Sekisui House, Ltd.

Transcript for Earnings Results Briefing for FY2023
(WEB Conference)

Date	:	Thursday, March 7, 2024, 5:00 p.m. to 6:00 p.m. (JST)	
Participants	:	Yosuke Horiuchi	Vice Chairman, Representative Director of the Board, Executive Officer
		Toru Ishii	Director of the Board, Senior Managing Officer
		Hiroyuki Kawabata	Operating Officer, Head of Investor Relations Department

<Presentation Summary>

Note: The following generally omits the details of the financial results presented in the "Summary of Consolidated Financial Results".

[Page 2] Results Overview

Record highs were achieved for sales and operating profit in the first year of the Sixth Medium-Term Plan. Despite lower sales and profit, Overseas Business achieved profit as planned owing to the recovery of the Homebuilding Business and Master-planned community Business in the United States. With this increase in profits, dividend per share increased by ¥5 from the initial plan to ¥123, achieving the 12th consecutive year of increase.

Net sales increased by 6.1% year on year to ¥3,107.2 billion. Profit in the Overseas Business decreased by ¥10 billion due to a decline of business in the United States and the impact of termination of business in China. Despite this, the increases of profit by ¥19.7 billion in the Built-to-Order Business, ¥37.3 billion in the Supplied Housing Business, and ¥126.6 billion in the Development Business, as well as housing business and property sales in Japan contributed to the overall increase in profit.

Gross profit increased by 6.8% to ¥623.7 billion. Gross profit margin improved by 0.2p to 20.1%. Despite the impact of the sharp rise in the price of raw materials, the Built-to-Order Business remained steady from the price pass-through effect in 2022, and the increase in profit in the Development Business contributed to the improvement.

SG&A expenses increased by 9.3% to ¥352.7 billion. The increase was partly due to increase of ¥10.7 billion from newly consolidated overseas subsidiaries Chesmar and Hubble as well as the increase in personnel expense in Japan. The SG&A ratio increased by 0.4% to 11.4%.

Operating profit increased by 3.6% to ¥270.9 billion. Operating profit margin was 8.7%.

Non-operating income/expenses increased by ¥1.5 billion to a loss of ¥2.7 billion. Foreign exchange gain/loss increased by ¥5 billion to ¥4.2 billion. Interest costs increased by ¥7 billion to ¥12.3 billion. Equity in earnings/losses of affiliates increased by ¥3.9 billion year on year to ¥1.9 billion with the sale of shares of the hotel in the Fukuoka Daimyo Garden City. As a result, ordinary income increased by 4.3% year on year to ¥268.2 billion.

Extraordinary income was ¥26.6 billion. This was due to gains from the sale of commercial facility in Singapore, as well as profit from the liquidation of condominium projects in Taicang and Shenyang in China during the fourth quarter.

Extraordinary losses of ¥4 billion from business liquidation loss was related to the termination of transport system Sky Rail in Hiroshima City.

Profit attributable to owners of parent increased by 9.6% to ¥202.3 billion. EPS increased by ¥32.71 to ¥309.29.

[Page 4] Current Year Results and Compared to Plan

Built-to-Order Business was slightly short of meeting the initial plan but Supplied Housing Business showed a steady growth. Sales of residential land and properties progressed better than planned. Although the Overseas Business was impacted negatively due to the downturn from goodwill which arose from the acquisition of Chesmar and worsening of sales conditions for Multifamily projects, profit was achieved due to recovery of the Homebuilding and Master-planned Community Businesses that exceeded expectations.

[Page 6] Financial Position

Total assets increased by ¥345.2 billion from the end of the previous fiscal year.

Current assets increased by ¥403 billion. Of current assets, cash and deposits fell by ¥39.7 billion. Real estate for sale increased by ¥428.4 billion. Domestic real estate rose by ¥144.6 billion following active purchases by Sekisui House real estate companies, while the ongoing construction of multifamily business in the United States boosted overseas real estate for sale by ¥283.8 billion, including ¥71.4 billion in foreign exchange gains. Non-current assets decreased by ¥57.8 billion. The progress of sales of urban redevelopment properties, which were changed to "real estate for sale," and goodwill decreasing by ¥11.5 billion due to allocation of the acquisition cost of Chesmar being determined. Goodwill at the end of the year was ¥17.8 billion.

Total liabilities increased by ¥218.7 billion due to an increase in interest-bearing debt. Interest-bearing debt increased by ¥167.7 billion. D/E ratio increased by 0.07p from the end of the previous year to 0.44x.

Net assets increased by ¥126.5 billion due to factors such as the recording of profit attributable to owners of parent and increase of foreign currency translation adjustment.

Equity ratio decreased by 2.0p to 52.3%.

[Page 7] Cash Flow, Investment Status

Cash flow generated by operating activities decreased by ¥109.7 billion mainly due to actively purchasing real estate for sale. Cash flow generated by investing activities increased by ¥96.2 billion year on year, mainly due to proceeds from the sale of investment securities connected with the sales of a project in Singapore, despite the progress in the acquisition of tangible fixed assets. As such, free cash flows declined by ¥13.4 billion. Cash used for financing activities increased by ¥162.2 billion year on year due to increases of short-term borrowings, etc. Cash and cash equivalents at the end of the year amounted to ¥292.9 billion.

Total investments include capital expenditures of ¥86.7 billion. Of this, investment in rental real estate comprised ¥63.1 billion.

Capital expenditures for FY2024 is ¥100 billion. Of this, ¥65 billion is planned for rental real estate.

[Pages 8, 9] Segment Information (Built-to-Order Business)

The classification of reportable segments has been changed and comparisons and analysis are based on the revised classification.

Net sales in the Built-to-Order Business overall increased by ¥19.7 billion to ¥1,269.8 billion. Operating profit increased by ¥4.2 billion to ¥131.9 billion.

Net sales in the Detached Houses Business declined by 1.1% to ¥471 billion due to an ongoing decrease in the initial order backlog following the decline in orders during the second half of FY2022. Gross profit margin improved by 0.5p to 23.3%. Profit margin improved due to price changes in FY2022 having been mostly completed and because of progress in the sales of high-value-added houses. Operating profit fell by ¥0.4 billion to ¥41 billion. Operating profit margin was 8.7%, remaining at the same level as the previous fiscal year as a result of improvement in the profit margin through continued cost-cutting efforts. Orders received fell by 1.0% to ¥465.6 billion, recovering to the previous year’s level. Despite new housing starts remaining stagnant, there was a strong 10% increase compared to the previous year in January of this year. The order backlog is almost unchanged. Increase in orders for land for sale contributed to the promotion of sales. Orders for the high-price 3rd range buildings with appealing spatial design proposals that utilize sophisticated technology also increased. The unit price per building increased by ¥3.36 million compared to FY2022 to ¥49.55 million.

Net sales in the Rental Housing and Commercial Buildings Business increased by 3.5% to ¥524.1 billion. Gross profit margin decreased by 0.3p to 24.1%. Continuing to make high-added value proposals has successfully led to turning positive in the past three months. Operating profit increased by 4.8% to ¥78 billion and operating margin increased by 0.2p to 14.9%, owing to the increase in sales. Orders remained strong, increasing by 5.7% to ¥550.2 billion. The adoption rate of ZEH for Sha Maison rental housing continues to grow, reaching 76%. Use of generated electricity by residents leads to reduction of utility costs and promotion of ethical thinking. By achieving a high occupancy rate and rent level and focusing on urban areas, the ratio of B-to-B has also increased. In addition to residential buildings, non-residential buildings such as offices, hospitals, and nursing care facilities have also increased. Structures that allow for flexible design and stable price are their strengths. The unit price per building increased by ¥23.82 million compared to FY2022 to ¥165.43 million.

Net sales in the Architectural/Civil Engineering Business increased by ¥7.3 billion to ¥274.6 billion. Operating profit increased by ¥1 billion to ¥12.9 billion. Steady construction progress and greater profitability when receiving orders have contributed to the increase in both sales and profit. This was underpinned by settling of the raise of construction materials costs and price indexation from orders received before the price rise. Orders received increased by ¥42.6 billion to ¥300.3 billion. While there is an increased appetite for capital investment by private companies in reaction to the COVID-19 pandemic, the lack of human resources in the industry as a whole is worsening year by year and leading to a more eased competitive environment. Multiple orders for nearly ¥10 billion properties were received and governmental projects have increased. Orders received increased for both governmental and private sectors due to recovery in the market in the Civil Engineering Business as well.

[Page 10, 11] Results by Segment—Supplied Housing Business

Net sales in the Supplied Housing Business as a whole increased by 4.8% to ¥821.5 billion. Operating profit increased by ¥3.6 billion to ¥73.6 billion.

Net sales in the Rental Housing Management Business increased by 4.8% to ¥646.5 billion. Operating profit increased by ¥2.5 billion to ¥50.1 billion. Operating profit margin improved by 0.1% to 7.8%, continuing a stable growth. Stable supply of rental housing and promoting increase in rents at the time of changing tenants was contributed to the improvement. The number of units under management exceeds 700 thousand with an occupancy rate of 97.7%. Flow of people to urban areas recovered after the COVID-19 pandemic. Although the occupancy rate remained at just a 0.1% decrease compared to the previous year, occupancy rate in regional urban areas is on the decline in the market as a whole.

Net sales in the Remodeling Business increased by 4.8% to ¥174.9 billion. Operating profit margin was 13.4%, remaining at the same level as the previous fiscal year. Remodeling for detached houses and rental housing remained strong in. The strength of this business is its extensive customer base, and its growth drivers are proposal-base remodeling such as "Family Suite Renovation," as well as remodeling proposal at the time of occupant replacement, which is indispensable for the long-term stable management of rental housing.

[Page 12, 13] Results by Segment—Development Business

Net sales in the Development Business overall increased by 31.3% to ¥530.9 billion. Operating profit increased by ¥28.3 billion to ¥64.8 billion.

Net sales in the Real Estate and Brokerage Business increased by 30.5% to ¥288.4 billion. Gross profit margin was 19.2%. Operating profit increased by ¥8.3 billion to ¥25.8 billion. Orders received increased by 33.3% year on year to ¥306.8 billion. This includes land for sales owned by Sekisui House but significant growth is seen in the sales of residential land owned by Sekisui House Real Estate companies. Sales increased by approximately 40% compared to the previous year, contributing greatly to the increase of both sales and profit of the segment. Demand for suburban areas has declined comparatively, indicating a trend of returning to urban areas. We have strengthened the purchase of lands in superior areas including increasing the number of commercial properties handled. Land inventory of the segment as a whole increased by about ¥90 billion from the end of the previous fiscal year.

Net sales in the Condominiums Business increased by 12.7% to ¥109.4 billion. Operating profit increased by 27.4% to ¥17.5 billion. Operating profit margin improved by 1.8p to 16.0% as a result of limiting areas to four major cities in Japan and making progress in the delivery of luxury properties. Completed housing stock decreased by 144 units from the end of the previous fiscal year to 101 units.

Net sales in the Urban Redevelopment Business increased by ¥46.9 billion to ¥133 billion. Operating profit increased by ¥16.3 billion to ¥21.4 billion. This was underpinned by the gain from the sale of shares of the Otemon Tower/ENEOS Building, The Westin Hotel Yokohama, and Hommachi Garden City Terrace. Occupancy rates increased for urban type luxury hotels with the recovery of inbound demand and Net operating income turned positive.

[Page 14] Results by Segment—Overseas Business

Net sales fell by 1.9% to ¥511 billion. Operating profit fell by ¥24.9 billion to ¥48.8 billion. Operating profit margin decreased by 4.6p to 9.6%. As a factor of the decrease in profit, there was a loss of approximately ¥8.5 billion from the impact of the delivery of condominium in Taicang, China in the previous year. Other factors are mainly due to the decrease in profits in the Homebuilding Business in the United States, but profits improved significantly compared to the initial plan. Orders received increased by ¥101.5 billion to ¥520 billion.

[Page 15] Overseas Business—Details by Country

In the United States, net sales increased by ¥24.3 billion to ¥458.8 billion. To break this down, Homebuilding Business, bolstered by earnings of Chesmar and Hubble, the latter of which we acquired this fiscal year, increased by ¥57.1 billion to ¥337.1 billion. Master-planned Community Business decreased sales by ¥1.2 billion to ¥72.9 billion. Multifamily Business decreased by ¥32.2 billion to ¥48.2 billion, as there were only two property sales this fiscal year due to the deterioration of the sales environment, compared to the sale of four properties in the previous fiscal year.

Operating profit fell by ¥20.9 billion to ¥42.4 billion. A closer look at the figures shows a gain of ¥15.5 billion in the Homebuilding Business. Reasons for the increase of ¥1.2 billion compared to ¥14.3 billion in the initial plan were due to increase of ¥7.8 billion from external growth from the acquisition of Hubble and internal growth of existing three builders. On the other hand, there was a downturn of ¥4.6 billion from goodwill which arose from the acquisition of Chesmar and temporary expenses of ¥3.1 billion from the acquisition of MDC, which were not included in the initial plan. There was firm growth in the main business. Master-planned Community Business accounting for ¥20.8 billion. The business showed a steady trend owing to the favorable new housing market, exceeding the plan by ¥10.8 billion. Multifamily Business accounted for ¥6 billion due to postponing of sales. Gross profit margin, excluding the effects of goodwill, is recovering.

Orders increased by ¥118.6 billion year on year to ¥458 billion. With the addition of Chesmar, orders in the Homebuilding Business increased by ¥158 billion year on year to ¥358.6 billion. Although the pace of sales declined due to the persistently high mortgage rates during the second half of the previous year, latent demand for new housing starts is strong with the inventory shortage of pre-owned homes and other factors. As such, favorable sales conditions can be expected in 2024. Order backlog increased by ¥14 billion from the end of the previous year to ¥148.7 billion, with the Homebuilding Business accounting for ¥102.8 billion and the Master-planned Community Business accounting for ¥45.4 billion. Investment balance increased by ¥210.4 billion from the end of the previous fiscal year to ¥1,055.7 billion. Land for sales of 57 SHAWOOD plots in California began in January, with ten contracts already signed and another two being applied, exceeding expectations.

In Australia, net sales decreased by ¥11.2 billion but operating profit increased by ¥6.3 billion to ¥11.5 billion. Profits increased due to delivery of condominiums and sales of development properties as planned, while number of detached houses sold declined due to the increase in mortgage rates. Orders received fell by ¥13.3 billion to ¥61.1 billion. The investment balance increased by ¥62.3 billion to ¥233.9 billion.

In China, net sales fell by ¥23.1 billion to ¥0.7 billion, while operating profit fell by ¥8.6 billion to a loss of ¥1.6 billion. The investment balance is ¥0.6 billion.

In Singapore, extraordinary income of ¥8.2 billion was recorded from the sale of a commercial facility. The investment balance is ¥49.9 billion.

[Page 17] Full-year Plan

In FY2024, net sales increased by 7.6% year on year to ¥3,342 billion. Operating profit is expected to increase by 3.3% to ¥280 billion, an increase of ¥5 billion from at the time of formulating the Mid-term Management Plan. Ordinary profit is expected to be ¥262 billion. Extraordinary income and extraordinary losses are expected to be ¥22 billion by net. Profit attributable to the owners of parent is expected to be ¥203 billion. EPS is expected to be ¥313.30. ROE is expected to be 11.3%. The annual dividend per share is planned to be increased by ¥2 from the previous fiscal year to ¥125, marking a 13th consecutive year of dividend growth.

[Page 18,19] Full-year Plan (Segment Information)

Net sales of the Detached Houses Business is expected to increase by ¥1.9 billion year on year to ¥473 billion. Operating profit is expected to increase by ¥1.4 billion to ¥42.5 billion. Orders received showed 10% increase in January and 5% increase in February year on year. With these recent increase in orders received, an increase in both sales and profit is expected. Material costs are continuing to rise but an increase in profit is expected as profit margin is continuing to improve from more added-value and costs reduction. Orders received are expected to increase by 4% through addressing latent demand for high-price 3rd range products and enhancing lifestyle design proposals. In the Rental Housing and Commercial Buildings Business, sales are expected to increase by 4.9% to ¥550 billion. Operating profit is expected to increase by ¥3.9 billion to ¥82 billion. We expect increases in both sales and profit with the amassing of order backlog and favorable trends in proposals for Sha Maison ZEH and B-to-B. A 5% increase in orders received is expected with the strengthening of proposals for Green First Office which utilize our knowhow in living and spatial design proposals for offices. In the Architectural/Civil Engineering Business, sales are expected to increase by 14% to ¥313 billion. Ongoing improvement of the order profit margin is expected and we expect operating profit to increase by ¥2 billion to

¥15 billion. We plan to focus on acquiring environment related construction orders. For the entire Built-to-Order Business, a 5.2% increase in sales and 5.7% increase in operating profit to ¥139.5 billion are expected.

In the Supplied Housing Business, rental housing management is expected to maintain high occupancy rates and stable growth. Operating profit is expected to increase by ¥2.8 billion to ¥53 billion. We not only plan to enhance services for residents but also reduce costs through DX and other means. Remodeling Business will aim for growth centered on large-scale remodeling such as renovating floor plan with the backdrop of strong customer base, and we expect net sales to increase by 6.0% to ¥185.5 billion, operating profit to increase by ¥1.5 billion to ¥25 billion.

In the Development Business, real estate and brokerage sales are expected to increase by 23.8% to ¥357 billion. Operating profit is expected to increase by ¥5.1 billion to ¥31 billion. In the Condominiums Business, net sales is expected to decline to ¥96.5 billion, but this is as planned in the Mid-Term Management Plan formulated last year. With the sales condition with favorable number of visitors to model homes, we expect to achieve operating profit of ¥11.5 billion. In the Urban Redevelopment Businesses, sales of ¥86 billion and operating income of ¥12.5 billion are expected. Of which property sales are expected to be around ¥55 billion, with a sales profit of ¥16 billion due to favorable investment in Japan from Prime Maison and other properties. We will implement active promotions for “Michi-no-Eki Hotel,” which require time to recover, and strive to increase its publicity.

Total Overseas Business sales are expected to increase by 24.8% to ¥638 billion. Operating profit is expected to increase by ¥7.6 billion to ¥56.5 billion. Master-planned Community Business is expected to align with the initial plan of the previous year. Homebuilding Business is expected to exceed the initial plan. In the Multifamily Business, we plan sales of three properties. For the Homebuilding Business, we have made plans taking into account the estimated recovery of sales from the decrease of goodwill in FY2023, order backlog being 1.5-times compared to the previous year, and condition which pre-owned houses rarely enter the market due to ease of inflation. Revision plan will be released again after the official closing of the acquisition of MDC.

<Summary of Question and Answer Session>

Note: Matters previously described in the financial statements and documents subject to timely disclosure are omitted.

Question

- Can you provide more details about the FY2024 plan for business in the United States?
  Specifically, the status of goodwill and orders received in the Homebuilding Business, expected profit in the Master-planned Community Business, and the time of the sales in the Multifamily Business.
- What is the reason for non-operating income/expenses worsening compared to 2023 in the FY2024 plan?

Answer

- For the Homebuilding Business, goodwill from Chesmar will decrease from FY2023. In terms of current state of orders, number of orders are very favorable and exceeded 400 houses in January, which is an increase of 30% year on year, and nearly 500 houses in February, which is an increase exceeding 30% year on year. For the Master-planned Community Business, favorable trends of sales and participation fees (fees received after contracting land if buildings are sold above the price agreed upon) contributed to its performance in FY2023 but we have not put significant weight on them due to uncertainty. As such, we expect a similar level as the FY2023 plan. This does not mean we are shying away from sales. For the Multifamily Business, sales of three properties are planned but none have been formally contracted at this time.
- For non-operating income/expenses, we expect an increase in interest costs related to completed properties in the Multifamily Business. Furthermore, FY2023 saw foreign exchange gains of ¥4.2 billion and profit from the sales (equity in earnings/losses) of The Ritz-Carlton, Fukuoka, but they are not included in the FY2024 plan and are factors behind the decline in profit. Foreign exchange has been planned at a somewhat conservative US$1 to ¥135.

Question

- What is the current trend of mortgage rates in the homebuilding business in the United States?
- What is the state of acquisition of MDC and revision to the plan?

Answer

- We cannot accurately track the trend of mortgage rates but we have an affiliated financial firm under the Homebuilding Business and promote sales by implementing buydown to reduce rates. Many of those making purchases now are hoping for the rates to be lower several months later when the construction is slated to be completed, which we expect is the reason why the sales are currently favorable.
- MDC's general meeting of shareholders is planned to be held on April 2 (local time) and the process is going smoothly at this point. We will release a revised business forecast at an appropriate time when the

acquisition is completed to explain the profit plan, etc. after the consolidation of MDC.

Question

- Will the recent news on a law firm in the United States advocating that prices for M&A acquisitions were unjustifiably low impact the acquisition of MDC?
- What is the reason for the gross profit margin of domestic rental housing resulting in 24.1%, which is below the FY2023 plan of 24.7%? What is the forecast for the next year?

Answer

- We do not think it would be a notable hurdle for the acquisition of MDC and the process is progressing solemnly.
- Order backlog is amassing favorably, with ratio of orders increasing in S and A areas, especially favorable locations in S areas, which are areas we are focusing on. As characteristics of the area, fire resistance standards are high and the exterior wall and other materials that meet fire resistance standards are increasing. Production of such materials has not caught up and the start of constructions are running behind initial plan. This has caused a decline in the profit margin as fixed costs could not be covered. We plan to resolve this issue in at least one year by making capital investments.

Question

- Is there a possibility of the acquisition of MDC to progress ahead of schedule? If earlier, what would the impact be?
- Can you provide details about profits in the Urban Development Business?

Answer

- Schedule is progressing steadily with the general meeting of shareholders planned to be held on April 2 (local time), and we expect about eight months of performance to be consolidated, which is more than the initial estimate. We will make an announcement when the acquisition is completed.
- The main impact will the profit from sales of Prime Maison properties.

Question

- What are the growth potentials of residential lands owned by Sekisui House Real Estate companies? Can you provide more details on the shift from suburban to urban area?

Answer

- Sales to builders are continuing their favorable trend but we also hear that the pace of sales by builders is slowing down in suburban areas. As such, we are increasing the turnover rate by shifting to urban areas and also handling land for rental housings, warehouses, computation centers, and other use.

Question

- Can you provide more details on the improvement of gross profit margin of detached houses and rental and commercial buildings in Japan?
- What are the characteristics of temporary costs of ¥3.1 billion related to the acquisition of MDC? Is the operating profit of the Homebuilding Business in the FY2024 plan a conservative forecast?

Answer

- We conducted price pass-through of 2% in FY2022, but price negotiations related to the increase in personnel costs of suppliers are ongoing. As we did not conduct price pass-through in FY2023, improvement of profit margin was insufficient. In FY2024, it is unavoidable to conduct price pass-through of around 2.5%. We hope to improve the profit margin by also working to reduce costs internally.
- Temporary costs related to acquisition is costs incurred during research and is included in the costs of the Homebuilding Business. Operating profit in FY2023 was 4.6% and we expect 6.4% in the FY2024 plan, which is an impact of goodwill from Chesmar. When the impact from goodwill and temporary costs are excluded, operating profit would be about 9% for both years.