Q&A Session on Financial Results for the 2nd Quarter of Fiscal Year Ending March 31, 2023

(Q) Given the growing uncertainty in the external environment, you have left your financial forecast for FYE3/2023 unchanged. However, are there any specific profit-depressing factors envisaged for the second half of this fiscal year, such as a weaker top-line due to the recession in Europe and the U.S., or an increase in credit costs?

(A) We don't see any specific profit-depressing factors. In fact, we re-estimated the expected net income on each business segment in advance of making this presentation, and the sum of such re-estimated net income slightly exceeded our financial forecast of 110.0 billion yen. However, given the growing uncertainties of the economic outlook in Japan and overseas, we took a conservative view and kept our financial forecast unchanged.
We have factored in a slowdown in the business growth in Europe and the U.S., but at this point we do not believe that the specific businesses will fall significantly due to the recession.

(Q) Regarding the performance next fiscal year and beyond, which businesses do you think will be the drivers for the profit increase in the environment that the market for marine container leasing calms down, the aviation business in Asia slumps, and European and the U.S. economies enter the recession?

(A) We have a well-diversified portfolio and many of our businesses have grown.
As a result, even amid the COVID-19 pandemic, the decline in the aviation business was offset by the real estate business in Japan, among others. Even if the top-lines mainly in Europe and the U.S. businesses were declined from next fiscal year, we hope to achieve solid growth through various businesses in conjunction with the gains on sales of the assets.

(Q) Apart from the external factors, could you also talk about the internal factors you think for contributing to the profit increase next fiscal year?

(A) Regarding the comparison with this fiscal year, we see the Aviation segment will contribute to the profit increase. In our latest results, we posted the impairment loss of several billion yen in the aviation business, however, the airline that was subject to the latest impairment loss made every effort to survive amid the pandemic, but eventually filed Chapter11 this year. At the same time, other airlines have seen a recovery in their earnings, and we do not estimate new impairment losses ahead. Therefore, the absence of the impairment loss and other negative impacts on this fiscal year's results will make a positive contribution to earnings next fiscal year on a YoY basis.

In addition, with regard to the foreign exchange losses incurred by JOLCO[1], which increased significantly this fiscal year, we think this will be also a positive factor next fiscal year on a YoY basis, provided there is no further weakening of the yen. Additionally, in the aviation business, if airline performance recovers and the market for used aircraft returns to pre-pandemic levels, this could be a factor for the profit increase next fiscal year.

(Q) Could you comment on the effects of the integration of the marine container leasing subsidiaries?

(A) We expect the acquisition of CAI to contribute just under 10.0 billion yen on a net income basis, taking into account the amortization cost on the goodwill. With regard to the business integration of CAI and BIL, we expect to post around 1.0 billion yen of PMI-related costs this fiscal year ahead of the integration in January 2023, but these costs will also be absent next fiscal year. Consequently, we believe the new company will contribute steadily from next fiscal year. Moving into the second half of this fiscal year and the next fiscal year, we see the utilization rate for marine containers is likely to fall somewhat from the peak of 99.9%, but we still expect to maintain a high level of utilization and do not consider this to be a significant negative factor for our growth.

[1] Exchange revaluation losses generated in the accounting process in relation to foreign currency-denominated borrowings for multiple deals booked at Mitsubishi HC Capital under Japanese Operating Leases with Call Option (JOLCO) originated for domestic corporate investors

(Q) Credit costs in the Global Business segment in 2Q FYE3/2023 (three months from July to September) increased compared to 1Q FYE3/2023. What were the factors behind that?

(A) As shown in 'Credit Costs by Segment' on page 32 of the Financial Results for the 2nd Quarter of Fiscal Year Ending March 31, 2023, cumulative credit costs in 2Q FYE3/2023 (covering a six-month period) decreased by 7.2 billion yen YoY, with improvements in Europe, the Americas and China contributing. In addition, there was a reversal of credit costs for miscellaneous small transactions in the Customer Solutions segment. There was also a reduction in the Aviation segment, which credit costs were posted mainly in Asia in the previous fiscal year. Only in the Real Estate segment, credit costs were posted for a certain project in the U.S. Therefore, we recognize that overall credit costs have improved YoY.

In terms of the quarterly change, credit costs in the Global Business segment amounted to 0.6 billion yen in 1Q FYE3/2023 and 1.4 billion yen in 2Q FYE3/2023. This includes 0.3 billion yen posted in the Europe region in 1Q and 0.8 billion yen booked there in 2Q. The figures were 1.1 billion yen in 1Q FYE3/2022 and 0.7 billion yen in 2Q FYE3/2022, so there has not been a noticeable increase compared to the same period of last fiscal year.
Comparing 1Q and 2Q of FYE3/2023, there was a slight increase in 2Q compared to 1Q, but this is within our expected range. In the Europe region, we are also involved in consumer finance, and interest rates in this business were originally set higher in anticipation of credit costs. Therefore, it is not something that will have a significant damaging impact on earnings in 3Q and 4Q of FYE3/2023.

(Q) Could you talk about changes in the risk outlook for the overseas businesses, including the Global Business segment, in the first half of FYE3/2023?

(A) We have managed to keep credit costs low level. With regard to the Aviation segment, considerable impairment losses and credit costs were recorded in the previous fiscal year, but we believe risk will diminish moving into next fiscal year, as we estimate that airlines will turn profitable. In the Global Business segment, even during the COVID-19 pandemic, there were no large-scale bad debts in Europe and the U.S., but we need to keep a close eye on the situation through the second half of this fiscal year, given the increasing risks about the recession. In Japan too, we will keep a close eye on the impact of the suspension of "zero-zero loans" through to the end of the year.

(Q) I understand the Aviation segment will be in a position to increase assets going forward, but how do you view the market in terms of the volume of assets?

(A) The aircraft leasing and aircraft engine leasing businesses essentially consist of lease revenues and gains on sales of used aircraft and engines. On the current basis excluding impairment losses and credit costs, we estimate that earnings are around 70% of what they were before the COVID-19 pandemic.

The International Air Transport Association (IATA) statistics show a recovery of air passenger demand to negative 18% for full-year 2022 (versus 2019), compared with negative 58% in 2021 (versus 2019). A return to pre-pandemic levels is forecast in 2023 for domestic flights, and in 2024 with international flights included. Total airlines' revenues are also expected to return to profitable levels in 2023.

Given these circumstances, we think we will be in a position to increase the number of aircraft. However, as before, we are carrying out new transactions mainly on a sales and leaseback basis in line with the actual demand of airlines, and, at the moment, we do not estimate to increase the number of aircraft through the direct order to the manufacture based on a certain demand forecast. We intend to engage in the business while carefully evaluating demand among airlines with taking advantage of the experience of the pandemic, including reviewing our credit policy.

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