Toyota Tsusho Corporation
Earnings Briefing for Second Quarter of Fiscal Year Ending March 31, 2023 (FY2022)
Condensed Transcript of Q&A Session

Date & time: Tuesday, November 1, 2022, 11:00-12:15

Attendees: Ichiro Kashitani, President & CEO
Hiroshi Tominaga, CSO
Hideyuki Iwamoto, CFO

Q. You will achieve the target profit of 250 billion yen noted in the mid-term business plan ahead of schedule, but how should we view the company's actual performance value? Also, can you please discuss the medium- to long-term direction?

A. As an overarching trend, in the 2000s and the 2010s, we broadened our business scope in response to the increase in automobile production overseas. In addition, following large M&A deals, including the 2006 merger with Tomen and the 2012 investment in CFAO, we have seen stair-like growth. The result of the merger with Tomen was not only the improvement in earnings immediately after the merger, but also the fact that we expanded our human resources and business domains. Meanwhile, in Africa we are gradually seeing the fruits of the pairing of the North and West Africa regions where CFAO is strong, and the East and South Africa region where we are strong. Also, in the past there were periods in which we had extraordinary losses on the order of tens of billions of yen, but as a result of thorough efforts to avoid unnecessary losses, we now have hardly any such losses. I think that these factors have contributed to our realization of organic growth. I view our actual performance value as being our profit excluding such factors as exchange rates and market prices, and I want to formulate next year's mid-term business plan after taking measure of such factors. With respect to the current mid-term business plan through FY2024, I am certain that we will achieve the target profit sooner than we expected when we initially formulated the plan, as well as sooner than we anticipated last year and the year before that.

To add a bit more context, when we analyze our actual performance value, if we compare FY2019 and FY2022, our operating profit margin has increased from 3.1% to 4.2% due to factors including our wise use of SG&A expenses and changes to our business model. The factors behind our increase in profit include the decline in one-off gains and losses, the impact of the depreciation of the yen, higher metals market prices, higher European electricity prices, and the increase in profit in Africa. Among these factors, we think that market prices of metals other than lithium, as well as European electricity prices, will not continue to boost profit as market prices settle down, and therefore we view our actual performance value as being as around 250 billion yen.

With respect to revising our mid-term business plan, we will make any revisions after closely examining a host of factors, including future business sentiment in China and the United States, exchange rates, metals market prices, and electricity sales prices.

Q. A cap on European electricity prices might be established. How would such a price cap impact your business? Also, it seems that your power generation capacity is rapidly increasing. Can you please discuss the details of that?

A. Our projects are a subsidiary in the Netherlands and entities accounted for using the equity method in both Spain and Italy, but these are primarily engaged in merchant sales so they are impacted by market prices. The situation is different depending on the country, but we do not think that we can continually post profits like we did this fiscal first half. On the other hand, with respect to power generation capacity, projects like the Fukushima-Iwaki wind power project and the power generation project in northern Hokkaido will begin operating in the 2023-25 period, so those projects will result in an increase in power generation capacity.

Q. Can you discuss the changes in the profitability of the Metals Division which contributed significantly to the current profit level of 270 billion yen?

A. The Metals Division's profit increased from 23.1 billion yen in the first half of FY2017 to 55.9 billion yen in the first half of FY2022, an increase of approximately 30 billion yen. The factors behind the increase in profit include the approximately 5-6 billion yen in profit from lithium and rare earth metals, which had almost no profit in FY2017, as well as an additional roughly 10 billion yen in profit from aluminum and scrap metal, despite the price volatility. The progress on the shift to EVs and lighter cars in line with carbon neutrality goals has resulted in deep-rooted demand for aluminum and scrap metal, and we do not think that prices will fall off too much. Profit in the automobile steel business is the same as it was in FY2017, and the number of vehicles produced has not grown, but the earnings structure has changed, and going forward we think that profits in the Metals Division will hold firm.

Q. Please discuss the reasons for the increase in profits in lithium as well as your future outlook.

A. We think that the price of lithium carbonate should be around 10,000 - 15,000 US dollars. On the other hand, the current spot price in China is around the 70,000 US dollar level, and during the fiscal first half it was at a high level, at 40,000 - 50,000 US dollars. Amid the shift to EVs, we do not think this level will fall off considerably. We are aiming for lithium production of 40,000 tons, but we are currently at just under 20,000 tons and will not see growth to our target level immediately, so we want to consider production volume and price assumptions when we formulate a new mid-term business plan.

Q. With respect to lithium market prices, my understanding is that there is a time lag between your long-term contract prices and market prices. Is my understanding correct that your prices will gradually rise going forward?

A. The lithium we handle is on long-term contracts, so the prices are different than the market price. However, many of these are one-year contracts, so we expect prices to increase depending on future market prices.

Q. Please discuss the factors behind the large increase in profit in the Africa Division.

A. Our initial profit target for the Africa Division for FY2022 was 30.0 billion yen, and we are on track to reach that. The GDP growth rate for Africa as a whole is expected to be +3.6% versus the previous year, so the continent is experiencing firm growth. Oil-producing countries are coming back to life due to the rise in crude oil prices, and industry is diversifying in non-oil-producing countries. Accompanying these boom conditions, the middle class seems to be expanding. In automobile sales, the Suzuki brand is performing well based on a precise capturing of the needs of the middle class. We have also been working to build out the value chain, which includes parts sales, after-sales service, sales financing, and other services. Furthermore, we will also steadily advance KD (Knock-Down) production according to the situation in each country. In addition to this, our aggressive implementation of M&A, including the acquisition of dealerships and the acquisition of a major industrial vehicles company, has been driving profits in the automobile field. In the healthcare and pharmacy fields, in addition to the market expanding due to a 3% annual increase in population, our entry into the downstream retail domain as a new challenge contributed to the widening of our scope of business as well as to earnings. We had been struggling in the retail domain, but one factor behind the improvement in profit is the fact that losses have contracted and the path to profitability has come into view.

Q. It was previously understood that areas such as Northwest Africa (Magreb) and South Africa, where there is a middle class which are your customers, were the main areas, but has the potential of Africa as a whole increased?

A. It is difficult to generalize, as there is high volatility in oil-producing countries, but there is solid growth in places other than oil-producing countries. There is firm growth occurring in sub-Saharan countries such as Kenya, Côte d'Ivoire, Cameroon and Senegal. In addition, South Africa is doing well and is providing underlying support.

Q. Your outlook was negative in many areas following your first quarter earnings release, but it seems that the trends with your second quarter results and forecasts have changed. Can you explain why this is the case?

A. At the end of the first quarter, our view was that there would be a downward trend from the second quarter, but this downtrend has not yet actually materialized, and we feel it has been pushed back to the fiscal second half. With respect to the second quarter's results, automobile production did not grow, and there are still some shortages in semiconductors, but automobile sales remained strong, and earnings stayed strong in the second quarter due to other factors as well, including European electricity market prices and lithium prices remaining high, as well as exchange rate effects. However, we do not have an optimistic view on future automobile production and sales, which form the base of our profits. There are concerns about automobile production in the fiscal second half, and although semiconductor prices rose at times during the fiscal first half due to price corrections, we think semiconductor prices will conversely decline in the fiscal second half. Thus, while profit of 270 billion yen seems to imply that we have a bullish outlook, it is actually due to the impact of electricity market prices, lithium market prices, as well as exchange rates.

Q. Will there be an impact from an automobile supply shortage? Even if business sentiment in developed countries deteriorates, the demand in developing countries is strong, so can you send automobiles there from other countries? From a sales standpoint, are you concerned about a deterioration in economic sentiment?

A. Automobiles have certain specifications and they have to be registered, so even if the economic situation worsens in North America, for example, we cannot simply send those automobiles to developing countries where economic conditions are good. With respect to automobile sales going forward, we are concerned that economic sentiment in the U.S. will deteriorate, and this will result in an impact on developing countries, which is our area of strength. Also, there is tremendous EV growth in China, and we are keeping a close eye on the impact of that on sales under our conventional business model. At the current point in time, there have been no impacts on our business in Africa or in other developing countries due to a deterioration in economic sentiment.