Toyota Tsusho Corporation
Earnings Briefing for Fiscal Year Ended March 31, 2018
Condensed Transcript of Q&A Session

Date & time: May 2, 2018 (Wednesday) 14:00–15:00
Attendees: Ichiro Kashitani, President/CEO
Hiroshi Tominaga, Member of the Board/Managing Executive Officer/CSO/CIO
Hideyuki Iwamoto, Member of the Board/Managing Executive Officer/CFO

As the new president, what message would you like to send to the equity market and what do you want to accomplish?

Because our businesses operate largely in emerging market and frontier economies, I would hope the equity market judges our performance over a somewhat longer-term, not short-term, timeframe.

What I want to accomplish is globalization and digitalization. I want the market to thoughtfully assess how well we capitalize on changes in society going forward.

Mr. Kashitani, when you were serving as vice president of CFAO, what did you feel were CFAO's weaknesses? In addition, do you think CFAO will be able to achieve earnings growth in line with market growth?

CFAO has a broad array of individual businesses and many professionals who are highly knowledgeable about products/merchandise and countries/regions. While CFAO has product depth, what I felt it was lacking is cross-organizational coordination. I realized that executives dispatched to CFAO from Japan should coordinate across divisions and build horizontal lines of communication, such as by sharing national/regional economic information with every business unit, while maintaining strong vertical lines of communication.

We believe the African economy bottomed last fiscal year, but the contrast between oil-producing and non-oil-producing countries seems to have become even more pronounced. Until now, CFAO has been functioning exclusively as a distributor for each of its brands. Going forward, we want CFAO to move into production/manufacturing also. We believe Africa will undoubtedly become the world's factory by around 2040. Leveraging our operational and management strengths in the realm of auto production, we intend to build a production/manufacturing platform in Africa ahead of other companies.

What role do you intend to fulfill and how will you add value in the context of the transition to EVs and other such transformative trends?

From the standpoint of reducing vehicle weight, we are currently preparing for changes in materials, namely replacement of steel with aluminum and/or synthetic resins. Specifically, we are identifying suppliers capable of adapting to technological changes, including new material bonding/processing technologies.

We feel a sense of crisis about the reduction in the number of parts per vehicle that will result from the transition to EVs. In addition to a reduced number of parts, the types of parts will presumably also change. We intend to first focus on what types of parts will be needed and then figure how to modify our supply chains.

Additionally, as autonomous vehicles gain prevalence, they will prevent accidents from occurring. Replacement-part trading volumes will consequently decrease, but demand for high-value-added parts, including ones with embedded sensors, will increase. We intend to recognize such changes and broaden our pool of suppliers accordingly.

What areas are you focusing on with respect to your Next Mobility strategy during your current medium-term business plan's term?

The area in which we have quantified our goals in our medium-term business plan is materials related to vehicle weight reduction. In the next-generation services domain, we believe network security will also start contributing to earnings within the near term. Another promising area is battery-related materials, including raw materials such as lithium, which we currently supply.

We are also focusing on changes in how cars are used. Our August 2017 equity investment in Grab Inc. is one example of our focus on this trend. Fleet users also are starting to change their standard approach of leasing and utilizing vehicles. Our Automotive Division is accordingly responding to changes in customers' needs, including financing needs.

I assume that the 140 billion yen that you plan to invest in R&E (Resources & Environment) businesses is mostly earmarked for renewable energy. Is there any possibility of you increasing your R&E investment budget?

Renewable energy is one business in which there are long lags from when we start working on a deal to when funds are actually invested and again to when the deal starts contributing to earnings. Even if we were to line up a new deal now, we would not actually invest in it for several years. The 140 billion yen that we currently plan to invest represents investments in deals dating back several years. We do not expect these deals to start contributing to earnings until several years after we have invested in them.

We plan to continue investing in business expansion while carefully considering how we finance such investments.

What is the earnings outlook for your lithium project in the fiscal years ending March 2019 and 2021?

The lithium project commenced full-scale production from the fourth quarter of the fiscal year just ended. In the fourth quarter, it contributed about 1 billion yen of after-tax profit, including both trading profit and income from our 15% equity stake in the Argentine lithium production business itself. In the current fiscal year, we expect its after-tax profit contribution to increase to around 3-4 billion yen, assuming production of 17,500t, which does not include any expansion.

In the fiscal year ending March 2021, we aim to expand production to 45,000t, but the price of lithium might drop below 10,000 dollars by then, so we are not anticipating much profit growth.

I assume that the composition of your earnings growth over the next three fiscal years through March 2021 will be consistent with that of your 330 billion yen of planned investments over the same timeframe, but do you expect the returns to be commensurate with the amounts invested?

The returns are basically commensurate with the investments, but we expect renewable energy investments in the R&E domain to take a bit longer to start contributing to earnings.

How is NEXTY Electronics faring one year after its launch?

It has performed better than we expected, largely by virtue of robust automotive electronics demand. We expect this trend to continue in the current fiscal year.

To what extent are you currently starting to realize synergies from your relationships with automakers such as Suzuki and Mazda?

In the Global Parts & Logistics Division, these relationships are starting to contribute to earnings, mainly earnings from parts sales and tire-mounting operations related to Subaru and Mazda. Other divisions, including Metals, Automotive, Chemicals & Electronics and Africa, also are starting to see earnings contributions, mainly in businesses related to auto production. The total earnings contribution amounted to several billion yen in the fiscal year just ended.

CFAO sold several thousand Suzuki vehicles across 22 countries last fiscal year. It also sold around 1,000 Subaru vehicles in South Africa and neighboring countries.

What is the breakdown of earnings growth in the fiscal year just ended and in your forecast for the current fiscal year and what level of auto production are you assuming?

In the fiscal year just ended, the Metals Division's results included a one-time loss. Excluding this loss, the Metals Division's earnings were roughly flat, with yen appreciation negating the benefit of the U.S. tax cut. The Global Parts & Logistics Division's earnings were adversely affected by yen appreciation. The Automotive Division's results for the fiscal year just ended included a one-time loss. We expect the auto market to improve a bit, though the stronger yen will weigh on the Automotive Division's earnings. The Machinery, Energy & Project Division's results for the fiscal year just ended included a gain on the sale of a natural gas project. Our current-fiscal-year forecast for the Machinery, Energy & Projects Division is somewhat conservative. The Chemicals & Electronics Division's results for the fiscal year just ended included a valuation gain triggered by divestment of equity holdings. Additionally, in the current fiscal year we expect its manufacturing costs to increase as a result of persistently high chemical prices. Overall, however, our forecast for the Chemicals & Electronics Division is a little conservative, assuming that the electronics business continues to perform well. Our current-fiscal-year forecast for the Food & Consumer Services Division reflects its actual earnings power, excluding an impairment loss on non-current assets booked in the fiscal year just ended. The Africa Division incurred a loss in the fiscal year just ended due to an impairment loss on non-current assets. For the current fiscal year, we have set a modest growth target in light of the African market's recovery trend.

Regarding auto production, we have internally formulated a slightly conservative budget. We do not expect model mix to continue improving in the U.S. like last fiscal year. At best, we expect it to be unchanged year on year.

Your liabilities corresponding to non-current assets appear considerably smaller than your net interest-bearing debt of 1 trillion yen. Why do you manage leverage using the net debt/equity ratio?

Although current assets differ from non-current assets, we believe they also entail risk. We do not distinguish between current and non-current assets in managing net interest-bearing debt. We are currently targeting a net debt/equity ratio of 1.0, a level at which we can remain in sound financial condition even when financing 300 billion yen of investment entirely with debt. However, we are not contemplating any further reduction in our net debt/equity ratio.

What can we expect in terms of shareholder returns going forward?

Our basic policy of maintaining a consolidated dividend payout ratio of at least 25% remains unchanged. We have been continually increasing our dividend for some time now. For the current fiscal year, we aim to pay an annual dividend of 100 yen per share by achieving our after-tax profit forecast.