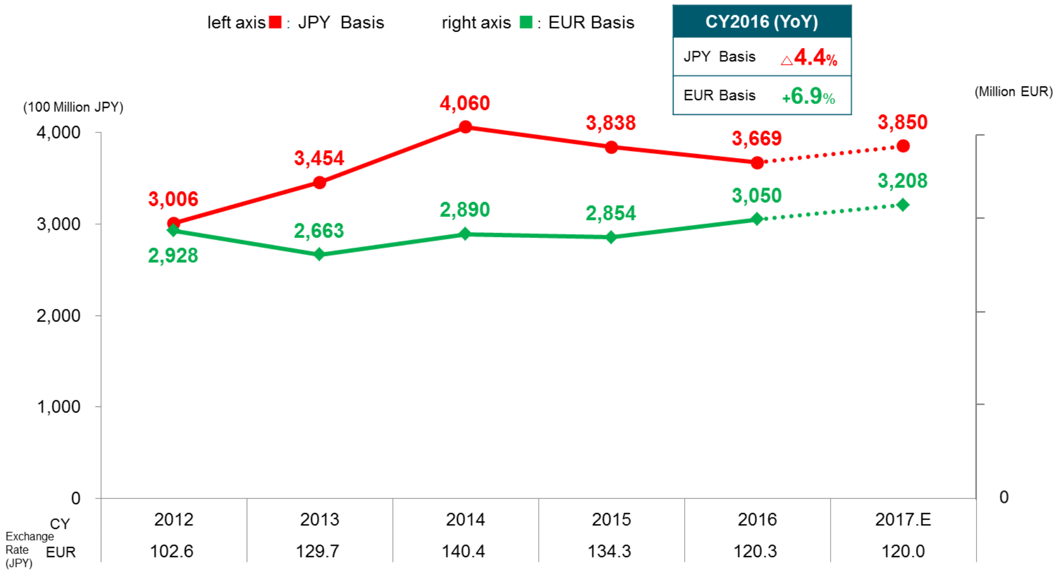
【Table of contents】

Q&A

Q : Market condition in 2017 by geography and by customer industry?

A : We expect our order intake in 2017 to be around JPY 385bn, or 4.9% increase in year-on-year basis. In geographical terms, we expect that Europe and the U.S. will continue to lead the demands. Although Chinese market was in a consolidation phase during the last years, it will begin to slightly improve. On the other hand, Japanese, Asian and other Americas' markets will still require some time to recover, although they seem to have bottomed out. As regards the industrial segmentation, automotive industry, aerospace and medical industry will continue to be strong. We see some improvements in SMEs (Small and Medium-sized enterprises : small to medium sized workshops) or die & mold industry. The inquiries from Energy sector are also increasing though it is still a long way to full recovery.

Figure 2: DMG MORI group Order intake



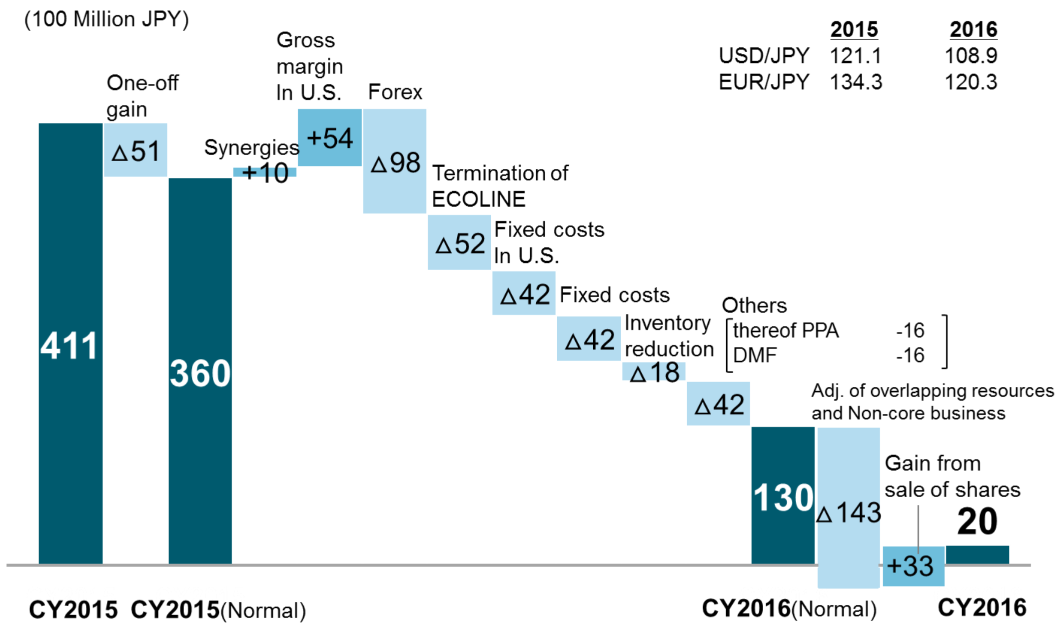
Q : What is the bridge between revenue in FY2016 with that of FY2015?

A : Sales revenue in FY2016 decreased by JPY 51.9bn to JPY 376.6bn from JPY 428.5bn in CY2015 (Pro Forma). Major factors are: minus JPY 33.7bn from forex factors, minus JPY 14bn due to the decline in sales during the transition from ECOLINE series to newly launched CMX series, and minus JPY 4.2bn from de-consolidation of German leasing company. These factors sum up to a total of JPY 51.9bn.

Q : What is the bridge between operating profit in FY2016 with that of FY2015?

A : Operating profit in FY2016 was JPY 13bn on a normal basis, which is JPY 23bn less than the operating profit of JPY 36bn in 2015. On one hand there are positive factors, such as JPY 1bn of synergies with AG (e.g. reduction in models or in components) and JPY 5.4bn of gross margin increase in US subsidiary from the switch to direct sales. They totaled to JPY 6.4bn. On the other hand the negative factors are: JPY 9.8bn from JPY appreciation (i.e. forex factors), JPY 5.2bn from sales' decline by the transition from ECOLINE series to CMX series, JPY 4.2bn of fixed costs' increase in US subsidiary due to the switch to direct sales, JPY 4.2bn of fixed costs' increase such as depreciation charge and personnel costs, JPY 1.8bn of impact from inventory reduction etc., JPY 4.2bn of expense increase from PPA (purchase price allocation) and de-consolidation of German leasing company and so on. These factors totaled to JPY29.4bn and negatively affected on our financial results.

Figure 3：2016 Operating profit analysis



Q：What are the factors that FY2016 operating profit on a normal basis fell short by JPY 2bn to JPY 13bn compared with previous forecast of JPY 15bn?

A : Although we achieved operating profit (normal basis) of JPY 9.6bn in Q4 (Oct to Dec) and operating margin of 8.8%, the profit is still JPY 2bn less than the JPY 11.6bn as per the previous forecast. The weaker than expected performance of the JPY exchange rates against other currencies during Q4 lead to favorable effects of around JPY 2bn. On the other hand, the decrease in sales revenue, which includes the impact from tightening the conditions for recognition of revenue in US, has negatively affected us by JPY 5bn, the reduction of inventory by JPY 1.8bn, as well as the promotion of stock machines and other cost increases by JPY 1.7b. They altogether had a negative impact of JPY 4bn.

Q：What is the bridge between operating profit in Q4 with that of the same period of previous year (2015)?

A：Operating profit in Q4 was JPY 9.6bn on a normal basis, which is JPY 3.4bn less than that of the same period in the previous year (JPY 13bn in Oct – Dec 2015). There was JPY 2.1bn of positive effect from the gross margin increase in the US subsidiary associated with the switch to direct sales. On the other hand, there were JPY 5.5 bn of negative factors, which comprised of JPY 0.5 bn from sales volume decline by the termination of ECOLINE series, JPY 2.3bn from forex factors, JPY 1.0bn from fixed cost increase, and JPY 1.7bn from factors like inventory reduction. Net result of these factors was an operating profit decrease of JPY 3.4bn.

Q：Is the group still confident about the turnaround of US subsidiary in 2017?

A：Our US subsidiary achieved black figure in 2016 Q4 despite the fact that its revenue and profit fell short of its plan due to the tightening in revenue recognition (final acceptance basis). For 2016, the loss of the subsidiary was JPY 3.5bn due to the increased fixed costs related to the increased headcount to 857 (from 669 as at end of FY2015) following the transition to direct sales and additional sales & service centers. However, as the order intake in 2016 had increased by 24% in local currency terms, and its order intake trend continues to look robust, we are confident that the US subsidiary can make a profit for FY2017 in total.

Q：The one-off expenses arising from the adjustments of overlapping resources and non-core business increased to JPY 14.3bn, compared to the previous forecast of JPY 13.0bn. Why?

A：The one-off expenses were mainly incurred in our group companies in Europe. The majority of one-offs are done in the fourth quarter. Initially, we assumed EUR/JPY exchange rate to be 110, but finally was around 120, which makes the expenses in JPY terms larger by JPY 1bn.

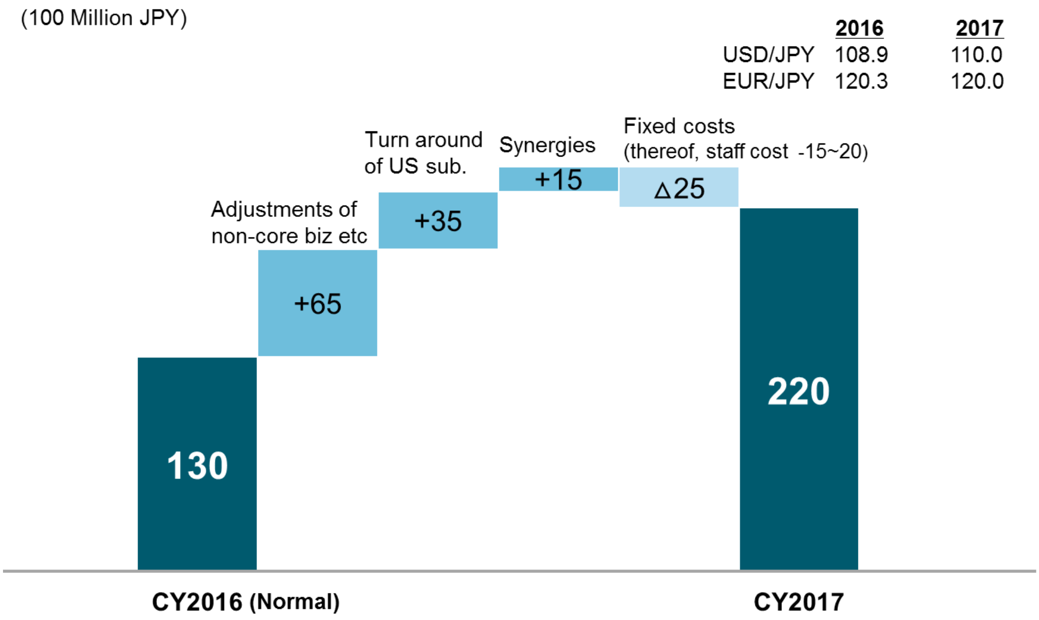
Q：DMG MORI made JPY 3.3bn of gain from the sale of marketable securities. Was this to compensate the shortfall in profit?

A：We held some shares in other companies with whom we have businesses, for the purpose of benefits in the actual business relationship. We think we enjoyed advantages in the supply chain from the holding of such shares. However, we have continuously reviewed the share holdings in other companies in recent years, taking the level of maturity in business transactions into consideration. The sales of shares this time were made under such context. We will regularly review our share holding in other companies and try to improve the asset utilization whenever necessary.

Q：How are you confident in achieving 2017 operating profit forecast?

A：We expect operating profit of FY2017 to be JPY 22bn. This means that the profit will increase by JPY 9bn from normal operating profit in FY2016 of JPY 13bn. The positive factors are cost savings from adjustments of overlapping resources and non-core businesses in the amount of JPY 6.5bn, turnaround of US subsidiary through the year in the amount of JPY 3.5bn, the synergies with AG, such as reduction of models and of components for JPY 1.5bn, which totals to JPY 11.5bn. On the other hand, although there will be no significant factors, we expect JPY 2.5bn negative impact, which comprises of JPY 1.5bn increase in personnel costs and JPY 1bn increase in other expenses respectively.

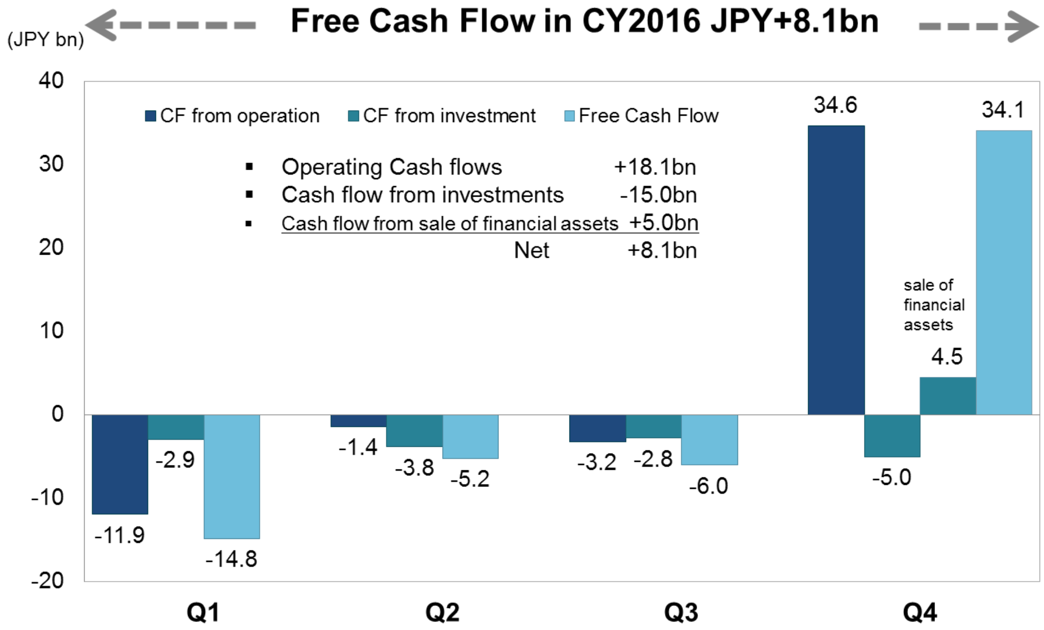
Figure 4 : FY2017 operating profit bridge



Q : We saw net cash flows in FY2016 turned to be positive. Will the tendency that the cash flows improve in 4th quarter continue or not?

A : In FY2016, the cash inflow from operation was JPY 18.1bn and cash outflow from investments was JPY 15bn, which resulted in the net cash inflow of JPY 3.1bn. Adding to this, JPY 5bn of cash inflows from sales of marketable securities made net cash inflow to be JPY 8.1bn. Our sales revenue tends to be concentrated in the 4th quarter, and therefore cash flow in the same quarter tends to increase significantly. Yet, we think it is important to smoothen the capacity utilization throughout the year, and we already have started some actions to smoothen our order intake, production and sales. Therefore, the cash flows will also be smoothed in the mid-term. However, as it will take time to change the whole operational cycles, we expect that such tendency with the cash flow concentrating in the 4th quarter will continue for another few years.

Figure 5：FY2016 quarterly cash flows



Q：How about the group's Cash Flows in FY2017?

A：We expect our EAT (earnings after tax) to be JPY11bn and our depreciation and amortization to be JPY 17bn, and hence we plan to generate JPY 28bn cash inflows. Oh the other hand, we plan to make JPY 10bn of Capex (capital expenditure) in FY2017 while our working capital will remain at the same level in FY2016 as our revenue will consistent. Consequently, we think we can generate free cash flows of JPY 18bn in FY2017. In addition to this, we aim to further improve our cash flows from the sales of some assets like buildings of the factories closed in FY2016.

Q：What is your sensitivity to fluctuation in foreign exchange rates in revenue and in operating profit, respectively?

A: As for USD, we estimate that fluctuations (or JPY 1 change) in the exchange rate of USD/JPY will impact our revenue by JPY 550mn, and operating profit by JPY 250mn to 300mn on a full-year basis. Fluctuations (or JPY 1 change) in the exchange rate of EUR/JPY will impact our revenue by JPY 2.2bn, and operating profit by JPY 300mn in full-year basis.

Q：What about dividend policy?

A：With regard to dividend, we are thinking of the payout ratio of around 30% for the time being. We experienced the change in our financial position, such as increase of net debt associated with integration of AG or decline in shareholders' equity arising from the additional share acquisition in AG. Yet, we already passed the worst period in terms of balance sheet stability, and from fourth quarter of FY2016, we have stepped forward to balance sheet improvement. We are confident that, from FY2017 onwards, we can maintain the payout ratio of 20% to 30% while strengthening our balance sheet structure with annual free cash flows of minimum JPY 15bn -20 bn. Given that we achieve our published profit forecast in FY2017, we plan raise the annual dividend per share to JPY 30.0 (2016：JPY 26.0/ share), or payout ratio of 36%.

Q：Does the group plan to announce its mid-term plan?

A：Our group has diversified our customer base both in geographically and in customer industry. As a result, our order intake and sales volume has rather been stabilized compared to those of before. However, since it is still difficult for us to fully eliminate macro-environmental effects such as fluctuation in foreign exchange rates, we do not think it be appropriate to publish our mid-term plan with concrete targeting figures. We think that our FY2016 Q4 results demonstrated our potential to achieve sales revenue of JPY 110bn and operating profit margin of around 9% on quarterly basis. Based on these figures, our target for the time being shall be the total revenue of around JPY 450bn for the whole year and operating profit margin of 10% on continuous basis.