Kubota Corporation

Result Briefing for the 2nd Quarter of FY2023

August 8, 2023

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 FY2023	
[Fiscal Period]	FY2023 Q2	
[Date]	August 8, 2023	
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[Time]	10:00 – 11:01 (Total: 61 minutes, Presentation: 27 minutes, Q&A: 34 minutes)	
[Venue]	Dial-in	
[Venue Size]		
[Participants]	120	
[Number of Speakers]	6	
	Masato Yoshikawa	Executive Vice President and Representative Director, GM of Planning and Control Headquarters
	Kazushi Ito	Senior Executive Officer, Deputy GM of Planning and Control Headquarters
	Hideo Takigawa	Executive Officer, GM of Corporate Planning and Control Department
	Wataru Kondo	Executive Officer, GM of Water and Environment Infrastructure Management Department
	Hitoshi Sasaki	Executive Officer, GM of Farm and Industrial Machinery Strategy and Operations Department
	Issei Matsui	IR Section Manager of Corporate Planning and Control Department

[Analyst Names]*	Tomohiko Sano	JPMorgan Securities
	Hikaru Mizuno	UBS Securities
	Tsubasa Sasaki	Mitsubishi UFJ Morgan Stanley Securities
	Kentaro Maekawa	Nomura Securities
	Yuichiro Isayama	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: The time has arrived. We will now hold a financial results briefing for Q2 FY2023. Thank you for attending the briefing session today. I am Matsui, IR Section Manager of Corporate Planning and Control Department, and I will be the moderator today.

As for today's schedule, Yoshikawa, GM of Planning and Control Headquarters, will give an approximately 30-minute presentation on the financial results. Then, a question-and-answer session follows for another 30 minutes. The end time is scheduled at 11:00 AM.

Please refer to the presentation materials for today's meeting on our website for investors.

Let me now introduce the attendees from Kubota. Here is Yoshikawa, Executive Vice President and Representative Director, GM of Planning and Control Headquarters.

Yoshikawa: My name is Yoshikawa. Thank you for joining us today.

Matsui: Here is Ito, Senior Executive Officer, Deputy GM of Planning and Control Headquarters.

Ito: My name is Ito. Thank you.

Matsui: This is Takigawa, Executive Officer, GM of Corporate Planning and Control Department.

Takigawa: My name is Takigawa. Thank you.

Matsui: This is Kondo, Executive Officer, GM of Water and Environment Infrastructure Management Department.

Kondo: My name is Kondo. Thank you for joining us today.

Matsui: [Here is Sasaki], Executive Officer, GM of Farm and Industrial Machinery Strategy and Operations Department.

Hitoshi Sasaki: My name is Sasaki. Thank you for joining us today.

Matsui: Now, Yoshikawa, General Manager of Planning and Control Headquarters, will explain the status of consolidated financial results for Q2 FY2023. Please have the financial results briefing materials ready.

Now, Yoshikawa, please begin.

Financial Summary for FY 2023 2nd Quarter

For Earth, For Life
Kubota

(Unit: billions of yen)	FY2023 2Q	FY2022 2Q	Changes Amount	Changes %
Revenue	1,520.0	1,259.3	+260.7	+20.7
Japan	315.1	299.1	+16.0	+5.3
Overseas	1,205.0	960.3	+244.7	+25.5
Operating profit	12.1% 184.6	9.4% 118.8	+65.8	+55.4
Profit before income taxes	12.6% 191.8	10.4% 130.5	+61.4	+47.0
Profit attributable to owners of the parent	8.5% 128.8	7.3% 91.5	+37.3	+40.7

	FY2023 2Q	FY2022 2Q
1USD (JPY)	135	123
1EUR (JPY)	146	134
1THB (JPY)	3.95	3.65

The effect of fluctuation in foreign exchange rate to Revenue this year was +82.0 billion yen.

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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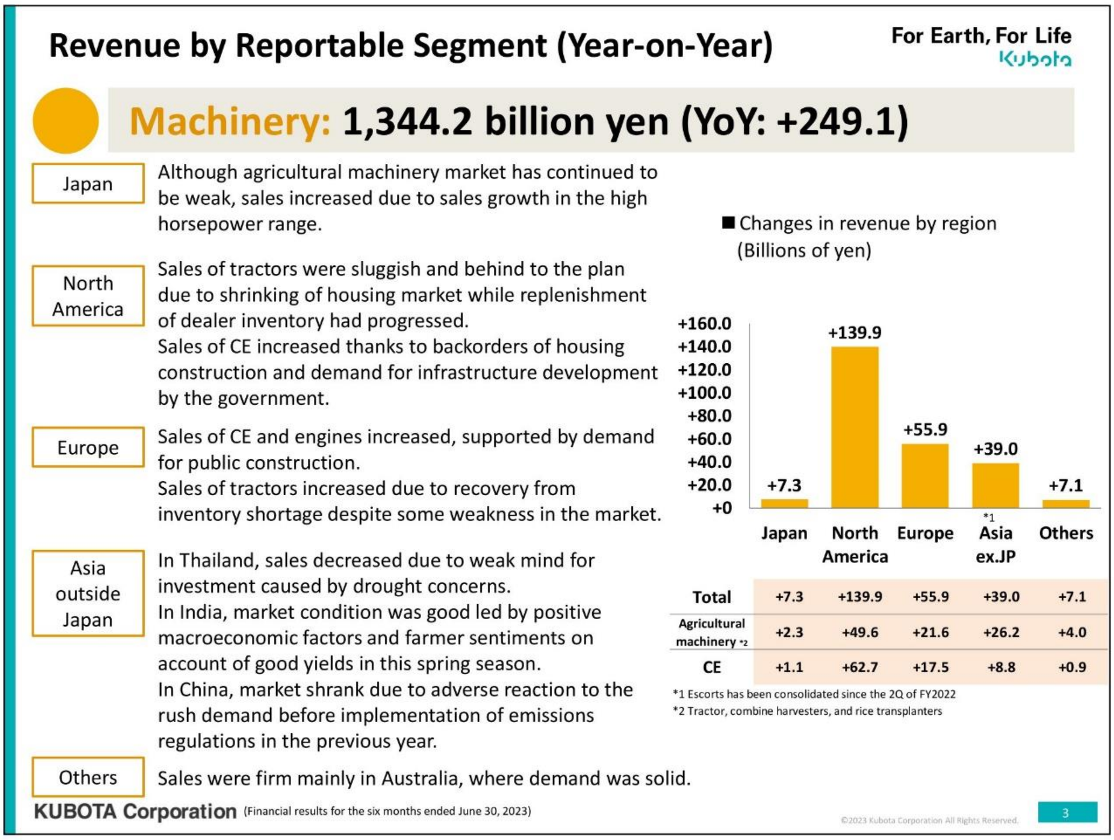
Yoshikawa: I am Yoshikawa, General Manager of Planning and Control Headquarters. I would like to explain our consolidated financial results for H1 FY2023 and our forecast for the full year.

See page two of the presentation.

Revenue increased 20.7% YoY to JPY1,520 billion, operating profit increased 55.4% to JPY184.6 billion, and profit attributable to owners of the parent increased 40.7% to JPY128.8 billion. Sales and operating profit exceeded the full-year forecasts by JPY40 billion and JPY34.6 billion, respectively.

The yen's depreciation against the major currencies of the US dollar and the Euro against the previous year and assumptions worked positively, including the impact of currency exchange conversion. The increase in overseas sales includes about JPY82 billion in foreign exchange effects.



	Japan	North America	Europe	Asia ex.JP	Others
Total	+7.3	+139.9	+55.9	+39.0	+7.1
Agricultural machinery *2	+2.3	+49.6	+21.6	+26.2	+4.0
CE	+1.1	+62.7	+17.5	+8.8	+0.9

See page three. We will look at the machinery business, by regions.

Domestic sales increased by 5% to JPY7.3 billion. Sales of agricultural machinery increased from strong sales of large machines, although the market remained weak due to the termination of subsidies for business operations and sluggish rice prices. Sales of construction equipment and engines remained steady with progress in infrastructure construction and other projects.

North America. Revenues increased by JPY139.9 billion, up 29%. Regarding the market, let's start with tractors. In addition to the slowdown in business confidence, demand for tractors for mowing was delayed due to low temperatures in early spring. As a result, the residential market, which is primarily for individuals and homeowners, was weaker than expected and remained at 2018 levels. The agricultural market has been strong, but prices for wheat and beef have begun to decline, indicating a slowdown.

On the other hand, construction equipment is performing well due to back orders for housing and demands on infrastructure developments by governments. Sales increased significantly from the previous year due to inventory fulfillments at dealers, favorable construction equipment and price hikes, as well as the exchange rate difference from the weaker yen. As in Q1, there has been no logistical disruption , and inventory fulfillments at dealers, especially for tractors and mowers, have progressed, bringing the inventory levels in the US to five months at the end of June 2023.

However, the inventory level has not progressed well enough to accommodate the strong demand for utility vehicles and construction equipment, and it remains in the low two month range.

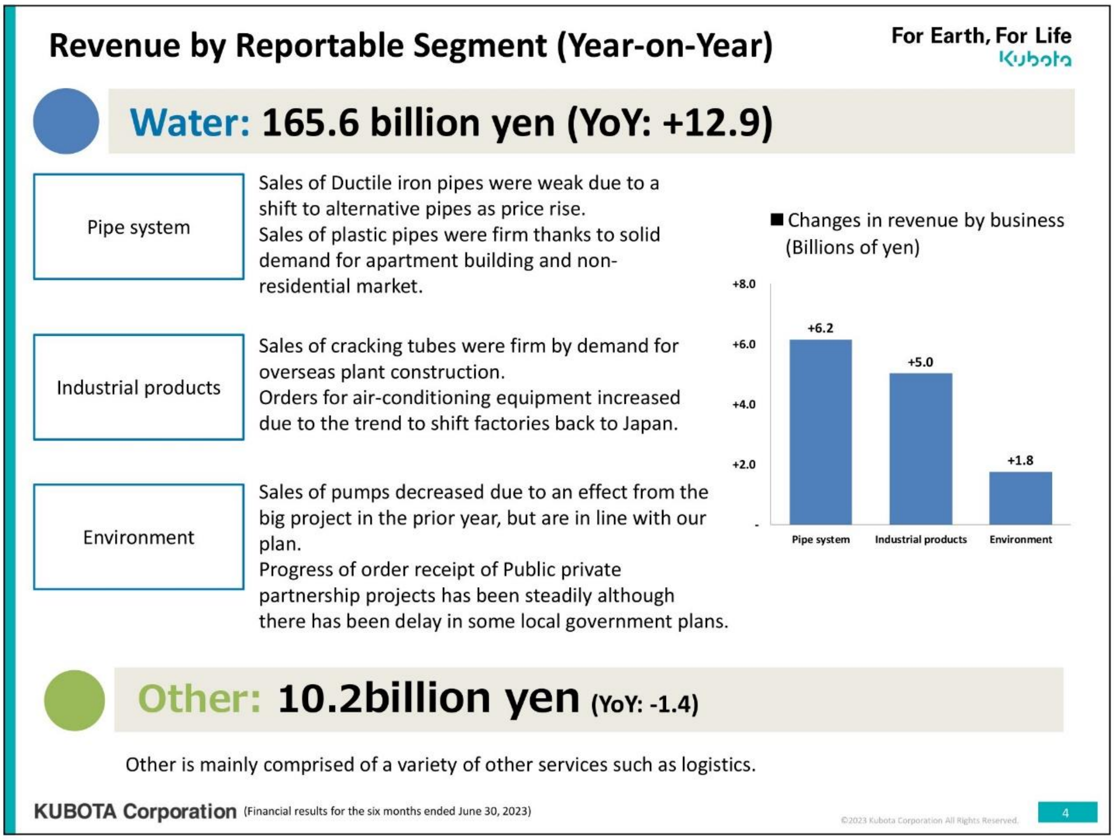
Continuing on, Europe. In Europe, sales increased by 34% to JPY55.9 billion. Construction equipment sales remained strong, supported by infrastructure construction projects. Engine sales have also been favorable due to the continued strong performance of the construction and industrial equipment market.

As for tractors, agricultural commodity prices remained high, but investment did not proceed due to various uncertainties, and the market weakened. Sales increased significantly due to the acceleration of shipments to resolve the extreme inventory shortage that occurred last year. The elimination of inventory shortages has also led to an increase in retail sales. That's for Europe.

Next, Asia. Asia posted 15% increase in revenues to JPY39 billion. In Thailand, farmers were reluctant to buy due to drought concerns, resulting in a larger decline than expected in both rice and field crop demand. It is said that the drought is caused by the El Niño phenomenon, and farmland hasn't had much rain, and rainfall has been lower than normal.

In India, the field crop market has been favorable with a rich harvest this spring as a result of good planting in the previous winter. As for China, last year, due to the enforcement of emission regulations, other companies did clearance of a large amount of their inventories. The agricultural machinery market has declined significantly in this fiscal year in a reaction to that. The construction equipment market also continues to be sluggish in China due to a decline in private-sector demand and a lack of government support on budget.

For other areas, sales increased by JPY7.1 billion and remained steady, mainly in Australia.



See page four. Water and environment. The Water and environment business increased by 8% to JPY12.9 billion. In pipe systems, the market of iron pipes has weakened due to a shift to alternative pipes in response to rising prices. On the other hand, there has been a shift away from iron pipes to plastic pipes, and private sector demand for multi-family housing and non-residential has been strong.

In industrial products, overseas projects for cracking tubes for ethylene plants remained steady. With regard to air conditioning, there is a movement toward returning to Japanese plants in line with the supply chain review, and orders for pharmaceuticals and semiconductor plants have been strong.

In the environmental field, sales of pumps were down from the previous year due to a decrease in large projects compared to the previous year, but sales are steady compared to the plan. PPP projects, which are public private partnership projects, have potential demand and orders are increasing. On the other hand, we are still experiencing a slowdown in orders and bids from municipalities.

Other sales decreased by JPY1.4 billion.

Operating Profit

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Kubota

(Unit: billions of yen)	FY2023 2Q		FY2022 2Q		Changes	
	Amount	%	Amount	%	Amount	%
Operating profit	**184.6**	12.1	**118.8**	9.4	**+65.8**	+55.4

Factors affecting operating profit (YoY change +65.8 billion yen)

1.Fluctuation in exchange rates	1USD (JPY) (123→135 *1) 1EUR (JPY) (134→146 *1) Other currencies	+33.0 billion yen +6.0 billion yen +5.0 billion yen	**+44.0** billion yen
2.Foreign exchange gain/loss			**-14.6** billion yen
3.Material	Machinery (Purchased parts, steel, etc.) Water (PVC, coil, etc.)	-10.9 billion yen -3.0 billion yen	**-13.9** billion yen
4.Change in sales incentive ratio	North America : -15.5 billion yen, etc.		**-13.8** billion yen
5.Impact of increased or decreased sales			**+15.8** billion yen
6.Sales price increase			**+80.7** billion yen
7.Other	Logistics expenses +1.9 billion yen, R&D expenses -8.0 billion yen, Depreciation and amortization -7.7 billion yen, etc.		**-32.4** billion yen

*1: Exchange rates, which affected profit of exported products from Japan in consideration of the period of transportation and inventory, were as follows: USD:115→138 EUR:130→143

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page five. Now I would like to explain the increase/decrease in operating profit.

Fluctuation in the exchange rate was a positive factor of JPY44 billion increase in income, while foreign exchange gain/loss was a negative factor of JPY14.6 billion decrease in income. Raw material was a negative factor of JPY13.9 billion decrease in income due to higher prices for purchased parts, steel, PVC resin, and such. However, the deterioration has been less than initially expected.

The change in sales incentive ratio was a negative factor of JPY13.8 billion decrease, and the impact of increased or decreased sales was a positive factor of JPY15.8 billion increase. Sales price increase was a positive factor of JPY80.7 billion increase, mainly the price increase effect in North America. The remaining a negative factor of JPY32.4 billion decrease is attributed to other factors.

Other included logistics cost of JPY1.9 billion, which was a positive factor in increase YoY. On the other hand, R&D expenses increased by JPY8 billion, depreciation increased by JPY7.7 billion, and personnel expenses increased by JPY2.2 billion, while selling, general, and fixed expenses increased by JPY11.5 billion. Other compositional differences and gains in Escorts Kubota Limited, also contributed to JPY4.9 billion decrease in profit.

Operating Profit by Reportable Segment

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(Unit: billions of yen)		FY2023 2Q	FY2022 2Q	Changes
Machinery	Revenue	1,344.2	1,095.1	+249.1
	Operating profit	198.4	115.1	+83.3
	OP margin	14.8%	10.5%	+4.3P
Water	Revenue	165.6	152.7	+12.9
	Operating profit	9.9	9.7	+0.2
	OP margin	6.0%	6.3%	-0.4P
Other	Revenue	10.2	11.6	-1.4
	Operating profit	1.1	1.7	-0.7
	OP margin	10.6%	15.0%	-4.4P
Adjustment*	Operating profit	-24.8	-7.7	-17.0
Total	Revenue	1,520.0	1,259.3	+260.7
	Operating profit	184.6	118.8	+65.8
	OP margin	12.1%	9.4%	+2.7P

*Adjustment includes administrative expenses, basic research expenses, and foreign exchange gain/loss at the parent company.

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page six. Operating profit by business segment.

In machinery, operating income increased by JPY83.3 billion. The effect of yen depreciation, the penetration of product price increase, and a reduction in the deterioration of raw material prices contributed to this result.

Water and environment increased by JPY0.2 billion. We have been promoting price pass-on of raw material cost, which had risen.

Statement of Financial Position

For Earth, For Life
Kubota

(Unit: billions of yen)	As of June 30, 2023	As of Dec. 31, 2022	Changes	Changes excl. the effects of fluctuation in exchange rates
Cash and cash equivalents	193.3	225.8	- 32.5	
Trade receivables	927.9	779.4	+ 148.6	+ 86.9
Finance receivables	1,878.9	1,684.5	+ 194.4	+ 42.1
Inventories	686.2	644.5	+ 41.7	- 6.5
Other	1,534.8	1,430.9	+ 104.0	
Total assets	5,221.2	4,765.1	+ 456.2	
Bonds and borrowings	1,942.9	1,611.1	+ 331.8	+ 216.1
Trade payables	295.5	454.8	- 159.3	
Other	626.3	596.7	+ 29.6	
Total liabilities	2,864.7	2,662.6	+ 202.1	
Equity attributable to owners of the parent	2,127.4	1,874.5	+ 252.9	
Noncontrolling interests	229.2	228.0	+ 1.2	
Total equity	2,356.5	2,102.5	+ 254.1	
Total liabilities and equity	5,221.2	4,765.1	+ 456.2	

Net debt equity ratio	0.82	0.74	+ 0.08
Net debt equity ratio (excl. financial services)	0.08	-0.03	+ 0.11

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page seven. Statement of financial position.

Total assets increased by JPY456.2 billion from the end of the previous year.

I would like to go through the main accounts.

First, trade receivables increased by JPY86.9 billion in real terms excluding the effect of exchange rates. The increase was due to progress in shipments in North America and Europe. Finance receivables increased by JPY42.1 billion in real terms. The amount of receivables has increased from higher unit sales prices.

Inventories decreased by JPY6.5 billion in real terms. Bonds and borrowing increased by JPY216.1 billion in real terms, both current and non-current. The increase in borrowings is due to an increase in the financial burden associated with the change in payment site in Japan.

The debt-to-equity ratio on a net basis was 0.82, and on a basis excluding finance services it was 0.08.

Statement of Cash Flows

For Earth, For Life
Kubota

(Unit: billions of yen)	FY2023 2Q	FY2022 2Q	Changes
Net cash used in operating activities	-98.1	-22.0	-76.1
Profit for the year and Depreciation	191.3	142.5	+48.9
Increase in finance receivables	-45.3	-37.9	-7.3
Other	-244.2	-126.6	-117.6
Net cash used in investing activities	-97.8	-226.6	+128.8
Payments for acquisition of property, plant, and equipment and intangible assets	-90.1	-80.6	-9.5
Other	-7.7	-146.0	+138.3
Net cash provided by financing activities	153.7	189.8	-36.1
Effect of exchange rate changes on cash and cash equivalents	9.8	15.6	-5.8
Net decrease in cash and cash equivalents	-32.5	-43.3	+10.9
Free cash flow	-195.9	-248.7	+52.7

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page eight. Cash flow summary.

Cash used in operation activities totaled JPY98.1 billion. The breakdown of outflow are depreciation and profit which was JPY191.3 billion, the increase in finance receivables accounted for JPY45.3 billion, and others accounted for JPY244.2 billion. Compared to the same period last year, expenditure increased by JPY76.1 billion.

Although operating cash flow continues to be negative due to the large decrease in accounts payable as a result of the change in payment site in Japan as I mentioned earlier, we are beginning to see some improvement, such as a decrease in inventories as a part of normalized operations.

Cash used in investing activities are shown in the table below. Free cash flow improved by JPY52.7 billion from the previous year to negative JPY195.9 billion.

Financial Services <Reference (unaudited)>

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Statement of Financial Position

(Unit: billions of yen)		As of June 30, 2023		As of Dec. 31, 2022	
		Financial services	Equipment operations	Financial services	Equipment operations
Total assets		2,146.4	3,186.0	1,952.2	2,946.2
	Cash and cash equivalents	31.4	162.0	23.1	202.7
	Trade receivables	30.6	898.5	29.3	752.1
	Finance receivables	1,878.9	-	1,684.5	-
	Inventories	-	686.2	-	644.5
	Property, plant, and equipment	15.5	668.9	11.1	624.6
	Other	190.1	770.3	204.3	722.3
Total liabilities		1,795.7	1,162.6	1,680.0	1,166.8
	Total interest-bearing liabilities	1,710.4	274.2	1,544.8	157.1
	Other	85.3	888.4	135.2	1,009.7
Total equity		350.7	2,023.3	272.2	1,779.4

Delinquency rate of retail financial receivables

(Unit: billions of yen)		As of June 30, 2023	As of Dec. 31, 2022	Changes	
		Amount	Amount	Amount	%
Balance of receivables		1,878.9	1,684.5	194.4	+ 11.5
	Over 90 days delinquent payment	16.9	11.3	5.6	+ 49.9
Delinquency rate		0.9%	0.7%	-	+ 0.2P

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page nine.

We would like to provide supplemental information of our finance service, operated mainly in North America and Thailand. In this page, we estimate the BS separately for the financial business and other businesses.

Most of the interest-bearing liabilities is used to cover the capital requirements associated with finance services, and the amount is limited on a core business basis, which without the financial business.

With respect to the risk of financing receivables, the Company maintains a sound quality of receivables at this point in time, with 0.9% rate of delinquency over 90 days.

Financial Forecast for the Year Ending December 2023

For Earth, For Life
Kubota

(Unit: billions of yen)	Year ending Dec. 31, 2023 (Forecast)	Year ended Dec. 31, 2022 (Actual)	Changes		Previous forecast (Feb. 2023)
			Amount	%	
Revenue	2,950.0	2,677.0	+273.0	+10.2	2,900.0
Japan	639.0	602.4	+36.6	+6.1	638.0
Overseas	2,311.0	2,074.6	+236.4	+11.4	2,262.0
Operating profit	9.7% 285.0	8.0% 214.4	+70.6	+32.9	9.3% 270.0
Profit before income taxes	10.1% 298.0	8.6% 231.2	+66.9	+28.9	9.6% 278.0
Profit attributable to owners of the parent	6.8% 200.0	5.8% 156.5	+43.5	+27.8	6.4% 186.0

1USD (JPY)	132	131
1EUR (JPY)	144	138
1THB (JPY)	3.88	3.75

The effect of fluctuation in foreign exchange rate to Revenue forecast is +17.0 billion yen against LY and +110.0 billion yen against the Previous forecast.

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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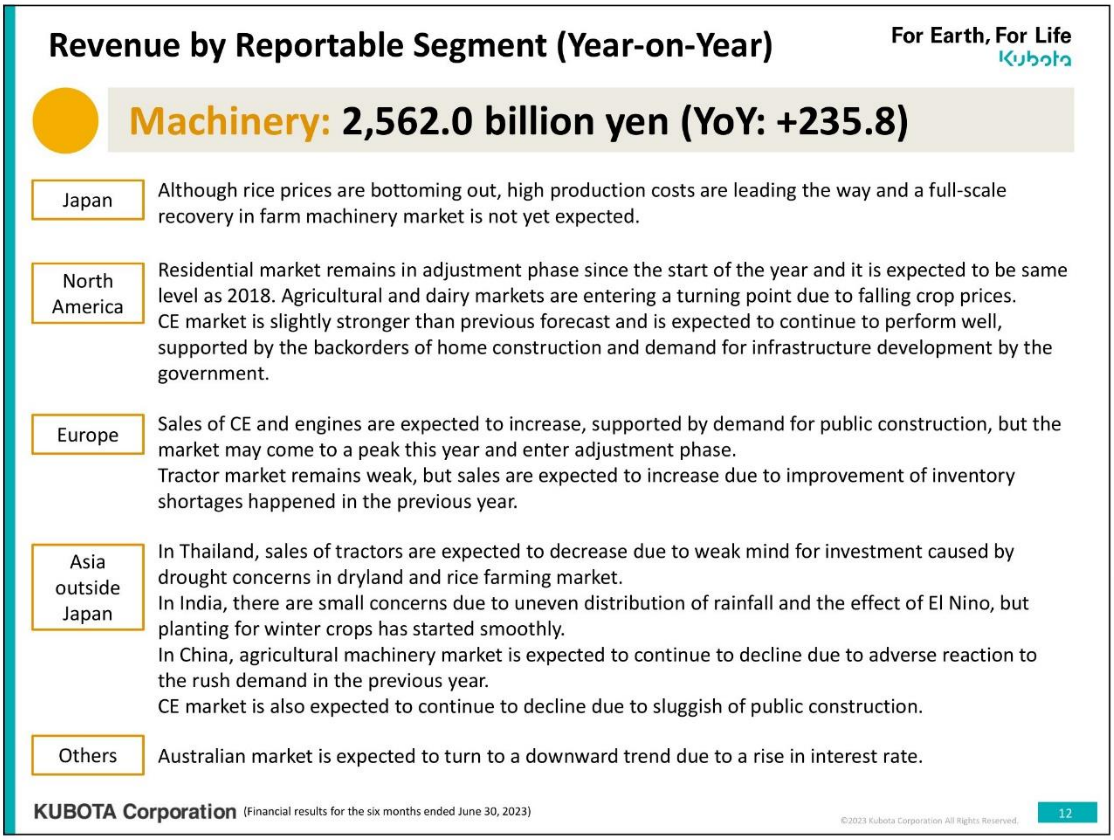
Next, we would like to explain our annual forecast as of Q2 FY2023. See page 11.

Net sales are projected at JPY2,950 billion, an increase of JPY273 billion, or 10.2% over the previous year. Operating profit is projected to increase 32.9%, or JPY70.6 billion, to JPY285 billion. Profit attributable to owners of the parent is set at JPY200 billion, an increase of JPY43.5 billion.

Although sales in local currency terms are expected to be lower than initially projected due to the contraction in the North American residential market and the Thai market, sales in yen terms are expected to increase from the depreciation of yen.



See page 12.

The machinery business is expected to generate JPY2,562 billion, JPY235.8 billion increase YoY.

Market trends by region.

In Japan, rice prices are bottoming out in the agricultural machinery market, but costs of fertilizers and others are still rising significantly for farmers. Therefore a full recovery is still expected to take some time.

Continuing on, North America. Regarding tractors, the residential market has been in an adjustment phase since the beginning of the year, and we continue to expect to remain at about 2018 level in H2. We expect that the medium to large market, such as dairy farms, is approaching a turning point due to the decline in agricultural commodity prices.

Meanwhile, in the construction equipment market, demand continues to be strong, backed by back orders for housing and demand for infrastructure developments by governments. Our initial forecast at the beginning of the year expected the housing market to shrink in H2 due to higher mortgage rates and the elimination of the housing backlog. Housing construction in the US has remained at the [1.4 million] level and is expected to hold up better than our initial forecast. As for engines, orders from construction equipment manufacturers have been favorable, pulled by the strong construction equipment market.

As for the dealer inventory situation in the US, we will reduce production of small tractors in H2 due to the shrinkage of the residential market. We will adjust their inventories toward the end of the year for the six-month period. As for other products in inventory shortage, such as utility vehicles, an impact from overall production cutback will be limited because we will increase production.

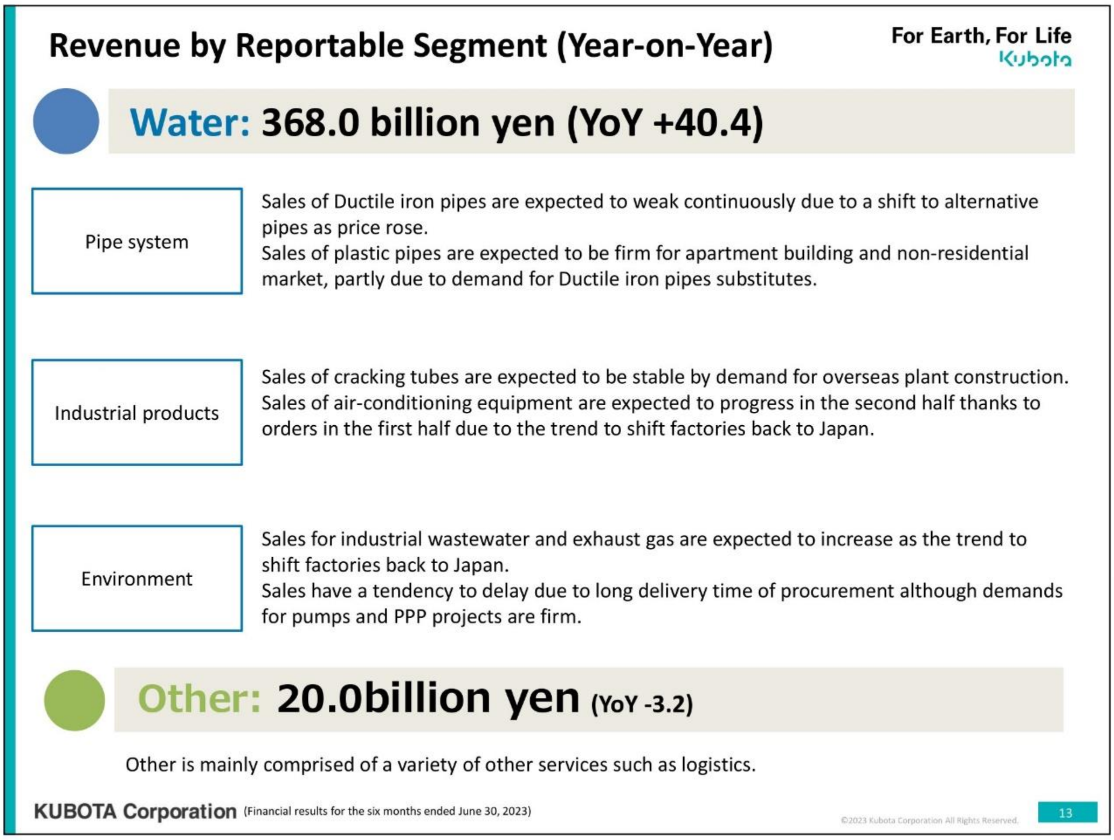
Continuing on, Europe. Sales of construction equipment and engines remained steady, supported by public construction projects. However, the housing market is beginning to shrink in Germany, in addition to France and Italy, and we expect its peak is in this year and then it will be entering a slight adjustment phase from the end of the year.

The tractor market continues to be weak due to a continued decline in investment sentiment. However, Kubota has been able to resolve the inventory shortage that was an issue last year by accelerating shipments, and has recovered its market share in the retail market. We have been accelerating shipments, resulting in an increase in sales.

Next, Asia. As for the market in Thailand, buyers have been reluctant to purchase tractors due to drought concerns caused by El Niño. The drought is forecasted to continue until next spring. Even though rainfall has recovered slightly since July and rice prices are on an upward trend, there are still concerns of pullback on spending, and we expect the market to recover next year or later. Construction equipment sales remained steady as infrastructure works delayed in the pandemic are being recovered.

In the Indian market, although there is a drought trend in the rice filed areas in the southern part of the country, field crops are doing well. In addition, we will soon introduce a new model of Farmtrac that incorporate the Kubota-style manufacturing and development process, which is the bland of Escorts which we acquired, and we are steadily realizing synergies and improvements between the two companies.

As for the Chinese market, the agricultural machinery market has been sluggish as in H1, and the saturation of market inventories is expected to be delayed until next year or later. The government's budget for construction machinery is not expected to be sufficient to stimulate the economy, and we expect the downward trend to continue.

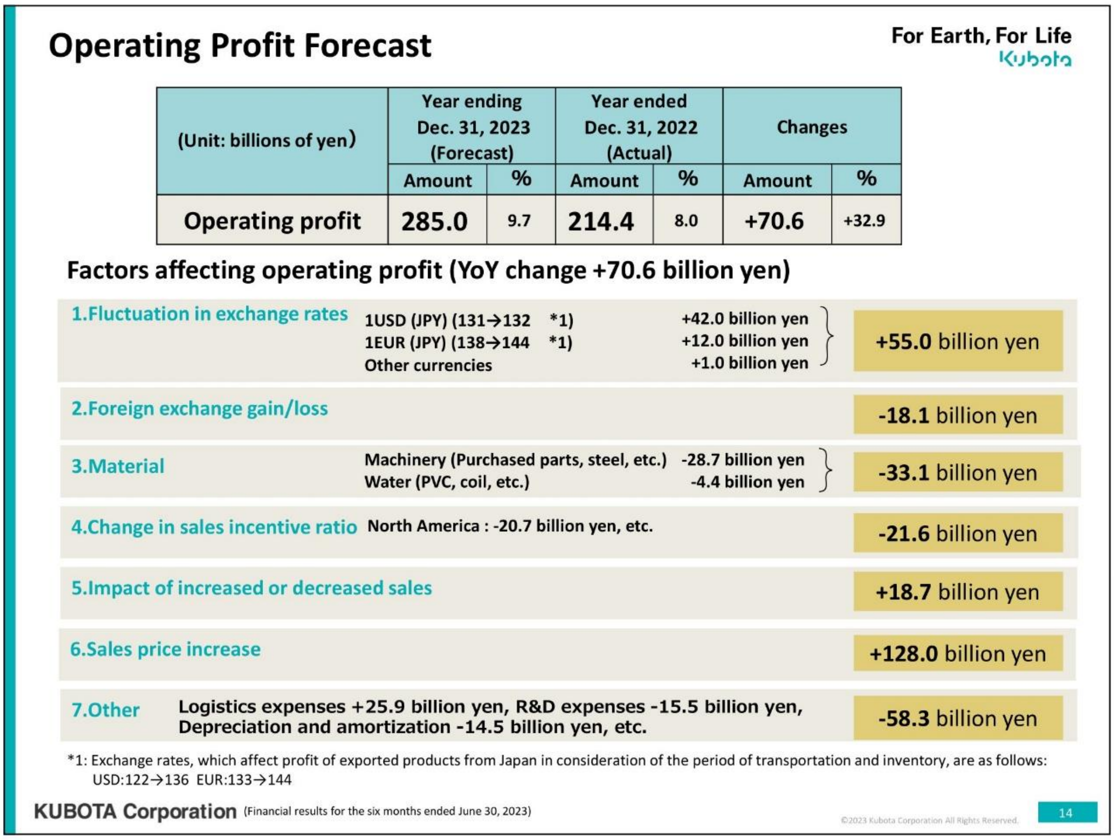


See page 13.

The water and environmental business is expected to generate sales of JPY368 billion. Compared to the previous year, it will be an increase of JPY40.4 billion. However, compared to the initial plan at the beginning of the period, this is a decrease of JPY3 billion.

There are no major changes in market conditions from H1 for pipe systems, industrial products, and environment. Although sales have been adjusted slightly due to delays in projects caused by personnel shortages and procurement problems, demand itself remains unchanged from the initial forecast.

Others is expected to be JPY20 billion.



Operating Profit Forecast

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(Unit: billions of yen)	Year ending Dec. 31, 2023 (Forecast)		Year ended Dec. 31, 2022 (Actual)		Changes	
	Amount	%	Amount	%	Amount	%
Operating profit	285.0	9.7	214.4	8.0	+70.6	+32.9

Factors affecting operating profit (YoY change +70.6 billion yen)

Factor	Details		Total
1.Fluctuation in exchange rates	1USD (JPY) (131→132 *1)	+42.0 billion yen	+55.0 billion yen
	1EUR (JPY) (138→144 *1)	+12.0 billion yen	
	Other currencies	+1.0 billion yen	
2.Foreign exchange gain/loss			-18.1 billion yen
3.Material	Machinery (Purchased parts, steel, etc.)	-28.7 billion yen	-33.1 billion yen
	Water (PVC, coil, etc.)	-4.4 billion yen	
4.Change in sales incentive ratio	North America : -20.7 billion yen, etc.		-21.6 billion yen
5.Impact of increased or decreased sales			+18.7 billion yen
6.Sales price increase			+128.0 billion yen
7.Other	Logistics expenses +25.9 billion yen, R&D expenses -15.5 billion yen, Depreciation and amortization -14.5 billion yen, etc.		-58.3 billion yen

*1: Exchange rates, which affect profit of exported products from Japan in consideration of the period of transportation and inventory, are as follows: USD:122→136 EUR:133→144

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page 14. Now I would like to explain the increase/decrease in operating profit.

Fluctuation in exchange rate is expected to be a positive factor of JPY55 billion increase. Foreign exchange gain/loss is not so much in absolute terms, but since the previous year had seen a large improvement, it is expected to be a negative factor of JPY18.1 billion decrease compared to the previous year.

Raw material is expected to improve significantly from the initial forecast; however, the increase in prices of steel and PVC is a negative factor of JPY33.1 billion decrease in profit. Change in sales incentive ratio is expected to be a negative factor of JPY21.6 billion decrease in profit due to increase in interest rates in the US, which has increased the cost of funding for the Finance business.

Impact of increased or decreased sales is expected to be a positive factor of JPY18.7 billion increase, which was reduced by the decrease in sales in North America and Thailand. Sales price increase is expected to be a positive factor of JPY128 billion, mainly due to the effect of price increase in North America. The remaining JPY58.3 billion of the decrease in profit is accounted for as other factors.

As for a breakdown of others, logistics costs will improve by JPY25.9 billion. On the other hand, R&D expenses will be increased by JPY15.5 billion, depreciation will be increased by JPY14.5 billion due to capital investment, and personnel expenses will be increased by JPY17 billion.

The increase in selling and fixed costs is JPY28.7 billion. The other components and the profit of Escorts Kubota account for the total JPY8.5 billion decrease in profit.

Operating Profit Forecast by Reportable Segment

For Earth, For Life
Kubota

(Unit: billions of yen)		Year ending Dec. 31, 2023 (Forecast)	Year ended Dec. 31, 2022 (Actual)	Changes
Machinery	Revenue	2,562.0	2,326.2	+235.8
	Operating profit	323.0	232.6	+90.4
	OP margin	12.6%	10.0%	+2.6P
Water	Revenue	368.0	327.6	+40.4
	Operating profit	26.0	17.3	+8.8
	OP margin	7.1%	5.3%	+1.8P
Other	Revenue	20.0	23.2	-3.2
	Operating profit	3.0	3.1	-0.1
	OP margin	15.0%	13.3%	+1.7P
Adjustment*	Operating profit	-67.0	-38.5	-28.5
Total	Revenue	2,950.0	2,677.0	+273.0
	Operating profit	285.0	214.4	+70.6
	OP margin	9.7%	8.0%	+1.7P

*Adjustment includes administrative expenses, basic research expenses, and foreign exchange gain/loss at the parent company.

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page 15. Operating profit forecast by segment.

For the machinery business, operating income will be JPY323 billion, an increase of JPY90.4 billion, or 38% over the previous year.

Water and environment is expected to increase by 51% to JPY26 billion, up by JPY8.8 billion.

Others is JPY3 billion, and the detailed item is that the increase in research expenses, resulting in JPY67 billion decrease in profit.

CAPEX, R&D expenses and Dividend

For Earth, For Life
Kubota

■ CAPEX and R&D expenses

(Unit: billions of yen)	Year ending Dec.31 2023 (Forecast)	Year ended Dec.31 2022 (Actual)	Year ended Dec.31 2021 (Actual)
Capital expenditures	180.0	169.4	121.4
R&D expenses	103.8	88.3	65.3

■ Dividend per common share

		Year ending Dec. 31, 2023	Year ended Dec. 31, 2022	Changes
Dividend per common share	Interim	24 yen	22 yen	+2 yen
	Year-end	(Undecided)	22 yen	-
	Total	(Undecided)	44 yen	-

KUBOTA Corporation (Financial results for the six months ended June 30, 2023)

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See page 16. Capital expenditures, and etc.

There is no change in the initial plan for both R&D expenses and capital expenditures.

Regarding shareholder returns, we have increased the interim dividend by JPY2 from the previous year to JPY24. In addition to the JPY20 billion already acquired and retired this fiscal year, an additional JPY10 billion has been set aside for share buybacks. The year-end dividend is undecided at this time.

Finally, I would like to talk about the future.

At the beginning of the year, I said that improving operating profit through operational improvements would be an important point for this year, and we have made some progress in this area.

As for price increases, we will complete passing on material and logistics cost to product prices in this fiscal year as a whole. However, we will continue to move forward in some areas in delays.

Although the effects of the yen's depreciation were offset in the past two years when costs soared, we are finally in a position to capture the effects of the yen's depreciation by passing it on to selling prices. On the other hand, infrastructure costs and labor costs are on the rise, and we will implement measures to address these issues.

In manufacturing, we have placed priority on production volume in order to meet demand in the past, and have repeatedly conducted operations that were somewhat excessive. As for tractors, outsourcing operation to supplement capacity will be cancelled and it will be switched to in-house production. Vice versa, returning in-house production from outsourcing, we are beginning to see an improvement in the factory's profit margin.

In terms of production, CTL, one model of construction equipment was moved from Japan to North American production. Although production will not be at full capacity this year, the first year of the transfer, it has started up smoothly and will contribute to filling CTL's inventory next year, minimizing sales opportunity loss.

With respect to production risk reduction, the buildup of manufacturing component inventories is progressing steadily. In addition, we will control the production volume in line with the market to maintain healthy dealer inventories.

Finally, on the business side, we will continue to review our business portfolio through selection and concentration. As released yesterday, we have decided to review the ductile iron pipe product group. Taking into account the business environment, we will review to balance sales and production costs and optimize the business to a sustainable scale to improve profitability.

In the next fiscal year, there are uncertainties such as a slowdown in the European and Asian markets and the possibility that the yen will become strong. By restoring operations that were damaged during the pandemic within this fiscal year, we will be fully prepared for these uncertainties and promote sustained improvement in operating income.

Now I have explained our consolidated financial results for H1 FY2023 and the outlook for the full year.

Question & Answer

Yoshikawa [M]: I will now take your questions. Please note that we are unable to disclose the forecast for the Indian operations of Escorts Kubota since the company is listed on a stock exchange in India. We appreciate your understanding.

Matsui [M]: Okay, we will now move on to the Q&A session. When the moderator calls your name, please ask your question after stating your company name and your name. Please limit the number of questions to two, so that more people can ask questions. Now, if you have any questions, please ask.

Now, Mr. Sano of JPMorgan Securities, please.

Sano [Q]: Thank you for your explanation. My name is Sano from JPMorgan Securities. Thank you for taking my questions.

My first question that I would like to ask you is about the downside and upside of the small tractor business in the US in H2. First of all, on the downside, I think you will see a decrease in wholesale in H2 due to inventory adjustments, but I am wondering if there is any downside risk in terms of prices, incentives, and etc.?

On the upside, the retail market itself showed a slight increase in June with models in less than 40 horsepower, which was the first increase in 16 months. I think housing starts and the US stock market will also have a positive effect. I wonder if announcement of new products release at dealer meetings or in the dealer network can be a positive factor. How do you view those upside risks? Please comment on that area.

Yoshikawa [A]: I, Yoshikawa, would like to answer. First of all, I would like to answer that there has been no significant change in prices, incentives, although it will change depend on competition. As I mentioned earlier, we have been steadily raising prices and passing on the prices to our customers in North America, as is the same for other companies. It has been steadily penetrating.

Other companies are maintaining strong incentives and 0% financing, and we are doing the same. However, there has not been a difference compared to other companies, so we think it is not necessary to assume much of a negative impact in this area.

On the upside, we need to consider two things about the small tractor market this year. One is that we may have captured a little bit of future demand in the midst of nesting demand in 2020 or 2021, as well as promoting the 0% financing program. I think that the market has seen a rebound in the last year or this year.

As I mentioned earlier, the temperature did not rise in the US in March and April this year. Since our small tractors are mainly used for mowing, there was a delay in the start-up of the market, and it has shrunk especially in March, April, and May.

However, while there is a backlash, we are not aware that this will continue to decrease, although I have said that it will be at the 2018 level. I believe that demand from people who enjoy country life in the suburbs is solid, and although it may take some time, I think we can expect to see another growth phase as early as next year or later. We are thinking that we will have to wait and see a little more.

This is the answer to your question.

Sano [Q]: Thank you, Mr. Yoshikawa. Second, I would like to ask a little more about the background of your strategy regarding the partial integration of ductile iron pipes in the water and environment business.

I believe the current profit margin for water and environment is 7.1% for the current fiscal year. In light of the goals of the mid-term plan, what is the current approach to the profitability of this iron pipe part, and what kind of profit margin or positive effect in terms of ROIC are expected for 2026 years and beyond as a result of this decision? Please give us your views on this area.

Yoshikawa [M]: Then, first of all, I would like to have Kondo, General Manager of Water and Environment Infrastructure Management Department, to explain a little about the background of the decision of transferring the iron pipes this time.

Kondo [A]: I am Kondo from the Water and Environment Infrastructure Management Department. I would like to explain the background of the merger announced yesterday between our company and Nippon Chutetsukan, with the aim of establishing a joint manufacturing company in 2026.

First of all, as background, the demand for ductile iron pipes has decreased by about half over the past 20 years. The first point is that the industry as a whole, including our company, has excess production facilities as it has shrunk by 30% in the past 10 years.

The second point is to response to carbon neutrality. Cupola furnaces in this industry has a fairly large impact on CO2 emissions, so we are working on switching them to electric furnaces. We have also switched to electric furnaces at our Hanshin Plant in Amagasaki, but when we consider CO2 emissions as the industry point of view, it may be difficult to continue to maintain cupola furnaces.

The purpose of this collaboration with Nippon Chutetsukan is to continue the stable supply of water pipes as I just mentioned, which are indispensable to the social infrastructure, and to achieve carbon neutrality through the transfer of production. We are in the discussion to protect the employment of all employees.

Yoshikawa [A]: I, Yoshikawa, would like to give supplemental information for Mr. Sano's question.

Ductile iron pipe is a highly public product, and we consider it important to fulfill our responsibility to supply it. On the other hand, as Kondo just explained, if we continue to maintain our facilities and invest in electric furnaces while the market shrinks significantly, the cost will become higher and higher. Although we may be able to fulfill our responsibility to supply in terms of quantity, we may not be able to fulfill our responsibility to supply in terms of price.

This will cause inconvenience to our customers. So we, Kubota, which has the largest market share in the industry, will take an initiative in talking with Nippon Chutetsukan to downsize the production facilities to an appropriate scale in order to fulfill our responsibility to supply products both in terms of volume and price.

On the other hand, we are a private company, so we naturally have to consider profit. In this case, we are naturally considering securing and improving the return on invested capital, as you pointed out, while optimizing the scale of facilities.

As for the pipe-related business in future, it will not only be limited to the hardware business such as manufacturing and sales of pipes as well as water piping works, but also there are changes in demands from both private and public sectors and we are having more opportunities to offer solutions to address various issues related to waterworks.

We will find business opportunities in these areas, and our company-wide target is to achieve an operating income margin of 12% or 13% of net sales. The entire company is facing the challenge of securing return on invested capital while also taking into consideration the cost of capital. We would like to make our pipe system business capable to accommodate these tasks, and we recognize that this decision will contribute to that end.

Sano [M]: Thank you very much for the details. That's all from me.

Matsui [M]: Thank you very much. Next, Mr. Mizuno, UBS Securities. Please ask your questions.

Mizuno [Q]: My name is Mizuno from UBS Securities. Thank you for taking my questions. Two questions please.

First of all, six months ago, President Kitao commented that 2023 would be a year of change, and I would like to ask how the Company is responding to this comment.

I would like to ask you about the revenue aspect. Looking at the contents of the increase and decrease in operating profit, and if I take out Q2 only, labor and distribution costs have already contributed to the increase in profit in the same period of the previous year. I think that the degree of decrease in the fixed costs is also decreasing compared to the Company's plan.

In the area of cost reduction, where you have set a figure of JPY50 billion for net profit increase, in your mid-term plan, for example. I would like to know how much progress you have made in this fiscal year, or whether you can already see an upside to your target by 2025.

In your explanation earlier, you mentioned measures to efficiently control personnel costs. I would appreciate it if you could tell me what exactly you have in mind. Please.

Yoshikawa [A]: Thank you, Mr. Mizuno. I would like to answer your questions.

We want this year to be a year of change, and we want to normalize our operations, which have been quite disrupted for the last two years. As I mentioned earlier, we have been working to normalize production and inventories, and I believe we have made some progress in this regard.

Second, in our mid-term plan, we have stated that we will review our product and business portfolios and promote structural reform of our businesses. Steel pipe, that I mentioned earlier, is one example, and we are also reviewing various other products and businesses. We believe we are making some progress in this area.

As for the JPY50 billion that Mizuno-san just mentioned, it is true that we are curbing the increase in fixed costs or reducing in some areas by improving operational efficiency, and etc. In the machinery business and the water and environmental business, the increase in sales of service parts is expected to be a source of earnings. In water and environment, our medium-term plan calls for strengthening and expanding our plant operation and maintenance business, which is more like a stock business than a flow business. I think such effects are included in the JPY50 billion.

In this sense, we have made a certain amount of progress in increasing sales of service parts. As for O&M, both volume and profitability are improving in the water and environmental business. I would like to give a little more push toward 2025.

In that sense, we are making a certain amount of progress, and I hope you understand that we are making progress online. However, I would appreciate it if you allow us to have a little more time to see if we can move to the upside. In order to improve and expand our operations, service parts, and O&M, as I mentioned earlier, it is necessary to utilize various digital technologies. We are seeing certain results, including progress in the utilization of these things. That is all.

Mizuno [Q]: Thank you very much. Second, could you please confirm the numbers, or rather, tell us where you are positioned in terms of numbers in the mid-term plan? I had a look at your integrated report and it seems to me that the two numbers are mixed up. In terms of operating income this fiscal year, I think you will come pretty close to the JPY300 billion in operating income that you originally proposed. The other figure is the JPY360 billion that the president mentioned six months ago.

These two figures are mixed together in the integrated report and I would like to know which figures the Company takes and operates with right now. I would like to know which way the Company takes or unifies the two and when is the timing. Should we consider the amount of investment and the Company's approach toward it, for example, and should we consider any changes in the contents of the financial statements for the next fiscal year? Please explain this area, although it is outside of the financial results.

Yoshikawa [A]: First of all, we announced the JPY300 billion figure in our mid-term plan two years ago in February. Also, the JPY360 billion in operating profit that you mentioned is the figure mentioned in February of this year. In that sense, I hope you understand that at this point we are moving toward with operating income of JPY360 billion, but there are some major differences from the stage of the mid-term plan.

For example, the acquisition of Escorts Kubota in India was not included in the mid-term plan. Also, there are both positive and negative aspects to the market's view of various businesses. I believe it is working positively overall.

On the other hand, as of this spring, material and logistics costs are very much on the rise. In response, we have to pass it on to the product price. That was this February. It has been progressing as planned, and sales have been rising due to M&A and price hikes, partly due to foreign exchange rates. We have to make sure to secure a solid operating profit in this situation.

Since the denominator has increased considerably due to M&A and price increases, we have lowered our target of 13% operating margin in the original mid-term plan, and are now aiming for 12%.

In this sense, JPY3 trillion [is for] JPY360 billion. With the yen's depreciation, sales are coming very close to JPY3 trillion. Even if the yen appreciates slightly, we would like to be able to maintain stable sales of JPY3 trillion and an operating profit margin of about 12%. Our goal for 2025 is to bring the business to such a state of operation. That is all.

Mizuno [M]: I understand. Thank you very much. I am wishing for the best.

Matsui [M]: Thank you very much. We apologize, but due to time constraints, please limit to one question per person, as we are receiving multiple questions per person now.

Mr. Sasaki, of Mitsubishi UFJ Morgan Stanley Securities, please ask your questions.

Tsubasa Sasaki [Q]: My name is Sasaki from Mitsubishi UFJ Morgan Stanley Securities. One question from me, but let me ask an additional question to the person who just asked.

I believe that the full-year plan has been revised upward this time, and you have set a target of JPY285 billion in operating profit. I also think that the probability of achieving the JPY360 billion goal in the new medium-term plan is increasing, and I would like to know what, in your view, will be the performance drivers to achieve an increase in profit of approximately JPY75 billion from this fiscal year to the year of the new medium-term plan.

Can you please tell me what, if any, specific factors that would bring JPY285 billion to JPY360 billion and expand the performance of the Company? For example, the growth of Thailand and India, and also the growth of construction equipment in North America. I would also like to know how you plan to achieve JPY285 billion of this fiscal to JPY360 billion, including the operational improvements you mentioned earlier. I would appreciate it if you could give me an idea of what you have in mind for the performance expansion plan.

Yoshikawa [A]: Thank you, Mr. Sasaki.

Basically, the themes that we expect to increase our sales have not changed significantly from those listed in our mid-term plan. I mentioned construction equipment in North America, and I also mentioned the growing demand in the ASEAN region. Although there may be some differences and fluctuations in business sentiment, I think we can expect this to continue in the future. I also think that India is just now being added to that list. I think those are the areas expected to increase in terms of top lines.

However, in order to generate a stable profit of JPY360 billion, we need to increase the top line and secure profit from increased sales at the same time. So we would need to focus more on operational stability. In the past, we had been manufacturing and delivering products in a quantity-driven manner, rather than cost-driven, as the quantity of products and demand were increasing.

I think there is still room for cost reduction within the Company. The business operation in India is contributing to increased sales, but it will also contribute to cost reductions in procurement. We also think India can become a development base in future. I think there is room to increase product competitiveness in such areas and strengthen it, including price competitiveness, rather than market growth.

Also, as I mentioned earlier, it will contribute to an increase in the top line of course but we are planning to further strengthen our solutions business in the water and environment business, as well as service parts and operations, as those businesses have high profitability potential. We would like to increase these activities in order to build a business structure that can stably generate JPY360 billion, which is a slightly high goal, but we will continue to aim for it.

That is our answer to your question.

Tsubasa Sasaki [Q]: If you do what Mr. Yoshikawa just mentioned, it will probably be done. That is the way I should look at it.

Yoshikawa [A]: Yes, that's fine.

Tsubasa Sasaki [M]: I understand very well. Clear. Thank you very much.

Matsui [M]: Thank you very much. Next, Mr. Maekawa, Nomura Securities. Please ask your questions.

Maekawa [Q]: My name is Maekawa from Nomura Securities. Thank you very much for your explanation. Just one quick point.

As for the situation in North America, there is a bit of overlap but inventory is now adjusting, especially for small tractors. I understand that this inventory adjustment will be completed by the end of this year, including a retail view for next year.

With the current 2018 level of retailing, or it may be a little less than that, at around 13,000 units in Q3 and Q4, as the current wholesale number is at around 11,000 units. I personally think that it is uncertain whether inventory can be sufficiently reduced, considering these figures to be honest. On the other hand, if retailing in the next year is rising quite a bit, or possibly from about Q4, there may be enough inventory adjustment at the current wholesale level, at 11,000 units or so.

I would like to know your view of retailing business in the next year including in those numbers in mind, and also the length of inventory adjustment and how should we have an image. I would like to know if there is a possibility that you put on the brakes further, in some cases. I would appreciate it if you can comment on this area as well. Please.

Yoshikawa [A]: Thank you, Mr. Maekawa.

First, I would like to watch the economic situation a bit more and make a decision on how to view next year once we have a better resolution. However, small tractors in particular, are used for mowing applications mainly, so unless dealers have ample inventory in March, they will not be able to sell them. So they will build up some inventory toward March.

However, we are still focusing on maintaining inventory at an appropriate level. So if retail sales drop a little, as is the case of this year, we will make adjustments in H2 to maintain an appropriate level. We would like to ensure discipline here.

As for next year, I am not so pessimistic at this point, but there may be some decrease due to the pent up demand that had been consumed as I mentioned earlier, but I have a feeling that the bottom is about to be hit, so I would like to make a decision while watching the situation a little longer. I think there is a range still between an optimistic view and a pessimistic view for small tractors.

In North America, however, construction equipment and utility vehicles are doing very well as I mentioned earlier. Although the mowing related products had a slow start due to the late arrival of spring, we do not feel that our current situation is weak.

In this regard, for the items such as utility vehicles and moving related which we lost a great deal of inventory last year because we were unable to produce them, retail sales have been steadily increasing as we have been able to fill our inventories. I think there is a possibility for these three products, which are construction equipment, utility vehicles and mowing related, to turn into a virtuous cycle for the next year, as we can increase retail sales by fulfilling inventory.

We will have to wait and see, but I am not too pessimistic about this either.

Maekawa [Q]: I understand. Thank you for mentioning construction equipment and utility vehicles. You also mentioned on page 12 that it is at a turning point in the dairy and agricultural market with regard to medium tractors. How should we look at this?

Yoshikawa [A]: As I mentioned earlier, agricultural commodity prices have been weakening a bit which had been rather rising, so I use the term “turning point” in that sense.

However, since the market is somewhat firm, we do not expect it to shrink too rapidly. In fact, until last year or the beginning of this year, dealers had machines but no implements to do the jobs. I think there are enough factors to secure the same level of retail and wholesale sales as this year by stocking well in these areas.

As I said, I would like to take a closer look at the situation and make a decision, the same as the small tractors.

Maekawa [M]: I understand. Thank you very much.

Matsui [M]: Thank you very much. Next, Mr. Isayama, Goldman Sachs. Please ask your questions.

Isayama [Q]: Thank you for your help as always. I am Isayama from Goldman Sachs. Thank you for taking my questions.

I am also concerned about inventory trends in North America, as Mr. Maekawa just asked, but this time, it is for construction equipment. Could you please comment separately on CTL and mini-excavators, respectively?

When I asked the same question six months ago, I think you mentioned that the CTL was still very tight and mini-excavators were building up a little bit. I would appreciate it if you could also mention characteristics of demands: one for the residential market, one for the commercial market, and one for the rental market.

Yoshikawa [A]: To answer your question, I don't see much change in the market environment. In fact, we feel that our retail business is determined by the availability of inventory at dealers.

Right now, as of the end of June, we only have about two months to three months of construction equipment inventory as a whole. We have are shy of 8,000 units but I would like you to know that we have about 800 dealers and stores in the US, so each of them has about 10 units in stock.

Backhoes range in size from 3 tons and less to 8 tons in various shapes. CTL, SSL, and others have many models in each as well. Therefore, an average inventory of 10 units per dealer is very low and this situation is ongoing. As you mentioned earlier, there were more backhoes. But, retail sales of backhoes have been rapidly increasing, and at this point, there is a shortage of both types of equipment.

Isayama [Q]: On the demand side, is it correct to think that normalization and restocking of inventory will not be completed in this fiscal year? Can you tell me again whether it will take more time until next year or not?

Yoshikawa [A]: We are working very hard to produce construction equipment, but with the increasing demand worldwide, I think it will be difficult to meet the demand.

Of course, this will depend on how the North American market for construction machinery develops in the future, but if the current retail situation continues, there is a strong possibility that the buildup of appropriate inventory will be delayed until the next fiscal year. This is because there are more retail needs than expected, which is not a bad thing for us. But unfortunately, we are still unable to fully meet the needs of our dealers.

Isayama [M]: I understand very well. Thank you very much.

Matsui [M]: Thank you very much. We have received other questions, but we have reached the end of our scheduled time, so we will now conclude the question and answer session.

With that, we now end the briefing. Thank you for attending today's briefing session.

[END]

Document Notes

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