**Sumitomo Forestry Group**

**The Second Quarter of the Fiscal Year Ending December 31, 2022**

**Financial Results Briefing**

・Time and date: 1:30p.m. - 2:30 p.m., on Wednesday, August 10, 2022

・Presenter: Toshiro Mitsuyoshi,

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

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We would like to go into the details of the full-year forecast for Q2 results, Mr. Kawata will explain the details later, but in H1 of the year, driven by the overseas housing and real estate business, net sales increased 23.7% YoY to JPY782.8 billion, and recurring income increased 81% to JPY93.6 billion.

Regarding the forecast for the full year, we have revised our business results upward, mainly due to the impact of the yen's depreciation against the US dollar, in addition to the fact that the overseas housing and real estate business is expected to perform better than planned at the beginning of the fiscal year. As a result, our company recorded net sales of JPY1,613 billion and recurring income of JPY175 billion. This is JPY89 billion and JPY40 billion higher than the initial plan for net sales and recurring income, respectively.

The Second quarter financial results have reached a record high on a recurring income basis, and we expect to reach the same record high for the full year.

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As we mentioned earlier, you could see that the overseas housing and real estate business, which has been doing well in the US, has grown significantly, both in sales and profit.

On the other hand, in the domestic housing and construction business, soaring prices for wood and other materials pushed up costs, resulting in significant pressure on profits. We expect this cost increase to continue throughout the current fiscal year, and we have a severe profit/loss forecast for the full year.

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In contrast to 2021, when we suffered cost increases due to the wood shock, our initial business plan for this fiscal year was based on the expectation that the soaring prices in raw material prices would subside to some extent.

However, Russia's invasion of Ukraine in late February has brought about supply instability in resources and energy around the world, resulting in inflation, and the sharp depreciation of the yen has also contributed to high prices, especially for wood and other construction materials.

As a result, the timber and building materials business saw an increase in both sales and profits due to higher unit prices of products. On the other hand, in the housing and construction business, sales were higher than in the same period of the previous fiscal year due to strong orders and higher unit prices of completed construction. However, profits have decreased, as we have not been able to compensate for the soaring prices in material prices.

In response to soaring material prices, we have continued to reduce costs through self-help efforts, such as streamlining construction methods, and following H2 of last year, we have revised prices and reflected a portion of the costs in housing sales prices since June of this year. The effect of the sales price review on business performance is expected to begin in the next fiscal year.

As for the outlook for wood prices, wood inventories in the market are increasing. We expect prices to gradually settle down to those based on the supply-demand balance.

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In this business environment, the housing and construction business continues to pursue its high added-value strategy, such as increasing the ratio of ZEH-specification homes, and as of the end of Q2, the ZEH ratio was 77.2%, which is in line with the target of 80% set in the mid-term management plan.
In April, we also launched LCCM homes as our environmental flagship model to respond to soaring energy costs and reduction of global environmental impact. LCCM homes reduce both embodied carbon, which is generated during construction, and operational carbon, which is generated during living, resulting in a minus $CO_2$ balance over the entire life cycle.

In addition, we have strengthened sales of the forest selection series, which has price competitiveness, according to area characteristics. We also focused on digital marketing using the Internet, which was effective for the COVID-19, and streamlined construction by pre-cutting and panelizing materials and expanding the use of precast foundations.

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The US Single-family homes business, which has grown to become a pillar of our business, continued to boom in H1 of this year. Sales and profits both grew significantly due to an increase in unit selling prices that exceeded increases in material and labor costs. However, the Fed's sharp and rapid increase in policy rates to curb inflation has caused the standard 30-year fixed mortgage rate to jump from around 3% last year to the current level of around 5%. The order situation has been under a steep brake due to rising home prices over the past couple of years, as well as declining affordability.

Since the second half of H1 of the year, customers have become more wait-and-see, and the slowdown in the order base has led to an adjustment phase in sales prices in some areas, which should result in a temporary slowdown in the market. However, we do not believe that this slowdown will lead to a prolonged slump in the housing market as once occurred after the financial crisis in 2008.

One reason for this is the soundness of the mortgage. At the time of the financial crisis in 2008, excessive lending by financial institutions to those with low ability to repay loans, represented by subprime loans, later caused serious financial instability, but currently, the ratio of loan lending to those with insufficient credit in the US is low, and we believe the situation remains healthy.

In addition, about 90% of mortgages are now fixed loans, and cases of sharp increases in repayments due to rising interest rates have become extremely limited, with low loan delinquency rates and virtually no foreclosed properties on the market due to insolvency. The existence of unrealized gains due to rising home prices and other factors may also be cited as reasons for the healthy loan balance.
Other factors include low housing inventory. The number of existing home inventories in the US as of the end of May this year was at a historically low level of approximately 2.5 months relative to the number of sales for the year, and the inventory of completed new homes was also at an extremely low level, maintaining a continued tight supply-demand balance.

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We mentioned that the US single-family homes market is currently in an adjustment phase. This does not mean that demand itself has been lost, but rather that customers are taking a wait-and-see attitude due to the decline in affordability caused by too rapid an increase in interest rates, in addition to the increase in housing prices to date.

At this point in time, some areas of the market are seeing declines in home sales prices, and a temporary slowdown in the overall US housing market is inevitable. At the same time, wood and other material prices are declining, and material delivery delays, particularly for windows, are gradually improving. Some think tanks are predicting that mortgage rates will peak in Q2 and Q3 of this year and then remain in the 4% to 5% annualized range. If the inflation is tamed and interest rates stabilize from the end of the year through next year, we expect customers to change their wait-and-see attitude and the firm latent demand will start to move again. Because of the large number of homebuyers, the existence of high demand remains the same, and the market is expected to stabilize and recover once this adjustment phase is over.

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We have responded to the current rise in interest rates by offering various incentives tailored to our customers, such as preferential interest rates in cooperation with financial institutions. In addition, our group as a whole currently has over 77,000 blocks of land set aside, of which approximately 1/2 are under contractual unacquired status, including option contracts promising future purchases in order to reduce the risk. Even for land that has already been contracted, more than 60% of the land has not been developed or is in the process of being developed, and the book value is low, so even if we were to terminate the contract and give up the land, the risk is extremely limited. We will continue to closely monitor sales conditions and strive to minimize risk.
In the real estate development business, all properties sold in H1 of the year were sold at prices that exceeded our plans, and leasing of our portfolio of multi-family residential properties has been very strong.

In the US, we are exchanging information and conducting joint projects among our group companies, including housing companies and real estate development companies, to further demonstrate synergies among our businesses and collaborate in new businesses, such as single family rentals housing and asset management.

We will further strengthen our business foundation by investing management resources in new businesses and remaining aggressive in the future. Therefore, we will continue to carefully select and consider M&A projects in promising areas where we have not yet entered.

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Our long-term vision is Mission TREEING 2030, which outlines our vision for the year 2030, which is also the target year of the SDGs. The theme of this vision is to promote decarbonization and wood cycle by maximizing the value of forests and trees. To achieve this, we will focus on promoting businesses in the fields of forestry, wood, and construction that will both further our company's growth and contribute to a decarbonized society. This diagram shows how Sumitomo Forestry, which is involved in everything from forest management to wood processing and distribution, wooden construction, and wood biomass power generation, contributes to the absorption and storage of $CO_2$ throughout society through our entire business by implementing the wood cycle.

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We also aim to establish a global forestry fund to help companies that need carbon offsets to decarbonize their operations by expanding forest and peatlands coverage around the world, particularly in Asia, but also in Oceania, North America, and South America.

As of 2030, the forest fund aims to have approximately JPY100 billion in assets under management and 500,000 hectares of owned and managed forests worldwide. Currently, SFC Asset Management, established in 2020, is acting as the operating unit, and this year, 2022, it has established and started managing a private real estate development fund in the US. Sourcing of forests in Asia and Oceania is also underway for companies requiring carbon offsets in Japan.

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In order to widely promote carbon credits from forests, it is important to ensure the quality of carbon credits, which is very difficult to obtain and manage accurate data. To this end, we will generate high-quality carbon credits through advanced forest management by combining the forest management technologies we have cultivated in Japan and overseas, ground data of forests, and IHI’s satellite-based observation technologies to manage water levels with a high degree of accuracy.

Currently, we are working to build a business operation system and establish the necessary technology for forest management consulting. In the future, we will strive to further improve our consulting level by accumulating data on forest peatlands around the world and enhancing the accuracy of observations, in addition to realizing an order for consulting services for peatlands management in Indonesia’s rainforest.

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In order to increase the competitiveness of Japan’s forest industry, we aim to improve self-sufficiency by establishing a timber industrial complex with a wood biomass power generation facility and cascading the use of domestic timber. Wood from forests will be collected at a single location, where sawmills and facilities for manufacturing high value-added laminated wood and CLT will utilize waste wood and woodland residue as an energy source.

It is expected to have such effects as the spread of wooden buildings and decarbonization by extending the carbon storage period, increasing the added value of wood, creating employment opportunities for forestry workers, and increasing the stable supply and price competitiveness of domestic timber.

We are currently working on our first project in Shibushi City, Kagoshima Prefecture, which will establish a manufacturing base for high value-added structural materials for construction using local wood that has been exported as log. In addition, we are considering the construction of new industrial complexes in several locations around the country, mainly in areas rich in wood resources.

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The construction sector accounts for about 37% of the world's CO2 emissions, and the so-called operational carbon (decarbonization during occupancy), which accounts for 70%, will be reduced through the spread of ZEH and ZEB.

On the other hand, it is essential to work throughout the entire supply chain to realize embodied carbon. We plan to standardize and expand the decarbonization of domestic buildings using One Click LCA, software that makes $CO_2$ emissions visualize before and during construction. We have begun pre-sales of One Click LCA in Japan, and the response has been extremely strong, with contracts already signed with several design firms, developers, and general contractors. We hope to create a major trend toward carbon neutral design in the future.

In addition, as part of our efforts of embodied carbon, we will work to replace steel and concrete for the structural framework with wood, which emits less $CO_2$ during the manufacturing process itself. There is a concept called HWP agreed to in the Kyoto Protocol. This concept is also recognized for its long-term carbon storage effect in wood used for construction. We intend to actively promote the superiority of wooden construction.

In Japan, we constructed the school building of Sophia University, Building No.15, which was completed in May, using pure wooden structure. In Sapporo, construction has also begun on a 10-story fire-resistant wooden building. Overseas, construction of a 15-story wooden office building in Melbourne, Australia, which began at the end of last year, and a 6-story pure wooden structure net-zero carbon office building in London, England, are scheduled to begin this year.

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Regarding dividends, taking into consideration our business performance and other factors, we have decided to increase the annual dividend by JPY45 from the originally planned JPY80 per share to JPY125 per share. Our company plan to increase the dividend for Q2 from the originally planned JPY40 to JPY60, and to increase the year-end dividend from JPY40 to JPY65.

We recognize that returning profits to shareholders is one of our highest priorities, and our basic policy is to do so in a continuous and stable manner. We will continue to improve return on equity and increase capital adequacy, and implement profit return measures at appropriate levels according to the status of profits, taking into account a comprehensive balance among management base, financial condition, cash flow, and other factors.

Thank you very much for your attention.

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