SWCC Co., Ltd.
Summary of Q&A Session at the Meeting for Institutional Investors
(Financial Results for Q1 FY3/24)
Date and time:
Monday, September 4, 2023
Part 1: 14:30-15:30, Part2: 16:00-17:00
Location: Nihonbashi Kabutocho, Chuo-ku, Tokyo

Rolling Medium-term Management Plan

Q: When rolling out the medium-term plan, will you be revising the overall figures, including final sales and operating profit targets, or will you only be changing the figures for the breakdown within segments without making significant changes to the overall plan?

A: The current medium-term plan sets a target of 15 billion yen in operating profit for the final year. However, we aim to increase our profits by investing in areas where we have a competitive advantage. The performance of the Energy and Infrastructure Business is approaching the target figures, and we are working on further improving its performance. Regarding the rolling over of the medium-term plan, our intention is to revise the target figures upwards for the overall plan rather than making extensive adjustments between segments. We will consider the target figures in light of uncertainties in the outlook for the global economy, including relations between the US and China, but we do not expect the figures to be lower in the current outlook

Q: Regarding the target profits by segment in the medium-term plan, the profit plan for the Energy and Infrastructure Business for this fiscal year appears to be close to the target profit in the medium-term business plan, while the Communication and Industrial Devices Business and the Electrical Equipment and Components Business seem weak. Could you please share your thoughts on the performance of each segment and the strategies to enhance performance over the remaining years?

A: The operating profit target for the Energy and Infrastructure Business in the final year of the medium-term plan is 8 billion yen, but this was a plan formulated in 2021. Considering the potential impact of the revised measures, we believe that the CAGR (Compound Annual Growth Rate) in the power market could exceed our current assumptions. Taking this market growth into account, we are thoroughly examining how to surpass the target figure. We aim to achieve a double-digit growth.

A: Regarding the Electrical Equipment and Components Business, while this fiscal year's operating profit target is 15 billion yen, the final year's target in the medium-term plan is 26 billion yen. In this business, we have a plan to steadily increase production investments throughout the medium-term period to meet the growing demand for the increasing adoption of xEVs. We currently have a strong foothold, and we are considering how we can achieve the operating profit target for FY2030 of 46 billion yen ahead of schedule.

A: As for the Communication and Industrial Devices Business, the largest deviation exists between the current figures and the final year's target in the medium-term plan. Over the past three years, our activities have been restricted due to the COVID-19 pandemic. There have been challenges such as the lockdown in Shanghai, significant supply chain disruptions, and difficulties in sourcing materials. However, during this period, we have been actively seeking local sources for materials, establishing new relationships with various material manufacturers, and creating a situation where we can handle similar challenges in the future. Leveraging this strength, we aim to recover from the impact of the pandemic, particularly in sales of wire harnesses and precision devices. While precision devices include products for individuals, office copiers, and industrial printing machines, the latter is a growing area, and we have seen an increase in order quantities.

Energy and Infrastructure Business

Q: What are your thoughts on when the performance of the Energy and Infrastructure Business is likely to peak and where do you see it as a target?

A: 2026 is a significant turning point. Performance in this area is expected to remain strong until 2026. This is due to the demand for the renewal of thermal power generation. Currently, thermal power generation accounts for 70% of the total electricity generation. However, the government's goal is to increase the share of renewable energy to 50% by 2030. Nevertheless, it's challenging to reduce thermal power generation to below 50% in terms of power supply stability. Therefore, we anticipate that the demand for the renewal of thermal power generation will continue for a considerable time. In the renewable energy expansion and power grid reinforcement projects, out of the government's 7 trillion yen plan, 3 trillion yen is allocated to undersea cables, and the remaining 4 trillion yen is in the market that we are foreseeing. We expect that this market will have sustained demand, at least until 2030 or even up to 2040.

Q: I would like to ask about the issue of labor shortage. Are there any instances where a shortage of construction personnel is posing challenges to the growth of SICONEX® and SICOPLUS®?

A: Securing construction personnel is indeed a very challenging situation at present. We consider this a problem that cannot be solved by our company alone. As a result, we are actively engaged in collaborations with various entities such as the EXEO Group, power companies, and construction firms. Among these, we have already completed the education of around 50 individuals at our in-house Construction Personnel Development Center. Furthermore, we are currently planning how extensively we can expand our network of collaborating companies. We have established a system where individuals who have received our construction education can assist with work at any time, and we are also progressing in seeking assistance from individuals overseas.

Q: I would like to confirm the collaboration scheme. Is it expected to increase profitability by collaborating with other companies in the special high-voltage area? Are there concerns about profitability decreasing as a result?

A: There is a possibility that profitability may decrease, but we are actively working on establishing a framework that enhances the ease of construction for cable specifications, connection materials, and terminal materials while keeping costs down.

Q: Is it correct to assume that an increase in the number of collaborating partners will lead to an increase in orders, thus expanding revenue?

A: That's correct.

Q: How will SFCC improve the ROIC in the construction sector?

A: SFCC achieved a cost reduction effect of 500 million yen through the integration of manufacturing and sales in July last year. We've reviewed selling prices and consolidated four factories into two, creating more productive facilities. Among the three initiatives we've set out, the first one is to improve gross profit. This includes some price increases but also increasing sales of high-margin differentiated products. The second initiative involves using the MTA method to align inventory with demand. The third one focuses on business processes and advancing improvements using AI technology.

Electrical Equipment and Components Business

Q: You are expecting growth in demand for xEV products, but in a competitive landscape with other suppliers, what are your strengths and challenges in gaining market share?

A: We manufacture the high-performance oxygen-free copper MiDIP®, which is the foundation for producing rectangular winding wires for automotive applications, in-house. Our strength lies in our advanced processing technology. As for challenges, while we receive a substantial number of inquiries, our focus is on increasing production capacity and improving the speed of product development to meet the demand.

Q: I anticipate that the profit margin will increase in the future, but I'd like to know the timeline for this.

A: We plan to increase the sales of highly processed products to secure a double-digit operating profit margin. We aim to do this starting from 2026 for Urban Air Mobility and around 2025 for Robotics and Precision Motors. We believe we can meet significant expectations in the next medium-term plan.

Q: Do you anticipate being able to achieve a 10% profit margin in this business by 2030?

A: That's correct.

Q: You mentioned the risk of Chinese manufacturers entering the market. How do you plan to address this?

A: Chinese manufacturers offer lower component costs. It's not just a matter of price, and it's honestly uncertain how far their presence will expand domestically. Our products are mainly adopted by Japanese manufacturers, but we have also heard of their adoption in the European and North American markets. While we are monitoring the risks associated with China, there are many growing markets that we can expand into.

Q: Are you considering selling to Chinese manufacturers?

A: We have heard that Chinese manufacturers are transitioning from round wires to rectangular winding wires for motors, and we anticipate an increase in demand. However, for products intended for Chinese manufacturers, we plan to address this through joint ventures.

Q: Your company seems to have an image of significant expansion for its attractive products in the future. However, the final year of the medium-term plan with an operating profit target of 2.6 billion yen appears rather modest in comparison. I would appreciate an explanation, including your approach to ROIC.

A: In terms of profit margin, we plan to change the product portfolio in the future to address the issue of low profit margins. If we consider unit profit from wire materials as 1, it becomes 10 times for rectangular winding wires, and for applications like Urban Air Mobility, semiconductors, and robotics, it can be 50 to 100 times. Therefore, increasing the level of processing will lead to an improvement in profit margins. In the future, the challenge is to increase the development speed while making use of the Mobility Development Center. ROIC in this business involves melting copper to make rough wire materials, and it is a business with good capital cost turnover. The approach is to raise ROIC by increasing profit margins in addition to the good capital cost turnover rate.

Communication and Industrial Devices Business

Q: There was talk of a slowdown in the Chinese economy. What is your view of the profit margin for wire harness products for local manufacturers?

A: We expect a tough price competition in products targeting local manufacturers. We are working on a comprehensive process review, including automation, to reduce the significant portion of costs attributed to processing. Moreover, the gross margin for the new areas that our company is venturing into is approximately 5-10% higher. We are not just focusing on main harnesses for automotive, but also targeting new markets like ADAS.

Q: If the decline in demand due to the COVID-19 pandemic returns, is it reasonable to consider a 10% operating profit margin?

A: We believe that aiming for a double-digit operating profit margin is achievable.

Shareholder Returns

Q: I would like to know the evaluation of the current stock price level and any measures related to it.

A: The current stock price level is currently below a PBR (Price-to-Book Ratio) of 1x. Our goal is to reach a PBR of 1x as soon as possible. Increasing our earnings steadily is one approach to achieving this goal. Additionally, we are committed to returning value to our shareholders. While we have disclosed a target of a dividend of 120 yen or more for the fiscal year 2026, we are also considering how to proceed with shareholder returns, including share buybacks, in the future.

Degree of dependence on China

Q: I would like to inquire about the degree of dependence on China. Specifically, I would like to know the recent sales and procurement composition of China's share, and in the event of a slowdown in the Chinese economy or further decoupling between the U.S. and China, I'd like to understand the potential impact on your company's performance and the corresponding measures.

A: The sales ratio for China within the group is approximately around 7%. While not a significant portion, it holds a substantial share within the context of our overall overseas revenue, which stands at around 9%. Particularly, the sales in the wire harness business of the Communication and Industrial Devices sector contribute significantly. The wire harness business has been operating in China for the past 30 years, but we are currently undergoing a business model change. Specifically, we are expanding our business into areas such as high-end household appliances and autonomous driving. Furthermore, we are establishing new relationships with partner companies and transitioning to business models that optimize product quality based on customer requirements. Additionally, to reduce our reliance on China, we are also focusing on expanding into Southeast Asia, with Vietnam as a central hub. In terms of procurement, our sourcing from China is not substantial. Conversely, we are promoting a localized approach for our operations in China.