Kubota Corporation

Result Briefing for the 2nd Quarter of FY2024

August 8, 2024

Event Summary

[Company Name]	Kubota Corporation
[Company ID]	6326-QCODE
[Event Language]	JPN
[Event Type]	Earnings Announcement
[Event Name]	Result Briefing for the 2nd Quarter of FY2024
[Fiscal Period]	FY2024 Q2
[Date]	August 8, 2024
[Number of Pages]	26
[Time]	10:00 – 10:58 (Total: 58 minutes, Presentation: 26 minutes, Q&A: 32 minutes)
[Venue]	Webcast
[Venue Size]	
[Participants]	120
[Number of Speakers]	5

Masato Yoshikawa	Representative Director and Executive Vice President, GM of Planning and Control Headquarters
Shingo Hanada	Director and Senior Managing Executive Officer, GM of Farm and Industrial Machinery Strategy and Operations Headquarters
Hideo Takigawa	Executive Officer, Deputy GM of Planning and Control Headquarters
Wataru Kondo	Executive Officer, GM of Water and Environment Infrastructure Management Headquarters
Issei Matsui	IR Section Manager of Corporate Planning and Control Department

[Analyst Names]*	Kentaro Maekawa	Nomura Securities
	Tomohiko Sano	JPMorgan Securities
	Sho Fukuhara	Jefferies
	Takeru Adachi	Goldman Sachs

*Analysts that SCRIPTS Asia was able to identify from the audio who spoke during Q&A or whose questions were read by moderator/company representatives.

Presentation

Matsui: Now it is the time. We will now hold a briefing on Kubota Corporation's Financial Results for Q2 of FY2024. I am Matsui, IR Section Manager of Corporate Planning and Control Department, and I will serve as today's moderator.

As for today's schedule, Mr. Yoshikawa, GM of Planning and Control Headquarters, will first give an approximately 25-minute presentation on the financial results. This will be followed by approximately 25 minutes of Q&A time. The end time is scheduled for 10:50 AM.

Please note that we have disclosed the materials for today's presentation on our investor website, so if you are attending the meeting by phone, we ask that you also read those materials.

For notes regarding today's explanation, please refer to the disclaimer regarding forward-looking statements in the financial results presentation materials. Please note that recording, videotaping, or communicating the method of participation in this information session to outside parties is not permitted.

I would now like to introduce today's attendees. Mr. Yoshikawa, Representative Director and Executive Vice President, GM of Planning and Control Headquarters.

Yoshikawa: My name is Yoshikawa. Thank you for your cooperation.

Matsui: Mr. Hanada, Director and Senior Managing Executive Officer, GM of Farm and Industrial Machinery Strategy and Operations Headquarters.

Hanada: My name is Hanada. Best regards.

Matsui: Mr. Takigawa, Executive Officer, Deputy GM of Planning and Control Headquarters.

Takigawa: My name is Takigawa. Best regards.

Matsui: Mr. Kondo, Executive Officer, GM of Water and Environment Infrastructure Management Headquarters.

Kondo: My name is Kondo. Thank you for your cooperation.

Matsui: Now, Mr. Yoshikawa, GM of Planning and Control Headquarters, will give an overview of the consolidated financial results for H1 of FY2024.

Yoshikawa: Greetings, I am Mr. Yoshikawa, GM of Planning and Control Headquarters. Thank you for your cooperation.

We will now explain the Q2 2024 results and the annual forecast for 2024.

Financial Summary for FY 2024 2nd Quarter

For Earth, For Life
Kubota

(Unit: billions of yen)		FY 2024 2Q	FY 2023 2Q	Changes	
				Amount	%
Revenue		1,579.6	1,520.0	+59.6	+3.9
	Japan	305.7	315.1	-9.4	-3.0
	Overseas	1,273.9	1,205.0	+68.9	+5.7
Operating profit		13.1% 207.3	12.1% 184.6	+22.8	+12.3
Profit before income taxes		13.7% 216.7	12.6% 191.8	+24.9	+13.0
Profit attributable to owners of the parent		9.5% 150.8	8.5% 128.8	+22.0	+17.1

1USD (JPY)	152	135
1EUR (JPY)	165	146
1THB (JPY)	4.21	3.95

The effect of foreign exchange rate on revenue against LY was +129.0 billion yen.

KUBOTA Corporation (Financial Results for FY 2024 2nd Quarter)

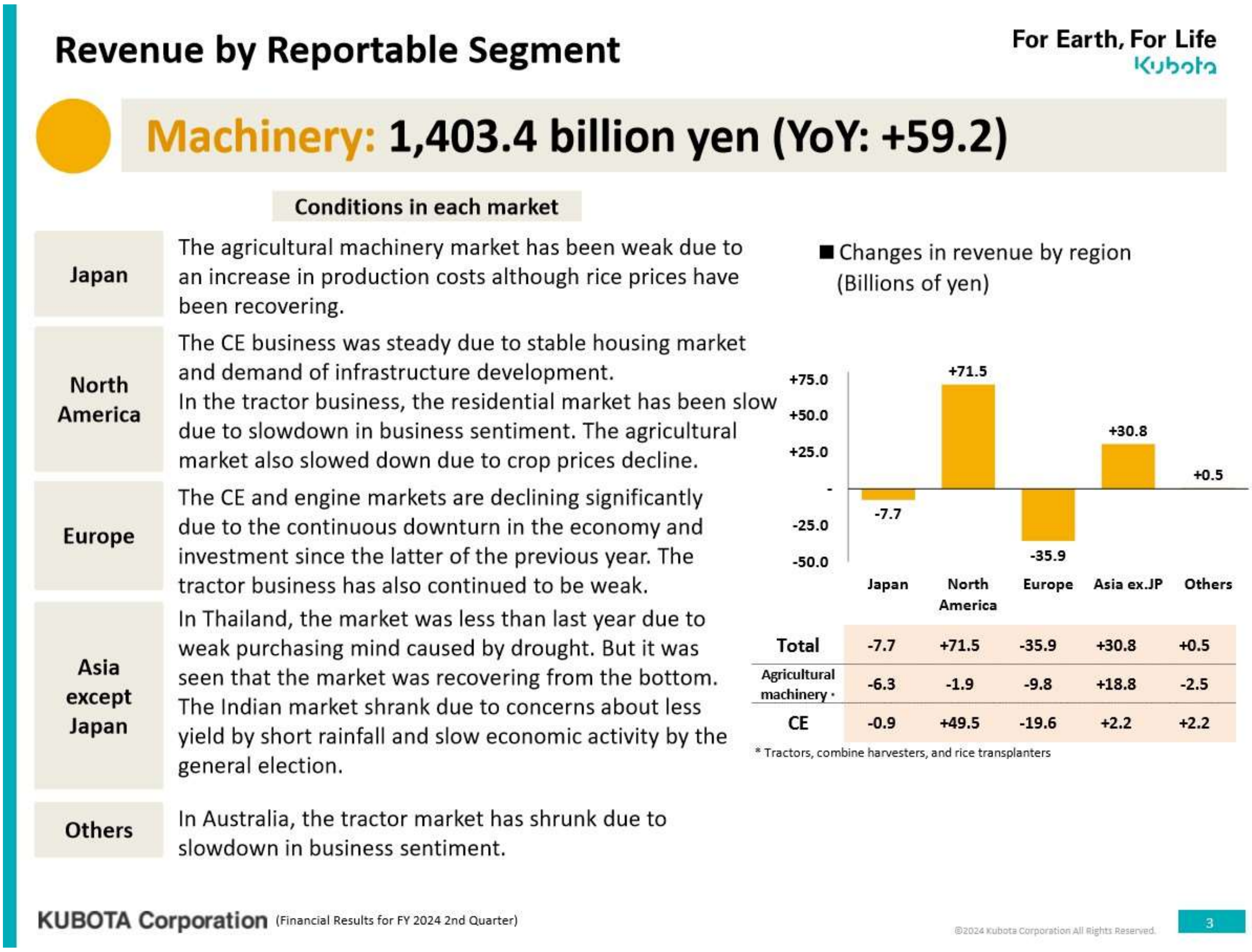
2

See page two of the presentation.

This is a summary of the Q2 results. Net sales increased 3.9% from the previous year to JPY1,579.6 billion, operating income increased 12.3% to JPY207.3 billion, and net income attributable to owners of the parent increased 17.1% to JPY150.8 billion.

Sales and operating income exceeded the initial forecasts by JPY29.6 billion and JPY27.3 billion, respectively. Regarding exchange rates, the yen has depreciated against the major currencies of the US dollar and the euro, as well as against the previous year as a whole, which has been positive.

The increase in overseas sales includes a negative impact of about JPY129 billion from foreign exchange rates, resulting in a real decrease in sales on a local currency basis.



See page three.

We will look at the machinery business by destination. First, Japan. This was a decrease of JPY7.7 billion. In agricultural machinery, although rice prices are on the road to recovery, the market remains weak as it has not been able to cover the rising production costs.

In the construction machinery sector, demand for factory construction and urban redevelopment demand has been slowing slightly due to construction delays. However, I would like to say that things are generally going well.

Next, let's look at the North American market. This was an increase of JPY71.5 billion. The market for construction equipment has remained strong due to stable housing demand as well as government demand for infrastructure development. Mini backhoe shipments have settled down slightly as market inventories have been filled, while shipments of compact track loaders have been strong as market inventories have yet to be filled.

For tractors, the residential market, which is mainly for individuals and homeowners, remained weaker than expected due to the slowdown in business confidence as well as the impact of anticipated demand during the pandemic.

In addition, the high level of market inventories has led to active inventory disposal through incentives, which has intensified competition. In addition, the agricultural market continued to shrink due to declining prices of agricultural products such as wheat and milk.

On the other hand, utility vehicles, which serve both the residential and commercial markets, and mowers are on a recovery trend compared to the previous year due to improved supply conditions.

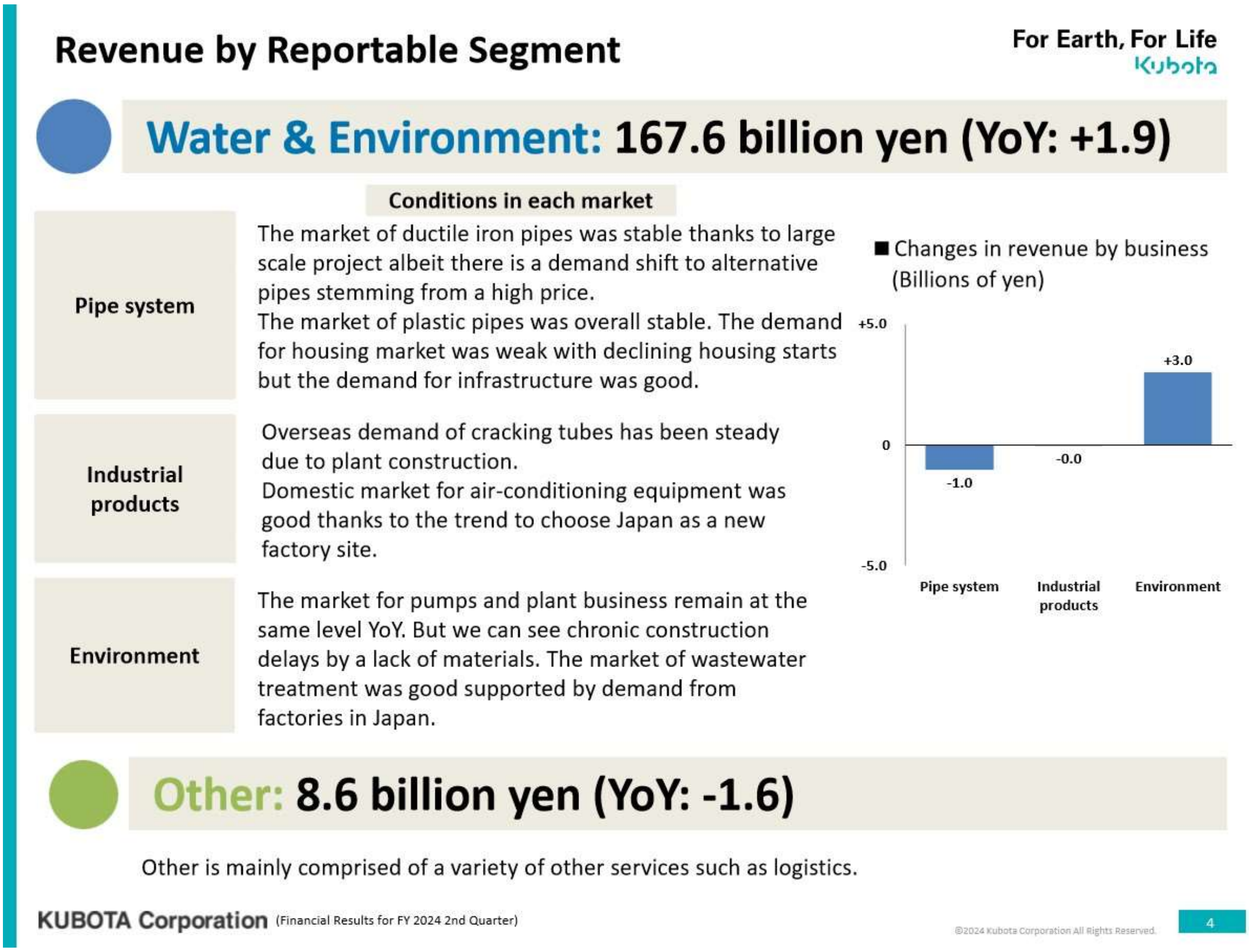
Next, let's look at the European market. This was a JPY35.9 billion decrease. The markets for both construction equipment and engines shrank more significantly than expected due to the slowdown in the housing market and the slowdown in investment caused by the persistently high interest rates. The tractor market continues to be weak due to poor agricultural prices and a slowdown in investment caused by high interest rates.

Next, let's look at the Asian market. Revenues here increased by JPY30.8 billion. In Thailand, farmers continued to be reluctant to buy due to the drought caused by El Niño from the previous year, resulting in a YoY decrease in both rice and field crop production. However, the impact of the drought is easing, and the results are slightly better than expected.

The Indian market is also experiencing water shortages due to the lack of rainfall caused by El Niño. In addition, the general election has caused general economic activity to stagnate, resulting in a larger-than-expected decline in the market.

Next, let's look at the Chinese market. The agricultural machinery market here has entered a slight recovery trend, but the situation is still weak. In addition, the construction equipment market has remained stagnant due to the lack of significant government intervention amidst stagnant private demand.

In other markets, sales increased by JPY0.5 billion. Although the residential market shrank due to the slowdown in business confidence mainly in Australia, sales in yen terms increased slightly due to the depreciation of the yen.



Please continue to page four.

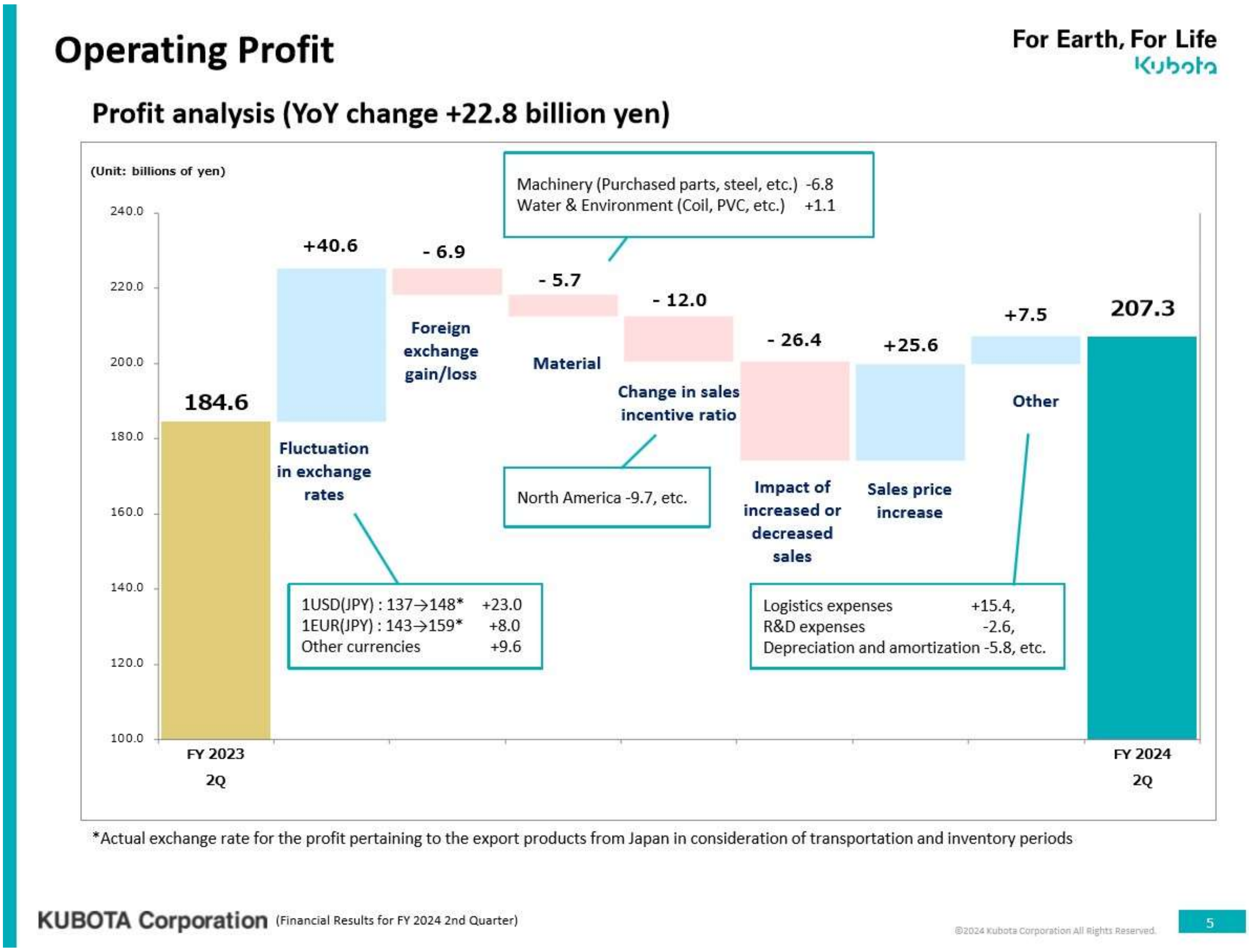
As for the water and environmental business, sales increased by JPY1.9 billion. As for pipe systems, the market for steel pipes has weakened due to a shift to alternative pipes in response to rising prices. However, we expect the business to be firm this fiscal year due to the delivery of a large public works project.

In addition, demand for synthetic pipes for infrastructure-related applications is firm, but housing starts are on a downward trend, and shipments to residential customers have been weak.

On the other hand, in the industrial equipment field, which we used to call raw materials or urban infrastructure, replacement demand for cast steel reaction pipes has been strong. In the air conditioning business, orders for pharmaceuticals and semiconductor plants have been favorable due to the trend of factories returning to Japan in line with the supply chain review.

In the environmental business, the situation for plant pumps is on a par with the previous year, but delays in construction work due to material shortages have become chronic, and deliveries are running behind schedule. Wastewater treatment is linked to the trend of returning to factories as I mentioned earlier, and sales to domestic factories have been strong. The O&M business is also performing well.

As for the other portion, it was JPY8.6 billion, a decrease of JPY1.6 billion.



See page five.

I will explain the contents of operating income. Compared to the previous year, income increased by JPY22.8 billion. The significant depreciation of the yen due to exchange rate fluctuations contributed to an increase of JPY40.6 billion, mainly in the US dollar. Foreign exchange gains/losses were slightly positive due to the weaker yen, but negative effects between foreign currencies were a factor in the JPY6.9 billion decrease in income.

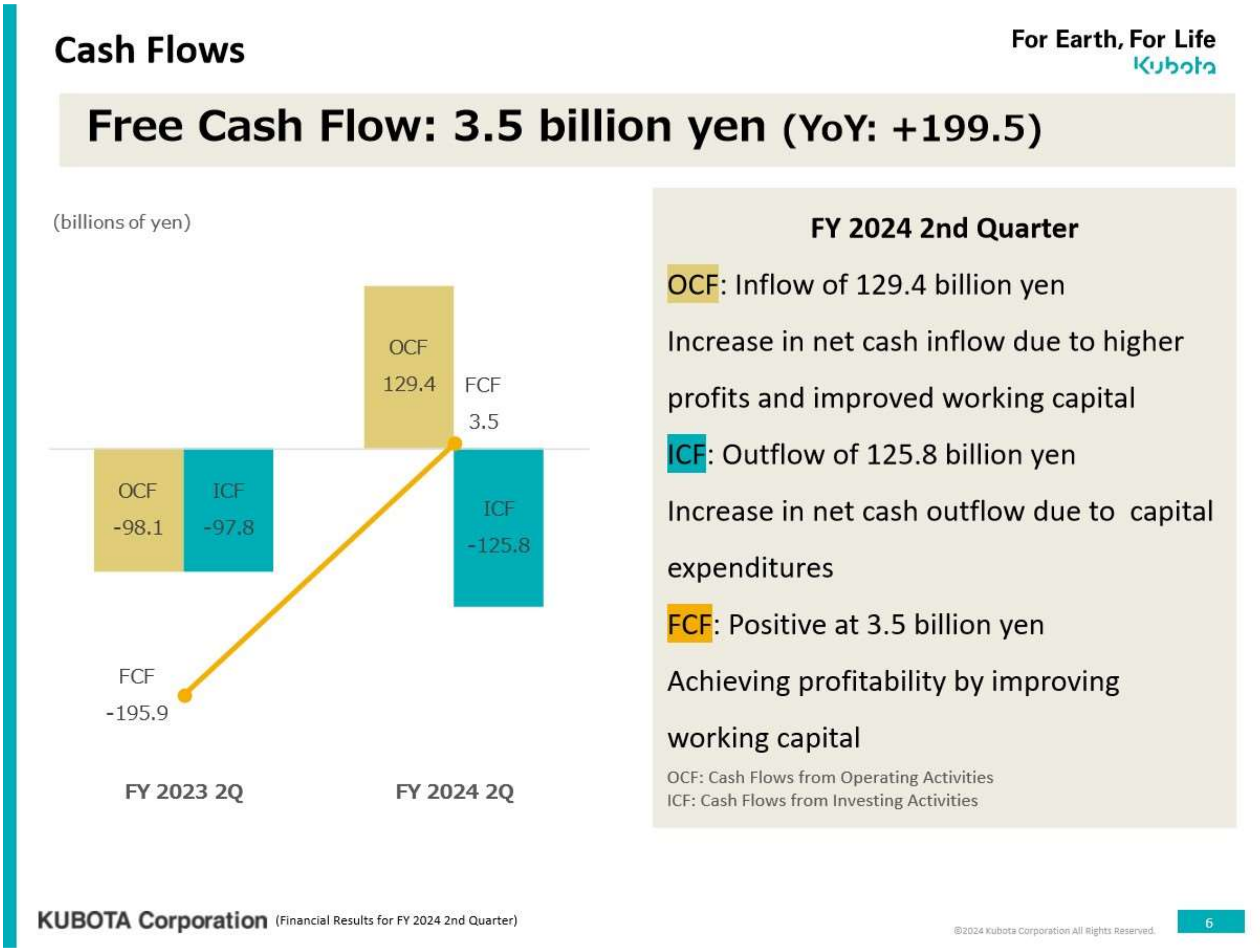
Raw material prices were a negative factor of JPY5.7 billion due to higher prices for purchased parts, steel products, vinyl chloride, and other materials. However, the decrease in profit was smaller than we had expected at the beginning of the fiscal year.

The change in the incentive rate was partly due to the YoY increase in the average interest rate level in the US and partly due to the evaluation of programs to optimize inventory, which contributed to the JPY12 billion decrease.

The increase/decrease in sales was mainly due to a decline in Europe, which was a factor in the JPY26.4 billion decrease in profit. On the other hand, we have been raising product prices and passing on prices, which contributed to an increase of JPY25.6 billion in profit, mainly in North America.

The other factors contributing to an increase of JPY7.5 billion included a decrease of JPY15.4 billion in distribution expenses. On the other hand, R&D expenses increased by JPY2.6 billion, depreciation increased by JPY5.8 billion, and the remainder is the increase or decrease in personnel expenses and fixed costs and their composition. Although labor costs in Japan and overseas have increased more than expected, we have minimized the impact by reducing various aspects of selling and fixed costs.

This represents an increase of JPY27.3 billion over the initial forecast. Although there were some effects of reduced sales, the positive effects of foreign exchange rates, suppression of raw material price hikes, and price increases enabled us to increase profits.



See page six.

It is about cash flow. The cumulative cash flow through Q2 was JPY129.4 billion in operating cash flow and JPY125.8 billion in investing cash flow, resulting in a JPY3.5 billion positive free cash flow, which is a significant improvement over the same period last year.

Operating cash flow improved significantly due to increased profits and the absence of the decrease in accounts payable due to a change in the payment term in the previous year. Other working capital items decreased as sales began to decline on a local currency basis.

Financial receivables are also expected to decline, although the accounts receivable site due to retail finance is longer than normal receivables and the movement is slightly different from accounts receivable. Inventories began to decline in H2 of the previous year due to inventory adjustments.

Investment cash flow increased from the previous year due to increased capital expenditures. This fiscal year, we have positioned the return to positive free cash flow as an important theme, and we have been working to improve our operations.

As of Q2, the Company was in the black, which means that it is achieving its goal early.

Financial Forecast for FY 2024

For Earth, For Life
Kubota

(Unit: billions of yen)	FY 2024 (Forecast)	FY 2023 (Actual)	Changes Amount	Changes %	Previous forecast (Feb. 2024)
Revenue	3,000.0	3,020.7	-20.7	-0.7	3,050.0
Japan	632.0	643.1	-11.1	-1.7	647.0
Overseas	2,368.0	2,377.6	-9.6	-0.4	2,403.0
Operating profit	11.0% 330.0	10.9% 328.8	+1.2	+0.4	10.5% 320.0
Profit before income taxes	11.6% 348.0	11.3% 342.3	+5.7	+1.7	10.9% 333.0
Profit attributable to owners of the parent	7.8% 235.0	7.9% 238.5	-3.5	-1.4	7.4% 226.0

1USD (JPY)	150	141
1EUR (JPY)	161	152
1THB (JPY)	4.12	4.04

The effect of foreign exchange rate on revenue forecast is +135.0 billion yen against LY.

KUBOTA Corporation (Financial Results for FY 2024 2nd Quarter)

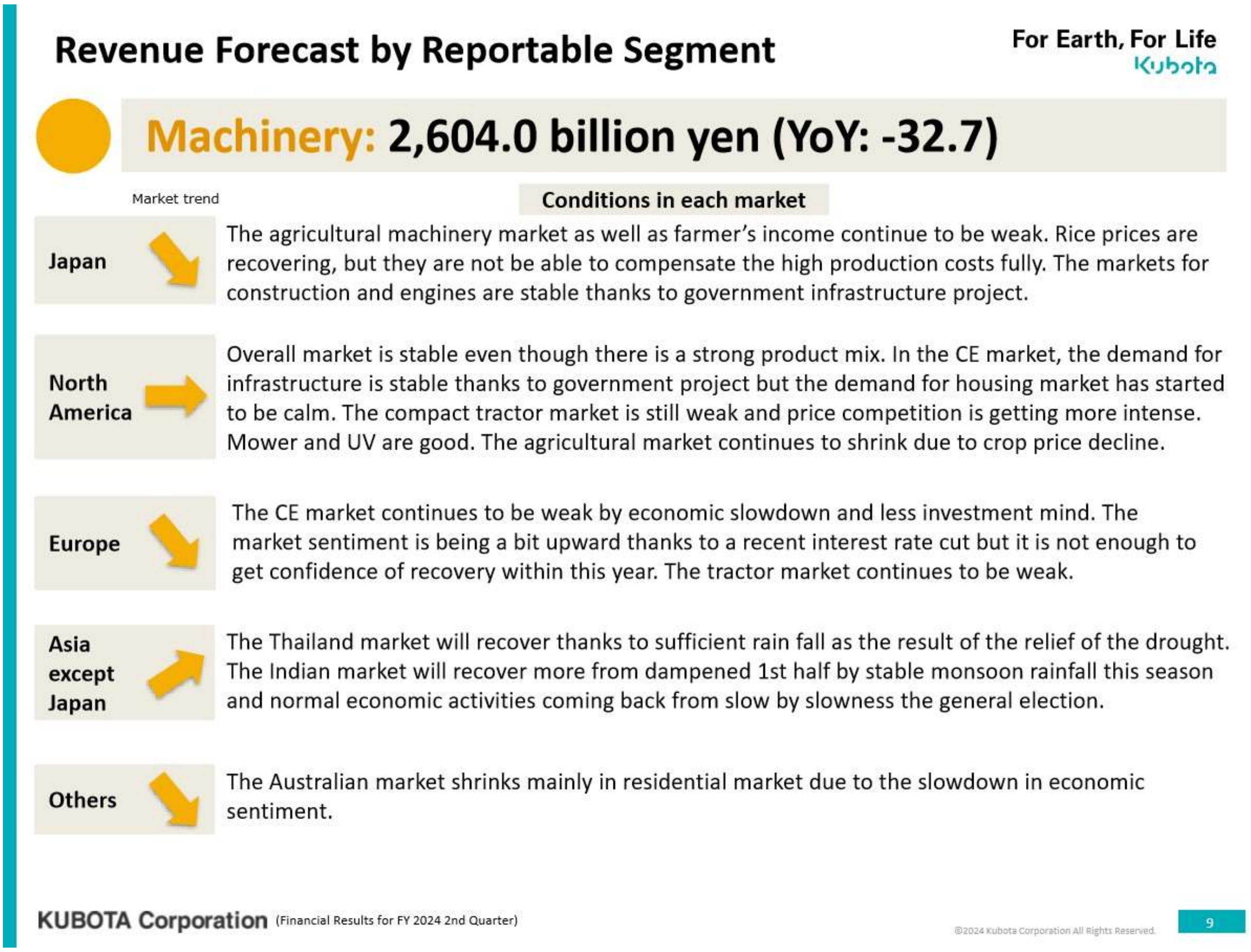
8

I would like to continue with the earnings forecast. See page eight.

Net sales are projected at JPY3 trillion, down JPY20.7 billion from the previous year; operating income is projected at JPY330 billion, up JPY1.2 billion from the previous year; and net income is projected at JPY235 billion, down JPY3.5 billion.

As for the negative net income, there was an increase in profit from the Thai business compared to the previous year, and since this is a joint venture business, the net income was negative while the operating income was positive.

For H2 of the fiscal year, we have assumed exchange rates of JPY148 to the US dollar, JPY158 to the euro, and JPY4.03 to the baht, for an average annual rate of JPY150 to the US dollar, JPY161 to the euro, and JPY4.12 to the baht. The foreign exchange impact on sales was JPY135 billion, which, as in H1 of the year, means a substantial decrease in sales in real terms compared to the previous year.



See page nine.

The machinery business is expected to post sales of JPY2,604 billion, a decrease of JPY32.7 billion from the previous year.

I would like to explain market trends by region. In Japan, rice prices are recovering in the agricultural machinery market, but high production costs such as fertilizers are leading the way, and it is expected to take some time for farmers' profitability to recover in earnest.

In construction machinery and engines, orders for infrastructure construction are firm, and we expect sales to remain steady at the same level as the previous year.

In North America, the situation differs from model to model, and even within the same market, there are variation of colors, but overall, we expect the situation to stabilize.

In the construction equipment market, demand from government infrastructure development remains strong, and housing demand is beginning to settle down, but we expect a slight slowdown in H2 of the year. The most recent US housing starts have been at a level of 1.3 million, slightly lower than last year. Although high interest rates and inflation have pushed housing prices down, the housing shortage has not changed, and we expect the market to recover again as interest rates fall.

In the residential tractor market, the small tractor market continues to be weak, but competition is becoming even tougher in the off-season due to additional incentives offered by competitors.

General-purpose equipment such as mowers and utility vehicles continued to recover moderately. As for the agricultural market, we expect demand to decline as agricultural commodity prices are not expected to recover.

I would like to mention the inventory of dealers in the US, which is meticulously handled on a model-by-model basis. Despite weaker-than-expected market conditions, tractor production adjustments are progressing well, reaching a level of 6.8 months at the end of June 2024.

On the other hand, we have increased inventories of mowers and utility vehicles, which were in short supply in the previous year, and have recovered to a level of five to six months. As for construction equipment, the overall level has returned to an appropriate level at 4.3 months. However, there is still a shortage of compact track loaders, while the number of mini backhoes is slightly high. In light of this situation, we would like to respond to the situation in more detail.

As for the inventory situation outside of North America, tractor inventory levels are slightly high in Europe, but are otherwise at appropriate levels. We will continue to make appropriate production adjustments based on market conditions.

I would like to continue with the European market. We expect both construction equipment and engines to continue to shrink as interest rates remain high and investment remains depressed. Although the interest rate cut in June has raised expectations of some improvement, the impact on the economy during the year is expected to be limited. We expect the market to remain in difficult conditions for the foreseeable future. The agricultural market for tractors is also expected to remain sluggish.

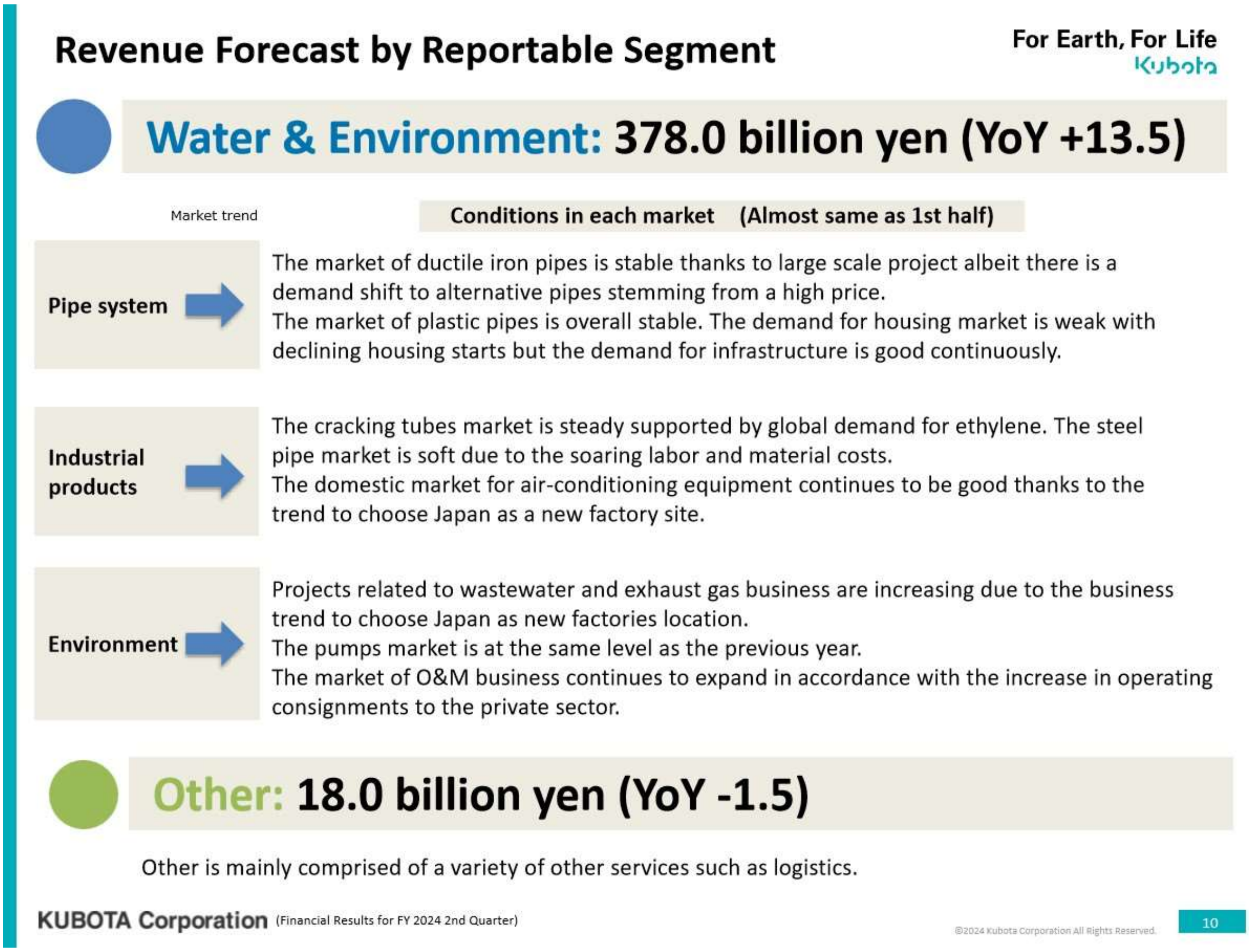
Continuing on, we have Asian relations. As for the Thai market, the drought caused by El Niño has been resolved, and we expect the market to recover in H2 of the year. Rice prices are on the rise, and farmers can now expect to earn more income.

The construction equipment market was slow in H1 of the year due to the delay in the government's budget decision, but in H2 of the year, the recovery of infrastructure work has been proceeding, and the market is expected to pick up.

As for the Indian market, it is expected to recover in H2 of the year, as it has emerged from the lack of rainfall caused by El Niño in H1 of the year and is also recovering from the stagnation of economic activities due to the general election. Although there has been a temporary contraction in the market, the baseline growth story of agricultural machinery due to economic growth and increasing mechanization is expected to remain unchanged.

In the Chinese market, although there has been a gradual recovery from the rush demand due to emission regulations, the recovery is expected to be limited due to the partial reduction of subsidies. Despite the announcement of various government budgets and measures, the construction equipment market has been in a poor state of implementation, and a major recovery is unlikely due to the sluggish real estate market and other factors.

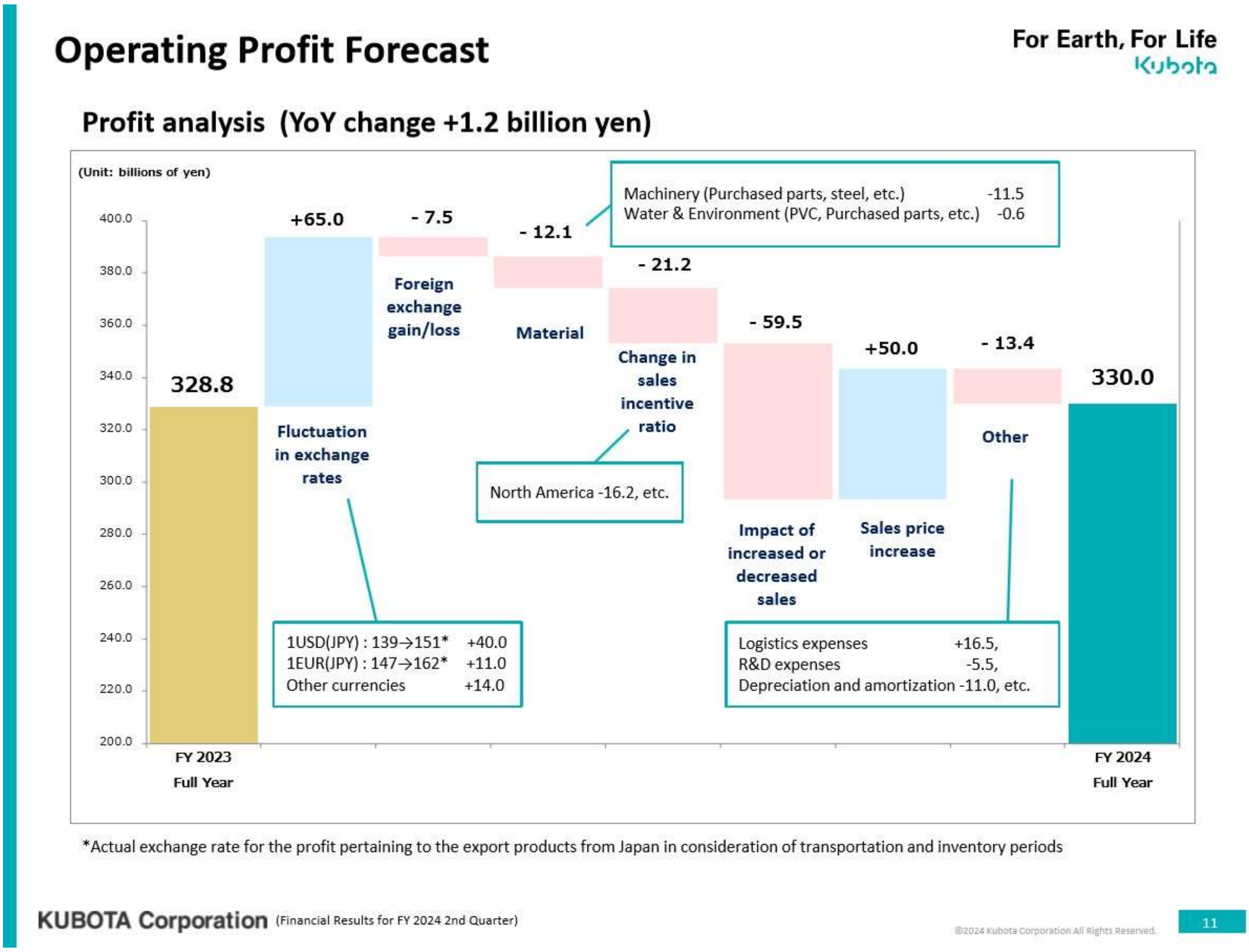
In other regions, the tractor market continues to contract in Australia due to the slowdown of business confidence caused by rising interest rates.



See page 10.

As for the water and environmental business, we are projecting JPY378 billion, an increase of JPY13.5 billion from the previous year.

Overall, the market situation has not changed significantly from Q2 and is expected to remain firm, although there are still delays in the progress of projects due to a shortage of labor at construction sites and delays in the procurement of materials. The other portion is set at JPY18 billion.



See page 11.

I will now explain the increase/decrease in operating income. We assume that the exchange rate fluctuation will be JPY150 to the US dollar for the full year, resulting in an increase effect of JPY65 billion. Foreign exchange gains and losses are expected to have a negative impact of JPY7.5 billion.

Although the price of raw materials is expected to continue to rise for purchased parts in Japan, it is expected to be an improvement from the initial forecast and will be limited to a negative factor of JPY12.1 billion.

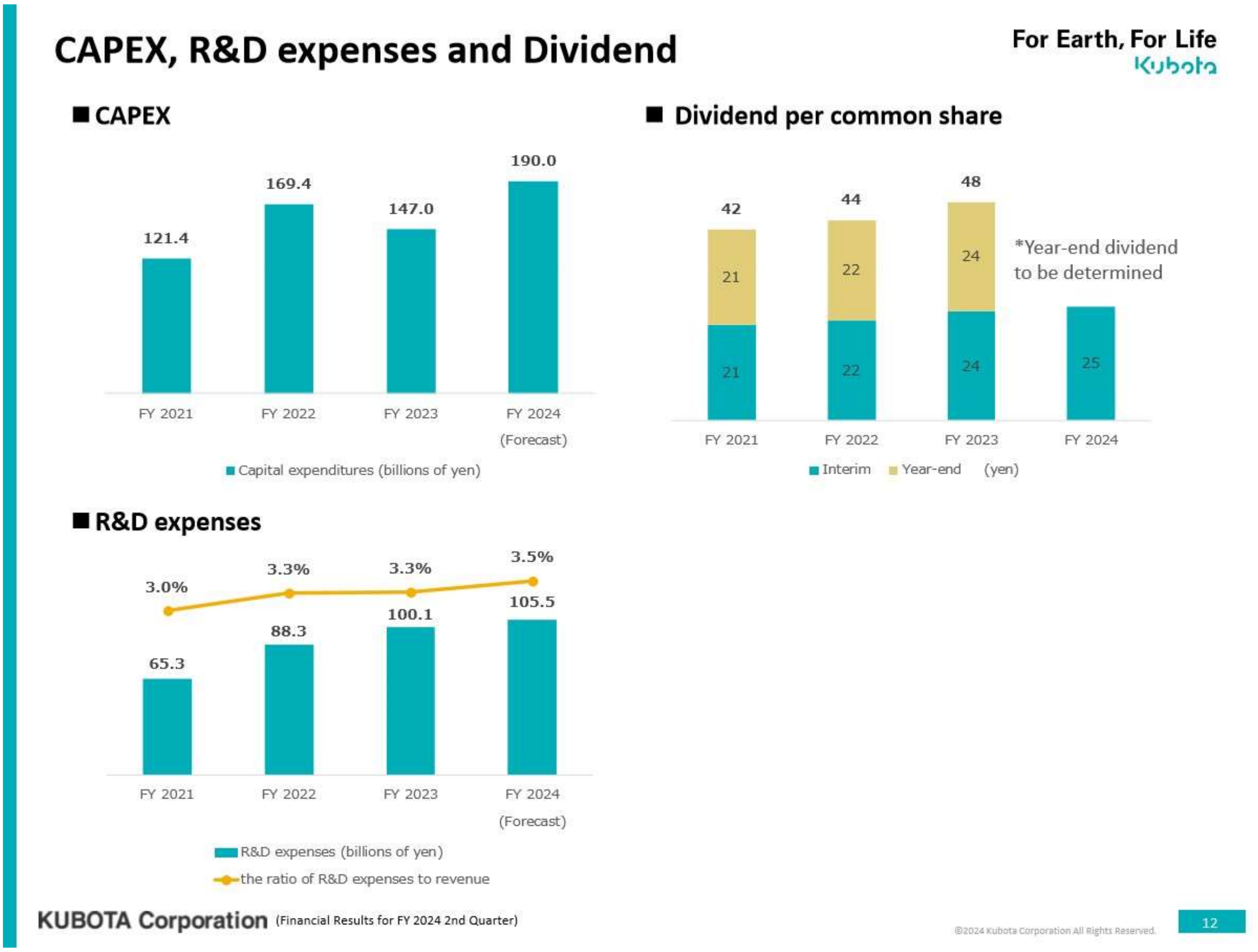
We assume that the change in the incentive rate will be JPY21.2 billion, which is a significant and worsening factor for profit decline.

We have revised our assumptions at the beginning of the period and have not factored in the interest rate cut in the US. On the other hand, we have assumed that this competitive environment will intensify and that the program will be strengthened, so we have made these projections.

The impact of increase/decrease in sales is expected to be a negative factor of JPY59.5 billion. Product price increases are expected to be a factor in the JPY50 billion increase in profit, mainly due to the effect of price increases in North America and Asia.

The remaining JPY13.4 billion of the decrease in income is accounted for as "other," which includes a JPY16.5 billion improvement in distribution expenses and a JPY5.5 billion increase in R&D expenses and cost increases.

The increase in depreciation expenses due to capital investment was about JPY11 billion, and other expenses included selling expenses, fixed costs, and composition differences, resulting in a JPY13.4 billion decrease in profit.



See page 12.

Capital expenditures are expected to be JPY190 billion, unchanged from the assumption at the beginning of the period. Research and development expenses are also unchanged at JPY105.5 billion. Regarding shareholder returns, we increased the interim dividend by JPY1 from the previous year to JPY25.

In addition, as cash flow is improving this fiscal year, we will increase the limit of share buybacks from the current JPY30 billion to JPY50 billion. Based on the policy as stated in the mid-term plan, which is to maintain a total return ratio of 40% and move as close to 50% as possible, we will continue to strengthen shareholder returns.

Page 13.

Finally, I would like to talk about strengthening earning power.

Although H1 of the fiscal year was numerically favorable, the weak yen largely compensated for the loss of sales due to the slowdown in the market, which in reality is not a desirable situation. However, looking ahead to next year, in addition to the uncertainty in the market, the yen has been appreciating due to the recent announcement of an interest rate hike in Japan, and we need to start taking further measures now.

First of all, we will firmly complete the inventory adjustment that is currently underway to optimize production volume and market inventory.

For product lines that were weaker than expected, such as the North American tractor market, we will make additional production adjustments in H2 of the fiscal year so that the adjustments will not be carried over to the next fiscal year.

The other is to strengthen earning power, including cost measures. We have been working to improve profit margins and to pass on the impact of inflation on selling prices appropriately, which is part of our mid-term plan. However, recently we have seen an increase in labor costs and other factors that cannot be absorbed by the measures we have taken so far.

In order to address these issues, we recognize that in addition to immediate measures, we must shift management resources to profitable businesses and products. Each department has already begun to consider specific measures, and we expect to see some of the effects of these measures during this fiscal year.

The next fiscal year will be the year of the finalization of the current mid-term plan. While promoting these measures, such as the introduction of new models of CTL in North America and sales expansion, we intend to build a structure that will enable us to secure a solid profit.

This is an explanation of the consolidated financial results for H1 of 2024 and the outlook for the full year.

We would now like to take your questions. Thank you very much.

Question & Answer

Matsui [M]: Okay, we will now move on to the Q&A session. If you have any questions, please ask.

Moderator [M]: First, Mr. Maekawa from Nomura Securities, please.

Maekawa [Q]: My name is Maekawa from Nomura Securities. Thank you very much for your explanation. Now, please let me ask two points.

I would like to confirm the first point in terms of the view of volume and demand for H2 of this fiscal year. Although the total for the full year has been revised slightly upward, looking at the volume effect alone, I am wondering if the factors that contribute to the YoY decline in profit will be greater in H2 of the year than in H1.

You mentioned about adjusting inventory, and the inventory level for mid-size tractors seems high, and I was wondering if you could add some more information on what factors are being considered in H2 of the year in terms of volume declines, along with your view of demand. Please do so.

Yoshikawa [A]: Now, I, Yoshikawa, would like to answer your question.

First of all, you must understand that our products, especially tractors, are seasonal. Since this summer season, spring through summer, is an important time, it is necessary to take a risk on how much we can sell here, and to ensure that dealers have a certain amount of inventory while making shipments.

When H1 of the year is over and the demand period is over, dealers' inventories are adjusted accordingly, i.e., production is reduced or increased, and shipments are increased or reduced.

To be honest, as I mentioned earlier, retail sales of residential tractors in North America and construction equipment and tractors in Europe have been weaker than expected. Therefore, we are making production adjustments mainly in these areas in H2 of the fiscal year. Looking at the YoY figures for Europe and North America, we have factored in a considerable decrease in shipments on a volume basis in H2 of this fiscal year.

Conversely, as I mentioned earlier, there are uncertainties for next year, but we want to keep dealer and distributor inventories as low as possible this year so that we can increase sales next year if the market does not hit a double-dip or triple-dip bottom. We have factored in a decrease in sales for H2 of this fiscal year.

Maekawa [Q]: Thank you very much. I understand very well.

What is your outlook for construction equipment in North America in H2 of the year? I wonder if the dealer inventory is getting close to adequate there, or if the situation may be different for CTL and backhoes.

Yoshikawa [A]: As I mentioned earlier, the construction machinery in North America is still going strong when we looked at from Kubota as a whole. However, the backhoe market itself has been shrinking YoY, and we are experiencing the same trends as that market, so we will probably take measures such as keeping shipments somewhat low and not increasing a certain level of inventory.

However, as I mentioned earlier, CTL sales have been very strong and have continued to increase YoY on a retail basis, and to be honest, we have not been able to meet the demand from dealers and users. These products are made in Japan and the US and are in full production.

This will be continued for the time being, and under the current circumstances, the situation is so strong that we are not sure if we will be able to reach the point where we can build up sufficient dealer inventories. Therefore, the situation in North America is a bit mixed.

Maekawa [Q]: I see. I understand. Thank you very much.

Just one more addition, and I think you just gave me a hint in your answer, but it is in the area of the idea of demand for the next fiscal year. However, I think that interest rates for small tractors for residential will come down in the future, but it may be a bargain with the weakness of consumption, et cetera.

As for the next term, do you still expect demand to be better than this term, or do you think that CTL will remain strong, but even if it is not so strong in the tractors for residential, or conversely, as you mentioned, you will adjust production in H2 of the year, so even in that situation, your wholesale and volume will increase. I would appreciate it if you could give me one more hint as to whether this is the case or not, including the demand for the next term. Please do so.

Yoshikawa [A]: First of all, to answer your question, the situation varies considerably by model. Residential tractors are a big business for us. We now see this as a reaction to the so-called COVID demand, and we believe that the market has shrunk last year and this year.

However, we are looking at this year with the expectation that this will start to bottom out this year, rather than decreasing further next year.

Then, since we have reduced our inventory this year based on this retail, I wonder if there is a little more room for increased production and sales there. Taking into account the economic and interest rate situation in the US, I wonder if we will have to wait and see if such a scenario will be the case.

As for construction machinery, although housing starts have decreased a little, they are still at a fairly high level, and as I mentioned earlier, if interest rates are going to be a little lower and inflation and price increases are expected to settle down to some extent, I think that demand for small construction machinery will remain firm. In addition, I think there is a strong possibility that demand for small construction equipment will remain firm due to the construction of various factories in the US and other factors.

We will have to see what happens next year, as we did with the residential, but I think the market will remain firm next year. Then, whether it is this backhoe or CTL, I think there is room for another increase, but I think it will remain firm to some extent.

The problem is Europe. Both construction machinery and agricultural machinery have been declining since last year, and we are not sure if they will bottom out this year or remain flat next year. As I mentioned earlier, there are moves to lower interest rates a little, so if these moves are successful and things brighten up a little next year, there may be room for an increase in production and sales compared to this year.

I think we need to look at the situation a little more closely, and I think we are a little cautious about this at the moment. That is all.

Maekawa [Q]: I understand. Thank you very much for the details.

Second, in the other part of the increase/decrease gains, I would like to know your thoughts on the next fiscal year rather than the current year.

I think there are a variety of factors, such as the positive effect of distribution costs this fiscal year, and on the other hand, the negative impact of retirement benefits compared to last year. I think there are other reasons, such as the fact that we have been able to control selling expenses, and also that the difference in product mix has been improving.

I wonder if the suppression of this increase in selling expenses and the product mix will continue into the next fiscal year, given the current view of Europe and the North American construction machinery, so there are a few more things to be considered, but I wonder if the other figures for the increase and decrease in profit can be suppressed to the current JPY13.4 billion or around the JPY10 billion level if this continues into the next fiscal year and beyond.

I think the details will be in the financial results at the end of the term, but I would like to know your stance for the next fiscal year and beyond, as it is related to the control of costs and the earning power at the end, which will be included in the others of this increase/decrease in profit. Please do so.

Yoshikawa [A]: As I mentioned earlier, we need to further strengthen our earning power and ability to make profits for the next fiscal year. In this sense, we were able to reduce logistics costs considerably from last year, especially in H1 of this year, but this will not be the case if they continue to decrease, So, I do not expect that to be the case, but I think that we should focus on how to control fixed costs, including labor costs, and selling expenses.

Two of the major items in the "other" category are depreciation from research and development expenses and capital investment. Since this is an investment for the future, we do not expect to reduce it, but expect it to remain at a plateau.

On the other hand, I wondered if we would then increase at the same level and speed as before, and I wondered if this was not also possible. We would like to consider measures to absorb the increase in personnel expenses, which we expect will continue in the future, while controlling fixed costs overall, while controlling research expenses and depreciation to some extent. We will consider such measures for next year's plan.

It may be difficult to suddenly reduce drastically next year, but we will first thoroughly control the increase, and then, although there is room for sales increase next year, we will ensure sufficient performance even without an increase in the top line, and next year, compared to this year, we will be able to absorb the negative impact of the exchange rate. If we cannot expect a positive top line, we will have to make further adjustments to the fixed cost base, although we have said that it will remain unchanged, and I hope you understand that we are currently considering this.

Maekawa [M]: Thank you very much.

Moderator [M]: Mr. Sano from JP Morgan Securities, please.

Sano [Q]: My name is Sano from JP Morgan. Thank you for your explanation. Two points, please.

On the first point, I would like to ask you about your approach to strategy in North America. I think it is difficult to say what the demand will be after next year, though. For example, at the dealer meeting, I heard that new small construction equipment products will be introduced, and in the area of residential's compact tractors, although I think the competition for incentives is tough, I heard that you are expanding your sales channels and that you will expand your business in the next fiscal year.

Rather than talking about demand, could you talk a little more about what you think is important in terms of your company's strategy, such as expansion for the next fiscal year and earning power? That is the first point.

Yoshikawa [M]: Mr. Hanada, GM of Farm and Industrial Machinery Strategy and Operations Headquarters, would like to explain this point.

Hanada [A]: I, Hanada, will explain a little bit. First of all, in North America, as I have already explained, one of the key points is how we should conduct our activities in the midst of a slowdown in the market situation.

Since last year, we have been working on how to manage our business more efficiently in the face of high interest rates, and we have been reviewing our retail finance practices considerably. We have moved away from a policy of uniformly providing retail refinancing to all models nationwide and have begun to deal with some models and regions in a more efficient manner, and this has gradually been gaining ground.

As a result, we have managed to keep incentives low even at such high interest rates and have managed to increase our market share in H1 of the year despite such policies.

On the other hand, we are not considering any drastic changes to our dealer network or channels at this time. Of course, we will make changes to our strong and weak dealers every year, and we will expand our dealer network in some areas of construction equipment where demand is high in urban and suburban areas, where we still have a weak dealer network, but we will not make major changes.

In addition, we expect to see more new products in construction machinery through next year, so our dealers will continue to expand their product lineups, introduce new products, and change their sales methods in order to support dealers and link them to retail sales, while the Company as a whole will continue to improve management efficiency and reduce costs.

We have been promoting the simultaneous efforts of streamlining management and reducing costs, and we expect to continue in this direction through next year. That is all.

Sano [Q]: Thank you very much.

Second, please tell us about free cash flow. H1 of the year turned positive first time in a long time. I understand that free cash flow was also behind the expansion of the share buyback program. I would like to know again how you see free cash flow at the end of this fiscal year, and although there are still issues to be addressed, mainly in working capital, such as inventories and accounts receivable, but could you tell us more about your efforts in these areas with figures? Please.

Yoshikawa [A]: I, Yoshikawa, would like to speak. I would like to say two things. First, as I mentioned earlier, inventory adjustments will be made in H2 of the year rather than H1, so from now until the end of the year, we will be working to reduce over-the-counter inventories at dealers and inventories at sales companies.

In addition, retail finance receivables, one of the uses of the funds, will peak in June and July, when retail demand is at its peak, and will tend to decrease slightly from now until December, so this will also have a positive effect on increasing free cash flow and returning to profitability.

Therefore, while we have already mentioned a free cash flow surplus of JPY3.5 billion in H1, we expect a larger amount in H2 as a free cash flow surplus.

We have decided to purchase JPY50 billion of our own stock. We have also increased the dividend by JPY1, and although the year-end dividend has not yet been decided, we are basically aiming to cover the shareholder return with free cash flow, if possible.

In addition, we have been reducing some of our strategic shareholdings for several years now, and we would like to use the new cash from these reductions to cover the cost of shareholder returns. In the future and beyond, we will continue to improve the efficiency of inventory, increase profits, and generate cash to increase returns to shareholders without increasing interest-bearing debt. This is the direction we are planning to go.

I cannot provide you with detailed figures today, but I think I can say that our basic goal is to cover shareholder returns with free cash flow. That is all.

Sano [M]: I understand very well. Thank you very much. That's all from me.

Moderator [M]: Mr. Fukuhara, please.

Fukuhara [Q]: I am Fukuhara from Jefferies. Thank you for your help. Thank you for today. I have only one thing to say.

I have a question about the competitive environment in the US. John Deere was mentioned in yesterday's conference call. What I'm concerned about is competition from Korean and Indian companies. There are differences in financing programs and prices, but if Kubota has lost market share in this aspect, how will it recover in the future? I would like to ask first of all whether you can recover or not.

Additionally, currently it is such competitive environment. Do you think it is temporary, or are consumers' shopping preferences changing? Can you also give us your perspective on whether this is temporary or long-term?

Hanada [A]: I, Hanada, will explain a little bit. The competition among what we call Tier-2 tractors from Korea and India, especially in the compact range, certainly began with the coronavirus pandemic and has continued. They had been in the North American market for a long time, but when we were facing competition and supply issues, especially with coronavirus pandemic, they took advantage of that and came in to increase their dealer network.

Their product competitiveness itself is also high. On the other hand, they are still trying to enter the market, so they have been expanding the market by attaching retail programs, financing, et cetera, quite forcibly.

In this situation, as I mentioned earlier, we have established a program to compete in the short term, focusing on regions and competing models. This is why we have managed to contain the situation.

Certainly, if we are asked whether this situation is short term or long term, we recognize that it is not something that will be resolved in the short term. Therefore, we must improve our cost competitiveness, and we are currently examining how we can do so.

Our Indian partners, joint ventures, and EKL have a very strong cost base, and we are currently studying how we can use this to compete with them on a company-wide basis, and we are thinking of using this as a long-term strategy. That is all.

Fukuhara [M]: I understand. Thank you very much. That is all.

Moderator [M]: Thank you very much. Finally, Mr. Adachi of Goldman Sachs Securities, please join us.

Adachi [Q]: Thank you for all your help. My name is Adachi from Goldman Sachs Securities. Thank you very much. Let me ask you two points.

First of all, as we have discussed many times, let me ask you once again about production and inventories in North America. I would especially like to ask about the mini backhoe part. Although it appears that some production adjustments have already been made here since H1 of the year, I think the inventory is still increasing.

In the earlier discussion, you mentioned that inventory adjustments would not be carried over to the next fiscal year, so I would like to know your judgment on whether, depending on the situation in H2 of the fiscal year, production will be further restrained and whether this will have the effect of lowering the mix improvement or lowering the quantity of goods sold.

On the other hand, if you have a special policy that allows an increase in inventory only in anticipation of interest rate cuts in the next fiscal year, I would like to hear about it as well. This is the first point. Best regards.

Yoshikawa [A]: I, Yoshikawa, would like to answer. Certainly, the market for mini backhoes has been weaker than last year, and I think we have a slightly larger inventory. As you pointed out, we have adjusted production and shipments slightly since H1 of the year, and I think it is fair to say that we will strengthen this adjustment in H2 of the year.

We are planning to make adjustments in the allocation of backhoes by region, since all backhoes for the US market are made at our plant in Japan. From now on, especially in December, it is a very important demand period for construction machinery, and we would like to bring it to an appropriate level, although we will have to wait and see how this will turn out.

However, since we do not have as much excess as tractors, I hope you understand that in terms of the magnitude of production adjustment, it will not have such a large impact on our business performance, and if we keep to the contents incorporated in the current business forecast, we will be well-positioned for next year. That is all.

Adachi [Q]: Thank you. Second, I would like to ask what you are considering in terms of fixed-cost reduction and sales-cost reduction. Are you considering the consolidation or relocation of production bases in some cases?

Specifically, the US portion. In particular, profitability is expected to be high, and we believe that CTL and construction machinery in the US will continue to be relatively strong through the next fiscal year, and if demand for tractors does not return to the level of before the coronavirus pandemic, you may be able to shift that base to construction machinery. Finally, I would like to ask you if you are thinking of doing so. Best regards.

Yoshikawa [A]: Thank you. To answer your question, we need to think about the global layout of production bases and production from various perspectives.

One is where to place the final assembly, and another is the procurement of various parts, for example, engines are brought from Japan, major parts are brought from Thailand, and so on. I think we need to consider various risks in the future, as well as what can and should be procured in the US.

The first point of my answer is that we cannot make major changes to our production bases in the next three or five years, although this does not apply to next ten years. It is not so easy to manufacture construction machinery in a tractor factory, so I think it is safe to say that we are not considering such a major change at this time.

However, there is also the risk of exchange rate fluctuations, geopolitical risks, and various logistics disruptions as we saw last year and the year before, et cetera. We need to consider where and how to assemble our products, and how much of the overall manufacturing cost is accounted for by procurement costs.

In addition, we are planning to increase procurement and production in India in the mid- to long term, so I can say that we are considering what kind of mid- to long-term production layout would be best while sorting out such factors and requirements.

However, I would like to say that we are not thinking of changing the layout in a very short-term situation. In this context, we would like to address how to lower fixed costs and selling expenses, which is another story. That is all.

Adachi [Q]: Thank you. Let me add one point. I believe there was also a reference to the exchange rate.

If we talk about CTL alone, the demand place is basically the US. I think right now you are producing in both Japan and the US and exporting some of the products. I think it is possible to produce all of these in the US, and of course export the engines, but is it possible to produce and assemble all in the US? Please answer my last question.

Yoshikawa [A]: Currently, we are making products in the US and Japan, but I think it is safe to say that it is unlikely that all of our products will be made in the US. It would require a considerable investment to move the entire volume of products currently manufactured in Japan to the US, and there is also the issue of whether or not skilled employees can be recruited. Therefore, if the situation changes, it may be possible that the entire production will be done in the US.

As you have pointed out, major parts including engines are currently being sent from Japan, so I would like to say that we do not expect to produce all of them in the US anytime soon.

Adachi [M]: Thank you for your detailed response. That's all from me. Thank you very much.

Matsui [M]: We have received other questions, but since it is time to end, we will conclude the briefing.

Thank you for attending today's information session.

Yoshikawa [M]: Thank you very much.

[END]

____

Document Notes

1. *Portions of the document where the audio is unclear are marked with [inaudible].*
2. *Portions of the document where the audio is obscured by technical difficulty are marked with [TD].*
3. *Speaker speech is classified based on whether it [Q] asks a question to the Company, [A] provides an answer from the Company, or [M] neither asks nor answers a question.*
4. *This document has been translated by SCRIPTS Asia.*

Disclaimer