Q&A for Telephone Briefing, FY2018 Nine-months Results (Summary)
Yaskawa Electric Corporation
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[Speakers]
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(Note):
Motion Control: Motion Control segment
AC servo: AC servo & controller business (Motion Control segment)
Drives: Drives business (Motion Control segment)
Robotics: Robotics segment
System Engineering: System Engineering segment
Other: Other segment

Q As per the fluctuation in quarterly orders on page 25 of the supplementary material, and for the period of September to November in FY2018, how is it like when dividing the fluctuation of each business by region?

A ・AC Servo
Japan: -26% YoY; -15% QoQ; the Americas: -38% YoY; +12% QoQ;
Europe: -12% YoY; -0% QoQ; China: -16% YoY; -21% QoQ;
Asia except China: -37% YoY; -24% QoQ.

・Drives
Japan: +7% YoY; -9% QoQ; the Americas: +34% YoY; +18% QoQ;
Europe: -10% YoY; -11% QoQ; China: -17% YoY; -19% QoQ;
Asia except China: -11% YoY; +2% QoQ.

・Robotics
Japan: +1% YoY; +4% QoQ; the Americas: -10% YoY; -4% QoQ;
Europe: -3% YoY; +7% QoQ; China: -22% YoY; -26% QoQ;
Asia except China: -10% YoY; -10% QoQ.

Q It seems that the inventory level is high and turnover period is prolonged despite production adjustment. What are your thoughts on inventory and production?

A ・We maintained the initial production plan in 3Q but resulted in the increase in inventory by around 4 billion yen in Motion Control and Robotics due to the slower order than expected.
・We are planning to reduce the inventory by abound 4 billion yen in 4Q.

Q There was a gain on acquisition of subsidiary by +6 billion yen on extraordinary profit. Are there any events expected in 4Q?

A ・We had a profit of +3 billion yen from the balance of negative goodwill of acquiring Suematsu Kyuki Co., Ltd. as a consolidated subsidiary in 1Q and a loss on step acquisition in the existing equity.

・In addition, we acquired the 50% equity of Yaskawa Siemens Automation & Drives Corp. (YSAD) from Siemens K.K. in accordance with making YSAD our wholly owned subsidiary in 3Q. This occurred gain on step acquisition by +3 billion yen due to the acquisition in higher price including goodwill than the book value of the equity.

・We expect extraordinary loss by around 0.5 billion yen in 4Q.

Q What is the main factor of the downward revision this time? Please share what changed in business environment since the forecast 3 months ago.

A ・We saw slow recovery in the semiconductor investment in AC servo business. The lingering trade friction between the U.S. and China also caused the slow investment. We had to take these impact into account.

・In Robotics, there were some orders pushed back into sales in 4Q due to issues of financing. We also pushed back some orders into the sales of the next fiscal year considering such delay.

Q How do you see the impact of U.S.-China trade friction?

A ・Keeping the volume of smartphone production, the industry is forced into automation in order to prevent profit from deteriorating due to labor shortages and increase in wages. It seems that the investment is resuming gradually thanks to the monetary relaxation by the government.

・We think that the situation will go back to normal soon due to the full-fledged government's intervention. The concerns related to the trade friction are gradually being overcome.

Q There was a huge decline in operating rate excluding the impact from unrealized profit in 3Q. What was the background of this?

A ・To compare with the same period of the last year, we built up inventory in 3Q of the last fiscal year while there was a little of it this year. And this led the gap in the operating rate.

Q In China, there are increasing companies which go into bankruptcy or carry out restructuring and the economy index shows deterioration. Do you think that the momentum of investment in automation and efficiency will be maintained?

A ・There is not likely restructuring in manufacturing industry. There seem to be some companies that went into bankruptcy due to the environmental regulation, but leading companies have intention to improve their profit through investment without increasing the number of employments.

・Those companies being eliminated haven't introduced automation in the first place. As manufacturing industry is still struggling to hire people and facing wage increase, it is not likely for the surviving companies to stop investments in automation.

Q Please explain the trends in the AC servo orders in China in 3Q.

A ・The order reached the bottom in September and has been in the recovering trend since October. The recovering speed is slower than expected.

Q Please share how you see the AC servo business from 4Q through 1Q in the next fiscal year.

A ・The investment in semiconductor didn't reach the expected level due to the partial push back although we had estimated it as the base of the recovery of AC servo in the last financial announcement (2Q). Recently, it is gradually recovering, and we see that it will not show a double bottom as SPE companies are not planning to reduce their production. Thanks to the effect of the financial relaxation in China, it is expected to see active investment toward Chinese New Year although there are less projects of large-scale investment compared to the last year. There is a reduction of income tax from the beginning of this year as well, so we see that the AC servo business will go on the recovery trend toward 1Q of the next fiscal year as China as a whole improves in financing.

Q In the 2Q financial results briefing held in October 2018, President Ogasawara mentioned that the quarterly order of AC servo will show a year-on-year increase in 2Q of fiscal 2019. How do you see it now?

A ・We see that it will possibly increase year-on-year in 2Q of fiscal 2019. It will definitely show the increase in 3Q.

Q How was the operating rate of AC servo production in 3Q?

A ・It was around 80-85%.

Q What thoughts do you have with the contribution of operation in Yaskawa Solution Factory to profits?

A ・Thanks to the smooth-flowing production without generating in-process inventory and multiproduct variable quantity production, we are demonstrating a large improvement in productivity. Although it is applied to Σ-7 production in Japan alone now, we aim to expand the effect by increasing in its volume.

Q What is the composition ratio of AC servo sales in 3Q (9 months total) by region?

A ・They were 32.6% in Japan, 16.5% in the Americas, 9.0% in Europe, 25.1% in China, 16.2% in other Asian countries.

Q What is the recent rate of AC servo orders for smartphone in China?

A ・We haven't heard any large orders as they stop the investment in smartphone, but we still receive orders related to glass processing.

・In addition, we see some orders for the test purpose in view of 5G migration.

・Our forecast of the ratio of order for semiconductor, LCD and electronic component which are highly related to smartphone is over 30% globally. We cannot see how much of it would go to smartphone.

・In China, electronic component is the market which is highly-related to smartphone that accounts for about 20%.

Q Please share the ratio of AC servo and Drives in Motion Control sales and the gaps of profitability in 3Q and 4Q.

A ・In 3Q, the ratio of AC servo business was 61%, while Drives business was 39%. There is almost no difference in profit ratios.

・In 4Q, the ratio of AC servo business is 62%, while Drives business is 38%. We expect a slightly higher profitability for AC servo.

Q Although the orders for drives in the U.S. are said to be favorable, are there any concerns of its slowing down as the oil price is declining?

A ・It is true that the oil price is declining, but its volume of production is to be increased as the U.S. policy and is still on a high level.

Q As you can see on page 25 of the supplements to financial results, the orders for both Motion Control and Robotics declined in 3Q while you have a sales plan that Motion Control remains flat and Robotics increase in 4Q. How do you achieve this sales plan in 4Q?

A ・We plan to increase the sales while reducing the inventory in 4Q. We stock robots produced in 3Q in overseas subsidiaries as the inventory and plan to sum up the sales in 4Q.

Q As the production and sales of automobile slow, how do you see the Robotics business from now onward which has a high exposure to auto market? How is the demand from 4Q through 1Q in the next fiscal year?

A ・Auto sales and capital investment does not necessarily link; therefore, the current demand for Robotics in auto market is still robust. Auto sales in China are slowing down but the demand for robotics is not declining much. The investment in automation should recover once the issues of financing or U.S.-China trade friction is resolved. We see that capital investment in auto market will be better next fiscal year than this fiscal year globally.

Q What is the background of decreased orders in Robotics in China QoQ?

A ・Deteriorated financial condition in 3C (consumer electronics, communication equipment, etc.) markets and small- to medium-sized enterprises largely affected Robotics orders. The investment in automation should recover once there are improvement in financing and clear direction in U.S.-China trade friction.

Q Is it possible to continue double-digit profitability in Robotics from now onward?

A ・We have been able to maintain the profitability at 10% level with the current volume, so that it is possible to keep that level if there wouldn't be a sharp decline in the volume in the future.

・We also think it is possible to increase in profitability on the grounds of increase in sales in the next fiscal year as well as the effect of the productivity improvement in factories and introduction of new products. We aim to achieve 15% of operating profit margin during the next mid-term period.

Q It is likely that there will be negative impact from reduced operating rate in 4Q, while the plan for the profit of Robotics is to increase in 4Q. Please share the reason of this.

A ・We plan to sell the inventory in 4Q and generate profit through increased sales volume.

Q How do you see the sustainability of the largely improved profitability in System Engineering in the future?

A ・What worked against the business performance last year were the two subsidiaries in clean power business and the operation in Japan.

・Wind-power generation related business became profitable thanks to the selection and concentration.

・Photovoltaic-related business improved the profitability by the introduction of new product and restructuring at the same time. We expect to become profitable in the latter half of the next fiscal year.

・System Engineering business will transfer its steel plant engineering business to Yaskawa Automation & Drives Corp. in order to realize operational efficiency and enhancement of sales.

・We aim to realize the profitability of 5% in System Engineering from the next fiscal year.

Q Profit attributable to the owners of the parent is forecast to reach the record high in this fiscal year partially thanks to the extraordinary profit and the impact of tax rate, which lead the annual dividend plan to remain at 52 yen. Please share your thoughts for the next fiscal year.

A ・The whole extraordinary profit of 6 billion yen became profit of this period as the tax effect is not included.

・We have to pile up our operating profit since we are not expecting such a special factor in the next fiscal year.

・To consider the current situation that we hit the bottom of order in 2H of this fiscal year and it is going to recover in China from now on, we see that the situation will not worsen in 1H of the next fiscal year. We can expect the prior investment in 5G and data center investment in 2H of the next fiscal year so that semiconductor-related business will gain momentum.

・If the same level of 1H of this fiscal year is realized in 2H of the next fiscal year, we can expect an increase in operating profit.

・We aim at 30% of payout ratio in 2020 in the long-term management plan "Vision 2025" and plan to increase from that level, so 30% is not the ceiling. We will clarify how to improve it in the next mid-term management plan.

・We carried out share buyback during this fiscal year and would like to consider it continuously from the view point of total return ration as well in order to plan returns as much as possible.