

Sumitomo Forestry Group
Financial Results for the Third Quarter of the Fiscal Year Ending December 31, 2022
Conference Call with Analysts and Institutional Investors — Transcript
Third Quarter Financial Results and Full Year Forecast

Time and date: 16:30 p.m.–17:30 p.m., Monday, October 31, 2022

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

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I will now give an overview of Q3 results and the full-year forecast.

Please see page two of the slides. This is the summary of the financial results for Q3 of the fiscal year ending December 2022.

In Q3, the Overseas Housing and Real Estate Business, mainly in the US, continued to perform well, and the Timber and Building Materials Business remained solid, resulting in overall sales of JPY1.2063 trillion, up 25% YoY; ordinary income of JPY141.9 billion, up 61% YoY; and net income of JPY82.7 billion, up 54% YoY.

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This is results by business segment.

In the Timber and Building Materials Business, in addition to higher sales and profit in the timber and building materials distribution business due to high prices for imported and domestic timber, the timber and building materials manufacturing business in New Zealand has improved, resulting in an increase in both sales and profit.

In the Housing and Construction Business, while unit sales prices rose in the mainstay detached housing business due to the rising ZEH ratio, the impact of rising costs for timber and other building materials remained significant, resulting in higher sales and lower profits for the segment as a whole.

In the Overseas Housing and Real Estate Business, although the single family homes in the US was affected by a decrease in the number of units sold due to a longer construction period and other factors, overall, the strategy of effectively raising prices while keeping an eye on market trends has been successful, and unit selling prices and profit margins rose. In addition, sales of real estate development properties progressed, resulting in a significant increase in both sales and income.

In the Environment and Resources Business, both sales and profits declined due to weak export sales in the New Zealand forestry business as a result of the slowdown in the Chinese economy, higher fuel procurement costs in domestic biomass power generation, and increased expenses related to new projects.

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The changes in ordinary income by segment for Q3 is as shown.

The impact of yen depreciation in foreign exchange is an increase of JPY19.6 billion. Excluding this effect, the substantial increase in profit from the Overseas Housing and Real Estate Business offset the weakness in the Housing and Construction Business and the Environment and Resources Business, resulting in a substantial overall increase in profit.

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This is the status of orders received and sales in the domestic housing business.

Orders for custom-built detached houses were lower than in the previous fiscal year in terms of both the number of houses and value, as the increase in demand for detached houses due to the "Cobit 19" pandemic slowed down, and partly because of the impact of the last minute purchase in September last year following the tax deductions for home loans.

Unit prices rose 6.4% YoY due to value-added proposals such as ZEH and price revisions in response to soaring timber and other materials prices.

Sales increased YoY in terms of both the number of units and amount, but the impact of increased costs was significant, and gross profit for the housing and construction business on a non-consolidated basis was down from the previous year.

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This is renovation business.

Orders from Sumitomo Forestry home owners continued to be strong, with both sales and orders up from the previous year.

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This is the performance of the Overseas Housing and Real Estate Business.

In the US, the single family homes business achieved a significant increase in both sales and profit, and in the real estate development business, the sale of properties proceeded better than expected, resulting in a significant increase in both revenue and income that far exceeded our initial forecast.

In Australia, although revenue increased due to the weaker yen, the business environment remained difficult, with higher costs due to material and labor shortages, longer construction periods, and intermittent construction delays caused by heavy rains and flooding, resulting in a recurring loss.

In other regions, real estate development projects in Vietnam continued to perform well from Q2.

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This is the status of orders received and sales in the overseas single family homes business.

Orders in the single family homes business in the US were more severe as customers took a more wait-and-see attitude in response to rising mortgage rates. Although the number of units sold was

lower than the previous year due to the extended construction time, the amount and unit price were significantly higher than the previous year on a local currency basis as well.

The backlog of orders received was 4,838 units at the end of September, a decrease from the previous period. However, the situation differs significantly from the previous period, when there was a particular increase in sales of the presale homes for which contracts were signed before construction began, whereas in the current period, the mainstream of properties for sale has been spec homes with a short lead time between contract and sale since Q2.

This is higher than the 3,750 units of order backlog as of September 30, 2019, before the COVID-19 pandemic, when spec homes were the norm.

Inventory blocks, including purchased lots and option blocks, are at a level of over 74,000 blocks. We will promote appropriate management of inventory risk by adjusting construction schedules, carefully selecting new acquisitions, and taking other actions in response to changing market conditions.

In the Australian detached housing business, the number of units ordered and sold declined YoY due to rising mortgage rates, as well as higher costs, longer construction time, and delays in the government's permitting and approval process. Although the number of units ordered and sold declined YoY, the sales amount increased due to the effect of foreign exchange rates.

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A summary of the balance sheet is as shown.

Total assets increased by JPY323.9 billion from the end of the previous fiscal year to JPY1.6381 trillion, mainly due to an increase in inventories in the Overseas Housing and Real Estate Business.

Liabilities increased by JPY152.9 billion to JPY927 billion, mainly due to an increase in borrowings for the acquisition of real estate for sale in the US.

Net assets increased JPY170.9 billion from the end of the previous fiscal year to JPY711 billion, mainly due to the accumulation of profits and a significant increase in foreign currency translation adjustments as the yen weakened.

The above was a summary of our financial results for Q3.

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Next, I will explain our full-year forecast for the fiscal year ending December 2022.

Overall results remain unchanged from the previous announcement.

As in the previous announcement, we forecast ordinary income of JPY175 billion, a new record high.

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There is no change in the forecast for segment earnings from the previous forecast.

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Next is the forecast for orders and sales in the domestic housing and construction business.

Orders have been revised downward in terms of both the number of units and amount in light of the current situation. We will continue to propose high environmental performance such as ZEH housing and our unique woody space to win orders.

On the sales front, the upward revision is due to an increase in the ZEH ratio and progress in deliveries following the price revision implemented in June last year, which is expected to result in higher unit prices.

With regard to custom-built detached housing, in addition to promoting orders, we will continue our efforts to reduce costs, particularly production costs.

In addition to the pre-cutting and panelization of components, which we have already begun, we aim to raise the level of profitability by establishing an appropriate construction system for each area and promoting digitalization.

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There are no revisions to the forecast for the renovation business.

We will continue to focus on sales to Sumitomo Forestry home owners and to win orders for large-scale properties.

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This is the forecast for the Overseas Housing and Real Estate Business.

In the US single family home business, while the forecast for the number of units sold was lowered, net sales and recurring income forecast were revised upward due to the effect of the yen's depreciation. Although the housing market in the US has become more difficult compared to Q2 due to the deterioration of affordability caused by rising mortgage rates, the Group will continue to take measures appropriate to the situation in each region, such as partially covering interest rates, offering various incentives, or reducing sales prices, in order to promote orders.

In addition, we will aim for further growth through the promotion of the FITP business, which will provide integrated services from panel design to manufacturing, delivery, and installation, following the recently announced acquisition of the Structural Group, as well as by considering expansion into new areas.

In the US real estate development business, sales have been revised upward based on progress through Q3. The forecast for ordinary income has been left unchanged due to expected personnel expenses such as bonuses in Q4.

The foreign exchange impact included in the difference between current forecast and the previous forecasts for the US single family home business and the US real estate development business is approximately a JPY6 billion increase altogether.

In the Australian detached housing business, both net sales and recurring income have been revised downward due to a worsening shortage of materials and labor, as well as ongoing delays in the government's permitting process.

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It shows the forecast for the number of units sold, sales amount, and unit sales price in the US and Australia.

In the US, the number of units sold was lowered by 300 units from the previous forecast, mainly due to the slowdown in contracts for spec homes that can be delivered during the period.

In order to achieve the sales forecast of 10,550 units after the downward revision, we will need to sell approximately 2,800 units in Q4, based on the 7,726 units sold up to Q3. However, we plan to have some from the properties already contracted, therefore we are on track to achieve it.

Sales amount and sales unit prices have been revised upward, taking into account the impact of the yen's depreciation. There is no revision to unit selling prices in local currency.

The forecast for Australia has been revised downward, partly due to the continued delay in improvement in the lengthening of construction time for order homes.

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I will now explain the progress of the long-term vision.

The long-term vision announced in February 2022 was formulated as Mission TREEING 2030, summarizing our vision for the year 2030, which is also the target year of the SDGs.

The Sumitomo Forestry Group is engaging in the businesses centered on trees, from forest management to the procurement and manufacture of timber and building materials, wooden construction, and wood biomass power generation, both in Japan and overseas.

This diagram shows how Sumitomo Forestry's wood cycle of logging, processing, reusing, and planting trees can increase the amount of CO₂ absorbed by forests and continue to fix carbon for a long time through the use of wood.

First, let me explain the progress on the forest business on the left side of the figure.

In the forest business, we will create a global forest fund to secure new CO₂ absorption sources and meet the carbon offsetting needs of companies and other societies.

We have recently established a forest asset management company in the US with two US partners who have been involved in the formation of forest funds. We plan to use their knowledge and network to create a forest fund that meets the needs of our clients, including Japanese companies already contacted by us who are interested in forest funds.

Next, please see the construction part on the right-hand side of the diagram.

Toward the standardization of decarbonized design, we are promoting medium- and large-scale wooden buildings in Japan and abroad. In Japan, we are constructing Building No. 15 at the Yotsuya Campus of Sophia University and a 10-story, wood-frame fire-resistant building in Sapporo.

Overseas, a 15-story building is under construction in Melbourne, Australia, with completion scheduled for 2023. In London, England, construction will soon begin on a six-story wooden office building that will achieve net-zero carbon emissions for approximately 60 years.

In addition, for One Click LCA, an application that visualizes CO2 emissions at the time of construction, we have concluded a sole agency agreement in Japan and began selling the product in Japan in August 2022. We are currently in negotiations with major construction companies and real estate developers.

On November 7, we will hold an information session with the participation of 150 major companies in the construction industry. We are striving to further promote the use of this tool and to make it a standard tool in the construction industry.

This concludes my presentation. Thank you very much.

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