2Q of the Year Ended December 31, 2024
Conference Call (Held July 25, 2024)
Presentation and Question & Answer Summary

Presentation

Moderator: Thank you very much for attending this Q2 earnings report for FY2024 despite your busy schedule. Today's presentation, we have the CEO and Representative President, Mr. Hidetoshi Shibata, and the CFO, the Chief Financial Officer, Mr. Shuhei Shinkai. Other members of the staff are present. Mr. Shibata will made an opening address. . Then, CFO Shinkai will talk about the earnings. After that, we'll have a Q&A session. We are planning 60 minutes for this meeting. The presentation material that is going to be used today is uploaded on the IR side of our company.

Mr. Shibata, please?

Shibata: Thank you very much. Good morning, everybody. I'm Shibata. In today's earnings, I think basically, we have to reflect on our performance. In Q2 numbers, putting that aside, the Q1 financial results, I think maybe our outlook is a bit optimistic. The reason I say this is mainly, one, the automotive business, we have been anticipating sustainable growth. We have been robust, but I think we have been adjusting to a more cautious outlook. That's the current state. That's number one.

Number two is that there’s a wider sense of industrial demand, there has been adjustment. Compared to our initial expectations, it seems that this adjustment is continuing longer and in-depth than participation. Initially, we thought that Q2 to Q3, we will start to see a recovery. Currently, Q3 continues to be tough. From Q4 onwards, at some timing, the recovery will be seen, but we'll have to be very cautious about the outlook. We are thinking about controlling the inventory more significantly.

In Q3, the channel inventory, to control that and to be able to manage that, the top line is going to go down. I think that is how we're going to manage our business. That said, sooner rather than later, the market will recover. That's our view. Going forward, our theme is, more than ever, growth. We are going to control the top line in Q3 in terms of OpEx and R&D, in terms of the investment, we are not going to put on the brakes and go forward. That means the operating margin will decline a bit in Q3. Even so, we will continue investing in R&D so that we will continue to conduct initiatives towards our growth.

In Q2, unintentionally, we have increased the channel inventory in Q3. Quickly, we will readjust that. On the other hand, towards growth, we will continue to invest for R&D. That will be our outlook for Q3. First, let's go into the details of Q2. I'll give you over to Mr. Shinkai about the financial results. Shinkai-san, please.

Shinkai: I'm Shinkai, the CFO. I would like to give a presentation about Q2 of this fiscal year utilizing the presentation material.

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 combinations with Panthronics AG ("Panthronics") has been revised at the end of three months ended December 31, 2023. These revisions to the allocation of the acquisition costs have been reflected in the consolidated financial results for the three months ended June 30, 2023 and for the three months ended September 30, 2023.
- **Change of the method for aggregating Reportable Segment:** Due to the Group's organizational changes in the three months ended March 31, 2024, the methodology for aggregating revenue for reportable segments changed from the use of product axis to the use of customer axis. Accordingly, previously reported segment information for the year ended December 31, 2023, has been revised using the new methodology in order to be comparable with the segment information for the year ending December 31, 2024.
- **Start of consolidation of Transphorm:** The Group completed acquisition of Transphorm on June 20 (JST), 2024. The Group has since begun the consolidation of their financial figures.

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On the very bottom bullet, on the 20th of June, we have completed the acquisition of Transphorm. End of June flags the consolidation of Transphorm. After we complete the calculation of PPA, we will retrospectively conduct a revision, but this PPA is expected to finish by Q4 of this fiscal year. The Q3 forecast reflects the contribution of Transphorm.

2Q 2024 FINANCIAL SNAPSHOT

NON-GAAP

(B yen)	2023		2024								
	2Q (Apr-Jun)	1H (Jan-Jun)	1Q (Jan-Mar)	2Q (Apr-Jun) Forecast	2Q (Apr-Jun) Actual	YoY	QoQ	Change from Apr 25 FCT*1	1H (Jan-Jun) Actual	YoY	Change from Apr 25 FCT*1
Revenue	368.7	728.4	351.8	355.0 (±7.5)	358.8	-2.7%	+2.0%	+1.1%	710.6	-2.4%	+0.5%
Revenue (Excluding Foreign Exchange Impact)	-	-	-	-	-	-8.6%	+0.4%	-0.0%	-	-8.4%	-0.0%
Gross Margin	57.4%	56.8%	56.7%	55.5%	56.7%	-0.6pt	+0.1pt	+1.2pts	56.7%	-0.1pt	+0.6pt
Operating Profit (Margin)	129.1 (35.0%)	253.8 (34.8%)	113.5 (32.3%)	30.5%	110.6 (30.8%)	-18.5 (-4.2pts)	-3.0 (-1.5pts)	(+0.3pt)	224.1 (31.5%)	-29.8 (-3.3pts)	(+0.2pt)
Profit Attributable to Owners of Parent	119.0	226.5	105.9	-	96.7	-22.3	-9.2	-	202.5	-23.9	-
EBITDA*2	149.0	293.3	133.8	-	132.8	-16.2	-1.0	-	266.6	-26.7	-
1 US$=	135 yen	134 yen	147 yen	150 yen	153 yen	18 yen depreciation	6 yen depreciation	3 yen depreciation	150 yen	16 yen depreciation	2 yen depreciation
1 Euro=	146 yen	144 yen	159 yen	161 yen	165 yen	19 yen depreciation	6 yen depreciation	4 yen depreciation	162 yen	18 yen depreciation	2 yen depreciation

*1: Each figure represents comparisons with the midpoint in the sales revenue forecast range *2: Operating profit + Depreciation and amortization

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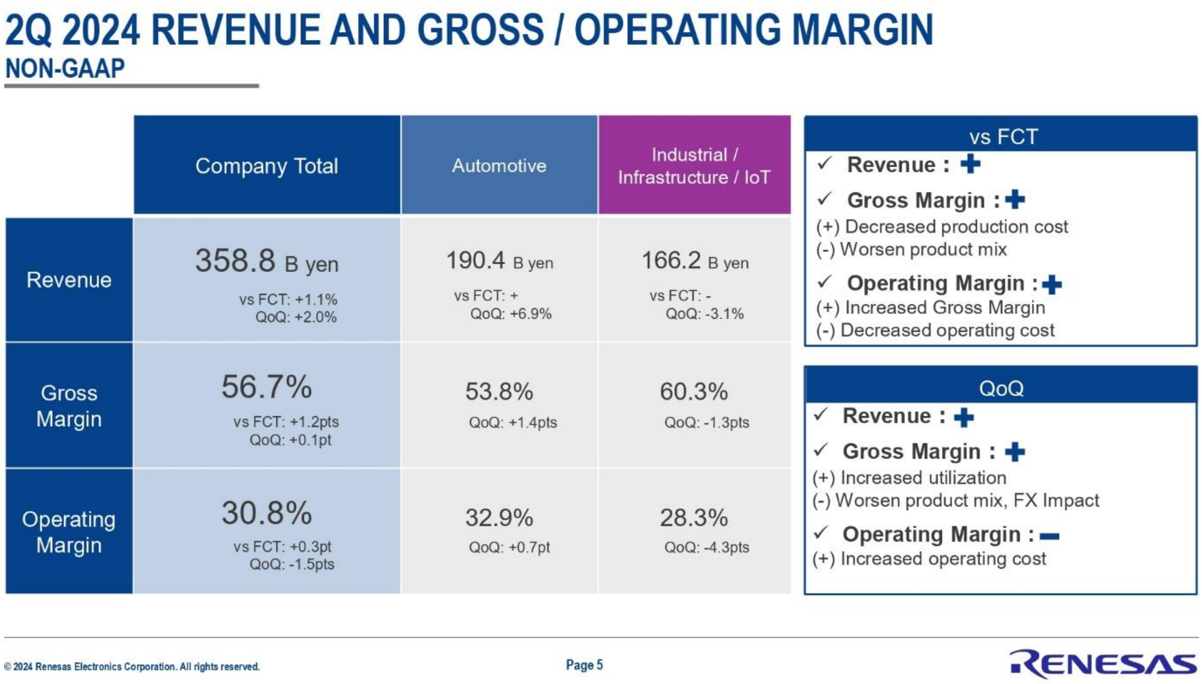
Next slide, please. This is the financial snapshot for Q2. In the middle darker blue column, please refer to that.

In terms of revenue, it was JPY358.8 billion, gross margin of 56.7%, an operating profit, JPY110.6 billion, at margin will be 30.8%. Net profit, JPY96.7 billion. EBITDA, JPY132.8 billion. In terms of the ForEx, JPY153 to a dollar, JPY165 to the euro. Against the forecast, if you want to make a comparison, it's on the very right-hand side, but I would like to refer to that later.



2Q 2024 REVENUE AND GROSS / OPERATING MARGIN

NON-GAAP

	Company Total	Automotive	Industrial / Infrastructure / IoT
Revenue	358.8 B yen vs FCT: +1.1% QoQ: +2.0%	190.4 B yen vs FCT: + QoQ: +6.9%	166.2 B yen vs FCT: - QoQ: -3.1%
Gross Margin	56.7% vs FCT: +1.2pts QoQ: +0.1pt	53.8% QoQ: +1.4pts	60.3% QoQ: -1.3pts
Operating Margin	30.8% vs FCT: +0.3pt QoQ: -1.5pts	32.9% QoQ: +0.7pt	28.3% QoQ: -4.3pts

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This page is about Q2 details. First of all, compared to the forecast, the company total at the very right-hand side, please look at the top box. In terms of the revenue, compared to the medium range, we have slightly overperformed its 1.1% outperformance. Basically, this is due to the currency impact. Excluding the currency impact, is flat against our forecast. The automotive has increased slightly, and the industrial infrastructure and IoT has decreased. In total, it was in line with expectations.

In terms of the gross margin, it is 1.2% above our forecast. The impact of the foreign currency is basically flat. In terms of the product mix, the industrial infrastructure and IoT within the segment make us worsen, internal manufacturing costs has gone down. Overall, we have been able to see a positive improvement.

In terms of manufacturing costs decrease, the cost of the ramp-up of the Kofu plant has gone down, and disposal and the inventory realization losses has not shown up. These are the factors for this situation. Operating margin is 0.3 percentage point increase for this quarter.

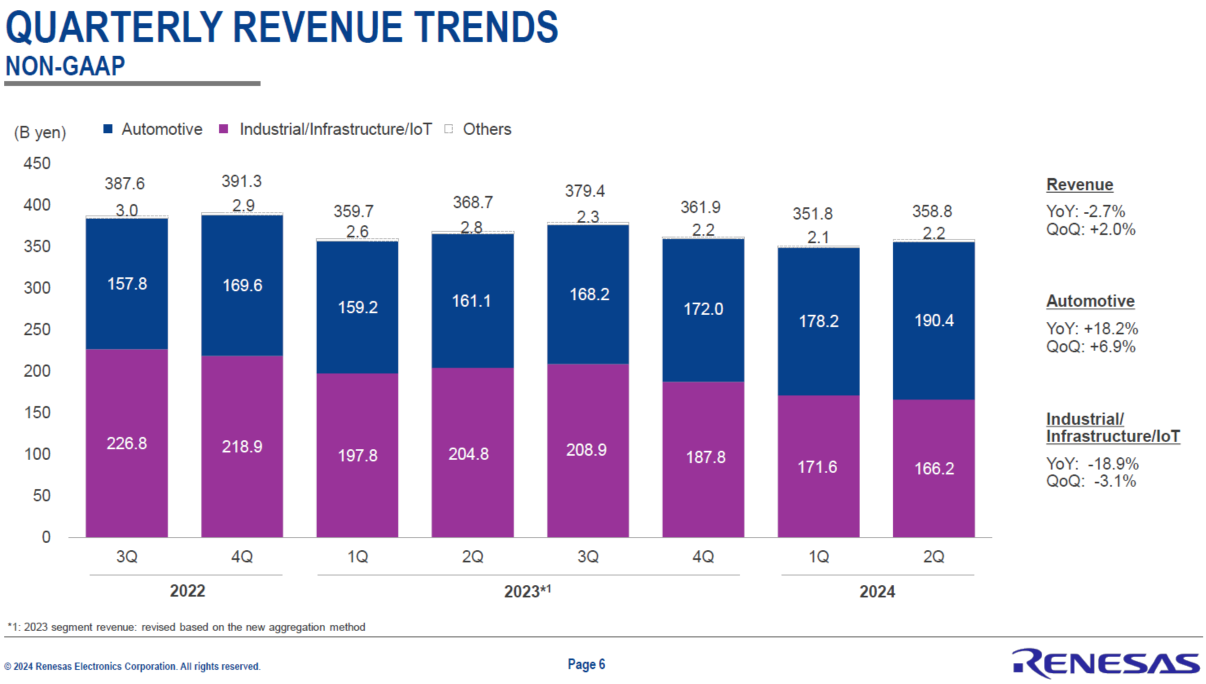
In terms of the operating expenses, compared to the forecast, it has increased. However, the impact is coming mainly from the currency. In terms of the calculation of the currency sensitivity, there has been an underestimation. There has been a big impact coming due to this ForEx.

To talk more detail, from the cost side to the non-major currencies has been impacted by the weaker yen, but we have underestimated this impact. That is the reason why we're seeing this level of impact. For R&D, basically, it's in line with our forecast. An NRE milestone adjustment has been transferred to that. There has been some increase there.

Going to the QoQ comparison, in terms of revenue, it has increased by JPY7 billion. This is a 2% improvement. In terms of the gross margin, it has been basically flat. In terms of the operating margin, it is 1.5 percentage points worsening. This is because of the increase of the R&D. Q1, basically, it has been at a low level. In the same quarter, the R&D level has gone up compared to Q1.

On the left-hand side, the segment situation, I would like to give us some more color there. In terms of the gross margin, the automotive due to the increase of utilization, it has improved. In terms of industrial, infra, and IoT, the product mix has worsened within the segment. The gross margin QoQ has gone down.

In terms of the operating margin, automotive, the cost of the volume increase, the top margin has improved. Industrial, infra, and IoT, due to less volume, the margin has worsened QoQ.



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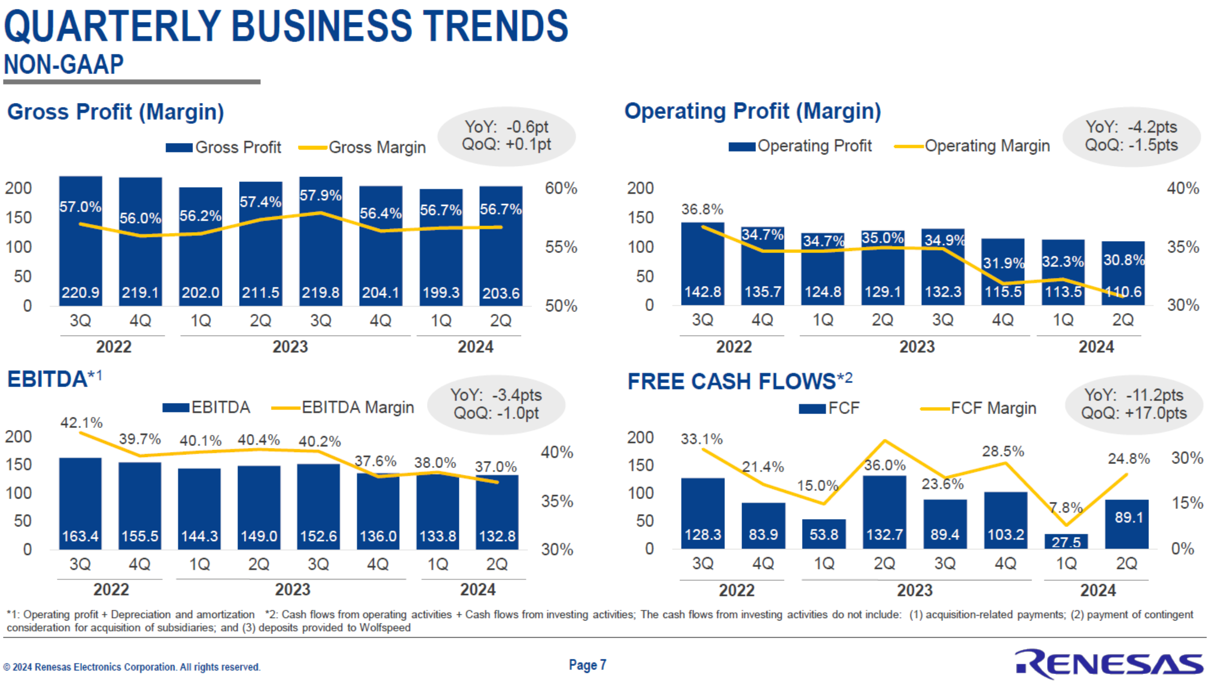
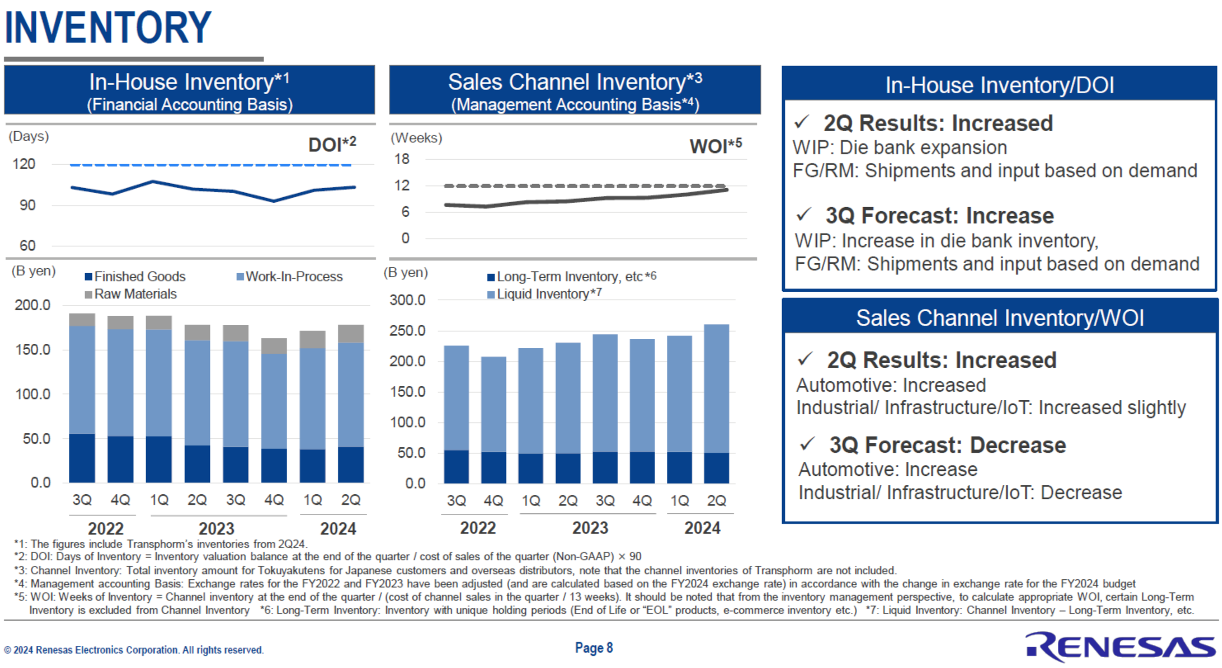
This is about the revenue of the quarterly revenue trends. Q2 is on the very right-hand side. Overall, YoY is at 2.7% decrease and QoQ, it is 2.0% increase. Excluding ForEx, YoY is 8.6% decrease, QoQ is 0.4% decrease. For automotive, YoY, 11.5% growth, in QoQ, up 6.9% 5.6%. As for IIoT, YoY, 24.5% decline, in QoQ, a decline of 5.5%.



Going on to the next page, here, we're looking at the financial indicators.

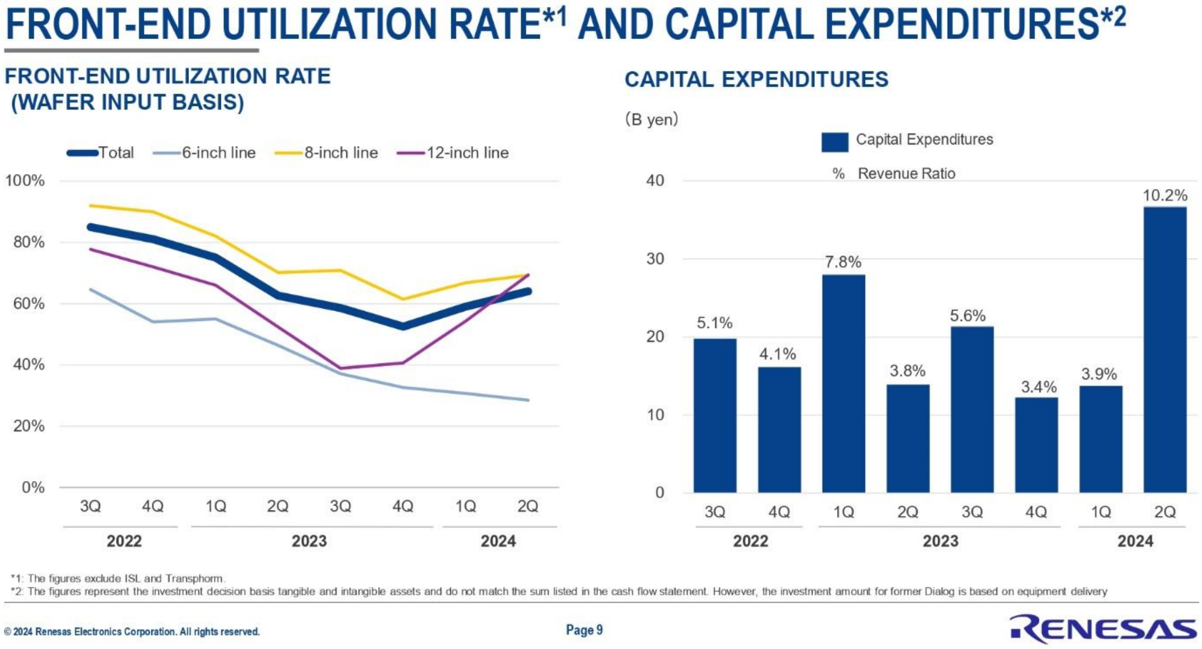
Down below, in free cash flow, Q2 has grown. This occurs in Q1. There has been intercorporate tax paid and also Q1 bonus payment, which have had an impact.



Here, we're looking at the inventory levels. QoQ, we are looking at the factors of inventory level change and outlook to the right. Now, DOI, on a QoQ basis, it has increased to 103 days. This is attributed to die bank expansion, which has pushed up work in progress.

The same applies for Q3 attributed to die bank expansion. The 40 nano microcontroller will be the focus of the expansion. Now, for the channel inventory QoQ, it is increasing to 11 weeks.

As for automotive, as expected, we have seen a rise. However, the rise was minimal. Q3, in actuals actual amount, as well as WOI with the inventory, we have expected growth. However, attributed to the prospects, we believe the pace will be slower. As for IIoT, Q2, we expected a decline. However, expectations are portrayed, and we have seen a rise. This is the impact of the change of trade flow. Basically, sell-through was weaker than expected, around industry and mass market. As for individual factors, infrastructure-related products, there has been a pushout observed. Therefore, overall, we have seen an accumulation of inventory. Q3 and beyond, for the actual amount and also WOI, we're expecting a decline. We expect growth in sell-through, which will have an impact.



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Here, we're looking at utilization. To the left, we have the front end on a wafer-input basis. Q2 is as expected. We have seen an increase. However, on the other hand, in Q3, because of the summer vacation in Q3, we have front-loaded production. Therefore, in 3Q quarter, as a reactionary trend, we expect utilization to drop QoQ, 10% point, a mid-10% point range is expected. To the right, we have CapEx, in Q2,. we have seen the IB purchase and also the integration of office in US, and we have decided on an investment of 10% of sales.

3Q 2024 FORECAST
NON-GAAP

(B yen)	2023		2024					
	3Q (Jul-Sep)	9 months (Jan-Sep)	2Q (Apr-Jun)	3Q (Jul-Sep) Midpoint Forecast (Range)*1	YoY	QoQ	9 months (Jan-Sep) Forecast	YoY
Revenue	379.4	1,107.8	358.8	348.0 (±7.5)	-8.3% (±2.0pts)	-3.0% (±2.1pts)	1,058.6 (±7.5)	-4.4% (±0.7pt)
Revenue (Excluding Foreign Exchange Impact)	-	-	-	-	-12.4%	-3.9%	-	-9.8%
Gross Margin	57.9%	57.2%	56.7%	55.5%	-2.4pts	-1.2pts	56.3%	-0.9pt
Operating Margin	34.9%	34.9%	30.8%	27.5%	-7.4pts	-3.3pts	30.2%	-4.6pts
1 US$ =	142 yen	137 yen	153 yen	157 yen	15 yen depreciation	4 yen depreciation	152 yen	16 yen depreciation
1 Euro=	156 yen	148 yen	165 yen	170 yen	14 yen depreciation	5 yen depreciation	165 yen	17 yen depreciation

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

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Next page, this is the forecast for Q3. Please look at the dark-shaded area in the center.

As to the revenue, the midpoint median of expected range of forecast is JPY348 billion. Gross margin of 55.5%, operating margin, 27.5%, ForEx assumption, USD157, EUR 170. As for revenue YoY, it's a minus 8.3% QoQ, minus 3 %, excluding currency impact, YoY, minus 12.4% QoQ, minus 3.9% is expected. In terms of gross margin QoQ, minus 1.2% is expected. The earlier numbers drove for revenue. As for the factors attributed to Q3, we're expecting a decline in utilization rate.

As for operating margin, 27.5% QoQ, there will be a 3.3%-point decline. This is attributed to utilization drop. Also, the size down on scale and other rise in expenses, and also ForEx working towards a weaker yen. These numbers are expected. As I mentioned, as for OpEx, we will remain R&D expenses. We do not expect to cut down on R&D investment.

STATEMENT OF FINANCIAL POSITION
GAAP

(B yen)	23/3	23/6	23/9	23/12	24/3	24/6
Total Assets	2,840.8	3,123.5	3,292.2	3,167.0	3,233.7	**3,661.6**
Cash and Cash Equivalents*1	361.4	458.1	392.5	434.7	231.8	**288.4**
Inventories	188.2	177.9	177.8	163.1	171.4	**178.1**
Goodwill	1,272.3	1,392.4	1,436.0	1,362.1	1,453.8	**1,602.8**
Intangible Assets	466.9	483.0	467.6	421.8	417.9	**456.2**
Total Liabilities	1,179.7	1,228.0	1,235.9	1,161.4	1,031.4	**1,193.9**
Interest-Bearing Liabilities*2	741.4	733.7	710.3	667.7	532.9	**619.4**
Total Equity	1,661.1	1,895.5	2,056.3	2,005.6	2,202.3	**2,467.8**
D/E Ratio (Gross)*3	0.45	0.39	0.35	0.33	0.24	**0.25**
D/E Ratio (Net)*4	0.23	0.15	0.15	0.12	0.14	**0.13**
Equity Ratio Attributable to Owners of Parent*5	58.3%	60.6%	62.3%	63.2%	68.0%	**67.3%**
Leverage Ratio (Gross)*6	1.2	1.2	1.2	1.1	0.9	**1.1**
Leverage Ratio (Net)*7	0.6	0.5	0.5	0.4	0.5	**0.6**
Average number of shares during the period (excluding treasury stock) (in million shares)	1,799	1,763	1,769	1,775	1,779	**1,789**

*1: This is comprised of cash on hand, demand deposit, and short-term investments that are readily convertible into cash, bearing low risk of changes in value and are redeemable in three months or less from each acquisition date
*2: Borrowings (current and non-current liabilities) + Lease Liabilities (current liabilities) + Lease Liabilities (non-current liabilities) + Bonds
*3: Interest-Bearing Liabilities / Equity attributable to owners of parent *4: (Interest-Bearing Liabilities - Cash and Cash Equivalents) / Equity attributable to owners of parent
*5: Equity attributable to owners of parent / Total liabilities and equity *6: Interest-Bearing Liabilities / EBITDA (Non-GAAP) *7: (Interest-Bearing Liabilities-Cash and Cash Equivalents) / EBIDTA (Non-GAAP)

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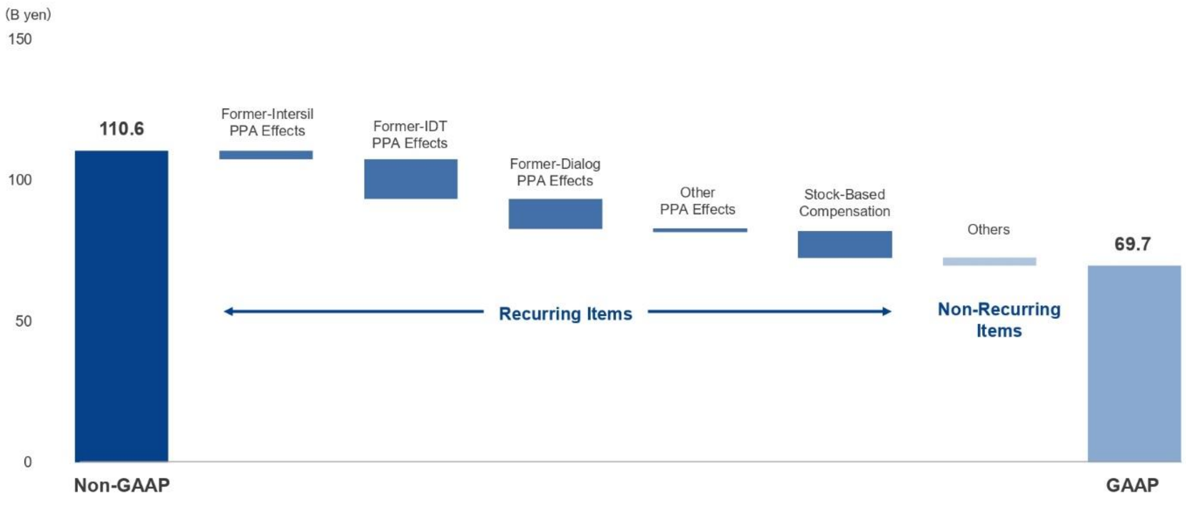
Going on to the next page, let's turn to page 14.

Here, we are looking at the balance sheet end of June. We have conducted a refinancing. Working capital Bullet is JPY260 billion, commitment line of JPY150 billion has been increased.

2Q 2024 CONSOLIDATED OPERATING PROFIT
BRIDGE FROM NON-GAAP TO GAAP



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Moving to page 16, this is a non-GAAP reconciliation. The second one on the right, the nonrecurring item. In Q2, JPY3 billion. This is attributed to noncash mainly for expenses for reorganization of operating business structure. Then, looking at the highlight, as we have mentioned we completed acquisition Transphorm. Also, for Altium acquisition, closing July 1.

With this, we would like to conclude the presentation.

Question & Answer

[Questioner 1]

Q: First, is about your free cash flow. Going to your numbers, in H1, it is about JPY110 billion positive. This is on page seven of the presentation. On the other hand, if you look at the tanshin, the free cash flow is minus JPY85.2 billion. There is a difference of about JPY200 billion. I think the Transphorm acquisition was JPY50 billion. but please explain what additional costs seem to be incurred in the acquisition of this subsidiary. That is the first question.

Second question is about Q3 guidance. Shibata-san, you said that there have been some forecasts, in terms of non-automotive, have to adjust. Could you please give us a little more detail here? It's difficult to understand in the mass market, but for example, was data center shifted, or was the major smartphone manufacturer shifted? I think you have already told us that the market share will decrease, so can you give us a direction in terms of what you're going to see going forward? That's all.

M: For your first question, Shinkai-san will answer the question. For the second question, I will give you the answer.

A: On page seven, we have a note on the bottom of this page. This excludes the impact of the acquisition of subsidiary shares and the payment of the deposits to Wolfspeed. The impact of this latter is one billion dollars in 2024, so that and the cost of acquiring Transphorm make up the difference. That's all.

A: Towards your second question, the industrial market, including the mass market, I think we have seen a major gap there. For instance, I give you an example, it was a specific customer at the smartphone manufacturers. Is there a major change in outlook? No. Basically, that matters, it's in line with our expectations.

In terms of the infrastructure business, this is a combination of AI that is growing tremendously and conventional data centers. At this point, the outlook is a little lower than it was in the Q1.

On the other hand, I think you can have more or less have an image. In the number of customer base is small in this industry. There are some fluctuations due to customer-specific, market-specific factors. In terms of our adjustment of our forecast, it's not because of demand itself has weakened. In fact, due to issues with our devices and other companies' devices used as companions, demand for the platform on which our devices are based has decreased in the short term. That's the reason why we are seeing an adjustment. In this area, it's not that there has been some substantial readjustment of the substantial change in our fundamental outlook.

I think we have seen a different gap in the industrial and the multimarket mass market outlook. In terms of industrial, we have downgraded our outlook substantially. Specifically, it's not a specific segment. If I'm pressed to say so, the so-called hard core factory automation, I think we have to downgrade our outlook substantially in this area.

Overall, industrial business, more or less, we have reduced our outlook here. For the mass market business, it is not a great magnitude that we are adjusting our forecast. Overall, it's a bit weak. That's the reason why we have made a tempered vision in terms of our forecast.

In terms of the mass market business, we have not adjusted our outlook by such a large magnitude, but we have adjusted it downward because it has weakened as a whole. As the questioner has mentioned, it's not the case that a specific segment is now performing worse because there are small industries here. If, by dividing the categories, in terms of geography, that is, Japan seems to be weak. China is rather robust. It's not that different from our initial outlook. Overall, for the mass market outlook, we have downgraded the outlook.

Well, let me summarize what I have just said. In terms of the content, we have made a downward revision for the industrial business and the mass market business. That's mainly where we have made an adjustment.

For the industrial business, factory automation, I think that's a major factor. Overall, the industrial market is weak. With the mass market, not as much as the industrial, but it's still continuing the adjustment. Japan, as a geography, seems to be weak. That's my view.

[Questioner 2]

Q: Just following up on the current discussion, automotive and non-automotive, as well as the breakdown of the three major non-auto segments, the growth rate of the sales in the July-September period is what I'd like to hear about. Based on that, will operations increase in the October to December period under the current scenario? Also, will we see any recovery in non- automotive applications?

As for auto application, will it remain brisk? Paying attention to the overseas market, it appears to be somewhat weak. I would like to hear about your thoughts.

A: As you have mentioned, as for automotive, well, the variance is not that large. Even while the market is strong, we are conducting a downward revision. Hence, what I have just mentioned is in reference to the end demand. It's not about our revenue, but it's about demand in the market. I think it will weaken a little in Q3 from here, 2~3% or around 2%.

In Q4, it's very difficult to predict at this stage. However, as of now, we are taking a more cautious look than before. Hence, for Q3 and Q4, we will continue to maintain a cautious approach for the automotive.

For the mid to long term, on a YoY basis, you can see that sales are growing moderately at a constant exchange rate. Hence, the trend in terms of growth remains unchanged. Therefore, Q1 next year and beyond, we will put in to shape the outlook based on which we will decide on Q4 utilization rate. As of this point in time, I am not taking a pessimistic view.

Non-automotive, on that point, as we have reiterated, for industrial use, we have applied a rather substantial revision of the outlook. As for Q3, from Q2, there will be a decline. At the Q1 earnings call, what we had envisioned was, I do recall that I used the word U-shaped recovery. But I had a rectangular image even though I said U-shaped. There is a bottom, and it goes up.

However, we are seeing somewhat of more of a mild UV curve, and that is what we expect to see up until Q3. In Q4, we expect a recovery. However, we cannot maintain an overly optimistic view. Therefore, for Q4 prospects, internally, we will take a cautious approach in pursuing operations.

Industrial in Q3, not to a large extent, but double-digit. It has been lowered internally by double digits compared to the previous outlook, and in terms of the Q4, it has been lowered quite significantly, by more than 20% from the figure we had in the previous outlook.

Compared to double-digit expectations that we have indicated previously, we're seeing somewhat a cautious approach in Q4, 20%. We will be reducing our outlook. That is how we will see Q3, and we expect there to be a gradual recovery into Q4. Therefore, Q4, the expectations were that we will see quite a substantial growth. However, in the earlier earnings report, we have not changed our outlook to see a mild recovery into Q4.

However, I think that it will still bottom out in the Q3 and rise a little more slowly in the Q4. At the last Earnings, our expectations were that we will see quite a substantial growth in Q4. but now I'm really changing my outlook to a slow climb around the bottom of the U-shape.

Mass market, there has not been a dramatic change. But for Q3 into the Q4, we maintain the view that there will be a pickup. However, we are now shifting to a cautious approach.

As for infrastructure-related, of course, the outlook in terms of substances remains unchanged. However, depending on the movement of specific customers, there are, of course, ups and downs, but the outlook remains basically unchanged.

Q: In terms of numbers, July to September, will you be able to quote?

A: To reiterate, what I mentioned is end demand. In terms of the numbers overall, Q2 into Q3, somewhat of a pickup is expected, so for market itself, we expect a recovery, and we do not expect to see a downfall again from here in the market situation.

However, as we mentioned in this current earnings call, of course, a reflection is that we had expected there'd be a strong recovery in Q2, and we have made our channel inventory numbers. However, we have seen somewhat of a slowdown, and therefore, the channel inventory situation has changed. Of course, this is where we will apply adjustment. In Q3, this will mean that there will be somewhat of a sacrifice in terms of revenue for the growth.

Q: For the second item, broadly speaking, in the half year, I'm sure that your operational excellence is very strong, and you're conducting an adjustment earlier than the peers to register outperformed. Then, in a long-term perspective, with acquisitions in place, you will grow more than the market trend.

However, I will be led to believe that you will be impacted by the cycle. In the six months to a year or anywhere in between, the external impact comes into play. Are you going to be more or less trending on par with the market or due to individual factors against your peers? How are you going to grow your top line in order to outperform? Or will you be able to see that? Of course, I understand it would be very difficult to, of course, overshoot in a very short term. However, six months into a year, will you be surpassing the market? Is there something that you will be able to factor in? How will you see this?

A: As you have pointed out, of course, really turning to the focal question. But in the short term, of course, we believe that it will be aligned with the market. Shall I say, idiosyncratic, in terms of a growth factor that is not, of course, shaken by market trends? Of course, we are looking towards AI. We have mentioned in Capital Market Day, in terms of the proportion to the overall company revenue, it's still very small. Hence, it will continue to grow on a secular basis, but it terms of company, for cyclical or industrial, overall, where there is a volume say, automotive, of course, we will be pulled by trends in these areas.

For ADAS/xEV in the automotive, compared to the past, the proportion is growing now topping 20% of overall, and with the growth factor against the overall revenue, as it continues to grow, the issue of cyclicality can be somewhat subdued. In terms of trends, we will be impacted by the market cycle trend, and this will likely continue.

Internally, we are studying how we will be able to establish a growth factor that is not to operate so that we are not impacted by the market cycle. In the Capital Market Day come next year, I do hope that we will be able to speak about the midterm prospects. As for the long term, the major theme is about the broad-based market, how we will be able to grow on the digital platform.

The market cycle, to begin with, of course, we are looking at the overall market, and hence we will be looking at the margin that we can enjoy so that we will not be impacted by a certain sector in the market. For the time being, as we have seen in direction of the revenue, we will be impacted by the cycle. However, we hope to be able to reduce or mitigate the impact of the market cycle, and we hope to be able to tie that into growth.

[Questioner 3]

Q: I have two questions. The first question is about the China-related business. For the FY2023, the sales of China ratio was 23%, and the previous year was about 28%. It has gone down YoY. Currently, you talked about the China situation, it is more or less robust. In terms of the economic situation and the competition, what is the situation of the China business? In the long term, looking at the semiconductor policy or the strategy of China, what do you think about your China strategy? That's my first question.

A: If you look at the current situation, it's a slight growth in China. Within China, I think things are kind of patchy. Some customers are growing. They are growing smoothly and aggressively. We will focus on customers that have the potential to grow. I think basically, our growth in China compared to the market trend is slightly stronger. Going forward, we are anticipating that is going to be stronger than the market go, so I think that in China, we are going to grow slightly.

In the mid- to long-term, there's nothing new that we are doing. But going forward, the local suppliers' competitiveness is going to become stronger. Our customers in applications, in the short term, they tend to have excess capacity and go into very aggressive price competition, and we are continuously seeing that trend. The pricing pressure coming from that situation is becoming stronger. I think going forward, it will come stronger than ever.

From our point of view, in the China market, rather than trying to increase the share, we would like to focus on the strength and to go into fields that we can leverage the strength and then try to compete in other areas. In terms of the top line, we want to grow that steadily. In some cases, even if we lose some shares to the local competitors, we have to accept that. In terms of top-line profit, that will be a focus in China. In terms of share in the China market, that will be our second priority. Specifically about this view, there's nothing new that we're doing. For the time being, I think there will be our stance in the China business. That's all for me.

Q: My second question is that under COVID-19, there has been some difficulty procuring semiconductors. There's some I think basically, some companies are arguing that they are more competitive because they have the enough capability to produce the semiconductors. Is your stance, fab-light strategy, is that becoming less of an advantage? If that becomes a disadvantage, then how are we going to respond to that?

A: Well, basically, it's not the case that we are disadvantaged in any area. I don't think that we are in a disadvantaged position. Of course, in the foundry partners, China plus one, plus one strategy, they are strongly aware of that type of strategy, and the foundry partners are taking necessary initiatives. It's not the case that if we are in a disadvantaged because we don't have an in-house fab.

As you know, during the pandemic, due to this situation, I think we have lost some positions. That's the mobile share losses. But I think the situation has changed since then, and the foundries have taken necessary measures themselves.. We are not worried. This fab-light strategy that we're taking internally, do we have any concerns? No. Absolutely not. I think we can go forward with our strategy going forward as well.

[Questioner 4]

Q: First of which is the following. This may be a repeat for industrial. I have a question. Beyond expectations, sell-through has declined, and therefore, logistics supply has increased, and therefore, you have had to conduct a downward revision.

With sell-through being weak, what is the backdrop? What is your analysis? I would like to inquire. Customers have their inventory. Was it more than expected? Or was it that the end demand was weak? In terms of supply and demand, the demand, is it just being pushed out, or on FA-related, demand layers are also increasing? The share of the customer might be declining. Is that because the demand is declining? If this is also a factor, we would like to hear about that.

A: As to the last point that you made mention of, as to the share, this is not a matter of much concern. Of course, as of now, the proportion of Japanese customers is very large, and that's a fact. But not just restricted to the West, but in China, there are many clients that are globally competitive, and their business is growing.

Just a little while ago, we have received quite a large design and order. Hence, depending on the variance of the customer share, will this have an impact on the mid- to long-term? That will not be the case. Of course, in the short term, say, on a QoQ basis, that might be the case. However, from the mid- to long-term basis, this is not a matter of concern.

However, when we look at the short-term demand situation for a certain specified rather than for certain segments within industrial, overall, demand continues to be weak, and that is how we see the situation. This might have been expected. However, when we look at the channel partners and together with our partners, we may have overemphasized some bright signs, or we do not want that to pass by. Hence, we took a rather aggressive sales. However, that bright signal dimmed as the days went by, and that is a situation.

Hence, overall, the market situation has continued to soften, and that will describe the situation. Subsequently, clients' consumption of inventory has taken time. Under COVID-19, inventory has piled up. Of course, we had expected that, that would be consumed, and things will turn for the better. However, right now, we are finding that demand is weakening and which has also indicated that consuming inventory has taken more time earlier than expected.

You might, of course, wonder if this has actually lagged to the future. Perhaps that could be described as such. Shifting to the future, some may have expired, that have been lost, especially when we look at the market situation in China, it's not really that bright. We understand that we need to take a cautious approach. Therefore, internally, we have applied a rather large adjustment. I do hope that this will be a response to your question.

Q: As for the second question, you have also pointed this out at the outset, Q3 guidance, SG&A is quite high on a QoQ basis, of course, the [inaudible] numbers are really increasing. What is your plan in terms of percentages of scale or scope? Will this continue in the days ahead? I would like to inquire.

A: Our CFO, Shinkai will fill in on the details, but we do not expect this will expand in terms of percentage. This is to increase the top line, where the OpEx has continued in this manner. If the top line does not grow and actually, we will have to cut down on the OpEx in terms of the percentage, but right now, this has been done for the sake of increasing the top line. What is maintained in OpEx will somewhat taper down. Now to you.

A: As for OpEx, basically will be maintained because of maintaining investment in R&D. And on QoQ, currency impact has raised the numbers. As a result, in terms of ratio, it appears to be very large. However, the impact of the top line will also drive this number. Therefore, in terms of the number, we expect the numbers to decline.

[Questioner 5]

Q: I think at the beginning, Altium acquisition is going to end in Q3. Of course, it is not reflected in your guidance. I understand that. In terms of Altium, do you have any new updates that you can give us?

My second question is a duplication of what has been asked on the previous person. But Q2 SG&A is about JPY4 billion increase compared to the midpoint of your guidance numbers. At the beginning of the presentation, besides the currency situation that you explained, you have underestimated the impact of the yen besides the key currencies, is it because it's currency? Or are there other factors? I think basically the JPY7 billion increase of SG&A, is it due to the currency between Q3 and Q4?

A: I would like to give a quick answer for the first question. Second question will be answered by Shinkai-san. Well, as Shinkai has explained currently, next week, the transaction has been closed for Altium, and if things go smoothly, in August, September, at least two months will be consolidated into our financial results.

That said, in terms of the numbers, it's not a big number. It won't move the needle that much. In terms of gross margin and operating margin, this will be operative to our business. That's true. Financially, there will be a positive impact. No negative impacts coming from this. In terms of the substance of this acquisition, we will give you an update in a timely manner.

Based on these discussions, the arm's length that we have initially anticipated, I think it has been more trying to do it together. I think that's the direction that we're looking at. In terms of neutrality, it will be 100% secured. On top of that, in terms of organizational initiatives, we will be working together more. I think a more integrated management will be conducted looking at digitalization. I think at the right timing, we'll give you an update. Shinkai-san, please talk about the OpEx situation.

A: Q2 forecast is about an increase of JPY4 billion against the forecast, about JPY1 billion is coming from R&D, the timing difference of R&D spending rather than spending is the incoming cash difference. The remaining JPY3 billion, half of that is coming from the minor currency sensitivityunderestimation and the remaining half is because of the weaker yen, R&D spending is going to become bigger.

For Q3, plus JPY4 billion and half is about currency, half is but non-currency factors plus our estimation. In the incoming cash, that's not finalized. We are taking an initiative [inaudible] transform is going to be contributing in Q3. That's reflected as well.

Q: You talked about to be able to grow the top line, you are going to use your OpEx. But for example, are you going to increase the R&D expense for next generation R-car?

A: Well, as an image, I think, yes, your image is correct.

[Questioner 6]

Q: The first of which is a reference to the acquisition of Altium. Semiconductor market is, of course, weak, and it comes at that timing. Once again, your expectations or any comments that you might have. As acquisition is completed, ultimately, will the situation improve more than what is visible today?

The second question is about China. China is stepping up investment into mature segments, into mature nodes. As we look at the future for Renesas, in the mid- to long-term, is it going to be a risk? I would like to hear your thoughts.

A: I do not have much to add from what we have discussed today. As for Altium, as we have mentioned, in terms of financial impact, it's basically negligible. As whether it's plus or minus, it will work to the positive, but the scale is limited. It is very negligible to the extent that you have to start the study very hard to find where that is. We hope to be able to accelerate our movement towards digital.

Of course, the momentum is built in on both sides. The transaction has not yet come to a close. Hence, it is still too early to say. Therefore, I would like to refrain from speaking further. After July, at the best timing, we will be able to update you, and you'll be convinced that more than before, we are working on integration for the introduction of a digital platform, and you will be able to see that we are working in that direction. There will be signs that will be visible, so please stay tuned.

As for China, there is also not anything more to add. As of now, the Silicon IGBT will have the largest impact. From last year, the impact has already become visible, and we're looking at the revenue of IGBT in China. As for the outlook ahead, to reiterate, we believe that it is very difficult. That is when we have said from the end of last year and conducted operations. Nothing really has changed, and we believe that we're still in a very tough situation.

As for power discrete, what is going to happen to SiC in mature node, Micon, analog, what is going to happen might be the question your thoughts. Micon and also analog from the mid- to long-term, we are expecting a large impact, but we believe that it is going to take time. We still have some time ahead. We will pursue digitalization so that we will be able to shift upstream in the value chain, and that is, of course, one of the themes of the acquisition.

As for SiC, it's very hard to say as for now because the situation is a mixed bag. Some will say that the China SiC device quality is already up to par. Others will say that they're still not there yet. A mixed view will be the right way of referring to the situation, but the market overall will grow. We are also ready to participate in that market. Of course, as a solution, it's important, and we will commit.

As we have mentioned, to continue to invest our resources in order to really scale the size of the business, that is not the way forward. Of course, we hope to build our presence, but it will be a part of the total solution in our portfolio. Nothing has changed. That is all. Thank you very much.

[Questioner 7]

Q: I would like to have two questions about the automotive sector. You said that you have reduced your outlook in terms of demand. In terms of, is it about the sales volume or due to the component makers' common factors, is there a change in how they hold the inventory? Can you give us more details?

The second question is that you have outlook in terms of demand. But in terms of US sales, on a QoQ basis, I think can we expect the QoQ sales is going to increase. In our consolidated basis, the top-line decline seems to be large into the QoQ sales. What is your outlook of your automotive business?

A: For our automotive business, in terms of the sales, we are changed to take a more conservative view. Rather than trying to grow aggressively, we want to observe the market situation closely and control the inventory. Specifically in Q3, we are going to reduce our outlook in Q4. Still early to say, but whether we're going to take more aggressive outlook, I think we're taking a more cautious stance.

The reason behind this is that, as you just pointed out. There's two factors that are playing. One is that the third party says that the worldwide you need outlook has been downgraded. We have had that type of information. If there is a situation, even your tier one customers, I think, basically, we'll have to be more cautious in terms of holding inventory, and I think that's natural.

In terms of the trend, I do not think that we have seen a major change in the trend. There are some customers that they are controlling the inventory to a level of very minor products or demand of the customers. I feel that maybe if you just reduce the inventory too much, maybe if the demand goes up, then they will be lacking this component. We do want to continue to confirm with the customers whether their inventory level is too low. From a customer's point of view, I think they had some internal pressure to reduce the inventory, and they want to control the working capital. I think that's a strong trend out there in the market.

For the automotive business, rather than us controlling the inventory, I think the trend is that the EBITDA is going to increase gradually. Rather than trying to aggressively increase inventory like before, I think our sense is that we look at the situation closely and be cautious rather than aggressively swinging positive and negative, we are decelerating, and that's the automotive. For industrial, I think basically, we're going from the positive to negative in the major manner. I think that's the difference of the perspective that we have for these two markets.

[Questioner 8]

Q: The first is in reference to, in a growth market, one component is AI. In AI, you have two HAIs, one is edge AI. I believe you acquired some company in that particular segment. What has happened?

As for data center generative AI, for example, the NVIDIA chip, if we look at their situation, not just so much to NV, but HBM or there are also other microprocessors that around that. I'm sure that could be a potential target. What is the current situation for data centers, acquired IDT, and the clock products, I think, will be viable for the data center. What are the circumstances? What steps are you taking?

A: As for generative AI, in terms of value, we are expecting growth. However, in terms of volume, the unit price is very high. In terms of volume, it will not really grow, possibly it might actually be lower. What is the implementation on our side? The system and the volume system is not going to grow, but the generative AI, how can we capture the demand for generative AI from our business? I think that's your question.

For what is particular to degenerative AI will be GPM and HBM. For HBM, the increase will not really have a great advantage to us. It's sorely positive, but the GPA growing and also considering the timing power, we will also be able to enjoy a tailwind in our power devices. Because of confidentiality, we are constrained from speaking further, but the number of customers is limited in that space with a single platform, due to various factors, Platform A could go ahead and Platform B could be delayed or the reverse. That's what we're seeing right now.

As to which platform and with whom we are aligned, in the short term, shift the situation. As of now, we're looking at the combination. Are we seeing a great tailwind in our favor? That's not the case, but we are seeing solid growth. In Q4, we have, of course, reflections. Hence, I would like to refrain from making any optimistic comments. As we look at the numbers within the company, Q4 and beyond, we can expect to see a good recovery, especially around GPU power products.

As for the timing and also for the microprocessors, of course, that's an advantage. But with generative AI, we do not expect to see a spike, and that is how we are seeing the situation. For edge AI, this is something of that is coming in, the edge AI in its truest form, as to whether it's going to be growth substantial. It's of course, it's indispensable. It's sort of like similar to how we've viewed connectivity. It will gradually grow, and we need to take necessary steps to prepare ahead thoroughly.

As for PC AI, in the short term, there are specific set makers and application processor vendors that are not really visible in the market yet, but when their presence is there from DDR5, there'll be a push-up, and there will be a positive impact. Generative AI, in the short term, there will be ups and downs.

In Q4, end of the year, we are hoping to see growth, especially around power. That's one thing. Before and after, with Client PC, there's also tailwind. While not directly felt, the impact will be indirectly felt. As for Edge AI, we need to take a mid- to long-term stance. It's very difficult to capture specifically, but I'm sure we believe that it will become indispensable.

Q: As for the second question, if we look at the Q2 performance, the overseas ratio, for instance, in terms of geography, Japan, United States, Europe, Asia, China, if you divide it by geography, roughly speaking, what is your breakdown by geography?

A: Overseas, of course, it is increasing. Roughly speaking, less than 80% is about overseas sales. Japan is around 20%, remaining would be US is stable, about 10% plus Europe, same as the plan, it's a soft market, maybe 50%, Europe going down to about around 15%. China, which is relatively strong, going up to 30%, and others. There will be the breakdown. China and US, they are relatively strong. Japan and Europe is weak. As a result, the oversea ratio has, all in all, increased a bit.

M: Thank you very much. With this, we would like to end the Q&A session. Lastly, Shibata-san, would you like to say a word?

Shibata: I think this guidance of Q3 about this earnings report, I think everybody is disappointed, and this is the inflection I have. We will try to start up once again, on Q4 onwards, especially in the fiscal year, we would like to maintain a speed of growth. In terms of R&D, we will put in efforts to invest there. Even if we have to control a top line, we will adjust the inventory in the short term. Q3, Q4, we don't know how this is going to trend, but I hope that we'll be able to satisfy you in terms of our performance and continue to satisfy it. That is the reason why we have changed our tracks at the current timing.

Moderator: Thank you very much for attending despite your very busy schedule. I thank you for your continued support.

[END]