Special Feature — Discussion on the Progress of Transformation and the Future Direction of Management —

Independent Outside Director Roundtable Discussion

1 **Masaaki Ito**, Independent Outside Director

2 **Toshiko Oka**, Independent Outside Director (Chair of the Audit Committee)

3 **Kazushige Okuhara**, Independent Outside Director (Chair of the Nominating Committee and Chair of the Compensation Committee)

4 **Nana Otsuki**, Professor at Graduate School of Management, Nagoya University of Commerce & Business

5 **Kiyomi Kikuchi**, Independent Outside Director

6 **Joseph P. Schmelzeis, Jr.**, Independent Outside Director

Nana Otsuki, Professor at Graduate School of Management, Nagoya University of Commerce & Business

Professor Otsuki engaged in research on financial systems at both domestic and international financial institutions and rating agencies. When she worked at a foreign-owned securities firm, she served as a banking sector analyst and earned high recognition from global investors. She has held positions as an outside director and statutory auditor of listed companies and served as a member of councils and committees under the Ministry of Finance, the Financial Services Agency, and the Cabinet Office.

The Hitachi Construction Machinery Group has positioned the period from 2022—when it started its own business development in the Americas and implemented the change in its capital structure—as a period of "second founding," and it has been accelerating business transformation under the medium-term management plan, "BUILDING THE FUTURE 2025." To achieve this transformation successfully, appropriate advice and oversight by independent outside directors are essential. For this roundtable, we invited Professor Nana Otsuki from the Graduate School of Management, Nagoya University of Commerce & Business as facilitator, who was joined by five of our outside directors to exchange views on the progress of the company's transformation to date and the future direction of business management.

Change in Shareholder Composition and Progress of Transformation

Otsuki: 2025 is the final year of the company's first medium-term management plan following the change of its major shareholder, which we have positioned as our "second founding." In July 2024, during the medium-term management plan period, a new concept called "LANDCROS" was also announced. From your perspective as outside directors, what are your views on the progress of transformation and the impact of the change of major shareholder?

Okuhara: In light of the change in the capital relationship and of the fact that it started to conduct business on its own in the Americas, the company has been conveying the message of "second founding" to all stakeholders. Breaking away from being a listed subsidiary, the company has established an environment where it can fully leverage its

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strengths. What the company needs now is agile business management, including the restructuring of the Americas business. Also, the company needs to accelerate its efforts to become psychologically independent from its former parent company. In other words, the company needs to “stand on its own.”
Oka: The company has transitioned from being a listed subsidiary to an equity-method affiliate and has gained a new major shareholder. When the company was a listed subsidiary, I felt there were many instances where the company was too dependent on the parent company. Now that it has broken free from that situation, the management needs to make decisions that are best for the company, while of course considering the interests of the new shareholder.

Structural Changes in the External Environment and Business Strategies

Otsuki: It seems that the Trump tariffs and the response measures taken by various countries are accelerating the deglobalization of the world economy. What are the potential impacts of these structural changes on the company’s medium- to long-term business strategies?
Schmelzeis: Japanese manufacturers, including the company, are now facing three types of headwinds. The first is foreign exchange rates. The recent trend of yen depreciation is showing signs of stabilization. The second is the uncertainty over the U.S. economy. A slowdown in the U.S. economy will inevitably affect the construction equipment market. The third is the U.S. tariff policy. Since the company’s business strategies are centered around its growth in the U.S. market, it needs to drive business model transformation and outperform its competitors in this harsh external environment. Just as Software Defined Vehicles (SDVs) are gaining attention in the automobile industry, I believe software will be a true source of competitive advantage in the construction equipment industry as well.
Kikuchi: The external environment will continue to change in the future. Rather than responding to individual issues each time, it is important to develop a clear long-term strategy and build a solid foundation that can withstand headwinds. The company should not remain on the defensive. Instead, I hope the company will proactively seize opportunities and act decisively in line with its long-term strategy. As a newly appointed director, I intend to closely monitor the progress.
Okuhara: The company has the Kenkijin Spirit of not being afraid of taking on challenges. It also has a history of pioneering untapped markets where even trading companies did not venture. Now that the company is no longer a listed subsidiary and has greater autonomy in management, not only its ability to formulate strategies but also the ability to execute them is being put to the test. I hope that the company will be able to demonstrate the Kenkijin Spirit to present its renewed identity.
Oka: When the yen reached its historical high against the dollar, the company’s export ratio was relatively low, therefore it seemed somewhat less resilient to the appreciation of yen compared to other export companies. Over the past five years, there were tailwinds of yen depreciation, however, going forward, the company needs to strengthen its corporate “core” so that it will be able to withstand a certain level of yen appreciation.
Kikuchi: Because the company cannot directly control exchange rates, I sometimes feel that there is a sense of giving up on taking countermeasures, however, I believe the company should thoroughly consider specific measures from a risk management perspective.

M&A and the Decision-Making Process

Otsuki: In terms of making decisions on taking proactive actions such as on investments and M&A, which will determine the future direction of the company’s business, what kind of discussions are taking place in Board of Directors meetings?
Oka: Information is shared and discussions take place prior to adopting resolutions, however, there are some issues. First, proposals tend to overly focus on the internal perspective, and lack comprehensive, rational explanations that take into account the competitive environment. Second, financial explanations often focus more on the perspective of debt providers and lack sufficient focus on the perspective of equity investors. Third, there is a lack of adequate checks and balances when proposals are discussed by the executive side before they are presented to the Board of Directors. If we are not provided with sufficient information, we have no choice but to keep requesting more information until we are satisfied.
Ito: Although explanations for important investment projects are provided in advance, presentation materials used in Board of Directors meetings are often repurposed from those used in executive committees, which makes the discussions prone to micromanagement. Ideally, we need to have information that gives a bird’s-eye view, including how a project aligns with the company’s long-term strategy and business portfolio transformation, how risks and opportunities are analyzed, and the feasibility of PMI. Also, it would be valuable if the minutes of executive meetings were shared as part of the reference materials.

Non-Financial Information and Corporate Value Creation

Otsuki: How do you see the relationship between non-financial KPIs and the process of creating medium- to long-term value? Also, how will achieving each of the non-financial KPIs lead to enhancing corporate value?

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Schmelzeis: As a statutory requirement, the Board of Directors must accurately understand and approve financial information, which takes considerable time. Nevertheless, because financial information mainly focuses on the past, discussions tend to be backward-looking. On the other hand, non-financial information is forward-looking, which gives us room to have discussions from the perspective of how the information aligns with the company's strategies. Going forward, I will continue to encourage the executive side to share more non-financial information.
Oka: If someone asks us which KPIs are most important for the company, we can promptly provide relevant financial metrics, however, with non-financial KPIs, some ambiguity remains. The portion of PBR exceeding 1x is essentially a reflection that the company's non-financial value has been recognized. To enhance the company's non-financial value based on its long-term strategy, we need to further clarify which KPIs should be prioritized.

Otsuki: How does the Board of Directors discuss and monitor the promotion of sustainability? Some materiality KPIs are included as ESG evaluation items and are linked to performance-based compensation for executive officers. How are these KPIs evaluated in the Compensation Committee?
Okuhara: In the company's executive compensation design, we increased the performance-linked portion while incorporating non-financial items as performance measures. In addition to setting quantitative targets, qualitative ESG goals are incorporated into the Management by Objectives (MBO) targets of each executive officer. These are key factors considered by the Compensation Committee in determining the amounts of compensation, and we believe they are effectively functioning as incentives.
Ito: While incorporation of ESG evaluation items is effective, there is still room for improvement in terms of monitoring. For example, there are issues such as the qualitative goals of each executive officer not being shared, or interim numerical targets not being shared although targets for the final year of the medium-term plan have been set. We have been informed that these issues will be addressed and improved.

Human Capital Investment and Monitoring

Otsuki: The topics of human capital investment and enabling employees to thrive were also featured in last year's Integrated Report, indicating that the company places a high priority on them. On the other hand, quantitative targets related to human capital remain relatively limited. How does the Board of Directors monitor the value creation process of human capital?
Oka: We are interested in not only the progress of materiality KPIs but also employees' motivation. This cannot be fully measured by numbers, so we ask the executive side questions, including how they see things in the workplace.
Okuhara: Frequent topics discussed at Board of Directors meetings include appointing female managers and building an HR evaluation system that includes overseas group companies. The company is committed to ensuring diversity; however, it is equally important to appoint younger employees to take on important roles and select future management candidates. Achieving a "second founding" and independence requires younger employees to take on challenges, however, mechanisms to support them are still insufficient. One of the roles of the Nominating Committee is to have in-depth discussions on this matter.
Kikuchi: As a newly appointed director who has only attended two Board of Directors meetings, my impression is that most of the reports focus on financial information, particularly P/L. For human capital investment, it would be valuable to receive reports on how HR initiatives are linked to engagement surveys, as well as the progress in fostering an ideal corporate culture, and to have discussions based on such reports.

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Strengthening of Governance and Consideration for Minority Shareholders

Otsuki: In your view, what is the mission of outside directors? Also, could you share your thoughts on relationships with major shareholders and protecting the rights of minority shareholders?

Okuhara: To be honest, as an independent outside director representing minority shareholders, I have encountered situations where communication becomes difficult when other outside directors represent certain shareholders. However, improving business performance by strengthening the ability to earn profits is a common expectation of all shareholders. We aim to accelerate decision making toward achieving greater goals while incorporating diverse opinions.

Schmelzeis: I would like to share an anecdote. I once asked an airline pilot whether he felt fear when holding the control stick with hundreds of lives depending on him. He replied, "Whether flying a jumbo jet or a small plane, the basics are the same. Protecting yourself comes first." Since I am also a minority shareholder of the company, I believe protecting myself will ultimately lead to protecting the interests of all shareholders, and I express my views with that in mind.

Oka: Looking ahead, one of the challenges we will face as independent outside directors is when the shareholder composition becomes more fluid. Major shareholders seeking to exit will likely focus on maximizing short-term shareholder value, while we pursue long-term corporate value. There, conflicts of interest may arise. Whenever that moment comes, we will be put to the test as independent outside directors.

Kikuchi: I believe the mission of outside directors is to monitor business management by the executive side and contribute to maximizing corporate value. In that sense, while major shareholders and minority shareholders may differ in position, the direction they are aiming is probably the same. To ensure proper monitoring, the company needs to clearly present its long-term strategies to achieve its vision to internal and external stakeholders. I also believe it is important for the company to equitably distribute the fruit of such strategies to stakeholders.

Ito: I believe one of my important roles is to ensure equity in the exercise of shareholder rights. If the shareholder composition changes in the future, frankly, it may be somewhat a challenging task to come up with ways to achieve this while taking into account the wishes of major shareholders.

Diversity of the Board of Directors and Operation of Committees

Otsuki: Evaluation of the effectiveness of the Board of the Directors conducted two years ago highlighted the issue of "rationalizing the skill matrix, selecting and appointing directors with the required expertise, and selecting candidates for future director positions." What kind of discussions are taking place for improvement?

Okuhara: In the Nominating Committee, we are discussing clarification of the skill matrix derived from the management strategy, and a systematic candidate selection process. While we have assessed that the current composition of the Board of Directors has reached a certain level in terms of independence and diversity of skills, we want to clearly define what the company's Board of Directors should be like with a forward-looking perspective.

Oka: The skills required of directors include both basic skills expected of all directors and specialized skills the team should have as a whole. I believe clarifying both of these skills will be a premise for achieving systematic succession.

Otsuki: Hitachi Construction Machinery is a company with a nominating committee, etc., and many of the directors concurrently serve as members of the Audit Committee, Nominating Committee, and Compensation Committee. Does this pose any challenges to the activities of the committees, and how heavy is the burden?

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Oka: I believe having all outside directors concurrently serve on all committees was based on the idea of valuing their independence. However, it makes it difficult to schedule meetings, and if there are too many members, responsibility may become blurred. Therefore, I recommended minimizing concurrent duties as much as possible and limiting the number of members of each committee to two or three.

Kikuchi: I agree. I am no longer a member of the Compensation Committee, but outside directors concurrently serving on all committees is not a common practice in other companies. Especially when discussing reappointment or non-reappointment of management members in the Nominating Committee, I feel that it is difficult to reach conclusions unless the committee is comprised of a small number of members.

Separation of Execution and Oversight, and Dialogue with Capital Markets

Otsuki: Currently, the Chairman and Executive Officer concurrently serves as the Chair of the Board of Directors. As outside officers, what do you think are the advantages and challenges of this arrangement in terms of governance?

Ito: I serve as the chair of the board of directors in a non-executive position at another company, and I feel it is somewhat difficult to separate execution and oversight when a CEO concurrently serves as the chair of the board of directors. I see it as one of the steps in the transitional phase of shareholder composition.

Schmelzeis: Although we are in a transitional phase, I believe execution and oversight should essentially be separated. It may not be an appropriate example, but I feel the “parent who gives birth” and the “parent who raises” do not have to be the same.

Otsuki: What role should outside directors play in communication with the capital markets? And how do you capture the voices of investors?

Okuhara: In the current transitional phase of shareholder composition, I believe there are certain constraints on independent officers having direct dialogue with institutional shareholders. However, through roundtables like this, we can share our perspectives.

Oka: So far, we have not received requests for dialogue, but I see this as a necessary step in the future. I met with institutional investors as an outside director in the past, and there were situations where I thought it would have been better if questions for the management and questions for outside officers were targeted in a more organized manner.

Ito: It seems that some institutional investors request for meetings simply because they have been asked by asset owners to “have dialogue.” I would like them to clarify the purpose of meeting outside officers, and the questions they want to ask. I see this as part of a process of mutual maturing.

Schmelzeis: The Board of Directors receive regular reports on investors’ feedback collected through IR activities. I place strong importance on the voices of shareholders and investors. Another key communication approach is the stock price. Market movements reflect various messages, and I want to interpret them as accurately as possible.

Kikuchi: Japanese buy-side analysts, etc. tend not to voice criticism as directly as overseas institutional investors, so if taken at face value, companies may end up not capturing negative feedback from the market. Therefore, I believe IR strategies are extremely important, such as properly capturing market voices and applying them to business management, as well as carefully selecting which investors to make an approach to. I hope to contribute to such efforts by leveraging my experience.

Otsuki: In today’s roundtable, I felt your strong enthusiasm for the company’s future and strong determination to carry out the transformation. Breaking away from the status of a listed subsidiary is only the starting point for a new growth trajectory. I sincerely hope the company will continue to take on bold challenges, hone the strengths it has gained, and continue to create value that exceeds market expectations.