Q&A at IR Teleconference for Analysts/Institutional Investors (Summary)
at Announcement of Financial Results for FY2019 4Q
(For the fiscal year from April 1, 2019 to March 31, 2020)

Date & time: From 16:00 to 17:00, Thursday, May 14, 2020
Presenters: Takeshi Kosokabe, Executive Vice President and CFO
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【Q1】

Please tell me about your earnings forecast for FY2020. The figures appear to be near bottom-line levels but is this due to you being extremely conservative in your forecast? It would seem that, even amid current conditions, you would be able to sell off logistics facilities and other properties that continue to draw strong market demand in order to generate profits. What are your thoughts on this matter?
(Reference)Financial Highlights: p12 "Business performance forecasts for FY2020(3)"
(Reference)Financial Highlights: p13 "Business performance forecasts for FY2020(4)"

【A】

-Regarding our FY2020 earnings forecast, we have engaged in various evaluations, including whether or not to release forecasts. Believing we should clarify our trajectory to a certain extent, we drafted plans based on the assumption that by the end of 2Q we will see an end to the current state of new infections being reported daily. Our conservative estimate of the impact of the coronavirus(COVID-19) on the current fiscal year is net sales of 830.0 billion yen and operating income of 190.0 billion yen and we hope our earnings forecast will end up being on the conservative side.
For reference, the earnings forecast summary we prepared in February of this year is indicated on P.12 of provided materials as Forecasts excluding the impact of COVID-19.
-As for the sale of development properties, this fiscal year we are planning on net sales of 190.4 billion yen and operating income of 59.0 billion yen, which would represent net sales that are largely unchanged from the previous fiscal year. There are also a few properties available for sale that we have not included in plans at this stage. We will evaluate these properties after a careful review of market changes caused by the impact of the COVID-19.

【Q2】

If, for example, the impact of the COVID-19 is smaller than assumed and conditions turn favorable, will you consider an upward revision of your earnings forecast or increasing shareholder returns?

【A】

-Regardless of the plan, if conditions turn favorable, we will consider an upward revision of earnings.
-There are Group companies struggling with worsening capital conditions due to the temporarily closure of facilities operations, including at hotels, commercial facilities, and sports clubs. We will evaluate shareholder returns based on consideration of those conditions.

【Q3】

There would seem to be strong need for the logistic facilities your company develops but what are your thoughts on selling properties to third-parties outside the Daiwa House REIT?

【A】

-There is a limit to the number of properties that can be acquired by a listed REIT. We are considering private REIT and other methods to ensure transactions that enable us to remain involved in the property after sale.

【Q4】

Excluding the impact of the COVID-19, you are forecasting decreased income of 21.1 billion yen for the current fiscal year. Please explain the factors behind that forecast? Will conditions make it difficult to generate income growth even after the COVID-19 subsides and is the plan for decreased earnings limited to this fiscal year? Please discuss your outlook for the future.
(Reference)Financial Highlights: p12 "Business performance forecasts for FY2020(3)"

【A】

-Regarding the plan outlining a 9.9 billion yen decrease in income from gains on sales of development properties, the income plan on P.12 of the summary calculations does not include a detailed examination of SG&A expenses, and is merely a simple summation of figures reported by each business division and Group company. If not for current conditions, we would have released earnings figures that reflect increased earnings and income.

-However, orders received for the Single-family Houses Business and the Rental Housing Business are sluggish and we are seeing a slight decline in gross margins for construction across each segments. As such, while we cannot be sure whether conditions will continue or not, currently conditions suggest that it will be difficult to achieve the income growth to which we are accustomed.

【Q5】

The Commercial Facilities Business saw a decline in gross margin ratio for construction in FY2019. Please explain the factors behind this and your future forecast.

(Reference)Financial Highlights: p17 “Commercial Facilities Business”

【A】

-The gross margin ratio for construction declined by 0.6pt compared to results through the end of the 3Q. The main reason for this is due to a significant decline in the gross margin ratio for the city hotel business included in this category over the three-month period. Since February, occupancy rates have declined due to the impact of COVID-19. This income decline factor is the impact amount of 2.6 billion yen.

-During FY2020, we forecast the gross margin ratio will decline by 1.8pt. This is mainly due to the forecast that the gross margin for the city hotel business will decrease by 15.0 billion yen. We are not significantly concerned about the cost-of-sales ratio for the Daiwa House construction business (non-consolidated).

-Furthermore, occupancy rates for city hotels are normally around 90% but this fell to approximately 20% in April.

【Q6】

You temporarily suspended work at construction sites in Japan from April 20 to May 10 but will there be an impact on earnings?

Furthermore, what is the impact of the COVID-19 on overseas business? Have there been sites subject to work stoppages? Please also tell me your future forecast.

(Reference)Financial Highlights: Highlight1 “Impact of the COVID-19 epidemic”
(Reference)Financial Highlights: p23 “Overseas business”

【A】

-Due to the short length of the work stoppages at domestic construction sites, we believe the impact on operating income will be minor. However, we are going to pay leave compensation to the workers of those construction sites so we have incorporated extraordinary losses of 4.5 billion yen.

-As for the status of construction sites overseas, although conditions do vary depending on the country, we are estimating the impact of the COVID-19 to be net sales of 78.0 billion yen and operating income of 8.0 billion yen. Thus, our original plan excluding the impact of the COVID-19 is a forecast of 288.0 billion yen in net sales and operating income of 8.0 billion yen. As mentioned previously, please note these are simple calculations. We have heard that Stanley-Martin in the US, which recorded favorable performance last fiscal year, is currently seeing an impact on sales activities. As such, we have also reflected such figures in our forecast.

【Q7】

You indicate that you have incorporated the impact of the COVID-19 in your plans for the Single-Family Houses Business and the Rental Housing Business. As you also have remaining orders received, this seems quite significant as an amount reflecting the impact of construction site work stoppages. In particular, the Rental Housing Business includes sites with long construction periods so one would assume that the impact would be greater next fiscal year rather than during the current fiscal year. Are there many sites for which construction has been halted?

【A】

-Since April, we have engaged in almost no sales activities. Not limited to Single-Family Houses Business, this is the case for all businesses. Current orders received will increase in accordance with the balance of contracts recorded. If this condition continues, we will run out of projects on hand. As such, we have no choice but to plan for reductions.

-The length of construction site work stoppages was 10 days so the amount of the impact will be minor. But some customers under contract are conveying that there is no need to rush to start construction so we can expect some impact.

【Q8】

In FY2019, in November you announced revised plans for operating income of 383.0 billion yen but actual results fell short at 381.1 billion yen. What factors resulted in this difference?

【A】

-Operating income was 1.9 billion yen below revised plans and additionally there were actuarial differences of 2.8 billion yen, meaning that operating income was 4.7 billion yen below revised plans. The impact of the COVID-19 lowered operating income by 6.0 billion yen but if not for that factor we would have achieved forecasts. Net income was impacted by 7.3 billion yen in additional losses attributable to equity in losses of affiliates due to the change in our rate of capitalization in Dalian Daiwa Zhongsheng Real Estate Co., Ltd. from 50% to 83.6%. Additionally, net income was impacted by having recorded 9.7 billion yen in extraordinary losses attributable to impairment losses on Group company goodwill.

【Q9】

Has there been progress with the problems of affiliate company in China?

【A】

The joint venture agreement expired in December of last year. While we have experienced procedural delays due to the impact of the COVID-19, the situation is progressing gradually. We will first conduct an assessment of the property and forecast beginning procedures for property sale before the end of the year. We do not yet have a specific transaction amount but based on our appraisal we do not expect needing to conduct any accounting treatments.

【Q10】

In March 2020 you issued a press release concerning a stock buyback. Please explain how this stock buyback is positioned within your company. Also, is there a possibility you will engage in dynamic stock buybacks in the future?

【A】

-We issued a general press release on the stock buyback on March 13 and currently are in the process of this buyback with acquisition limits set at 10 million shares and 30

billion yen. We believed the stock price to be significantly below what we view as an appropriate price. Although we were engaged in various investments and did not have the capital resources to make additional returns, we decided to engage in this buyback even if it meant using future cashflow.
-At present, cash flow from operating activities is below expectations. As such, we will allocate capital and then carefully evaluate conditions after the COVID-19 situation has subsided. Any future additional stock buybacks will be evaluated based on an assessment of conditions.

【Q11】
You incurred one-time expenditures in FY2019 but can you tell me the amount? Also, can we assume that expenditure will not occur in the future?

【A】
We allocated 15.6 billion yen to two large-scale Fujita projects overseas and in Japan. This is the reason we are planning for an improvement in the gross profit ratio for the Logistics, Business & Corporate Facilities Business. Furthermore, we recorded 9.7 billion yen as goodwill amortization for subsidiaries and 7.3 billion yen as additional losses in Dalian Daiwa Zhongsheng Real Estate Co., Ltd. And while we allocated 1.5 billion yen for off-specification components problems in FY2018, this fiscal year use was limited to a 0.5 billion yen. We forecast restoring the remainder this fiscal year.

【Q12】
You have highlighted the impact of COVID-19 on each business. Among those highlights, for the Rental Housing Business you indicate delays in supplier parts and material shipments. We have heard from other housing manufacturers that plants in China are returning to normal. Is it your opinion that more time will be required for supply chain recovery?

【A】
- COVID-19 started in China so we were concerned about the impact on properties that influence annual reporting. However, we successfully transferred the ownership of properties scheduled to be transferred in March. As such, at present our supply chain has recovered.

【Q13】

Recent news reports indicated that Daiwa House Industry will provide rent relief for rental housing occupants. The report indicated that, of your 500,000 rental housing units in Japan, you will make case-by-case considerations for people struggling with rent payments for up to three month's rent. Do you think conditions requiring rent payment relief due to COVID-19 will continue for some time? Also, with talk of the partial lifting of the emergency declaration on a region-specific basis, do you think the situation will subside? Please tell me what portion of the COVID-19 impact amount reflects plans for rent relief.

【A】

-We have incorporated 6.0 billion yen each as the impact on net sales and operating income caused by COVID-19 in relation to rental housing management. This amount is not due to rent payment forbearance but instead reflects occupancy rate decline risks related to COVID-19, including people vacating units due to lower income and difficulty making rent payments. As for payment forbearance, we are accepting applications through June and at present have received around 900 applications. However, our definition of payment forbearance is the acceptance of installment payments. In other words, we view these as advances to be collected at a later date. As such, there is no impact on our P/L statement.

【Q14】

If the situation recovers, including the partial lifting of the emergency declaration, which domains do you think will recover first? Please also explain your expectations for a recovery in orders received.

【A】

-While we are not sure of the timing, we are certain that the hotel business will recover. A typical operating rate for hotels is roughly 90% but at present we are planning for earnings based on an assumption that hotels will only recover to roughly 50% by the end of FY2020.

-Of the 830.0 billion yen we are forecasting as the impact of the COVID-19, the majority will be the impact on construction. As such, although the recovery period for construction orders received will be critical, at present it is too difficult to forecast the timing of this recovery. Even if the pandemic subsides, consumer sentiment will not quickly return to previous trends. Although we hope for a quick return to a positive consumer sentiment, we think it is too early for such expectations.

-By the way, net sales for orders received during FY2019 were approx 1 trillion yen. We are planning on 1,570.0 billion yen as orders received for Daiwa House (non-consolidated) during FY2020 but of this amount we are only expecting to record 700.0 billion yen in net sales on orders received for the fiscal year. As such, we are focusing on activities to recover orders received.

【Q15】

Can you please provide a summary of extraordinary losses?

(Reference)Financial Highlights: p10 “Business performance forecasts for FY2020(1)”

【A】

- During FY2019, we recorded extraordinary losses of 21.2 billion yen. As a breakdown, this includes items such as overseas subsidiary goodwill impairment losses of 9.7 billion yen, First Cabin (Hotel) investment losses. These are transitional losses.

-During FY2020, we are planning on extraordinary losses of 7.1 billion yen but these include 4.5 billion yen in expenses for COVID-19 countermeasures (leave compensation).

【Q16】

Your plan calls for decreased net sales but increased income for the overseas Single-Family Houses segment during FY2020. Can you please explain why?

(Reference)Financial Highlights: p11 “Business performance forecasts for FY2020(2)”

【A】

We have conducted the market valuation for land acquired during the Rawson acquisition. Amortization for that land was recorded through the previous fiscal year but that is off the books this fiscal year so our operating margin has improved.

【Q17】

Your inventory of completed condominiums has increased and it appears that the per-unit price is dropping. Can you please explain the reasons for this?

(Reference)Financial Highlights: p16 “Condominiums Business”

【A】

-This does not indicate that price reductions have become standard. This is because completed inventory increased and we sold certain units with a long time-to-sale at prices below cost.

-In our sales activities, we respond to inquiries individually but currently we are unable to engage in aggressive sales activities. While we are unable to ascertain market trends in great detail, we are concerned about the possibility of an increase in consumers concerned about income security.

End