

Question & Answer at IR Meeting on Financial Results for FY2021 Q1

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List of Questions (Detailed Question & Answer follows)

<Q1>

- Please explain the reasons of profit increase for the segments that initial forecast was revised upward. Even after the revision, it still looks conservative. Please tell us about your thoughts on this.
- If mineral resources market conditions continue, I think there is a good chance that it will be able to surpass the annual forecast of JPY290 billion raised for this fiscal year. In that case, what is the current discussion on the concept of dividends? In addition, please explain the possibility of one-off losses in the second half of the year.

<Q2>

- The recovery in Transportation & Construction Systems has been strong. What is outlook considering the current situation including the impact from COVID-19 re-outbreak? Also, please confirm that there are no more deficits or concerned projects in this segment.
- Regarding the guideline for investment selection, what kind of projects have been failed or should not have been taken up? Also, it is stated as “in principle”. Does it mean that there are case that you can invest to the project as exception?

<Q3>

- Please tell us how much you value the profit, excluding one-off profits and losses, of your company's current capability. And what is your thought on the profit increase plan for next fiscal year and onward.
- As to Fyffes and TBC which are the major turnaround projects, what is the background of profit increase and the outlook for the future?

<Q4>

- As to nickel mining and refining business in Madagascar, please tell us the operation plan and how you think about the profit contribution.
- As to Infrastructure segment, in the long run, I think that the main projects will need to shift from thermal power generation to other forms. Could you explain how you will achieve it?
- Will there be a temporary gap in profit level when shifting to renewable energy business?

<Q5>

- What was the background of not revising the forecast for Media & Digital and Living Related & Real Estate segments, while those segments seem to be making good progress?
- Although Mineral Resources, Energy, Chemical & Electronics segment revised upward to JPY35 billion, is it correct that there are no revised price forecasts disclosed for mineral resources?

<Q6>

- Please tell us about the scale of your revenues for business portfolio in agricultural input mentioned on page 33 of the presentation.

Question & Answer

<Q1>

Questioner 1: I would like you to explain the reasons of profit increase behind the upward revisions in the following segments: Metal Products: plus JPY10 billion , Transportation & Construction Systems: plus JPY5 billion, Mineral Resources, Energy, Chemical & Electronics: JPY35 billion, and Corporate and Eliminations: JPY 10 billion. Even after the revision, it still looks conservative. Please tell us about your thoughts on this.

Shiomi: As for the factors behind the upward revision, the performance of Metal Products and Transportation & Construction Systems segments were declined in the last fiscal year, since the global supply chain was disrupted and manufacturing site was affected by the COVID-19 pandemic. However, we have benefited greatly from the steady recovery of economic growth, which is a result of successful economic policies of each country and the policies to prevent the spread of the COVID-19 pandemic.

On the other hand, due to the shortage of semiconductors, the impact on profits in the second quarter and beyond needs to be closely watched.

Therefore, I believe that we can maintain the current robust performance in the first half of the fiscal year. However, we have revised the figures by JPY10 billion for Metal Products and JPY5 billion for Transportation & Construction Systems based on our current estimates of changes in the economic and business environment in the second half of the fiscal year which may be conservative to some extent.

In the segment of Mineral Resources, Energy, Chemical & Electronics, the mineral resources prices have been rising sharply. Our projects are also benefiting from these prices, and we are making considerable progress. But we expect that it will gradually be adjusted in the second half of the year.

Regarding nickel mining and refining business in Madagascar, last year, we had to suspend operations for almost a year due to COVID-19 pandemic. Since we resumed production in the second half of March this year, we have been able to put production on track and are producing at a pace that exceeds our plan.

Against this backdrop, we have increased our forecast for Mineral Resources, Energy, Chemical & Electronics by JPY35 billion for the current fiscal year from the initial forecast.

Questioner 1: What exactly are the areas that revised upward in Metal Products and Transportation & Construction Systems?

Shiomi: As for Metal Products, steel sheets prices are very high. In addition, demand for steel sheets is strong in both Asia and North America, and the performance is recovering. In terms of tubular products, the business

in North America shows recovery. However, the rig count is still only about 500 rigs as shown in page 28 of the presentation, so the speed of recovery is very gentle, and we have not yet reached the pre-COVID-19 pandemic level, partly because of the pressure for using fossil fuels. We must be conservative to some extent, so that is our assumption.

As for Transportation & Construction Systems, it is still difficult to predict when the bottleneck of semiconductor will be resolved. Also, the prices of material and parts for automotive manufacturing and shipbuilding are hiking, so that will have a negative impact in the second half of the year. This is the background to the figure of JPY5 billion of upward revision.

Yoshida: In anticipation of business recovery, the earnings of business unit increase and tax costs will be increased at business unit side. From the internal allocation perspective, the tax factor at corporate side is expected to be JPY10 billion of increase.

Questioner 1: If mineral resources market conditions continue, I think there is a good chance that it will be able to surpass the JPY290 billion raised for this fiscal year. In that case, what is the current discussion on the concept of dividends? In addition, I would like you to explain the risks involved other than business environment in the second half of the fiscal year, for example, the possibility that one-off losses such as the structural reform costs are expected to be larger than the initial estimate.

Shiomi: Regarding dividends, there is no change in our dividend policy announced in this medium-term management plan. The payout ratio is 30%. The net profit forecast is JPY290 billion for the full year, and we haven't changed the dividend of JPY70 considering the payout ratio of 30%. If the result surpasses JPY290 billion, we will consider again in accordance with dividend policy.

As for the progress of structural reforms, we are progressing according to the plan. And we do not foresee any major one-off losses currently since we have worked on short-term structural reforms intensively last fiscal year and have posted necessary costs already.

<Q2>

Questioner 2: The recovery in Transportation & Construction Systems has been strong this time. I have the impression that the automotive manufacturing business and automotive finance business in Indonesia are improving. What is outlook considering the current situation that COVID-19 pandemic has been spreading in Indonesia again?

Yoshida: As for the status of the Transportation & Construction Systems segment, the automotive manufacturing business is recovering, reflecting the recovery in automobile production. Aside from that, leasing business is also recovering well. Since there have been various fiscal stimulus packages and financial policies around the world, the economic activity is recovering, and so as our construction equipment business and other fields. In automotive financing business in Indonesia has also been recovering. This is because, in April and May, the number of new contracts accumulated, and credit costs were controlled.

On the other hand, since June, delta variant is spreading rapidly in Southeast Asia, including Indonesia. So, we need to watch closely on the current situation in Indonesia.

Questioner 2: Can I understand that there are no more deficits or concerned projects in Transportation & Construction Systems?

Yoshida: That is correct. The companies that are in the red have overall improved.

Questioner 2: On page 7 in the presentation, regarding the guideline for investment selection, what kind of projects have been failed or should not have been taken up?

Shiomi: We have prepared an internal paper of the “Seven Disciplines of Investment” which was deliberated at the Management Council and reported to the Board of Directors. This guideline is disclosed for employee’s awareness. In this context, it’s based on an evaluation of the past specific cases and they are listed in the paper to make it easier to understand. Typical investment cases are listed, for example, projects that have come up opportunistically which doesn’t fall in SBU’s strategy, and in addition, the projects not appropriate in terms of time frame, or large projects that exceeding SBU’s financial strength.

Questioner 2: It is stated as “in principle”. Does it mean that there are cases that you can invest on the project as exception?

Shiomi: Even if the project has conflict with these disciplines, there is possibility to conduct investment if the investment committee or the Management Council are convinced that there is enough allowance to go beyond these points. However, we are going to apply this discipline strictly, so we will make sure that we do not fall short in name.

<Q3>

Questioner 3: As per page 2 of the presentation, the profit for the first quarter was JPY93 billion excluding one-off profits and losses. Please tell us how much you value the profit of your company's current capability. And what is your thought on the profit increase plan for next fiscal year and onward.

Shiomi: In terms of current capability, we expect to maintain the first quarter’s level of performance in the second quarter. However, in the second half of the fiscal year, we assume that the situation will gradually return to the initial plan assumption. This may seem a bit conservative, but the prices of all mineral resources are very high now and will possibly be adjusted. Then there are the soaring prices of steel sheets and bottlenecks of semiconductor.

My current view is that next fiscal year will be similar to the second half of the current fiscal year, and we have not revised our profit and loss plan for FY2022. I believe that we will be able to get a clearer picture to some extent during the second quarter, and at that time, we will be able to reexamine the figures and make an announcement.

Questioner 3: So, does it mean that you have not improved your view of the economy for your profit forecast for the second and third years?

Shiomi: Yes. The current situation is more of a short-term adjustment phase, and having the assumption that it will gradually be adjusted to previous level, we are maintaining the 3-year plan.

Questioner 3: As to Fyffes and TBC which are the major turnaround projects, the profits have been improving in the first quarter. What is the background to this, and what is the outlook for the future?

Yoshida: As to Fyffes, the performance of bananas, pineapples, and melons were lower than expected in the last fiscal year. We see the recovery of market conditions and it progressed well, and at the same time, we are working to withdraw from unprofitable businesses and reduce costs. Specifically, bananas and pineapples are processed close to where they are consumed, and they are withdrawn from so-called unprofitable areas as well. Bananas and pineapples are being improved while addressing these issues. As for melons, sales will be recovering steadily in response to the recovery in the Americas.

As for TBC, there has been quite a bit of fiscal stimulus in the U.S., and the economy has been recovered. By catching up with these consumer trends, business performance is recovering, especially in wholesale. However, due to the rising cost of shipping and other factors, we are watching closely whether the current trend will continue. We are also working on structural reforms to firmly increase our capability.

Questioner 3: As to Fyffes, the profit for the first quarter was JPY1.1 billion compared to the JPY0.8 billion of initial forecast for the full year. Can I understand that it is exceeding the initial forecast?

Yoshida: Melon's performance is quite strong. But the melon season are off in the second quarter, and the next season starts in the third quarter, and there is seasonal factor. In addition, shipping costs and other costs are expected to increase here and we will not be able to progress as same as the first quarter. We are working hard to achieve JPY0.8 billion or more while promoting structural reforms in this area.

Yamane: About Fyffes, we have changed our fiscal year end last year and was a 15-month fiscal year. So last year's first quarter figure of minus JPY1 billion reflects January to March in 2020 when the COVID-19 pandemic started in China. This first quarter reflects April to June 2021. Please keep in mind that it is a little different.

<Q4>

Questioner 4: As for nickel mining and refining business in Madagascar, it is recovering to minus JPY2 billion. Please tell us the operation plan and how you think about the profit contribution?

Yoshida: As for the Ambatovy, we started operations in March, and the production has been progressing well. The annual production volume is expected around 40,000 ton per year, and it is progressing according to the plan. On the assumption that this operation will continue, if the price will exceed a certain level, the profit will be recorded firmly. Madagascar is also concerned about the COVID-19 pandemic. We are working to prevent infection and if we can keep this operation running, we will be able to achieve good numbers.

Questioner 4: As to Infrastructure segment, in the long run, I think that the main projects will need to shift from thermal power generation to other forms. Could you explain how you will achieve it?

Shiomi: As for the future plan for Infrastructure, we will continue to work on airports, water related, railways, and ports in these areas. We have accumulated a great deal of know-how in the coal-fired thermal power generation business and EPC business, and in view of the current environment, we will have no choice but to shrink our business. As a result, power generation will inevitably shift to renewable energy sources. We are now aggressively promoting the use of wind power. We will take up offshore wind power in Japan in the future and using our know-how in power generation business to create a solid profit base. About social infrastructure, we will be using the know-how of project management to make the projects profitable for the ones we are currently working on around the world.

Therefore, although the business model will inevitably change from the past, which was based on accumulating coal-fired thermal power generation projects, recognizing profits based on construction progress, and collecting cash, the experience, skills, and know-how that the Infrastructure has acquired up to now will be inherited in the future.

Questioner 4: Will there be a temporally gap in profit level when shifting to renewable energy?

Shiomi: I think there will be a gap. Even though we are working on more projects in renewable energy, its profit contribution will be later while the profit for coal-fired thermal power generation business is falling in the foreground. On the other hand, the social infrastructure initiative is to fill the gap between the two, which will be the stable profit pillar for future. The current basic strategy is to increase the profitability here.

Yamane: As for the overseas IPP business, we do not anticipate a large drop in this figure.

<Q5>

Questioner 5: What was the background of not revising the forecast for Media & Digital and Living Related & Real Estate segments, while those segments seem to be making good progress?

Shiomi: For this upward revision of the forecast, we have not accumulated the figures from the business unit because it is first quarter and there is high degree of uncertainty. We made certain assumptions and discussed this in our management side. We have confirmed internally that there are no major changes in those two segments.

Questioner 5: Although Mineral Resources, Energy, Chemical & Electronics segment revised upward to JPY35 billion, is it correct that there are no revised price forecasts disclosed for mineral resources?

Shiomi: Yes. The current price level will probably remain unchanged in the second quarter. However, for the second half of the year, we assume that there will be gradual adjustments to the prices and they will be the level of our initial forecast.

Yamane: The 37% for Living Related & Real Estate is in line with our plan for the year because of the delivery of large-scale properties in real estate business.

<Q6>

Questioner 6: Please tell us about the scale of your revenues for business portfolio in agricultural input mentioned on page 33 of the presentation.

Yamane: We have two main divisions in Chemical and Electronics, and FY2021 forecast for two divisions is approximately JPY20 billion, of which about half comes from Life Science Division and agricultural inputs business contributes to more than half of the profit of this division. We have substantial footprints. Therefore, one of the main pillars of our growth strategy for Chemical and Electronics is to continue to strengthen this area.

Shiomi: Last year, we reluctantly ended up in the red, which caused us a lot of concern, and we received a lot of criticisms. We are proud of the fact that we have been able to complete what we needed to do for the past year, rather than simply accepting the deficit. Our short-term structural reforms are producing results, and we will continue to work on them this fiscal year without slowing down.

First, our primary goal is to complete the 3-year medium-term management plan that we have announced, and although we have just finished the first quarter, we are making good progress now, thanks to the tailwind of the environment. We would like to ask for your continued support, and we will continue to work hard to achieve a recovery in business performance and a V-shaped recovery.

Thank you for your continued support.

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