

Sekisui House, Ltd.

Transcript for Question and Answer Session of the Management Plan Briefing for the Second Quarter of FY2019

Date: September 6th, 2019, Friday 13:30 – 15:00 JPT

Participants: Yoshihiro Nakai, President and Representative Director
Toru Ishii, Managing Officer and Chief Manager of Overseas Department
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< Summary of Question and Answer Session >

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

Question

- What is the background of the sharp rise in orders received in China? Please tell us about the future outlook for the business as well as the possibility of reinvestments there going forward.
- With regard to the continuity of the repurchase of your own shares, do you intend to announce a new shareholder return policy in the next mid-term management plan?

Answer

- The U.S. - China trade issue had a positive impact, facilitating the expansion of domestic demand in China. This demand expansion has led to approvals granted to the sale of our condominiums there. We had been confident that we would be able to achieve good sales if only approvals were given. With approvals granted for the sale of more properties, we were able to increase sales steadily. We have set a goal of selling all properties currently in stock within three years, and we have been moving sales forward accordingly. With contracts concluded for almost half of the properties that are expected to be sold in the next fiscal year, the chances are high that we will accomplish the goal. As for the possibility of reinvestments, we do not have such a plan for the time being. It is difficult to exercise effective management control in China. We will therefore ensure to facilitate collections, and we will use the funds for reinvestments in Japan, the United States or other countries.
- Overall returns including dividends for the current year will exceed 40% by around 7%. During the period of the fourth mid-term management plan, we have been conducting management with an emphasis on enhancing the financial conditions. The goal is within reach. With respect to the fifth mid-term management plan, we intend to make an announcement, highlighting the balanced implementation of growth and financial strategies, in which funds will be allocated not only to the repurchase of our own

shares, but also to other measures with a view to growth investments.

Question

- The U.S. business appears to be a driving force for this fiscal year. Although investor sentiment is improving due to the Fed's interest rate cuts, there is concern about the peaking of the U.S. economy. What are your forecasts for the next fiscal year and beyond? Please tell us your direction based on the situations in the respective countries.
- With respect to the Rental Housing segment, accumulated orders were increasing despite a decline in sales in the first half. Are you confident that such accumulated orders will be posted as sales in the second half as expected? What is the background of the fact that unlike other companies, your company alone recorded an increase in orders received for the Rental Housing, besides the rise in the ratio of three- and four-story houses?

Answer

- In the United States, the multifamily business promoted mainly on the West Coast, has contributed significantly to the current fiscal year's results, with sales of six of seven large properties posted as sales in the first half. Taking this into consideration, it can be said that demand for rental housing is stronger than expected on the West Coast. House rents are rising sharply, and low interest rate is another factor. We also feel that the U.S. employment situation is extremely favorable in a range of industries including the IT industry, in particular, and we expect that its economy will grow at this pace. Having said that, we also consider that we need to have a careful response for the upcoming turning point. As for properties with high yield, we consider to hold some of the properties in the fifth mid-term management plan. The Chinese business will also have a very strong outlook in the next fiscal year, based on our assessment. Our business is still sluggish in Australia during this fiscal year. In addition, we started to witness purchase hesitation in August, with the conservative party winning the election and the government announcing measures to support first homeowners starting from next year. Still, we expect that the gap between supply and demand will eventually be reversed and that the policy will contribute to higher sales in the next fiscal year. As for the overall Overseas Business, whose overview will be announced in the fifth mid-term management plan, we forecast that the operating income generated in the four countries will reach a total of ¥35.0 billion this fiscal year. We will work to achieve a minimum of ¥35.0 billion per year over the three-year period starting from 2020.
- It is true that the Rental Housing business is experiencing headwinds due to stricter loan standards for apartments that have been applied in regional areas since last year. Even so, our business has been steady in urban areas thanks to the area marketing strategy. According to our internal materials, the growth ratios of 20% and 10% year on year were recorded in Tokyo and Kanagawa, respectively, while they were lower than the previous year's levels in Chiba, Kitakanto and Sendai. Chubu, Kansai and Chugoku (Hiroshima) showed strong performance, registering growth ratios of 80%, 20% and 60%, respectively. Even today, it appears that urban areas are continuing to show strong performance overall. With respect to accumulated orders, we will ensure that progress is made in construction works. The

risks we should address include construction capabilities in the Built-to-Order Business. Accordingly, progress in construction will lead to the achievement of the target in the Built-to-Order Business.

Question

- Which business models will drive profit growth in the fifth mid-term management plan? Which area has priority in terms of conducting real estate investment, Japan or overseas?
- Please tell us about the progress of platform houses.

Answer

- In terms of the trend of housing construction starts through 2030, it is expected that the number of new housing units constructed will remain at around 800,000 for the next 10 years based on an analysis undertaken by us and some think tanks. This is based on the assumption that despite a policy of shifting from quantity to quality advocated by the government in conjunction with Japanese housing units, there are still many low-quality housing units, and demand for their reconstruction is expected to arise. We believe that our role is very important in promoting the government's policy of facilitating a shift from quantity to quality. For the Custom Detached Houses, Rental Housing and Remodeling segments, we have set the continuation of growth of 5% as an internal goal. In the Real Estate Management Fees segment, we need to accomplish growth that surpasses the increase in the number of housing units under management. The key to accomplish growth that surpasses the rate of an increase in the number of housing units under management is how successfully house rents can be raised, given the fact that the occupancy rate is reaching the upper limit. For the Development Business, the balance between investments and collections is important. If growth targets that are too aggressive are set, the financial balance is not maintained. We will therefore facilitate growth while simultaneously examining such targets along with financial strategies. With respect to investments in the development of real estate, our fundamental policy is to facilitate collections in China while at the same time making investments mainly in the United States. We consider that investments include not only those in real estate but also those in the research and development such as the Platform House concept. Based on this concept, we will work on investments to study the desired role of housing units from the perspective of the Next Sekisui House vision as we celebrate the 60th anniversary since our establishment and move forward to the third phase. We will announce not only real estate-focused investments but also a range of investment models in the fifth mid-term management plan.
- We commenced a joint demonstration experiment on the Platform House with a university and other institutions. To be more specific, we will announce the progress of the demonstration experiment at next year's CES in Las Vegas and other opportunities.

Question

- Regarding the balance between investments and collections, looking at the progress to date, you have been giving priority to collections in the current mid-term management plan. Have you been doing this intentionally, taking the surge in land prices and construction costs into consideration,

or is this just the way the result has turned out? Will you aim for a turnaround in the next mid-term management plan?

- Regarding the concept behind the sale of properties in the multifamily business in the United States during this fiscal year, with regard to the plan for the sale of seven properties, the sale of six properties has been completed, with one property expected to be sold in the second half. In this situation, is there a possibility that you will choose to sell additional property if you receive a serious inquiry?

Answer

- We disclosed the balance between investments and collections in the fourth mid-term management plan for the first time, which we had not disclosed until then. In the fourth mid-term management plan, priority was given to collections because we wanted to rectify the financial imbalance attributable to the emphasis that had been placed on investments for growth. Our plan prioritized on collection based on the idea we wanted to recover from this in the fourth mid-term management plan. We are heading right direction for the destination. If we succeed in this financial strategy in the fourth mid-term management plan, we will announce the fifth mid-term plan to feature a strategy aimed at maintaining the balance between growth strategies and financial strategies.
- We may consider selling an additional property if we receive an unexpectedly favorable inquiry. Basically, though, we will keep it until the next fiscal year rather than making an additional sale in the current fiscal year.
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Question

- Will the repurchase of your own shares continue to be executed along with the elimination of cross-shareholdings as a package going forward? How many cross-shareholdings do you still have, and how many of such cross-shareholdings must be eliminated?

Answer

- During the period of the fourth mid-term management plan, we repurchased our own shares, which totaled ¥4.7 billion last year and ¥10.0 billion in the recent buyback. We executed these purchases in a timely and flexible manner. For the fifth mid-term management plan, we are examining cash flows to decide whether we should emphasize such flexible repurchases or fixed amount-based repurchases. We do not have a policy that limits the repurchase of our own shares to that of those offered by parties with cross-shareholdings. Accordingly, we hope to announce repurchases in a manner that is a little more straightforward and impactful than “flexible.” The number of brands of cross-shareholdings was reduced by three from 48 to 45 in the previous year. We will reduce this number by at least 10 by the end of this fiscal year. We will reduce it further in the next fiscal year.

Question

- In conjunction with *Sekiwa no ki no ie*, the second product brand, were you affected by the

consumption tax hike (a last-minute surge in demand or a reactionary decline)?

- With regard to the Chinese business, we understand that you are doing well in Suzhou and Taicang. Please tell us about the progress in Wuxi and Shenyang.

Answer

- The average selling price with the Sekisui brand is ¥40 million per unit, while that of those with the *Sekiwa no ki no ie* brand is in the range from ¥22 million to ¥24 million, or an average price of ¥23 million yen per unit. Sales in this price range remained free from fluctuations, with no highs or lows in sales attributable to a last-minute surge or reactionary decline. More last-minute surges in demand occurred to mid-range and high-end properties among high income earners.
- Contracts have already been concluded for all units in Wuxi and Shenyang, China, whose sales are planned in the current fiscal year.

Question

- We believe that the Rental Housing business grew to date thanks to the synergy effect of the inheritance tax reduction measures and your rental housing products using materials shipped from your own factories. What other possibilities does the business offer on top of the three applicable areas; namely proposals of rental housing as inheritance tax reduction measures, non-housing properties using materials shipped from our own factories and proposals of rental housing as asset management means?
- Looking at the proposals of rental housing from the perspective of inheritance tax reduction measures alone, demand for inheritance tax reduction measures will potentially increase in line with a rise in the number of people who die, although the rental housing market will continue to shrink in terms of both supply and demand due to a decline in the population. In this situation, is there a possibility that you will propose inheritance tax reduction measures through other measures?

Answer

- Going forward, we will continue to make proposals of rental housing as inheritance tax reduction measures. In addition, we will keep an eye on the possibility of rental housing management as an investment. There are a number of properties that are expected to produce high occupancy rates and high yields if they are offered to good tenants who wish to live in good areas and are managed by Sekiwa Real Estate companies. We consider that proposing rental housing as asset management measures is where we, as an industrial housing company, could advance further. Looking at the non-residential sector, there is demand for the reconstruction of public housing, although we need to make more of an effort to become competitive and make effective advertisements in this sector. A challenge in public housing is how we can break down local authorities' fixed idea that the public housing for a bid should be RC housing. We will work proactively on solutions. In terms of hotels, we will promote the Fairfield series in the Michi-no-Eki project. In addition to the Michi-no-Eki properties, we are receiving a growing number

of inquiries from property owners in the S and A areas of Kyoto, Fukuoka and other areas that attract large numbers of tourists, with respect to inheritance tax reduction measures by way of the construction of rental housing or hotels with simple accommodation facilities. If a location is good, hotels with simple accommodation facilities may produce better yields than rental housing units. We therefore make dual proposals, taking both possibilities into consideration. If a customer chooses a hotel business, we propose the construction of *LDK*-type hotel rooms as a basic risk-hedging step so that they can be remodeled easily for use as rental housing units. If such a case arises, Sekiwa Real Estate companies are able to make another proposal for management. As this shows, by leveraging the β system construction method and the management capabilities of Sekiwa Real Estate companies, we can make proposals from diverse points of view in a number of business areas.

- We are focused on the S and A areas and are able to provide a range of proposals including those on the construction of rental housing and hotel-type properties for customers who own inherited land in these areas. Simply put, it depends on the location. It is very difficult to make proposals to heirs who have acquired inherited properties located in places other than these areas. We have no intention of accommodating such demand.