Q&A at IR Teleconference for Analysts/Institutional Investors (Summary)
at Announcement of Financial Results for FY2020 1Q
(For the fiscal year from April 1, 2020 to June 30, 2020)

Date & time: From 15:00 to 16:00, Friday, August 7, 2020
Presenters: Takeshi Kosokabe, Executive Vice President and CFO
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【Q1】
Please tell us why you did not revise your business performance forecasts. Despite concern that the COVID 19 will continue to impact hotels and commercial facilities, there appear to be positive elements such as accelerated sales of development properties for logistics facilities and favorable sales of single-family houses in the United States.
(Reference) Financial Highlights: P.10 "Business performance forecasts for FY2020 (1)"
(Reference) Financial Highlights: P.11 "Business performance forecasts for FY2020 (2)"

【A】
-We want to take a closer look to evaluate what level of recovery we see in monthly orders received from July through September.
-Through online marketing and the resumption of face-to-face sales, sales activities have returned to near pre-COVID 19 conditions. Regardless of the number of infected, if current conditions continue, we think orders received will recover. After these evaluations, we are hoping we will be able to announce revised upward full-year plans at the time of the second quarter.

【Q2】
First quarter SG&A expenses decreased by 5.7 billion yen year on year but what is your forecast moving forward?
(Reference) Financial Highlights: P.4 "Summary of Profits (2)"

【A】
-We remain engaged in cost reduction initiatives. Speaking on a non-consolidated basis, 60% of Daiwa House operating expenses are personnel costs but as bonuses represent a large portion of those costs, we want to take a flexible approach that is based on earnings.

-As for business travel expenses and advertising & promotion expenses, actual expenses are significantly below budget due in part to being unable to engage in business travel and promotional activities because of the COVID 19. We plan to continue the shift to remote meetings so we think there is more room for reduce business travel expenses.

【Q3】

Looking at month orders received, is the Single-Family Houses Business in Japan showing signs of recovery?

【A】

-Conditions are not as bad as we were assuming.

-Inquiries regarding houses in housing development projects in the Tokyo suburbs are increasing as young households with dual-working couples seek single-family housing with individual rooms that lend to working from home, even if it means being farther from the city.

【Q4】

Recently, there was a report that you are selling four logistics facilities (55.0 billion yen) to Blackstone Group. Is this already reflected in plans?

(Reference) July 31, 2020 News Release “Concerning Sales Contract and Agreement with Blackstone Group” (Japanese only)

【A】

-We are planning on net sales of 190.4 billion yen from the sale of development properties and the transactions indicated in that release have already been incorporated into plans.

-We are receiving inquiries from companies other than Blackstone Group so there is the possibility that property sales will increase moving forward.

【Q5】

Please tell us about the NOI yield for investment real estate.

The yield for real estate currently being rented has declined significantly, particularly for rental housing and commercial facilities. What are the factors behind this and what is your future outlook?

(Reference) Financial Highlights: P.9 “Breakdown of Investment Real Estate”

【A】

-Of the book value of 20.0 billion yen recorded for rental housing, half is attributable to hotel projects in the rental housing segment. Hotels near Tokyo Disneyland have seen a significant decline in yield due to the COVID19.

-One factor influencing commercial facilities is the fact that we have sold some high-yield properties. Also, yield for large-scale commercial facilities held by the Company declined due to the impact of the COVID 19

【Q6】

The gross margin ratio in the construction category for the Commercial Facilities Business declined by 6.8 points. I believe this includes city hotel operations but what is the impact of hotel operations and what is the gross margin ratio for construction alone? Also, can you tell us the factors behind the decline?

(Reference) Financial Highlights: P.16 “Commercial Facilities Business”

【A】

-One factor behind the 6.8 points decline in the gross margin ratio is the city hotel business. The gross margin ratio for the previous fiscal year was 22.1% but declined significantly this year. On the other hand, the gross margin ratio for construction alone declined by 2.9 points.

-Factors behind the decline in gross margin ratio for construction include the continuation of recent initiatives to increase unit prices. Excluding special orders for large-scale projects involving land and tenants as a set, some projects are competitive bids that result in a higher cost-of-sales ratio. While our response will depend on changes in the overall operating environment, we are evaluating how to maintain balance.

【Q7】

Looking at trends in orders received in the construction category for the Commercial Facilities Business, last year hotels accounted for 20% of orders to contribute to earnings. What are conditions for the current fiscal year and what type of tenants will you target to compensate for the decline in hotels?

【A】

-The ratio of hotels among FY2019 construction orders received was 19%. This ratio was still 17% for FY2020 1Q. However, negotiations were for projects that concluded during the previous fiscal year so we anticipate this ratio will decline.

-As alternative tenants, we are similarly focused on medical and nursing care facilities.

This segment has been impacted by labor shortages, meaning that the segment has been unable to expand despite need in the segment. However, the problem of labor shortages is slowly being resolved so we will continue to focus on this segment.
-We also hear there remains strong demand for drug store openings.
-We are working on large-scale logistics facilities in the Logistics, Business & Corporate Facilities Business. In the Commercial Facilities Business, we will take advantage of our relations with diverse range of tenant companies to develop relatively small-scale logistics facilities and "last mile" facilities. We believe there is room to develop new tenants that involve land deals as well.

【Q8】
Please tell us the impact amount of the COVID19 for the first quarter.

【A】
-The impact amount of the COVID19 cannot be calculated.
-For example, first quarter construction sales were significantly impacted by the orders received balance at the beginning of the fiscal year and while the impact of the COVID19 was minor. Although there was some impact from the 10-day temporary suspension of operations at construction sites, that impact was at a level that could be recovered following the resumption of operations.
-One segment we can say definitely impacted by the COVID19 was the accommodation business. Our subsidiary Daiwa Royal, which operates the Roynet Hotel line of city hotels, recorded Q1 sales of 24.1 billion yen during the previous fiscal year but Q1 sales declined to 15.3 billion yen this fiscal year. Also, although operating income for Q1 of the previous fiscal year was 4.0 billion yen, this term resulted in an operating loss of 2.4 billion yen. Daiwa Resort, which operates resort hotels, recorded sales of 12.5 billion yen for Q1 of the previous fiscal year but sales of 1.1 billion yen for Q1 this fiscal year. Also, despite breaking even for Q1 last fiscal year, Daiwa Resort recorded an operating loss of 2.7 billion yen this term. This segment was most impacted by the COVID19.

【Q9】
It appears that your COVID19 impact amount estimate is based on the assumption of severely restricted operations during Q1 and Q2 followed by gradual recovery from Q3 onward. Can you provide your impression of actual performance during Q1?

【A】

-As expected, the hotels and sports clubs were significantly impacted by the COVID 19.
-Our impression is that construction orders were not as significantly impacted as expected.
-However, the resumption of operations has not resulted in a complete recovery. Ahead of our full-year forecasts, we want to further examine how long it takes to recover.

【Q10】

Do you plan to increase sales of logistics facilities to outside groups? Please tell us how you will divide sales between outside groups and the Daiwa House REIT?

【A】

-As usual, our priority for the sale of development properties is to the Daiwa House REIT. Daiwa House REIT fulfills an important financing function for Daiwa House and is part of our long-term concept for Daiwa House to redevelop deteriorated buildings 30 or 40 years in the future. As such, there is no change in our policy to sell properties to the Group REIT.
-We recently announced revisions to sales plans for the 6th Medium-Term Management Plan increasing sales from 400.0 billion yen to 670.0 billion yen. This indicates the diversification of our transaction partners.
-While currently in the evaluation stage, we executed an agreement with the major investment fund Blackstone Group to serve as a partner capable of identifying potential logistic facility development opportunities in Europe and the United States.

【Q11】

While SG&A expenses are likely subject to seasonal factors and the status of sales activities, can you provide your full-year forecast?
(Reference) Financial Highlights: P.11 "Business performance forecasts for FY2020 (2)"

【A】

-Q1 decreased by 5.7 billion yen year on year but we recorded extraordinary losses of 7.5 billion yen as one-time expenses related to the COVID19. We treated personnel costs and other expenses incurred during the closure of facilities in April and May as extraordinary losses. Of this 7.5 billion yen, 2.3 billion yen were SG&A expenses. As such, this means that the actual decrease in SG&A expenses was 3.4 billion yen.

-Furthermore, our full-year plan for SG&A expenses called for a year-on-year increase of 15.9 billion yen but this includes 8.0 billion yen in natural increases related to the companies newly added to the scope of consolidation. We are implementing initiatives to prevent SG&A expenses from exceeding the previous fiscal year to the extent possible.

【Q12】

Please tell us about Q1 sales and operating income for Stanley-Martin Communities, LLC and Rawson Group Pty., Ltd. Also, it appears that sales are favorable thanks to demand being driven by increased telecommuting in the USA but what factors are influencing the strong demand for single-family houses?

【A】

-Stanley-Martin Communities, LLC (USA)
  Net Sales: ¥29.4 billion (YoY ¥+11.0 billion)
  Operating Income: ¥1.8 billion (YoY ¥+800 million)
-Rawson Group Pty., Ltd. (Australia)
  Net Sales: ¥4.2 billion (YoY ¥-5.6 billion)
  Operating Income: ¥-400 million (YoY ¥-500 million)
-Looking at conditions on the USA housing market, the COVID19 pandemic has led to increased time spent at home so demand for larger, more comfortable houses is increasing.

【Q13】

The debt-equity ratio is increasing. Towards the end of the fiscal year will you advance property sales to reach your goal benchmark of 0.5 times?
(Reference) Financial Highlights: P.8 "Consolidated Balance Sheets(2) Liabilities and Net Assets"

【A】

-I do not think we can achieve 0.5 times by the end of this fiscal year. Q1 debt-equity ratio reached 0.8 times due to the decision to increase capital on hand in light of the COVID 19 pandemic.
-We increased development property sales plans in our 6th Medium-Term Management Plan from 400.0 billion yen to 670.0 billion yen. We think we will get relatively close to 0.5 times by the end of FY2021.

【Q14】

Construction for the Logistics, Business & Corporate Facilities Business appears worse than expected. It seems that Fujita was a factor but it also looks like construction was low for Daiwa House on a non-consolidated basis. Please discuss current conditions.

(Reference) Financial Highlights: P.17 “Logistics, Business& Corporate Facilities Business”

【A】

-Competition is intensifying in segment where we compete with general contractors. The current operating environment is also seeing a decline in project numbers so major general contractors have begun targeting smaller projects. This is taking a toll on margins.

【Q15】

Are there things you can do to convert conditions caused by the COVID19 pandemic into business opportunities? Among existing businesses, are there initiatives that can be linked to social contributions?

【A】

-From June 1, we started sales of products geared towards telecommuting to reflect changes in living conditions. We originally sold these products with soundproofing specifications as “homes where you can play instruments”. We converted this sales strategy to promote these products as home with soundproofing that provide a reliable environment for telecommuting and video conferencing. We executed over 50 contracts in the first month since the start of sales.

-Since last November, we have been selling products through a website called Lifegenic. At the beginning of sales, website access was around 30,000 hits per month but following the COVID 19 flare-up in March and May, access increased to over 200,000 visits per month and is leading to sales. We see this environment as an opportunity to change our sales methods.

-Generally speaking, there is no change in our approach to business as a Group that co-creates value for individuals, communities, and people's lifestyles. We will continue to conduct business focused on contributing to society by engaging in effective land use and urban development. We will continue to value long-term relationships with customers through our Liveness Business and will continue to develop properties on the strong logistics facilities market as we remain committed to initiatives that take advantage of opportunities even as the COVID 19 continues to impact our environment.

【Q16】

One change in society will be changes in communications technology. This is likely to create increased demand for data centers but how is Daiwa House engaged in this sector?

【A】

-We also see that data center demand is rising. We are receiving inquiries and are already engaged in development.

【Q17】

Please tell us about the current environment for orders received for the Single-Family Houses Business and the Rental Housing Business.

【A】

-We were concerned due to the inability to engage in order receipt activities in April and May. However, once we resumed activities, we saw that the impact of the COVID 19 was smaller than expected. In fact, we are beginning to see opportunities for new business in the form of proposals for new styles of housing.

【Q18】

The gross margin ratio for construction in the Rental Housing Business improved by 1.0 points but can you tell us the factors behind this improvement?

(Reference) Financial Highlights: P.14 "Rental Housing Business"

【A】

This is due to some very profitable medium-to-high-rise properties. Low-rise pre-fabricated housing saw an increase in the indirect cost ratio due to lower net sales, resulting in a gross margin ratio was 2.1 point decline year on year.

End