Sumitomo Forestry Group
Financial Results for the Fiscal Year Ended December 31, 2020
Conference Call with Analysts and Institutional Investors - Transcript
FY12/20 Financial Overview and FY12/21 Forecast

Time and date: 1:00p.m.-2:00p.m., Tuesday, February 16, 2021
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As already noted, the Sumitomo Forestry Group is consolidating fiscal year-ends on December 31, so the fiscal year ended December 2020 was a nine-month period from April to December.

In this material, the results for the fiscal year ended December 2020 are compared with the results from the third quarter of the fiscal year ended March 2020. As such, for those overseas subsidiaries that already had fiscal years ending in December, the numbers from April to December 2020 are compared to the numbers from January to September 2019.

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Overview of the financial results for the fiscal year ended December 2020

In the fiscal year ended December 2020, the timber and building materials distribution business, manufacturing business, and domestic housing business saw sluggish results due to COVID-19. On the other hand, the increased units sold and improved profitability in the US detached housing business contributed significantly. As a result, overall net sales were up 4.6% year on year compared to the third quarter (cumulative) of the previous year to 839.9 billion yen, recurring income was up 19.1% to 51.3 billion yen, and net income was up 34.4% to 30.4 billion yen.

We record actuarial differences associated with retirement benefits all together at the end of the year in which they occur. In conjunction with the increase in the discount rate used to calculate retirement benefit obligations and pension asset improvements, there was an actuarial gain of 4.8 billion yen in the fiscal year ended December 2020. Recurring income excluding actuarial differences was 46.5 billion yen, exceeding the previous record high achieved for a nine-month period in the third quarter (cumulative) of the previous year.

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The results by segment

In the Timber and Building Material Business, there were some positive factors as well, such as the variable costs of raw timber material trending at lower levels than anticipated in the New Zealand

MDF manufacturing business. However, the sales volume in the distribution and manufacturing businesses declined as domestic housing-related markets slowed as a result of COVID-19, and the production volume decreased in the Indonesian manufacturing business as well. This created a difficult business environment, which resulted in a decline in both revenues and earnings.

In the Housing and Construction Business, orders received have been recovering in the midst of the COVID-19 pandemic, but delays in construction of custom-built detached houses, a decrease in the number of units completed in the renovation business, and other factors arising from measures to prevent the spread of the virus resulted in a decline in both revenues and earnings. Cohnan Kensetsu, which was brought into the Group to expand our medium- to large-sized wooden buildings business, will be included within the scope of consolidation starting in the first quarter of the year ending December 2021.

In the Overseas Housing and Real Estate Business, increased demand for new detached houses in the United States owing to record-low mortgage interest rates and other such factors and home buying subsidies and low interest rates in Australia provided a boost leading to a significant increase in the number of units sold. There was also a decrease in amortization of goodwill, so both revenues and earnings were up substantially. As mentioned previously, please note that this is a comparison between April to December 2020 and January to September 2019.

Revenues were up in the Environment and Resources Business owing to stable operations in the wood biomass power generation business and an increase in the sales volume in the New Zealand reforestation business, but a loss on step acquisitions recorded in conjunction with the conversion of an equity-method affiliate engaged in the reforestation business in Indonesia into a consolidated subsidiary resulted in a decrease in earnings.

In other businesses, revenues and earnings were up owing primarily to Elegano Nishinomiya, a serviced senior housing facility opened last May, and improvement in the occupancy rate in the elderly care facilities business. Note that other businesses includes equity in the earnings of affiliate Kumagai Gumi Co., Ltd.

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Orders received and sales in the domestic housing business

Orders received in the custom-built detached housing business were up 11.9% compared to the third quarter (cumulative) of the previous year in terms of monetary amount. Visits to housing display centers were down due to COVID-19, but both the number of units and the amount have been up year on year since July owing to the number of online materials requests greatly exceeding that of the previous year and our focus on online sales activities and proposals tailored to new lifestyles. Sales were down 3.6% year on year in terms of monetary amount. Although we worked on construction while implementing thorough measures to prevent viral spread, the lower operating rate at subsidiaries engaged in design support resulted in a shortage of construction starts.

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Orders received and sales in the renovation business

Due to concerns about the spread of COVID-19, customers were hesitant to have construction performed in their homes while they continued living there, and non-essential, non-urgent construction contracts were put off into the future. The business continued to struggle in July and thereafter, especially at large-scale properties, so the amount of orders received was down a steep 18% compared to the third quarter (cumulative) of the previous year.

The number of units completed was also down 19.8%. This was due to the drop in construction completed for new orders as well as the smaller backlog of orders received at the beginning of the year resulting from sluggish orders received the previous year.

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Overseas Housing and Real Estate Business

As already noted, the numbers from April to December 2020 are compared to the numbers from January to September 2019.

The US economy is in the midst of a recovery overall. Since economic activity was resumed in May, the market for new houses has been active owing to historically low interest rates and a low inventory of existing houses as well as demand from those looking to move from the city to the suburbs. As such, our group companies saw a substantial increase in the number of units sold. There was also an increase in profitability from the increase in selling prices and a decrease in amortization of goodwill, so recurring income was up substantially. In Australia, government subsidies for home buying and low interest rates provided a boost, and that along with the inclusion of West Australia-based Scott Park Group in the scope of consolidation resulted in an increase in both the number of units sold and net sales. On top of this, profitability improved at Henley, so income was also up.

On page 8, you will see a year-on-year comparison of segment profit and loss for April to December, provided for your reference.

On page 9, you will see the trends in the quarterly number of units sold provided for your reference.

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Capital expenditures

These numbers are compared to the full-year results from the fiscal year ended March 2020. For the year ended December 2020, the amount was 23.9 billion yen. This consisted mainly of investment in profit-earning real estate development in the United States, housing display centers in Japan and other countries, IT-related investments, and production equipment in the manufacturing business.

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The balance sheet summary

Total assets as of the end of the fiscal year ended December 2020 were up 86.4 billion yen from the fiscal year ended March 2020 to 1.0912 trillion yen. The increase was attributable mainly to an increase in investment securities resulting from an increase in the market value of listed shares held and an increase in real estate for sale, primarily in the US housing business. Liabilities were up 44.0 billion yen from the end of the previous year to 691.7 billion yen. This was due mainly to an increase in commercial paper issued and borrowings. Additionally, net assets came to 399.5 billion yen, and the equity ratio was 33.7%. Free cash flow was a positive 2.2 billion yen.

This concludes the overview of the financial results for the fiscal year ended December 2020.

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The plan for the fiscal year ending December 2021.

As mentioned at the beginning, the fiscal year ended December 2020 was a nine-month period due to a change in the fiscal year-end. For that reason, the plan for the fiscal year ending December 2021 is compared to the results from the fiscal year ended March 2020.

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The forecasts of Statements of Income

In the fiscal year ending December 2021, we forecast increases in revenues and earnings with net sales up 13.8% compared to the fiscal year ended March 2020 to 1.257 trillion yen, recurring income up 36.0% to 80.0 billion yen, and net income up 72.3% to 48.0 billion yen.

We expect to record record-high earnings due to continued favorable performance of the detached housing businesses in the United States and Australia, which expanded in the fiscal year ended December 2020 and have accumulated backlog of orders received, and a certain degree of recovery in the Timber and Building Material Business and the domestic custom-built detached housing business, which were impacted by COVID-19.

As President Mitsuyoshi already mentioned, net sales and recurring income will fall short of the targets in the Medium-Term Management Plan, but the tax burden dropped due to the increase in revenue from overseas where the tax rates are lower, so we expect net income to come in at around the target set forth in the Medium-Term Management Plan.

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The forecasts by segment

The comparisons are with the fiscal year ended March 2020.

In the Timber and Building Material Business, the results of overseas manufacturing companies impacted by the suspension of operations early on in the COVID-19 pandemic are expected to recover, but the sales recovery in the distribution business will be delayed.

In the Housing and Construction Business, we expect the custom-built detached housing, renovation, and real estate brokerage businesses to recover owing primarily to our online sales activities and the development of a telecommuting environment. Net sales will be up due to the inclusion of Cohnan Kensetsu in the scope of consolidation, but recurring income will be down slightly due to an increase in labor costs and system-related expenses.

In the Overseas Housing and Real Estate Business, we expect group companies in the detached housing businesses in the United States and Australia to perform well as they focus on quickly starting construction on the sizable backlog of orders received in the fiscal year ended December 2020. In the past, we had limited our business to areas where hiring and populations were expected to grow and developed our detached housing business in 11 states, including Washington, Utah, Texas, and North Carolina. Most recently, we have expanded our business area to include 14 states, entering the markets in Georgia and Alabama in December of last year and in Colorado in February of this year. This year, we plan to sell 11,000 houses in the United States.

In the Environment and Resources Business, we expect revenues to increase but earnings to decrease. This is because while net sales of the reforestation operating company in Indonesia, which was made a consolidated subsidiary in the fiscal year ended December 2020, and equity in the earnings of the biomass power generation business in Kanda-machi, Fukuoka, which will be commissioned in July 2021, will contribute to results, the existing biomass power generation business is expected to see a decline in earnings compared to the fiscal year ended March 2020 due to the measures to address dramatic changes coming to an end.

We expect earnings to increase in other businesses owing to improved profitability of the elderly care business and a decrease in amortization of goodwill at equity-method affiliate Kumagai Gumi.

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The forecasts for orders received and sales in the domestic housing business

The comparison is with January to December 2020.

We have incorporated a slight year-on-year decrease of 4.2% in the number of orders received for custom-built detached houses. We will focus on sales activities in a peri- and post-COVID-19 environment through development of MYHOME PARK, which allows customers to experience home building online, promotion of online business talks, and design capabilities that address new

lifestyles.
We expect the number of custom-built detached houses completed to increase 2.4% compared to the same period of the previous year.

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The forecasts for the Renovation Business

We expect the amount of orders received and the number of units completed to both recover from the struggles of the previous year caused by COVID-19 and forecast year-on-year increases of 24.4% and 12.8%, respectively. The renovation business got off to a very difficult start due to the declaration of a state of emergency in January, but we aim to achieve the targets of the plan by focusing on increasing orders received for large-scale properties via an increase in the number of engineering personnel and on improving relationships with owners of Sumitomo Forestry homes.

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The forecasts for the Overseas Housing and Real Estate Business

The comparison here is with the fiscal year ended March 2020. We expect a substantial increase in earnings owing primarily to increased earnings in the US housing business and a decrease in goodwill.

On page 18, you will see the performance and number of units sold over three years at five housing companies in the United States, three housing companies in Australia, and Crescent Communities, which is engaged in the real estate development business.
In regard to the number of units sold in the housing business, we expect a 21.6% year-on-year increase in the United States to 11,000 units and a 28.6% year-on-year increase in Australia to 3,550 units, both of which exceed the targets of the Medium-Term Management Plan. As for recurring income, we expect it to be about the same as the previous year in the United States and higher than the previous year in Australia.
Crescent Communities, which runs a real estate development business, posted a recurring loss in the fiscal year ended December 2020, but this was due to sales of some properties being postponed until 2021 in part as a result of COVID-19, so this year we expect it to be in the black.

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The forecast for the capital expenditures

The plan for this year is 33.0 billion yen. The main breakdown is as you see here. Constant investments such as profit-earning real estate development in the United States, display centers and equipment and machinery for the manufacturing business account for most of it, but we will make careful decisions on projects that are in the planning stage as well.

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The trends in profit and loss and various indicators

Net sales and recurring income were both down in the fiscal year ended December 2020 due to the fact that it was a nine-month period. As already explained, however, in the fiscal year ending December 2021, we expect both revenues and earnings to increase compared to the fiscal year ended March 2020, which was pre-COVID-19.
ROE excluding actuarial difference was down due to the shortened period, but in the fiscal year ending December 2021, we expect it to come in significantly higher than in the fiscal year ended March 2020 at 12.4%.
We will continue to focus on improving profitability while striking a balance between improving ROE and enhancing shareholders' equity.

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This concludes the briefing. Thank you.