Third Quarter of the Year Ended December 31, 2023
Conference Call (Held October 26, 2023)
Presentation and Question & Answer Summary

Presentation

Moderator: Hello, everyone. Thank you very much for taking time out of your busy schedule today to participate in the financial results briefing of Renesas Electronics Corporation for Q3 of FY2023.

Today's attendees are Hidetoshi Shibata, Representative Director, President, and CEO; Shuhei Shinkai, Senior Vice President and CFO; and other staff members.

After the greeting from Mr. Shibata, Mr. Shinkai will give an explanation of the Q3 financial results, followed by a Q&A session. The entire meeting will last 60 minutes. The materials used in today's briefing are the same as those posted on the IR site of the Company's website.

Shibata: Hello, everyone. I am Shibata.

I think you have seen the results for Q3 itself. There are no particular surprises, achieving a little better result than expected.

On the other hand, you may feel that the outlook for Q4 is a bit different compared to the beginning of the fiscal year. For automotive, the situation is almost stable, and for industrial, it is stable in FA as a whole but is a mixed picture depending on the region.

Also, for PC and mobile, after bottoming out in Q2, the trend is toward recovery. However, it is a very slow trend, and we expect a seasonal decline in Q4. For consumers in general and the mass market, we expect Q4 to be down, as they are a little behind the other segments and now inventory digestion is finally underway.

As a result, we have issued a guide that anticipates a slight slowdown for Q4 as a whole.

Also, I would like to gradually increase the channel inventory. We have already shortened the lead time for orders for some time now, but as the uncertain environment continues, orders with short delivery times are becoming more noticeable. Therefore, in order to capture such orders and not lose them, we are increasing channel inventories a little more than before to get closer to our original target line.

So far, during the period up to Q3, we have gone well, but we expect a slight drop in Q4. We will continue to drive cautiously and safely.

From here, CFO Shinkai will talk to you about a few more details. Mr. Shinkai, please.

Shinkai: I am CFO Shinkai. I will explain the details of the Q3 financial results based on the presentation materials.

DISCLAIMER

- **Adoption of IFRS:** With the outlook that the Group will continue to expand globally and to provide financial figures that can be compared on a global scale, the Group discloses its consolidated financial statements in accordance with IFRS starting from the annual securities report for FY2018/12.
- **Non-GAAP figures:** Non-GAAP figures are calculated by removing or adjusting non-recurring items and other adjustments from GAAP (IFRS) figures following a certain set of rules. This adjustment and exclusion include the amortization of intangible assets recognized from acquisitions, other PPA (purchase price allocation) adjustments relating to acquisitions, stock-based compensation, as well as other non-recurring expenses and income the Group believes to be applicable.
- **Presentation of financial forecasts:** Starting from the consolidated forecasts for the three months ended March 31, 2019, the Group presents its financial forecasts as a range, and gross margin and operating margin figures in the non-GAAP format. The gross margin and operating margin forecasts are given assuming the midpoint in the sales revenue forecast.
- **Purchase Price Allocation (PPA):** The allocation of the acquisition costs for the business combination with Steradian Semiconductors Private Limited, which was completed on October 17, 2022, has been revised at the end of three months ended March 31. This revision to the allocation of the acquisition costs has been reflected in the consolidated financial results for the year ended December 31, 2022.

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First is the disclaimer. There is nothing new here in itself, but the system integration that we announced in the previous financial results briefing is scheduled to be implemented in H1 of next year. Therefore, we expect a slight impact on revenue and inventory in Q1 and Q2 of next year. During Q3 and Q4 of this year, there are no impact. We will update you when we are able to foresee more details.

3Q 2023 FINANCIAL SNAPSHOT

NON-GAAP

(B yen)	2022		2023								
	3Q (Jul-Sep)	9 months (Jan-Sep)	2Q (Apr-Jun)	3Q (Jul-Sep) Forecast	3Q (Jul-Sep) Actual	YoY	QoQ	Change from Jul 27 FCT*1	9 months (Jan-Sep) Actual	YoY	Change from Jul 27 FCT*1
Revenue	387.6	1,111.4	368.7	370.0 (±7.5)	379.4	-2.1%	+2.9%	+2.5%	1,107.8	-0.3%	+0.9%
Revenue (Excluding Foreign Exchange Impact)	-	-	-	-	-	-5.1%	+0.3%	+0.3%	-	-	-
Gross Margin	57.0%	58.0%	57.4%	56.5%	57.9%	+0.9pt	+0.6pt	+1.4pts	57.2%	-0.8pt	+0.5pt
Operating Profit (Margin)	142.8 (36.8%)	423.7 (38.1%)	129.1 (35.0%)	32.5%	132.3 (34.9%)	-10.5 (-2.0pts)	+3.2 (-0.1pt)	+12.0 (+2.4pts)	386.1 (34.9%)	-37.6 (-3.3pts)	+12.0 (+0.8pt)
Profit Attributable to Owners of Parent	96.4	268.0	119.0	-	108.3	+11.9	-10.7	-	334.8	+66.8	-
Profit Attributable to Owners of Parent (Excluding Foreign Exchange Impact)*2	115.4	343.6	108.2	-	104.6	-10.8	-3.6	-	319.5	-24.0	-
EBITDA*3	163.4	483.8	149.0	-	152.6	-10.8	+3.6	-	445.8	-37.9	-
1 US$=	135 yen	125 yen	135 yen	138 yen	142 yen	7 yen depreciation	8 yen depreciation	4 yen depreciation	137 yen	12 yen depreciation	1 yen depreciation
1 Euro=	139 yen	135 yen	146 yen	153 yen	156 yen	16 yen depreciation	9 yen depreciation	3 yen depreciation	148 yen	13 yen depreciation	1 yen depreciation

*1: Each figure represents comparisons with the midpoint in the sales revenue forecast range *2: Profit attributable to owners of parent – foreign exchange gain/loss *3: Operating profit + Depreciation and amortization

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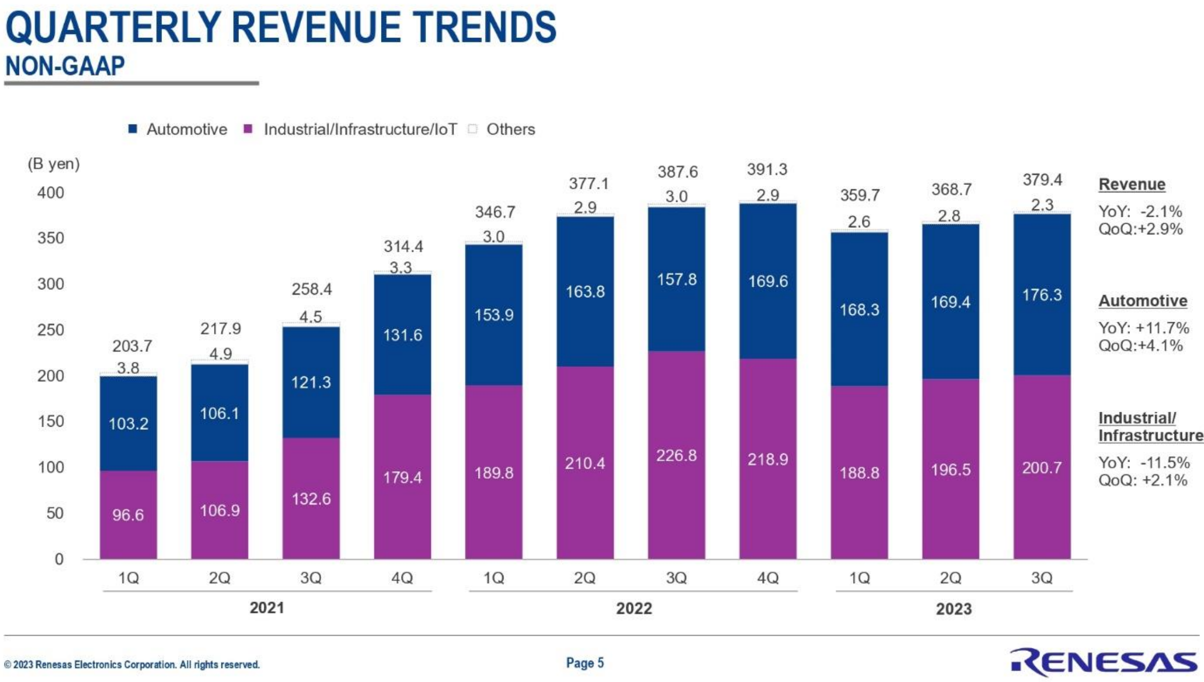
Please take a look at the dark blue column in the middle for Q3 results. Revenue was JPY379.4 billion, gross margin was 57.9%, operating profit was JPY132.3 billion, operating margin was 34.9%, profit attributable to owners of parents was JPY108.3 billion. After excluding foreign exchange impact, it was JPY104.6 billion, and EBITDA was JPY152.6 billion.

Regarding foreign exchange rates, in Q3, the results were JPY142 to USD1 and JPY156 to EUR1.

The changes from the forecast are shown on the right, three more to the right, and will be explained later.

For the nine-month accumulation, please see the dark blue column further to the right.



Next is quarterly revenue trends. For Q3, it is on the far right. Overall, revenue was down 2.1% YoY and up 2.9% QoQ. Excluding foreign exchange impact, revenue was down 5.1% YoY and up 0.3% QoQ.

The breakdown for automotive and industrial/infrastructure/IoT is as shown below.

3Q 2023 REVENUE AND GROSS / OPERATING MARGIN

NON-GAAP

	Automotive	Industrial / Infrastructure / IoT	Company Total
Revenue	176.3 B yen vs FCT: + QoQ: +4.1%	200.7 B yen vs FCT: + QoQ: +2.1%	379.4 B yen vs FCT: +2.5% QoQ: +2.9%
Gross Margin	52.8% QoQ: +1.3pts	62.9% QoQ: +0.3pt	57.9% vs FCT: +1.4pts QoQ: +0.6pt
Operating Margin	34.0% QoQ: -0.9pt	35.8% QoQ: +0.4pt	34.9% vs FCT: +2.4pts QoQ: -0.1pt

Operating Margin vs FCT +2.4pts

- ↑ **Revenue**
- ↑ **Gross Margin** vs FCT: +1.4pts
  - → Currency Impact
  - ↓ Product Mix
  - ↓ Production Recovery
  - ↑ Production Costs, etc.
- ↓ **Operating Expenses**

Operating Margin QoQ -0.1pt

- ↑ **Revenue**
- ↑ **Gross Margin** QoQ: +0.6pt
  - → Currency Impact
  - ↓ Product Mix
  - ↓ Production Recovery
  - ↑ Production Costs, etc.
- ↑ **Operating Expenses**

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This page shows revenue, gross margin, and operating margin for Q3. As for the company total, the operating margin exceeded the forecast by 2.4 percentage points, as shown in the results against the forecast on the right.

First, revenue was 2.5% above the median compared to the forecast. About 2/3 of the increase was due to currency impact and 1/3 to non-currency impact, with most of the increase coming from automotive.

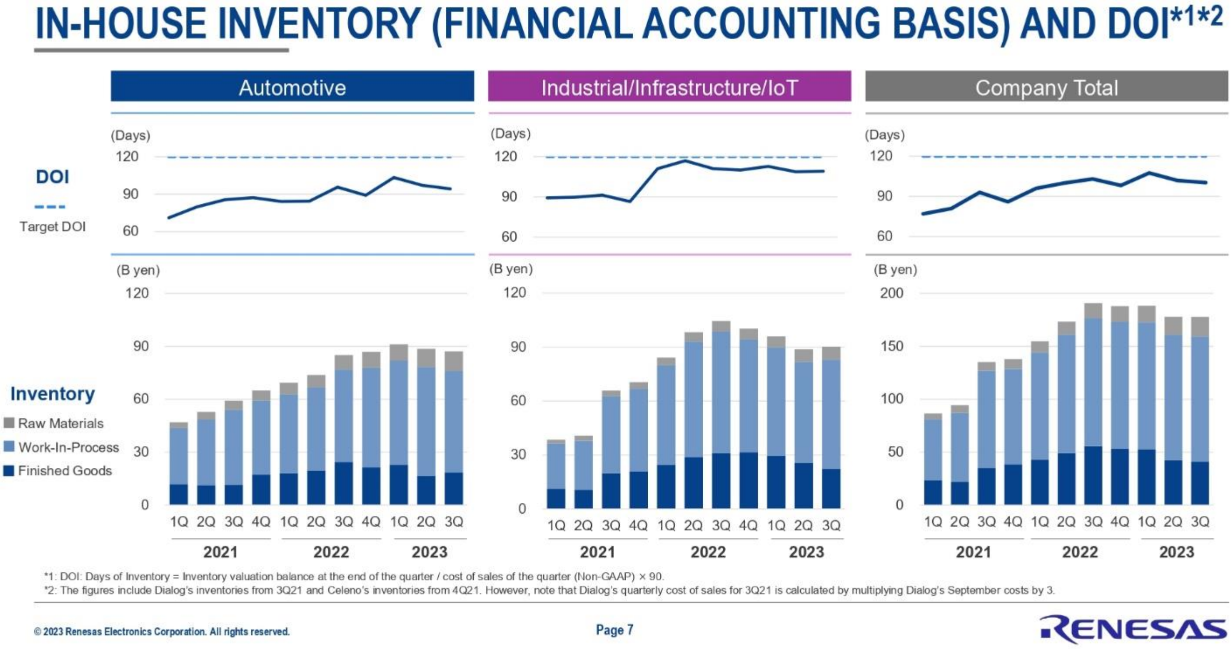
The gross margin was up 1.4 percentage points from the forecast. Currency impact was flat, product mix deteriorated slightly, and production recovery deteriorated slightly due to production adjustments. On the other hand, production costs, which included lower-than-expected manufacturing costs due to lower production and utilization rate, lower-than-expected start-up costs for the Kofu Plant, and lower-than-expected costs for inventory write-downs, contributed to this positive result. The result was an upward revision of 1.4 percentage points to the forecast.

Operating expenses decreased slightly, and after all, as mentioned at the beginning, the operating margin improved by 2.4 percentage points against the forecast.

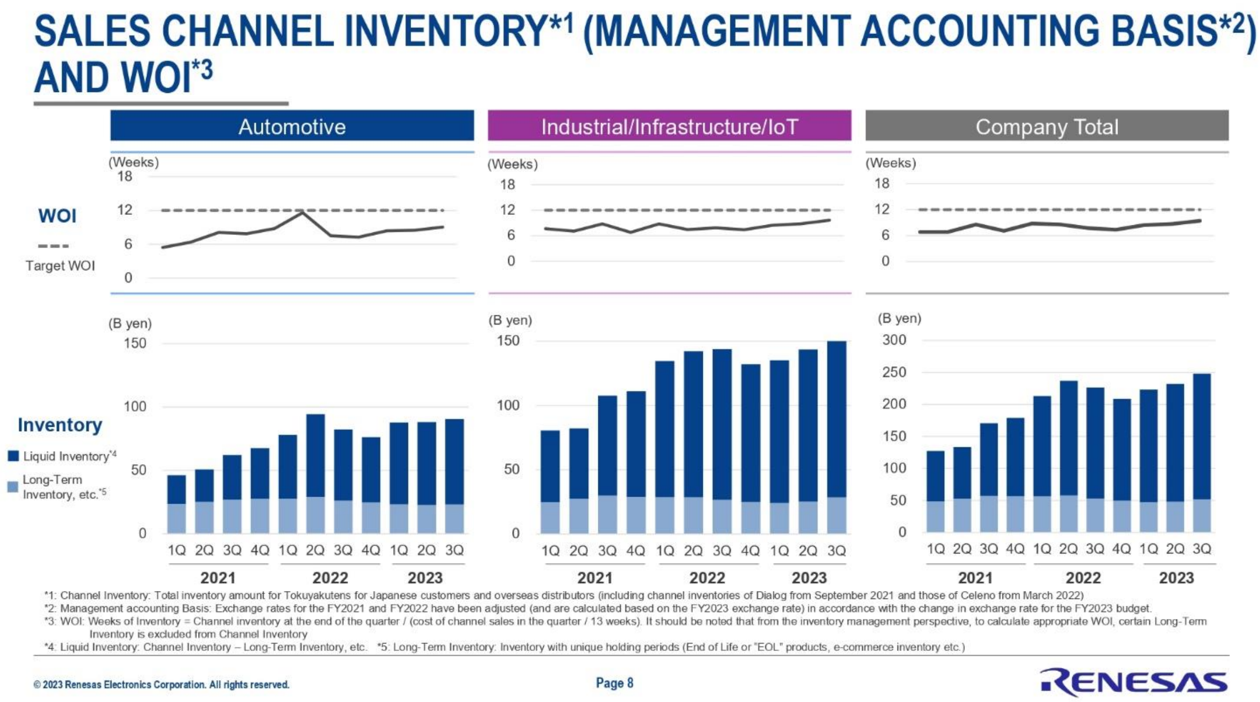
Below that is QoQ, which was almost flat with regard to operating margin. As for gross margin, currency impact was almost flat, and mix was slightly deteriorated, with an increase in automotive and a decrease in industrial, infrastructure, and IoT. Then, production recovery showed a slight decrease due to a decline in utilization rate caused by production adjustments. On the other hand, production costs and other costs improved, which resulted in a nearly flat performance.

Operating expenses increased mainly in R&D, which offset the increase in operating margin.

You can see the results by segment on the left. As for Q3, it should be noted that the operating margin for automotive decreased by 0.9 percentage points. R&D has been increasing in business for automotive in particular since H2, so the operating margin declined QoQ.

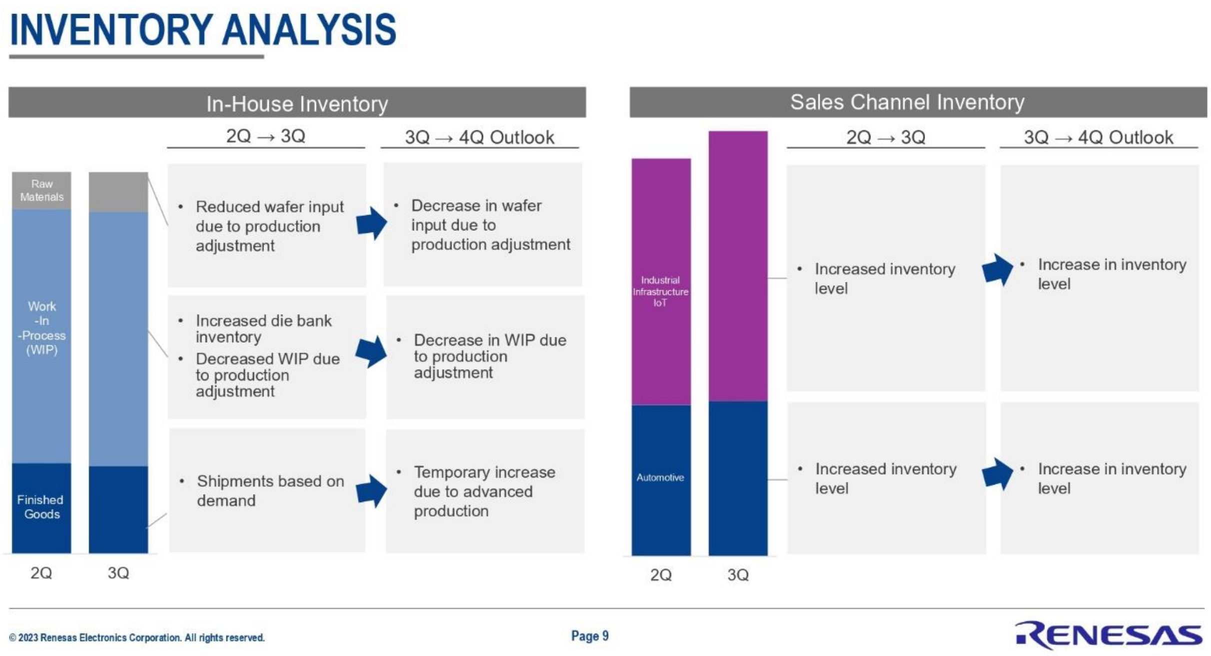


Next is inventory. This is in-house inventory. Overall DOI decreased QoQ to 100 days. By segment, we saw a slight decrease in automotive and almost flat in industrial, infrastructure, and IoT. In-house inventories were also almost flat QoQ.



This is sales channel inventory. WOI and inventory levels in both segments increased QoQ as expected. This means a slight increase in automotive and an increase in industrial, infrastructure, and IoT. Both results were just over nine weeks, and the company total was also just over nine weeks.

The actual value of inventory for industrial, infrastructure, and IoT increased QoQ. This is due to the fewer number of sales for the mass market than expected, resulting in an increase in the actual value of inventory.



This shows the factors that contribute to increases and decreases in in-house and sales channel inventories. As for the in-house inventory on the left side, there was an increasing trend for raw materials, which have been in line with the decrease in wafer input due to production adjustments. We expect an increase in Q4 as well. Regarding work-in-process, first of all, from the viewpoint of die bank expansion, except for 40-nano MCU, we believe that we have almost completed what we need now at the end of Q3.

In the future, we plan to continue optimizing this mix of die bank by digesting those with weak demand and increasing those that are needed.

In Q4, we will make production adjustments while digesting the die bank of product groups with weak demand. Therefore, we expect work-in-process to decrease.

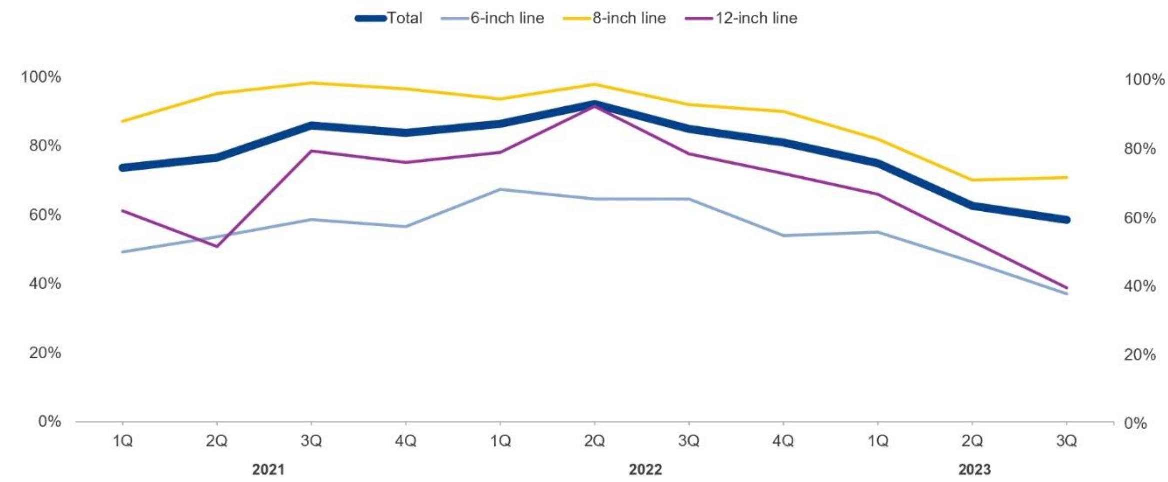
Meanwhile, we plan to gradually increase the die bank of 40-nano MCUs, which is still insufficient, but it is expected to take a little more time until next year or later.

Then, as for finished goods at the bottom, they got slightly lower than expected due to shipments in response to demand in Q3. In Q4, we expect a temporary increase due to advance production, which is in preparation for slightly fewer operating days in the back-end process in Q1.

On the right is channel inventory. In Q3, inventory level and WOI increased in both automotive and industrial, infrastructure, and IoT. We plan to slightly increase the inventory level in Q4.

In terms of inventory value, we expect industrial, infrastructure, and IoT to be mostly flat to slightly lower in actual value terms, while automotive is expected to be mostly flat.

QUARTERLY TRENDS IN FRONT-END UTILIZATION RATE*1
WAFER INPUT BASIS



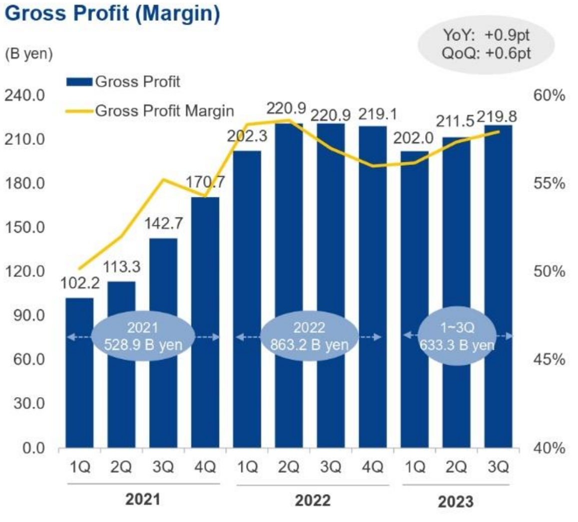
*1: Utilization rates are calculated by excluding the 6-inch line capacity of the Shiga Factory (closed in August 2021) and the Yamaguchi Factory (closed in June 2022) from 1Q21 and 1Q22 onwards, respectively.

This is the front-end utilization rate based on the amount of wafer input. In Q3, it was just under 60%, slightly lower than expected due to production adjustments, as I mentioned earlier. For Q4, we expect a further slight decrease from this level.

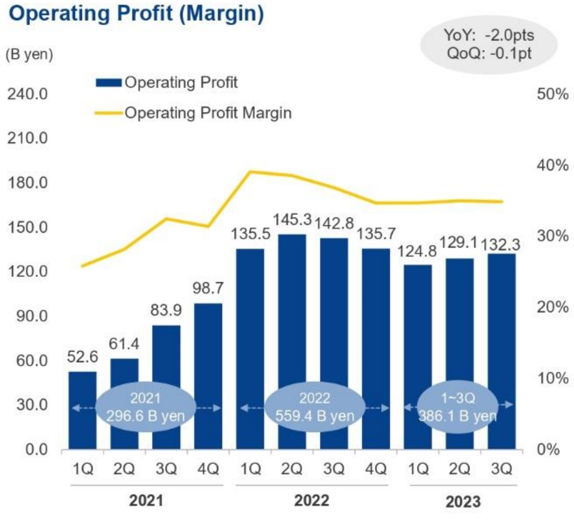
We expect that Q4 will be the immediate bottom of the utilization rate on an input basis.

GROSS PROFIT AND OPERATING PROFIT QUARTERLY TRENDS
NON-GAAP

Gross Profit (Margin)

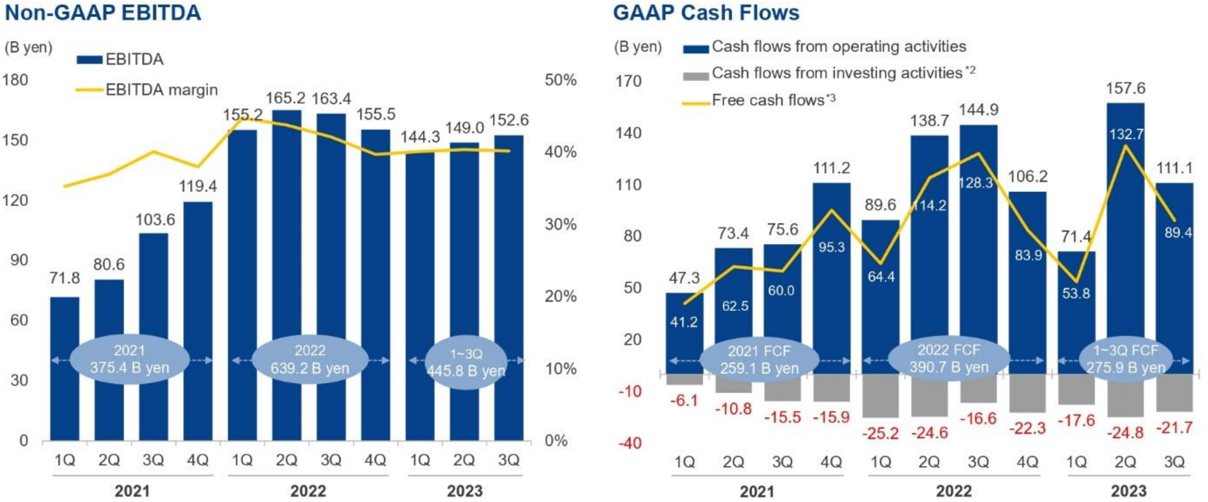


Operating Profit (Margin)



Here are the trends in gross profit margin and operating profit margin. This is just for your information.

NON-GAAP EBITDA*1 AND GAAP CASH FLOWS



*1: Operating profit + Depreciation and amortization *2:The GAAP cash flows from investing activities do not include: (1) acquisition-related payments; (2) payment of contingent consideration for acquisition of subsidiaries; and (3) deposits provided to Wolfspeed. *3: Cash flows from operating activities + Cash flows from investing activities

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Next is EBITDA and free cash flows. The cash flow graph on the right side excludes the impact of the deposits provided to Wolfspeed. In Q3, cash flows from operating activities were JPY111.1 billion, and free cash flows were JPY89.4 billion.

The main reason for the difference from Q2 was that corporate income taxes were paid in Q3.

4Q AND FULL YEAR 2023 FORECAST
NON-GAAP

(B yen)	2022		2023					
	4Q (Oct-Dec)	Full year (Jan-Dec)	3Q (Jul-Sep)	4Q (Oct-Dec) Midpoint Forecast (Range)*1	YoY	QoQ	Full year (Jan-Dec) Forecast	YoY
Revenue	391.3	1,502.7	379.4	358.0 (±7.5)	-8.5% (±1.9pts)	-5.6% (±2.0pts)	1,465.8 (±7.5)	-2.5% (±0.5pt)
(Excluding Foreign Exchange Impact)	-	-	-	-	-8.2%	-6.8%	-	-6.9%
Gross Margin	56.0%	57.4%	57.9%	56.0%	+0.0pt	-1.9pts	56.9%	-0.6pt
Operating Margin	34.7%	37.2%	34.9%	30.5%	-4.2pts	-4.4pts	33.8%	-3.4pts
1 US$ =	144 yen	130 yen	142 yen	147 yen	3 yen depreciation	5 yen depreciation	139 yen	10 yen depreciation
1 Euro=	144 yen	137 yen	156 yen	156 yen	12 yen depreciation	0 yen depreciation	150 yen	13 yen depreciation

*1: Each figure represents comparisons with the midpoint in the sales revenue forecast range

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The following is the forecast for Q4 and full year. First, please refer to the dark blue column in the middle for Q4. Median revenue is expected to be JPY358 billion, down 8.5% YoY and down 5.6% QoQ. Excluding foreign exchange impact, as shown in the row below that, we expect a negative 8.2% YoY and negative 6.8% QoQ. Gross and operating margins are expected to be 56.0% and 30.5%, respectively.

The gross margin is expected to be down 1.9 percentage points QoQ, mainly due to a slight deterioration in the product mix, a decrease in utilization rate due to production adjustments, and an increase in production and other costs.

The operating margin is expected to be down 4.4 percentage points QoQ, and this will be the result from an increase in both R&D and SG&A in Q4 due to the concentration of OPEX at the end of the period.

Please refer to the column three more to the right for the full-year forecast. We project a revenue of JPY1,465.8 billion, gross margin of 56.9%, and operating margin of 33.8%.

GAAP / NON-GAAP RECONCILIATION*1

(B yen)					Full-Year 2022 (Jan-Dec)				2023			
	3Q (Jul-Sep)								3Q (Jul-Sep)			
	Gross Profit	Operating Profit	Net Profit	EBITDA	Gross Profit	Operating Profit	Net Profit	EBITDA	Gross Profit	Operating Profit	Net Profit	EBITDA
Non-GAAP (vs Revenue)	220.9 (57.0%)	142.8 (36.8%)	96.4 (24.9%)	163.4 (42.1%)	863.2 (57.4%)	559.4 (37.2%)	377.3 (25.1%)	639.2 (42.5%)	219.8 (57.9%)	132.3 (34.9%)	108.3 (28.5%)	152.6 (40.2%)
Recurring Items	-1.1	-32.1	-27.2	-4.7	-6.0	-127.2	-107.5	-21.5	-0.6	-32.9	-28.8	-6.3
Former-Intersil PPA Effects	-0.1	-3.6	-2.7	-	-0.3	-14.6	-8.7	-	-0.1	-2.8	-2.2	-
Former-IDT PPA Effects	-0.1	-12.7	-11.2	-	-0.5	-48.4	-42.7	-	-0.1	-13.3	-11.7	-
Former-Dialog PPA Effects	-0.6	-10.7	-8.3	-0.5	-2.2	-41.0	-33.0	-1.8	-0.1	-9.7	-7.9	-
Former-Celeno PPA Effects	-	-0.9	-0.9	-	-1.5	-5.0	-5.0	-1.5	-	-0.8	-0.8	-
Former-Reality AI PPA Effects	-	-0.0	-0.0	-	-	-0.0	-0.0	-	-	-0.0	-0.0	-
Former-Steradian PPA Effects	-	-	-	-	-	-0.0	-0.0	-	-	-0.0	-0.0	-
Stock-Based Compensation	-0.4	-4.2	-4.2	-4.2	-1.5	-18.1	-18.1	-18.1	-0.4	-6.3	-6.3	-6.3
Non-Recurring Items	0.2	7.2	5.5	7.2	-3.2	-8.0	-13.2	-7.5	0.3	-1.4	-4.2	-1.4
Naka Factory Fire Impact	-	-0.0	-0.0	-0.0	-0.9	-0.0	-0.0	-0.0	-	-	-	-
Others	0.2	7.2	5.5	7.2	-2.3	-8.0	-13.2	-7.5	0.3	-1.4	-4.2	-1.4
Non-GAAP Adjustments Total	-0.9	-24.9	-21.7	2.6	-9.2	-135.2	-120.7	-29.0	-0.3	-34.3	-33.0	-7.6
GAAP (vs Revenue)	220.0 (56.8%)	117.9 (30.5%)	74.7 (19.3%)	165.9 (42.9%)	854.0 (56.9%)	424.2 (28.3%)	256.6 (17.1%)	610.2 (40.7%)	219.6 (57.9%)	98.0 (25.8%)	75.3 (19.9%)	144.9 (38.2%)

*1: From 3Q 2021 onwards, Non-GAAP adjustments have been also applied to the revenue following the implementation of PPA

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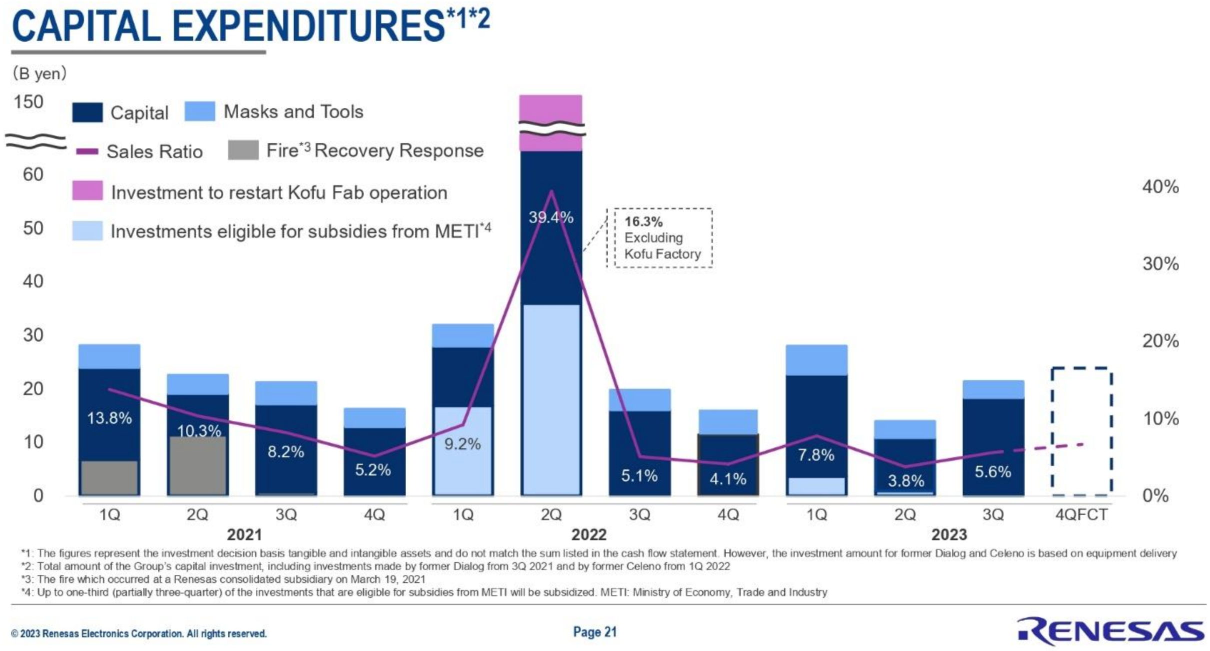
Now, please turn to the appendix on page 18. Regarding the reconciliation between GAAP and non-GAAP for Q3, one additional point I would like to mention is the net profit of others in the non-recurring items, which is the third row from the bottom, second column from the right. This is an adjustment to the profit or loss related to the mark-to-market valuation of Wolfspeed's depository receipts, and a write-down was recorded in Q3 due to a decrease in the value of the bonds as a result of rising US interest rates.

Since this is a non-cash valuation profit or loss, it is excluded from non-GAAP financials. This portion will continue to fluctuate with trends in US interest rates, which means that it may appear as a non-recurring adjustment item again in the future.



Then please turn to page 21. Regarding the status of capital expenditure, in Q3, we have made a decision to invest in the mass production of SiC at the Takasaki Plant as the second stage investment in the line. For Q4, we expect to invest in fields such as R&D and IT, rather than in production, and expect capital expenditures to be several percent of sales.

This concludes the explanation.

Moderator: Thank you very much.

Question & Answer

[Questioner 1]

Q: I have two questions. First, I would like to ask about the utilization rate. According to the financial results presentation materials, the overall utilization rate has been declining, but there is a slight difference between 8-inch and 12-inch, or by inch. What is the background of this difference?

Also, Mr. Shinkai suggested that Q4 is the bottom of the utilization rate for the time being, but what is your outlook after Q1 of next year?

A: Both will be answered by Shinkai. Mr. Shinkai, please.

A: Regarding the utilization rate in Q3, we have been seeing the movement through the inventory adjustments, as well as the optimization of the die bank's mix and other factors, as I mentioned earlier. As for 8 inches, it means that we have created the part of the die bank that was not sufficient by the end of Q3. On the other hand, for 12 inches, the replenishment was completed, and the utilization rate dropped. That is the difference by inch.

As for the outlook for Q4 and beyond, we expect the same trend to continue in Q4, but to be more specific, we expect a slight decline in the 8-inch because the replenishment of the die bank has been almost complete by the end of Q3. On the other hand, as for the 12-inch, the mix is improving and will go up somewhat. However, we expect the overall utilization rate to be slightly down.

Production in Q1 and beyond will depend on demand in Q2 and H2 of next year. One key is the 40-nano MCU or microcontrollers at the 12-inch plant. We expect that the effect of investment to increase production of these MCUs will appear and that the utilization rate for these MCUs will increase from the latter half of Q1. Therefore, we expect it to boost the overall utilization rate. That is all.

Q: Thank you. The second point may be a similar question to what you just said. At the beginning of the presentation, Mr. Shibata explained that orders with short delivery times have been increasing and that you are increasing channel inventories in order not to miss out on such demand. I would like to get some hints as to the sector in which you see such an increase of orders with short delivery times and what your forecast is for next year's revenue, as far as you can see now. That is all.

A: There is no specific sector with an increase of short delivery orders. This is about the so-called mass market, where each application is not well visible, and the situation is also similar for automotive applications. In fairly various sectors, there is a customer base that feels a bit uncertain and controls inventory quite tightly, so there are a lot of places where things are really needed as soon as demand rises a little bit. So, our intention is to make sure that such things are not overlooked.

It is difficult to predict how long this trend will continue, but we expect that the focus on inventory control will continue until Q1 of next year since many of our Japanese customers have fiscal years ending in March.

At the same time, this also depends on the macro economy, but for now, I am assuming that the landscape will change a little and that we will see an upward trend from Q2 of next year.

Again, we will watch carefully so that we do not take too big a step, and we will do so while controlling inventory, our in-house inventory, and channel inventory as necessary. For the time being, our current thinking is to deal with this by keeping in-house inventory really low and increasing our channel inventory levels a bit. That is all.

[Questioner 2]

Q: First of all, I would like to ask what is in your sales forecast for October to December in more detail. As for automotive, which area is strong or weak, including the regional aspect? In addition, other than automotive, I would like to know the strength and weakness of the three traditional categories.

I would also appreciate it if you could indicate whether this is due to actual demand or seasonal factors, such as inventory adjustment at the end of the fiscal year, or the end of December.

A: I would say that a meaningful trend is in the area of automotive and region. In the US, we have factored in the fact that the strike situation is going to make our sales lower. However, the data we are looking at right now has not been affected. We expect that it will not be unaffected after all. I think it will go down somewhere. I don't know if that will happen in Q4 or if it will carry over into next year, but we have incorporated the assumption into the Q4 forecast in advance, which will probably go down somewhere.

Also, as you know, there is a concentration of large Tier 1 customers in Europe, and we expect that they will greatly reduce their inventories there. We expect automotive in Europe to fall significantly.

In contrast, we expect a slight growth trend in Japan, China, and other countries, while we do not expect a large growth. In addition to the strike mentioned earlier, our sense is that we may be overcautious in our estimation of automotive, but we do not want to make too much of a downward swing, so we have decided to make a cautious estimation for Q4.

In terms of products, as the usual pattern, SoCs are inevitably very fluctuated. Therefore, I don't think it makes much sense to say that it went up or down QoQ. In the short term, we expect power to be a little lower. Our power is centered on IGBTs, and we are not yet in a situation where we are expanding our sales so widely here and there because there is no capacity. In accordance with the original plan, we are operating based on a very small number of customers until the full-fledged launch in 2025.

Therefore, we expect that IGBTs in Q4 will be a little more sluggish, as they are likely to be affected by sales and competitiveness of specific customers. There is nothing special in terms of products when it comes to automotive.

Aside from automotive, I would say, to repeat what I said earlier, that FA will remain flat or grow at a slightly higher level. On the other hand, I think that the mass market and the white goods market in the consumer-focused areas will probably see a double-digit decline, including seasonality.

Other than automotive, a very large growth area is cloud computing. The double-digit growth here would be expected. This is the same as last time, but the current growth is being driven by the demand for DDR5. DDR4 inventory on the customer side will probably continue to be depleted until the next quarter or so, but since DDR4 shipments from us are already quite limited, there is almost no impact on our sales.

We also expect that power for AI servers will start up in Q1 or Q2 of next year, which will further accelerate the growth of cloud data center applications.

As I mentioned earlier, the underlying tone for PC is recovery, but for Q4, we expect it to drop due to seasonality or something like that. That is all.

Q: Thank you very much. Second, I'm going to ask you once again about what you just said, and it's going to be a summary question of the whole thing. Then, can you say that as the scenery of Europe and the US, so-called parts adjustment and inventory adjustment in automotive and seasonal adjustment for consumer use will appear clearly in Q4 and will be normalized in Q1? In other words, is it more correct to think that Q1 will be more normalized than Q4? Or do you see it now as if the trend is continuing into Q4 and beyond?

A: It is still too early to talk about Q1, but our current assumption is that it would be safer to see it in the same way as Q4, I think.

The main reason is that we expect that the inventory adjustment, which I mentioned earlier, mainly from Japanese customers, will probably come in significantly in Q1 of next year. In Q4, in terms of our regional exposure, mainly in Europe, the inventory adjustment due to the calendar year has been coming with a bang, as well as in the area of consumer use and mass-market in other regions.

At the same time, for Japanese-affiliated customers, there will probably be inventory adjustment in anticipation of the end of the fiscal year ending March 31, so we are now assuming that the mutual offsetting of these two factors will prevent a large increase from Q4 to Q1.

I have such an image that the movement will go back to normal after Q2 or beyond.

[Questioner 3]

Q: I would like to ask you again about the inventory adjustment. I think you talked about inventory adjustments on the customer side in spring or so. You said that would happen mainly in Q4 in Europe and for Japanese-affiliated customers in Q1 of next year. Have you expected that the inventory adjustments in Europe will be finished completely in Q4?

Also, do you currently expect that the volume of inventory at Japanese-affiliated customers could be cleared only in Q1 and could be normalized from Q2 onward? This is the first question. Thank you.

A: It is difficult to say definitively, though. I have the same sense as you just mentioned. As I said before, there are some areas where the inventory may be too tight. While we are talking about these things, we are also saying at the same time that the line will be down here and there and cause problems.

Therefore, as there is a need to manage cash tightly, there are some areas where this is going too far. So, it is difficult to imagine that this situation will continue for a long time. This is my real feeling.

Q: I understand. Thank you very much. Second, I would like to ask you about shareholder returns. I understand that you have been buying back shares from INCJ, the largest shareholder, in the recent past, but since this summer, INCJ has been releasing its shares not through your share buyback.

First of all, how did this come about? I think that they had approached you once before releasing their shares, but what is the background behind the decision not to accept their share buyback this time, and will you basically refuse the share buyback in the future, or did you make the decision this time not to do that due to the level of the share price? Is there still a possibility that you might accept the share buyback depending on the level of the share price? That is all.

A: Our current priority is to resume, or rather to start dividends as soon as possible, so our honest view is that our appetite for share buybacks is much lower than it was before the beginning of this year.

We will naturally consider and implement shareholder returns that combine share buybacks, whether from INCJ or the market, depending on the level of the share price, but now we finished the share buyback at the beginning of this year, and our focus is on dividends. That is all.

[Questioner 4]

Q: I have a couple of basic questions, or two questions.

One is about the utilization rate, as someone asked earlier. It dropped in Q3, but in other words, I would like to know in what kind of areas it dropped, for example, final products or other product areas, and in what kind of areas it will recover in the future. I know this is a basic question, but please tell me.

A: In terms of products, in Q3, as I mentioned earlier, we did not have enough die banks for MCUs, so we were making them. Therefore, other items were slightly adjusted in Q3.

For Q4, we generally expect adjustments in overall products. In Q1, facilities that will increase production will be for 40-nano MCUs, so we expect that the utilization rate for MCU will rise there. That is all.

Q: How is this affected by the market environment in terms of the end product or the customer's domain, in short? For example, can you say that the market for MCU for this is recovering, so the utilization rate will grow from Q4 onward? Or am I taking it wrong?

A: Well, as for demand, as Shibata explained earlier regarding the Q4 forecast, I think a simple answer would be that we are basically making products in line with that forecast.

The 40-nano MCU I mentioned are in very short supply, and supplies continue to be tight in some areas, but they are mostly for automotive applications. Therefore, we hope you understand that the driver for Q1 of next year will be MCU for automotive applications.

Q: I see. Basically, can I recognize that the automotive applications that were sluggish in Q3 will recover?

A: Not really. I might as well explain the concept of die bank. We have been working for some time to have a certain level of semi-finished products in our inventory. One of the objectives of this initiative is to shorten the lead time from customer order to shipment, and from the viewpoint of so-called business continuity, including natural disasters, we are also working to have semi-finished products called the die bank.

On the other hand, until the end of last year, we were in a situation where everything was sold as soon as it was made, so although we said we were going to have die bank, we were not able to do it at all. This year, with the market weakening a bit, we have finally been able to expand that die bank here and there, but some things were done quickly, and some things took a little longer. It took some time, especially for products such as MCUs which are made on 8-inch wafers with slightly thicker lines, but we were finally able to expand the die bank a little in Q3. In other words, the factory was used for this purpose.

In terms of whether the market environment is strong or weak, the current situation is a repeat of what I have just said from the beginning, but the automobile market is strong or stable. On the other hand, I feel that the market environment is really weak in the consumer use and, if we limit our discussion to Q4, PCs and mobile phones are expected to decline sharply. If we compare automotive with consumer products, the current view is that consumer products are clearly weaker.

Q: I understand. If possible, I would like to know the appropriate level of utilization rate. Of course, it would depend on the product, but it is 60% now, and I think it used to be around 80%. What level do you consider appropriate? It's an adjustment [inaudible].

A: Appropriateness is a difficult thing to define. Our hope is to always operate close to 100%. Ideally, we would like to aim for 80% or 85%. However, demand for semiconductors fluctuates considerably, so it is not always possible to achieve what we are aiming for.

[Questioner 5]

Q: First, I would like to have a few comments on the price trends of your products. I think prices have been going up for the past three years, but what will happen in the future in a bit of a surplus situation? Should we assume a normal or a slightly decreasing trend in the future, or should we assume a price increase since various costs are still rising? Please give me your sense of direction, to the extent possible, regarding price trends.

Second, in the Chinese market, I think there are quite a few moves to strengthen the old process, or rather the mature node, in the flow of the so-called US-China friction. I am concerned that your company will face a severe competition in MCU and Power to some extent, so could you tell me a little about the current competitive situation in the Chinese market? These are the two points I would like to ask.

A: On the first point, we think that the current price level is appropriate after considering various factors, and it would be desirable to maintain it to the extent possible.

As you pointed out, the balance between supply and demand indicates that there is a bit of a margin for demand, but on the other hand, costs have not fallen that much, so we are not in a situation where we can easily say that we will lower prices.

Second, IGBTs are already in trouble in China. I don't think we are the only company that faces this situation. IGBT competition in China has been intensifying so fast that I think it is unlikely that we will be able to expand IGBT in China in the future.

As for our future plans, we are operating under a plan that does not focus much on China, and I think it is unlikely that this situation will change a lot. When it comes to MCU and the Analog field, I don't have the sense that there are more and more local competitors appearing at the moment, not at all.

However, since this may be a matter of time, we have been working for a long time on areas where higher performance and reliability are required, and we have also focused on selling solutions, not just selling single products. We would like to continue to expand our high-value-added MCU business and our Analog business by moving away from the business of measuring with weights and telling how much we have sold or bought in grams.

Power is tough, but I think MCU and Analog will still do well enough depending on how we do. However, it is not quite right to expect a very large growth in both MCU and Analog, so I think we should assume moderate growth. That is all.

[Questioner 6]

Q: Please tell me about the aim of the recently announced reform of the organization, or dividing the organization by product, and why you are doing this at this time.

A: As we have already announced, the common answer to both questions is that it is because our phase as a company has changed. We have been trying to produce solid results in a shorter period, so we have been focusing more on segments, and I don't know if this is the right word, but we have been emphasizing speed even if there is a little inconsistency or waste. We have been focusing on speed.

I believe that we have achieved a certain level of success in this area, and we will focus on the medium- to long-term and use various internal resources more efficiently in order to achieve solid growth. Our main focus is on both short-term and medium- to long-term initiatives.

So, the reason for the timing is that we decided that now would be just the right time to do so. That is all.

[Questioner 7]

Q: In the foreign exchange market, the yen has been weakening considerably and is now at JPY140 level to USD1. What is the impact of the current exchange rate level on the business environment for your company, and is it a comfortable level, or is it undesirable because the yen has weakened excessively?

Also, the exchange rate landscape seems to have changed considerably compared to a few years ago, and I wonder if there is any possible impact on your investment strategy, such as increasing the domestic production ratio.

A: CFO Shinkai will answer. Mr. Shinkai, please.

A: The answer is that I honestly don't know if the level of exchange rate is comfortable. However, we do not think it would be good for our business performance to be affected too much by the exchange rate, so we have taken two measures.

For one thing, our target financial model is based on a flat exchange rate. That is JPY100 to USD1 and JPY120 to EUR1, and that has continued for several years from the past.

The other is currency hedging to reduce the volatility of performance due to exchange rates, thereby hedging the risk from the yen's appreciation. In other words, we are doing this by protecting the downside, the downside of performance due to the strong yen, and abandoning the upside of the weak yen.

Therefore, I believe that a large swing in the exchange rate would have a greater negative impact on performance than the level of the exchange rate.

As to whether there is any impact on the direction of investment, there is not so much impact from the exchange rate itself. The very area or region to be invested in is considered based on its characteristics and the high or low cost, which includes not only the exchange rate but also inflation and so on. We will also decide in terms of whether the necessary resources are there. That is all.

[Questioner 8]

Q: I would like to ask a question about infrastructure. You mentioned earlier that DDR5 is leading the way, but I understand that infrastructure sales this year, perhaps due in part to the DDR4 adjustment, have not increased that much overall compared to last year. Since you mentioned that the portion for DDR4 has become much smaller, can I assume that next year, you will see a very large increase in memory content with DDR5, as you have mentioned in the past, and that the mix is such that you can expect a reasonable increase in revenue? That's my first question.

The second point is a bit detailed, but you mentioned that PMIC for AI servers will be launched in Q1, but I would like to get some hints as to how much meaningful or rather, how large a scale we can expect. That is all.

A: I assume that it will grow a lot with DDR5. Therefore, on a yes or no basis, I can say yes. It is difficult to say definitively whether it will be Q1 or Q2, but PMIC, or power stage, will be launched for AI, but compared to the current infrastructure business, it is not that big yet. Rather, it is helpful there, or something like that, I guess.

We do not expect that the business for AI will drive the scale of the business for infrastructure to grow by 50% or 100% per year. We will not think so yet at least at this stage. It is possible, though, that this may happen by chance as the customer base continues to expand. We will start with one company, one customer, so we think it will be a good underpinning or cushion, and that's about it. That is all.

[Questioner 9]

Q: I would like to know two things about the organizational changes you announced on the 19th.

Where will in-vehicle MCU and R-Car fit into these four product groups?

A: It is generally into high performance computing.

Q: I understand. Second, are the people who provide support to customers in the product group, or do they belong to the software digitization or operations group?

A: They are mainly in sales. I think it's usually called a field application engineer, but they are in the sales group. I think that is generally true of any company.

[Questioner 10]

Q: One point I wanted to ask, if it is possible, is that when you talked earlier about European cars, you mentioned that you were going to squeeze in inventory and that the market would drop from Q4 onward. What is the background to this? How do you expect the market for automobiles in Europe will develop from Q4 and next year?

A: I did not say European cars. I said that there are several very large-scale Tier 1 global customers in Europe.

Q: I understand.

A: I mentioned that there is a noticeable movement to squeeze inventory quite tightly around here.

Q: How do you see the reasons for that?

A: This is the same story I have been telling you for some time, but I think that Tier 1 is in a very difficult financial situation. However, we are not at all at liberty to talk about others. In addition, it is naturally impossible to decrease investment in areas that will grow in the future, so I think it is a trend that can be seen across the board that cash must be managed very tightly. Our view is that this has been the case for the past several quarters.

Moderator: Thank you very much. There is still time for more questions, but since there appears to be no further questions, we will conclude the Q&A session.

Lastly, Mr. Shibata would like to say a few words. Mr. Shibata, please.

Shibata: I think it was not a very newsworthy financial statement, which was reflected in the small number of questions this time.

We will proceed cautiously for the next one or two quarters, and then we will focus on the market recovery at the appropriate time next year and the growth of cloud computing centering on AI. Furthermore, Kofu Plant for EVs will start its operation in 2025, and the next-generation products for ADAS will launch in 2025 or 2026. Before that, we will work hard to maintain growth in 2024 and Q1 of 2025. We look forward to your continued support.

Thank you for your time today.

Moderator: That concludes the financial results briefing for Q3 of FY2023. Thank you for your participation.

[END]