**Sumitomo Forestry Group**

**Financial Results for the Fiscal Year Ended December 31, 2022**

**Conference Call with Analysts and Institutional Investors - Q&A**

Time and date: 1:30 p.m.– 2:30 p.m., Wednesday, February 15, 2023

Answers:

Toshiro Mitsuyoshi, President and Representative Director, Sumitomo Forestry Co., Ltd.

Tatsumi Kawata, Director and Senior Managing Executive Officer, Sumitomo Forestry Co., Ltd.

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Q

What is the outlook for achieving the 9,000-unit sales plan for the U.S. single family homes business for FY12/2023, given the order backlog at the beginning of the fiscal year and the current order situation? Also, when do you expect to make a decision on controlling new housing starts, with a view towards achieving 9,000-unit sales?

A

In terms of the current market situation, in January 2023 mortgage rates were moving around the 6% level, and onsite customer footfall has recovered, with the number of contracts recovering to about 70% of the same month last year. Cancellation of contracts has also decreased compared to the fourth quarter of FY12/2022. Although various risk factors remain, if interest rate increases can continue to be kept down, we believe we will be able to increase contracts this fiscal year, mainly for spec (built-for-sale) homes, and reach our planned total sales of 9,000 units. As for the outlook for the annual number of new starts, we expect to have a clearer picture after the January to March period, which is said to be spring season. As for profits relating to the 9,000-unit sales plan, although unit sales prices will vary depending on the area, overall, we are anticipating a 5.2 point price reduction compared to the previous year, in addition to which, assuming higher land costs and a slight decrease in construction costs, we are forecasting that the five companies engaged in the U.S. single family homes business combined will report a 12.9% recurring income ratio.

Q

In terms of returns to shareholders, if the recovery in the U.S. housing market is slower than expected could this impact dividend payments in this fiscal year and the next, or do you still have some leeway in that regard?

A

Although I can’t give you any specific information at the current time about what we would do if, for example, the U.S. market were to plunge into a situation like the financial crisis of 2008, what I can say is that there is no change to our policy of providing a stable dividend to shareholders, and that barring some unforeseen event we do not expect any significant reduction in the dividend of 125 yen per share.

Q

Page 20 of the document “Business Environment and Progress on Medium-Term Management Plan,” includes forecasts from two thinktanks about the outlook for the U.S. housing market, but there is a tremendous difference between the two forecasts. Which of these two scenarios are you basing your forecasts on? Also, in terms of the 9,000-unit sales forecast in the U.S. market for FY12/2023, does this include build to rent housing, or is there a possibility that all units will be sold off together?

A

Although the market forecasts of the two thinktanks are included in the distributed materials, our forecast for the number of units is based on the total compiled from the actual numbers verified by each of the five companies in the Sumitomo Forestry Group. Also, the forecast for sales of 9,000 units is purely for spec homes sold by the five companies and does not include single family rentals of Southern Impression Homes. Southern Impression Homes’ total sales of single family rentals in FY12/2022 was around 500 units, so these sales can be viewed as an additional figure.

Also, as we have robust inventory control structures in place we are not in a position where we have to sell off inventory all at once for cash flow or other purposes. Our figures are based on the assumption that we will start construction and sell spec homes, while continuing to monitor backlog and market conditions.

Q

Regarding sales of single family homes in the U.S., you have indicated the plans of the five U.S. companies are based on a cumulative method, so could you tell us from when you anticipate the number of homes sold to start moving upward?

A

In areas like Seattle in Washington, Phoenix in Arizona, and Austin in Texas, where price increases have been steeper, due to the severe deterioration in affordability we plan on using measures such as discounts to secure the volume of units sold. On the other hand, along the East Coast, from Washington D.C. to South Carolina the deterioration in the market has not been as severe, so we can still make sales without having to discount too deeply. We are working on a scenario of responding appropriately to market conditions.

Q

The current state of Japan's housing market is such that even the slightest indication of an increase in interest rates can impact sales. Could you tell us if you anticipate the number of detached houses for sale to grow in the future and also what your strategy is.

A

Our share of the number of new starts for owner-occupied houses in Japan previously stood in the upper 2% bracket, but in FY12/2022 it has grown to 3.28%. By ensuring that we start construction of 8,500 homes annually, we believe that we can steadily increase our market share, even as the overall number of new starts is falling.

The challenge is to secure orders from mainly first-time home buyers for homes of 30 million yen or less. Our response strategy is to promote "Forest Selection," a semi-custom-built-to-order product with a unit price of around 30 million yen and a wide variety of 1,100 floor plans to choose from. In addition, by strengthening our real estate alliances and providing land together with the Residential Property Development Dept., which is engaged in the spec home business, we aim to secure first-time home buyer customers.

Although we anticipate a tough battle, we aim to maintain our market share and win a good balance of orders, from the high-end segment to the volume zone, and the under-30-million-yen segment.

Q

In terms of real estate development properties in the U.S. in FY12/2023, you anticipate sales on a similar level to FY12/2022, but with a significant drop in recurring income. Could you share more about your approach to this fiscal year's plan, including the environment for the sale of commercial real estate?

A

In real estate development, we have formed SPCs through which there are a good number of projects in which we have a minor stake, and most of the profits from the sale of properties are recorded as equity in earnings of affiliates. It is for this reason that net sales and recurring income are not linked. Given that in FY12/2022 we sold 11 properties, and in FY12/2023 we plan on selling eight, we are forecasting a year-on-year decrease in recurring income.

Looking across the overall market situation, while demand for rental housing has increased since last year, driven by a housing shortage as affordability has become more challenging due to rising home prices, rents are showing signs of peaking out. This means that we are not in a situation where we can sell properties at a high price ahead of schedule amid low rental occupancy rates, as was the case in FY12/2022. As for office buildings, also the market environment is severe, we will seek to differentiate ourselves by focusing on medium- to large-scale wooden office buildings.

Q

What is the background to the anticipated improvement in the recurring income to net sales ratio in the domestic housing business for this fiscal year?

A

In FY12/2021, due to cost increases arising from the "wood shock," losses in the custom-built detached housing business amounted to 6.4 billion yen, which further expanded in FY12/2022 to a loss of approximately 10 billion yen due to rising housing costs. However, two rounds of price revisions have finally meant that since the second half of last year through to this fiscal year we have been able to cover cost increases slightly. The 1.8-point year-on-year downturn in the gross profit margin ratio for FY12/2022 includes a 2.7-point decrease in building materials, and a 0.8 point increase due to price revisions. For FY12/2023 our plan is to achieve a 2.7-point year-on-year increase, and we are projecting a 1.1-point decrease in building materials, and a 3.6-point increase through price revisions.

Q

Against the backdrop of a current order backlog of 2,899 homes in the U.S. single family homes business, what are your plans for progressing to sales of 9,000 units? Also, how consistent do you think sales trends are with mortgage rates in the U.S.?

A

The plan for realizing sales of 9,000 units represents an accumulation of various plans formulated in response to the varying conditions in the locations where we do business. Although there are regional differences, given the current preference for spec (built-for-sale) homes, we believe that we can achieve this goal by working hard to build up the spec properties that are required by customers. Although the cancellation rate also increased in the previous fiscal year, it has now returned to its normal level of approximately 20%. Towards the end of FY12/2022 although there were some cancellations, the backlog of orders on the books at the beginning of this fiscal year indicates a high degree of certainty for sales going forward. After deductions for cancellations, sales in January 2023 stood at 650 units.

It is a fact that fluctuations of 1% either way in the U.S. mortgage rates make a major difference to the repayment amount on a mortgage. At the same time, however, in addition to an environment in which wages are increasing and unemployment is low, coupled with the fact that the volume of pre-owned homes in circulation continues to be very low compared to previous conditions, when there were 5 to 6 existing homes for every 1 new home built, the general consensus among local management personnel is that the market will start to move once mortgage rates drop below 6%.

Q

How accurate do you think your forecasting is for the figures for income items for FY12/2023, or do they represent a best guess?

A

The forecast figures we have issued are the best that we can come up with at the current time. Since the U.S. accounts for a large portion of the total, the outcome will be greatly affected by business in the U.S. While fluctuations either up or down are possible, we want to maintain recurring profit at the very least around the 100 billion yen level, so we would want to keep any downturn to a level of around 10 billion yen.

$\boxed{\text{Q}}$

What weighting would you give to finance, investment, and shareholder returns if the total of these three came to 100?

$\boxed{\text{A}}$

Our basic stance is to maintain balance, so the ratio would be 1:1:1.

However, as we have designated the Medium-Term Management Plan to FY12/2024 as an investment phase towards the realization of our 2030 long-term vision, our policy is to place a little extra weighting on investment rather than finance.

For shareholder returns we will basically continue to follow our stable dividend policy.

$\boxed{\text{Q}}$

Investment appears to be lagging behind initial plans, so where do you intend to prioritize investment going forward?

$\boxed{\text{A}}$

At the end of the first year of the Medium-Term Management Plan investment stood at 60 billion yen, or 21% of the planned three-year total of 300 billion yen. Among these investment activities there were some M&A deals that we did not invest in, not because we were unable to do so, but because we made a conscious decision not to after calmly considering their future potential. We would definitely want to invest in a timber industrial complex that would serve as a very important domestic base for promoting the forestry industry and as a timber manufacturing and processing center in Japan. In the case of a large industrial complex investment would be in the range of 15 to 30 billion yen, and we would like to consider next another location after Shibushi in Kagoshima Prefecture.

In our long-term vision we have set a target of achieving sales of 23,000 houses in the U.S., and we will continue to secure land on an organic growth base.

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