Mitsubishi Electric (6503)

Key takeaways from small meeting with CEO and CFO

Overweight

6503.T, 6503 JP
Price (26 Jun 26):¥5,858
Price Target (Dec-26):¥6,500

Japan Equity Research
Technology - Consumer Electronics/ Industrial Electronics/Precisions

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We took part in a small meeting for sell-side analysts with President & CEO Kei Uruma and CFO Kenichiro Fujimoto on the 26th. Momentum is likely to remain strong this fiscal year, as in the previous fiscal year, driven by factory automation systems and optical semiconductors, and medium-term growth can be expected for DC800V-compatible power supplies/equipment and IT cooling systems. Defense systems, which the executives did not discuss much this time, also remain a focus. Regarding physical AI, which prompted many questions, attention is on synergies between strong components and the operational technology (OT) security business, which has been strengthened by the acquisition of Nozomi Networks. However, our impression is that it is slightly premature to factor the synergies into earnings estimates at this stage. Key comments from the executives are as follows.

- **Data center-related business:** The company is developing next-generation DC800V-compatible power systems for AI data centers using a combination of rectifiers and converters as well as solid state transformers (SST). Combining this with IT cooling technology, it aims for a power usage effectiveness (PUE; a measure of data center energy efficiency) of 1.1, the highest level of energy efficiency. So that sales start benefiting in FY2027, the company is collaborating with Nvidia and communicating with GAFAM and Hon Hai Precision Industry. The traditional UPS-based data center power supplies/equipment business is to be transformed into a cutting-edge one.
- **Factory automation-related business:** The company needs to increase laser processing equipment production capacity further, as demand, which fluctuated sharply in the past, has not declined at all since last year. Demand for servo motors and numerical controllers (NC) has continued to grow, rather than plateauing. The company cannot keep up with demand by manufacturing spindle motors in Japan alone; it needs to produce them in China also. In the power semiconductors business, SiCs have been recovering sluggishly, but trends are improving for factory automation systems.
- **Physical AI:** The business is easy to discuss but requires massive development. AI models may be able to acquire onsite knowledge and production technology, but they are not necessarily applicable to other industries or companies. Management thus wants to expand applications by developing base software applicable to various industries and companies and incorporating it into sequencer and servo motor software. In the area of OT security, the acquisition of Nozomi Networks has made it easier to collect data. The company will constantly monitor data traffic from production site equipment and networks, and shut them down in the case of abnormalities from cyberattacks or other factors. By asking customers to share this underlying data and inputting it into Serendie, the company aims to improve the efficiency of production site operation and management.
- **Margin targets and capital allocation:** Management aims for an FY2030 operating margin of higher than the 12%+ target in the medium-term plan while steadily investing in growth. It plans on ¥3 trillion in cumulative five-year capex and growth investments, broken down as roughly ¥1 trillion for capex and up to ¥2 trillion for M&A and alliances. For the latter, management is also

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considering such areas as construction and maintenance.

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Investment Thesis, Valuation and Risks

Mitsubishi Electric (6503) *(Overweight; Price Target: ¥6,500)*

Investment Thesis

The company is currently intensifying its efforts to reform its earnings structure, including reviewing sales prices and contract terms, as well as reducing fixed costs, in order to improve profitability. We expect the positive impact of these measures to materialize over time, through to FY2027. We also expect to see continued growth in infrastructure businesses, including defense, as well as optical semiconductor businesses. With sustained buybacks, we hold the view that ROE will rise to 11% in FY2026.

Valuation

Our end-December 2026 price target of ¥6,500 values the shares at a 10% conglomerate discount to the theoretical share price derived using an SOTP model based on our FY2027 forecasts. Target multiples in our SOTP model are based on EV/EBITDA multiples of comparable companies.

Price target based on sum-of-the-parts valuation (FY2027E)

	EBITDA			EV/EBITDA	EV	
		OP	D&A			Per share
	(mn JPY)	(mn JPY)	(mn JPY)	(x)	(mn JPY)	(JPY)
Infrastructure	250,000	210,000	40,000	17.5	4,375,000	2,165
Industry and Mobility	245,000	175,000	70,000	14.8	3,629,000	1,796
FA Systems	169,000	120,000	49,000	19.0	3,211,000	1,589
Automotive Equipment	76,000	55,000	21,000	5.5	418,000	207
Life	268,000	193,000	75,000	12.6	3,382,000	1,674
Building Systems	102,000	72,000	30,000	12.0	1,224,000	606
AC Systems & Home Products	166,000	121,000	45,000	13.0	2,158,000	1,068
Digital Innovation	23,000	15,000	8,000	12.0	276,000	137
Semiconductor Devices	100,000	50,000	50,000	15.7	1,569,000	776
Total	886,000	643,000	243,000	14.9	13,231,000	6,548
All Other / Corporate	32,000	7,000	25,000	14.9	477,869	236
Corporate value					13,708,869	6,784
Net debt					-589,793	-292
Market value					14,298,662	7,076
Number of outstanding shares (K)					1,995,066	
Theoretical value (JPY)					7,167	
Discount					-10%	
Target Price (JPY)					6,500	

Source: Bloomberg Finance L.P., J.P. Morgan estimates.

Risks to Rating and Price Target
Upside Scenario to Target Price/Rating

- Structural reforms and their effects exceeding expectations
- Improvement in the FA (Factory Automation) cycle and recovery in the automotive market
- Expansion of defense budget and infrastructure investment

Downside Scenario to Target Price/Rating

- Scale of structural reforms falls short of expectations
- Slump in automobile output and capex due to weak macro demand

- Stiffer competition in electronic devices
- Delays responding to rapid changes, such as xEV trends in the automobile industry

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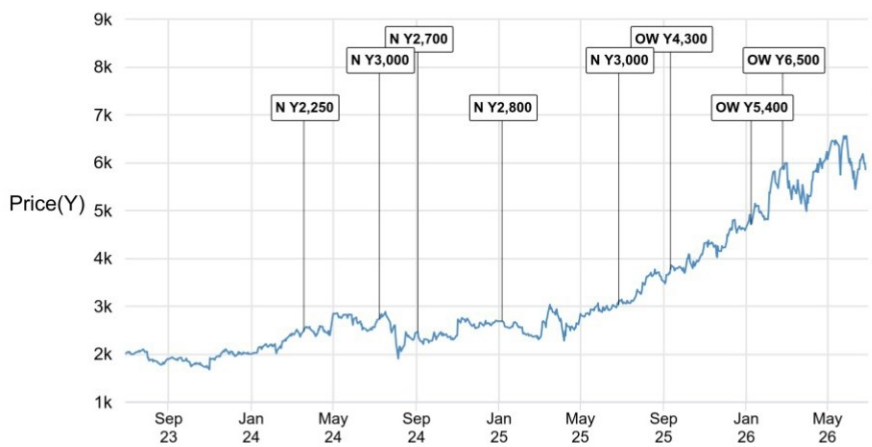
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Mitsubishi Electric (6503) (6503.T, 6503 JP) Price Chart



Date	Rating	Price (Y)	Price Target (Y)
19-Mar-24	N	2474	2,250
09-Jul-24	N	2734	3,000
04-Sep-24	N	2448	2,700
06-Jan-25	N	2687	2,800
27-Jun-25	N	3034	3,000
12-Sep-25	OW	3766	4,300
09-Jan-26	OW	4711	5,400
25-Feb-26	OW	5916	6,500

Source: Bloomberg Finance L.P. and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Jul 02, 2001. All share prices are as of market close on the previous business day.

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