Major questions and answers for the explanatory meeting for business results for the second quarter ended September 30, 2023

Date:	**Thursday October 26, 2023, 16:30-17:30**	
Speaker:	Masafumi Senzaki	President and Executive Officer, COO
	Keiichiro Shiojima	Vice President and Executive Officer, CFO
	Hidehiko Matsui	Vice President and Executive Officer, CMO
	Eiji Fukunishi	Vice President and Executive Officer, President of Spare Parts & Service Business Unit
	Tooru Sugiyama	Executive Officer, Vice President of Mining Business Unit
	Tatsuya Kubo	President of Corporate Brand & Communications Group

※Some excerpts are included in this report.

1. Market Environment and Business Outlook

Q: You said that the business environment is doing well, especially in North America. The North American market is good now, but future market conditions are viewed with skepticism. How do you view the future?

A: Senzaki: In North America, there are two aspects: demand and our unique factor. Regarding demand, housing starts are weak but at a high level, and public investment is strong. For our company, demand is firm, with dealers saying that inventory levels are not sufficient. Mining also shows strength in both North and South America. Given these circumstances, there is room for further growth.

Q: How do you see the impact of the situation in Israel?

A: Shiojima: In the Israeli market, we are doing business through an independent dealer from a regional headquarters company in the Netherlands. Considering the overall volume, the scale of revenue in Israel is small, and the direct impact on our business performance is minimal. On the other hand, we need to consider the impact on the Middle East market as a whole, which is booming due to Turkey’s earthquake reconstruction efforts, as well as on the European market, and the impact on logistics. We will continue to gather information and examine the situation closely.

Q: You said that, in the 1Q, the foreign exchange impact was higher than expected, but the results on a local currency basis were in line with expectations. Please explain how the 2Q results compare to the original plan, separating foreign exchange impact and other factors (net increase). Also, you revised the full-year forecast for adjusted operating income upward by ¥20.0 billion, but please explain the factors that contributed to the upward revision in the 1H and 2H.

A: Shiojima: In the 2Q, there was a large upward revision due to the exchange rate, but, on a local currency basis, revenue was generally in line with expectations. Although revenue in the Americas grew, the risks that were factored in at the beginning of the period became apparent, such as a decline in orders in some regions and some cases in which products did not reach end users due to shipping disruptions. The 1H of the current fiscal year saw a considerable year-on-year increase in income, as we were unable to provide products due to disruptions in the supply chain in the 1Q of the previous year. For the 2H of the fiscal year, since the 2H of the previous year was also strong, we have factored in a slight year-on year increase in revenue and income on a local currency basis. By region, the tide of demand has turned in Europe and Asia, so we have factored in a reasonable amount of risk in the 2H forecast. On the other hand, sales in the Americas are growing, and we plan to recover from the impact of the depressed region through growth in the Americas.

Q: Is the expected drop in demand in Asia temporary due to elections in various countries or are there other factors?

A: Shiojima: A major factor is elections. Indonesia will hold a presidential election in February next year. Also, although we are strong in the forestry and agricultural industries, palm oil prices are weakening a little in the agricultural sector, and users are becoming less willing to buy.

A: Matsui: The impact of the Indonesian election and the political situation in Thailand has been factored into our original demand forecast. Demand in the forestry industry is still strong, and we will continue to win firm orders, but we expect demand in Asia as a whole to decline.

Q: Regarding the factors behind the change in income and loss in the 1H, why was the year-on-year increase in income due to selling prices slowed down to ¥6.8 billion in the 2Q from the ¥8.3 billion in the 1Q? Also, you plan to increase income by ¥19.8 billion in the 2H due to selling prices, and how certain are you of this?

A: Shiojima: Our policy is to increase selling prices throughout the year, and, especially in the 2H of the year, we will launch the ZX-7 series with improved fuel efficiency in North America. The price increase in the 2H of the year will be large because the price increase effect of the new product launch will be effective.
A: Matsui: Demand was strong in the 1Q. In particular, demand grew in Japan, India, and the Middle East. As for Western Europe, we originally expected a decline in housing-related demand due to rising interest rates. North America is very strong. In Europe, dealers' inventories are gradually normalizing, and we expect the market to remain in line with our forecast.

Q: In the full-year forecast, adjusted operating income was revised upward by ¥20.0 billion. In the new full-year forecast of income fluctuation factors, the exchange rate impact has been revised upward by ¥26.3 billion (from -¥19.4 to ¥6.9 billion) from the 1Q forecast, and "sales volume, model mix, & others" has been revised downward by ¥2.9 billion from the 1Q forecast. Please give us a breakdown of the revised forecast.
A: Shiojima: In the annual forecast, the sales volume is up from the previous year and from the July forecast. The downward revisions are for changes in selling prices and unrealized gains on inventories, which are included in "sales volume, model mix, & others." The selling price was revised downward conservatively, from the July forecast to the initial forecast, considering market conditions in Europe and Japan. The revision to unrealized gains on inventories is due to a review of the extent of inventory reductions.

Q: How do you see risks in regions other than the Americas for the full year? Do you see little year-on-year growth in any of the regions in the 2H of the year?
A: Matsui: Demand in Europe is slowing, but in line with our forecast. We expect a -5% year-on-year decrease in the 1H, a -25% year-on-year decrease in the 2H, and a -15% year-on-year decrease for the full year. We will ship to dealers while controlling current inquiries. We expect the same ratio for Asia in both the 1H and 2H. In addition to the impact of the election, coal prices and other factors are weakening, but the forestry industry remains strong. Japan is expected to remain firm, with the same ratio in both the 1H and 2H.
A: Shiojima: Foreign exchange rates have a complex effect on revenue. Looking at the overall trend, the yen is weakening, but, in the southern hemisphere, such as Oceania and Africa, the yen is assumed to be strong, so the figures appear low. In Oceania, we expect revenue to increase by ¥9.1 billion year on year, but the breakdown is a net increase in revenue of ¥15 billion and a decrease of about ¥6 billion in foreign exchange rates. The

same applies to Africa. Growth in North America is certain. Mining sales are also expected to grow in Africa and Oceania. There is a sense of slowdown in Europe and Asia, but we see Asia as transitory. Mining in Asia is strong, and, after the six-month presidential election in Indonesia, demand for general-purpose construction machines will probably pick up.

Q: According to the full-year forecast of income fluctuation factors, "sales volume, model mix, & others" will be a negative factor of ¥6.6 billion in the 2H of the fiscal year. Why do you expect a negative figure for "sales volume, model mix, & others" while revenue is expected to grow?

A: Shiojima: There are two negative factors compared to the forecast announced in July in terms of income fluctuation factors. The first is a decrease in selling price. This was due to a partial reduction in price increase in light of declining demand in Europe and other factors. The second is the other model mix. This is due to a review of unrealized income from inventories, which will be incorporated into next year's income. The current forecast is to increase production volume, including an increase in shipments to the Americas, which will lead to longer lead times and an increase in intermediate inventories. This is the background to the revised inventory forecast.

A: Senzaki: Regarding the FY2023 demand forecast, we have explained that there is a sense of slowdown in Europe and other regions, but we have not changed our forecast since the announcement of the 1Q results, and this is within our expectations. We are aware that inventories are high, and we were aiming to reduce them toward the end of the fiscal year. However, we hope that you understand that this is the result of our careful and appropriate judgment in order to have the necessary inventories in reality.

Q: What is your outlook for ocean freight costs in the FY2023 full-year forecast?

A: Shiojima: The "other model mix" of ¥6.8 billion in the income fluctuation factors includes approximately -¥4.0 billion in logistics costs. This is a reduction in the negative figure from the forecast announced in July.

Q. How do you plan to control the next market adjustment phase?

A: Senzaki: We have completed one-sixth of the current medium-term management plan three years from April this year. We are not satisfied with our performance, although there is a certain amount of response. Inventories can be further reduced. In preparation for major changes in the demand environment, we are already trying to adjust to the demand environment from this fiscal year. As a manufacturer, we would like to advance the sophistication of our supply chain, as shorter lead times will lead to improved performance. At the same time, it is our natural responsibility to promote sales and provide appropriate services and financing.

2. The Americas Business

Q: Revenue in the Americas declined quarter on quarter from the 1Q to the 2Q. How long will the buildup of dealers' inventories continue?

A: Matsui: In the Americas, there were some effects of delay in sales realization due to tight shipments, but demand remains strong and there are no problems with shipping bookings in the 2H of the year. Dealers' sense of inventory shortages will continue throughout this fiscal year. Dealers are saying that they do not have enough inventory. We are supplying products to the Americas in response to reduced demand in Europe.

Q: In the U.S., housing starts declined slightly. When interest rates rise, real estate investment is weak, so there is concern that demand for non-residential construction will fall and North American demand will slow down.

A: Matsui: Infrastructure investment is firm, but we will closely monitor future trends. Current negotiations with regional general rental companies are focused on small models for the next fiscal year, and inquiries are strong.

A: Shiojima: The infrastructure investment policy of the Biden administration, which moved into the implementation phase this year, has led to increased demand. In addition, the policy of attracting state-of-the-art factories to the U.S. through "reshoring" has enriched private investment. We expect this situation to continue for a while. As we continue to develop our own business, we expect shortages in dealers' inventories to continue throughout this fiscal year. Although the rate of increase in sales in the Americas appears to be lower in the 2H of the year than in the 1H, we plan a 15% year-on-year increase in the 2H in sales of our developing own business, including a 25% year-on-year increase in construction machinery sales to approximately ¥70 billion. Mining machinery, on the other hand, has limited supply and has been allocated from the Americas to Australia and Africa, where it received orders earlier. The specialized parts & service business is planning for a slight decrease in the 2H of the year.

3. Market Share

Q. I would like to ask you about your company's market share trends. What was your market share in terms of volume in the 1H? Is there a decline in market share in regions other than North America?

A: Matsui: I will answer regarding the product share of our mainstay hydraulic excavators. In Western Europe, the market share increased steadily due to an adequate supply of products. In North America, the market share is also increasing. Although the competitive environment is tough in Asia, our market share is expanding in the 2Q. A stable market share was maintained in Japan. Overall, the market share is rather expanding.

Q. What factors have contributed to the increase in market share and how do you expect them to continue?

A: Matsui: In wholesale, the European market in particular has recovered from a delay in supplying products to dealers. In Asia, where retail sales are the main channel, we have been able to continuously provide products to our best customers. We recognize that our market share has increased particularly for the forestry industry.

A: Senzaki: In Asia, we have increased our market share and held off Chinese manufacturers as a result of our ongoing approach to the value chain. We are also expanding our dealer network in India with "service support" as the keyword. In Europe, we were able to recover product supply. The company also gained market share with its newest 7 series of hydraulic excavators and wheel loaders. In general, the market share is growing steadily.

4. Dividend Policy

Q: Will you not be releasing a dividend plan from the beginning of the fiscal year? It has been pointed out that you seem to have no confidence in your earnings plan.

A: Shiojima: We would like to determine the annual dividend after seeing the results of the 4Q, when revenues are concentrated. We will take your comments sincerely and consider them in the future.