Message from the CFO

New Financial Model in Line with Equipment Market Expansion
Targeting World-Class Profitability and Capital Efficiency While Maintaining Downward Cost Flexibility

1. A New Phase of Growth in the Semiconductor and Display Industries

Tokyo Electron finished fiscal 2017, the year ended March 31, 2017, with very strong results. The gross profit margin, operating margin and net income all reached new highs. Net sales in the semiconductor production equipment (SPE) segment also set a new record high.

Previously, the growth potential of the semiconductor market had been called into question, but today both the semiconductor and display industries are booming. Using the 2008 financial crisis as an approximate milestone, we can perceive a clear change in worldwide trends and our very lifestyles. An example of this in everyday life is the increasing prevalence of video content on social media. Enormous numbers of users take and simultaneously upload videos. All that data is stored in the cloud; these users typically do not keep it on their own PCs. A different example is Uber, Lyft and other ride sharing services, which have been attracting a great deal of attention. These services use apps to display the current locations of their drivers, data that must be gathered, processed and distributed in real time. This requires real-time data transmission systems all throughout society. A decade ago, people mainly thought about things like vehicles in terms of personal ownership. In recent years, however, we have begun to see the emergence of the sharing economy and other new approaches. As networks increasingly connect all aspects of society, forming one, enormous interconnected system, the uses of semiconductors are expanding in every field. These changes have been propelling the semiconductor and display industries into a new phase unlike anything we have yet seen.

2. Medium-Term Management Plan Initiatives

(1) Financial Goals

Tokyo Electron announced its medium-term management plan in 2015. The plan’s targets for net sales, operating margin and ROE were based on two scenarios regarding the future size of the wafer fab equipment (WFE) market.
Message from the CEO

In light of changes in the semiconductor industry, however, we have now increased the WFE market size assumed in the plan’s financial model and raised the plan’s targets. We now aim to grow the Company even more than we set out to under the 2015 plan. From a financial standpoint, however, as the Company expands, we intend to restrain fixed costs. The SPE market has long been regarded as particularly volatile. We are therefore taking care to maintain downward flexibility in order to remain profitable even if economic conditions deteriorate.

Success in the SPE business requires the consistent release of innovative products to accommodate the latest next-generation technologies. For an SPE company, generating profit while continually developing new equipment is the key to sustainability. It is therefore essential to develop products and services that offer greater customer value and then make sure that customers fully appreciate that value. Our development divisions as well as sales and service divisions must all keep this in mind. Specific measures we are taking are as follows:

- Develop products and services with high profit margins
- Avoid discounting to gain market share
- Advance R&D and capital investment on scale with targeted future returns
- Optimize logistics and improve operational productivity
- Make more efficient use of trade notes and accounts receivable, inventories and other assets

Through these initiatives, under the new financial model we are targeting an operating margin of 26% (assuming a WFE market of US$45 billion) and ROE of 20–25%.

(2) Non-Financial Goals

a. Human Resources System

In July 2017, Tokyo Electron launched a globally unified job rank system based on job responsibilities. This system clarifies the position of every Group employee, better empowering the Group to find the right people for the right job on a worldwide basis. In Silicon Valley, diverse human resources are constantly interacting and influencing one another, leading to the creation of new ideas. Similarly, by promoting global exchange within the Tokyo Electron Group, we are working to foster cross-pollination of ideas and spark innovation.

In addition, when we launched the current medium-term management plan, we raised the share purchasing subsidy offered through the employee shareholding association to 15%. This was intended to align the interests of employees with those of other shareholders. The number of employee shareholders has increased as a result, but participation in the employee shareholding association is still limited to employees in Japan. To address this, we are considering a stock-based compensation system utilizing a trust that would allow executive-level employees to receive capital gains on Tokyo Electron shares even if they reside outside Japan. These measures are aimed at securing talented human resources globally.

Furthermore, the Company conducts training for current and future top-level managers, and has instituted a special selection and training program for future management candidates. This program includes training camps held several times annually and lectures from outside instructors, and ends with participants making proposals to current top management. The systematic development of successors is essential to sustainable growth.

b. Intellectual Property Strategy

Since its establishment, Tokyo Electron has made securing its intellectual property rights a priority. We file 600 to 800 patent applications in Japan each year. A major feature of our intellectual property strategy is our relatively high global application rate. The average global application rate among Japanese patent applicants is about 30%. In contrast, the Company’s rate is closer to 70%. By acquiring numerous patents in the countries where our customers’ manufacturing sites are located, we are building a framework to both maintain the competitiveness of our products and ensure that our customers can use our products with confidence.

* Global application rate: The percentage of patent applications filed in Japan that are also filed in other countries

Patent Holdings by Country/Region

<table>
<thead>
<tr>
<th>Country/Region</th>
<th>Patent Holdings</th>
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<tbody>
<tr>
<td>Japan</td>
<td>31%</td>
</tr>
<tr>
<td>U.S.</td>
<td>26%</td>
</tr>
<tr>
<td>Europe</td>
<td>15%</td>
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<tr>
<td>Taiwan</td>
<td>11%</td>
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<tr>
<td>South Korea</td>
<td>10%</td>
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<tr>
<td>China</td>
<td>9%</td>
</tr>
<tr>
<td>Others</td>
<td>20%</td>
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At March 31, 2017, Tokyo Electron had cash on hand of ¥315.3 billion. We will keep an eye on the macro economy as we determine the specific uses for it. The equity ratio as of March 31, 2017 was 67%, and the Company has no interest-bearing debt. Although we have not ruled out capital procurement from external sources if necessary, I believe we can generally meet our own capital needs internally.

4. In Closing

Technological innovation moves extremely quickly in the semiconductor and display industries. I truly feel that the motto of Intel’s Andrew Grove gets to the heart of what it means to operate in these industries: “Only the paranoid survive.”

For fiscal 2018, Tokyo Electron targets net sales of ¥980 billion, operating income of ¥216 billion (for an operating margin of 22.0%), net income attributable to owners of the parent of ¥163 billion and net income per share of ¥993.44.*

The Company is growing, but we will stay vigilant and alert to market changes as we work toward the goals of the medium-term management plan.

3. Capital Policy and Shareholder Returns

Since fiscal 2016, the Company has maintained the shareholder return policy of targeting a payout ratio of 50% and flexibly considering share buybacks. In step with recent profit growth, we have paid a record high annual dividend per share (DPS) for three consecutive years. At the end of fiscal 2017, Tokyo Electron had cash on hand of ¥315.3 billion. Our first priority for this cash is investment in Tokyo Electron’s future growth. We will keep an eye on the macro economy as we determine the specific uses for it. The equity ratio as of March 31, 2017 was 67%, and the Company has no interest-bearing debt. Although we have not ruled out capital procurement from external sources if necessary, I believe we can generally meet our own capital needs internally.

Policy for Shareholder Returns

Dividend payout ratio: 50%
Annual DPS of not less than ¥150

We will review our dividend policy if the company does not generate net income for two consecutive fiscal years.

We will flexibly consider share buybacks.

* Results forecasts announced April 20, 2017

Message from the CFO