

Financial Results for the 1st Quarter of FYE 2024 Analyst Briefing Q&A

August 2, 2023
SUBARU CORPORATION

Q : What is your assessment of first quarter results? What are the risks and opportunities for the full-year plan?

A : There were few special factors at work overall, and this result was fairly close to what we can actually achieve. The current full-year plan has been left unchanged because of the wide fluctuations in forex that we have seen recently and the difficulty of reading such fluctuations going forward, and also because the production was in line with initial plans. Still, even excluding forex, I think there are opportunities to increase profits. If production increases due to improvements in semiconductor supply and this leads to higher shipments to the highly profitable U.S. market, it will contribute to increased profits. While we need to take the competitive environment into account, we are also considering revising prices further depending on circumstances. Taking a long-term view that includes the current fiscal year and beyond, based on the idea of costs settling at a more reasonable level due to falling commodity prices and the stabilization of production, I think there is room for some improvement in profitability. On the other hand, the risks would be semiconductor supply, which has not been completely resolved, and logistics constraints.

Q : I would like your thoughts on demand trends in the Japanese and U.S. markets.

A : We struggled a little in the Japanese market in July despite beginning sales of the new Impreza and Crosstrek, but we plan to add a new model going forward and we will work to recover the situation. Demand remains strong in the U.S. market; if we can deliver the cars, they will sell. However, for the market as a whole, the level of inventories is rising and competition is intensifying, so we are watching the situation closely.

Q : Why did you choose this point in time to shift your focus towards BEVs?

A : The decision to shift our focus towards BEVs at this time was the result of a comprehensive assessment that took into account the speed of the move towards BEVs in the U.S., which is our most important market, environmental regulations, moves being made by other manufacturers, and of course the most important issue, which is acceptance of BEVs among our customers and trends in market development. Based on this, we concluded that we should begin production of BEVs in the U.S. as well, which led to a significant change in objectives for 2030.

Q : Previously you said you would first start production of BEVs in Japan and then transfer the know-how thus accumulated to the U.S., but it seems the production launch in the U.S. has been accelerated. Is it feasible?

A : As for BEV production in the U.S., we are considering the details, including location, based on a comprehensive investigation into the supply chain, battery supply, and other issues. Once we get a grasp on the differences between Japan and the U.S. in terms of quality, cost, productivity, and other factors, we believe that it is probably possible to start production of BEVs in the U.S. by carefully transferring Monozukuri (Manufacturing) Innovation and Value Creation, and to do this as an initiative implemented in parallel with the construction work being undertaken in Japan to launch a dedicated BEV factory.

Q : Is the production capacity figure of 1.2 million units an ideal that has been established to target growth? Or is this a figure that has been temporarily inflated during the transition period, with the number of models and capacity to be reduced to improve profitability once BEVs become mainstream within the business?

A : We have no intention of pointlessly pursuing volume, and our basic approach is qualitative growth. We are considering the level of 1.2 million units strictly in terms of our production capacity. Because there are many uncertain elements, including trends in environmental regulations and the degree to which acceptance of BEVs has developed, we want this level of production capacity available during the transition period to enable a smooth switchover. In addition, as we move forward with Monozukuri Innovation, we aim to further increase volumes by raising production capacity per line. It was based on these factors that we set the level of 1.2 million units.

Q : What is the “Retaining Value” concept?

A : There is a strong trend for SUBARU customers, primarily in the U.S., to use our vehicles with affection over long periods of time, and many people feel that driving the same vehicle for a long time is good for the environment. The concept of “Retaining Value” was born from the idea of wanting our customers to enjoy driving the vehicle for a long period of time by utilizing technology and services to maintain and add value even after purchase. As software will become central to the value provided by cars in the future, we are also working to maintain and increase value through the use of OTA updates, among other initiatives. In the Japanese market, as part of after-sales services we offer a program of paid updates to customers of the Levorg STI Sport equipped with an electronically controlled suspension. This has been extremely well received by customers, who say it creates new value by broadening the specification of the suspension, and we will use cases like this as reference points for our initiatives going forward.

Q : Specifically, what do you mean when you say that cutting the number of processes in half and the number of parts in half is something that is achievable because of the size of SUBARU?

A : The details are still under consideration, but we need to make Manufacturing simpler. To that end, we go back to the planning and design stage to rigorously discuss the kind of vehicle we want to build, the structure it will have, and the production method we will use. Then we will move ahead with cutting the numbers of processes and parts in half to realize a highly profitable BEV. For that to happen, we need design, development, manufacturing, and other divisions to work as one with the supply chain to forge ahead with Monozukuri Innovation. I believe this is only achievable because we are a relatively small company, and it will also serve as one of our strengths.

Q : As you move forward to introduce a considerable volume of electrified products, what are your thoughts on partnerships?

A : There has been no change in our approach of strengthening the alliance relationship with Toyota. Both companies agree to continue sharing insights in areas where we can collaborate. As for batteries, in addition to using the alliance for procurement, we plan to set up our own unique procurement network under a medium- to long-term partnership with Panasonic Energy, which was announced the other day. Our alliance with Toyota is based on the idea that sharing common batteries, with each company working on its own to expand the range of technologies, contributes to the growth of both companies, so we would like this to be seen as an evolution of collaboration.

Q : What kind of external environment are you assuming when you talk about U.S. sales of 400 thousand BEVs in 2028?

A : We think we will have the capacity to serve a market of 700 thousand to 800 thousand units in 2028. We believe that if we can sell up to 400 thousand BEVs, which is slightly more than half of that, we will be able to meet environmental regulations in the U.S. While there is still uncertainty around how the BEV market will develop, we have started development and preparations for production with the determination to create products that can achieve sales of 400 thousand units, and products that customers will want to choose, through our “Monozukuri Innovation” and “Value Creation” initiatives.

Q : What made you choose cylindrical lithium-ion batteries out of all the various types of battery?

A : Different batteries have different advantages and disadvantages, but the merit of the cylindrical type is that it is easy to adapt to the low-center-of-gravity, low-floor approach that is SUBARU’s strength. In addition to technological advances going forward, we also considered the perspective of who would be a reliable partner to struggle together with us on development, preparations for production, launching production, and raising and stabilizing yields.

Q : If you average the ¥1.5 trillion in investments for electrification up to around 2030, it comes to approximately ¥200 billion annually. This year you are planning ¥300 billion in capex and R&D expenditures. Will this level rise further in the future?

A : By squeezing down capex in traditional areas as much as we possibly can, we aim to make it so that investments in BEVs are not just an add-on. On the other hand, previously we had maintained R&D expenditures at a level of around ¥120 billion annually, and we assume that will rise slightly going forward.

Q : What are your expectations for profit margins over the long term to 2030?

A : There is a view that the cost of batteries, which significantly affects the profitability of BEVs, will change in an innovative way along with the times, but at the same time we will take steps to improve profitability by reducing manufacturing costs through “Monozukuri Innovation”, and combine this with “Value Creation” that will leave customers satisfied even if we raise the price slightly , and thus achieve industry-leading profit margins in 2030. Because we expect the period through to 2030 to be one of violent change, we set this as a goal to be accomplished when we have achieved the initiatives outlined today.

Q : Will you be able to increase net cash towards 2030?

A : With regard to maintaining a net cash position, previously we had set two months’ worth of revenue as a lower limit, but we will change the net cash level going forward, as required by the timing. While we are currently in the phase of accumulating net cash for growth investments, going forward we do not expect it to keep growing.

Q : Have there been any changes in the shareholder returns policy?

A : Basically there have been no major changes. Going forward, we will pay stable and continuous dividends, and implement share buybacks after taking into account the share price, ROE, and cash flow, with the aim of delivering a total return ratio of 30-50%. We will also be making major investments going forward, but I hope you will understand this as a message that we will continue to generate shareholder returns in accordance with cash flow.

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