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August 23, 2024

Q & A on the 2Q/62nd (2024) Financial Results Presentation

Date and time: August 20, 2024 (Tue) 10:00 - 11:20

Answered by:

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In the revised Previous Forecast (disclosed on August 13, 2024), the Operating Income Margin is lower than the same period of the previous year.

Is it because of the increase in personnel expenses due to securing human resources and human capital investment?

The increase in labor costs is one of the reasons for the decline in Operating Income Margin.

We reviewed our re-employment system for retired employees in April 2024. Under the revised system, even after the mandatory retirement age of 60, the personnel treatment system (including grades, performance reviews and remuneration) will continue to be applied until the age of 65. This also contributes to an increase in labor costs. Another factor is the increase in labor costs due to wage increases.

You explained that you are actively working to secure human resources.

What are the areas in which you are particularly focusing on expanding and strengthening your human resources?

Most of the new graduates recruits are from the civil engineering field. Many of them are often assigned to our core businesses. In order to expand our business, we want to strengthen human resources in the fields of telecommunications and energy. In these fields, mid-career employees who are ready to work immediately are employed and strengthened.

With regard to efforts to prevent errors, what business fields are targeted by systems for reducing design errors?

Also, how do you expect the results of measures to prevent errors to have the effect on business performance?

We developed the error prevention system for bridges and river structures (sluice gates and sluice pipes) in this term. From the next fiscal year, we plan to expand to other fields.

As a result of error prevention measures, it is expected that labor costs will be reduced by preventing repair work and rework work due to errors, leading to higher income and productivity.

What causes the difference between forecast and actual results in 1Q and 2Q?

We have many public works in the consultant business which our company receives the order. For this reason, we have many works whose construction period ends in 1Q, and there are also many contract changes such as an increase in the amount at the same time. As of 1Q, it is difficult to estimate the number of contract changes, so there is a gap between the earnings forecast and the actual results.

According to the data on orders received by business sector, Orders Received by the Water and Land Sector decreased from the previous quarter. What is behind the decline?

This is because the timing of projects in the river sector that has been pushed back to the second half of the fiscal year.

In recent years, an increasing number of projects in the river sector are carried over from one fiscal year to the next.

As a result, orders for the year have been pushed back to the second half. We expect to secure profits in the current fiscal year if it receives orders for work to be ordered in the second half of the year.

Will the upward revision of the earnings forecast for this fiscal year affect the earnings from the next fiscal year? Please tell us if you have a policy for the next fiscal year and beyond.

Now We can't tell you the numerical target, etc. for the next term at this point. We are making the next Mid-Term Management plan. This is because the current Mid-Term Management plan enters its final year.

As for securing human resources, do you plan to increase and expand the number of employees at the current pace?

We recognize that strengthening human resources is the source of our sales growth. We plan to continue to secure human resources while taking into account the workload of employees.

In Q2 alone, Sales were down ¥ 1.3 billion Yen, while Operating Income was down ¥ 2.7 billion Yen. How much of the decline in Operating Income is due to an increase in labor costs?

Although the specific extent of the impact cannot be explained, the increase in labor costs affects the Cost of sales and SG & A expenses.

The increase in labor costs in the Cost of sales is mainly due to the strengthening of human resources and the strengthening of checks to prevent errors.

SG & A personnel expenses increased along with the strengthening of human resources. In addition, an increase in Labor costs due to the reform of the personnel treatment system implemented last year has also an effect.

What changes in the business environment have you noticed in your Overseas Business from the beginning of the year to the present?

As for Waterman, which operates in the United Kingdom, we feel the impact of the change of government on the Labor Party. At present, Orders from the public sector have stopped due to the change in government. The Labor Party itself has a manifesto to strengthen investment in infrastructure and other public works and housing. We think that's a boost for Waterman.

What forecast do you have regarding the domestic political environment changes and their impact on public works investment?

Under the current administration, it is expected that National Resilience will be continuously and stably promoted based on the "Mid-Term Plan for Implementation of National Resilience."

On the other hand, it also assumes a scenario of a reduction in public works budgets and recognizes that it will be important to secure orders through technological competition when the competitive environment becomes severe.

You explained that the initial plan for this fiscal year was aimed at reducing the workload of employees by reducing the amount of Orders Received.

Are we making progress according to the initial plan?

The workload is under control to a certain extent, and progress is generally in line with the initial plan. In the future, we plan to secure a certain amount of Order Received while taking into account the workload of employees.

What is the OI Margin target for Overseas Business?

As for the Domestic Business, how is the sustainability of the 2Q result of around 13%?

In the Overseas Business, there are many uncertain factors such as the increase in labor costs at Waterman, high interest rates and inflation worldwide, and the economic slowdown in the United States. However, business order volume is expected to recover in the United Kingdom, and infrastructure needs are expected to continue in Asia. Both companies will strive to increase orders and improve profitability. I cannot give a specific target for the Operating Income Margin, but I would like to aim for an improvement from the current level.

As for the Domestic Business, there is a limit to cost reduction from the viewpoint of quality assurance, and we believe it is difficult to secure gross profit. In addition to reducing SG & A expenses, we want to secure profitability by improving operational efficiency through the use of AI, etc.

How do you see the goal of increasing the number of employees?

How many employees will need to be secured in the future to eliminate the burden on employees?

We regard working hours as a benchmark, and we believe that if the total annual working hours fall below the current target of 2,000 hours, it can be regarded as the elimination of employee load to a certain extent.

In addition, it is important not only to increase the number of personnel but also to improve productivity by utilizing DX, AI, and IT.

After the change in accounting standard in 2022 (adoption of the new revenue recognition standard), the quarterly profit amount was recognized as leveled, but it seems to be volatile this quarter. Will the quarterly fluctuations in profits continue?

In general, the yield on the percentage-of-completion basis tends to be more uniform than that on the percentage-of-completion basis. However, as mentioned in the above answer, the fluctuation factor in 1Q is large for us. In the future, the range of fluctuations in 1Q and 2Q, which is affected by 1Q, is expected to follow the same trend, but considering the first half of the year as a whole, it is not expected to fluctuate so much.

How do you anticipate the impact of the revision of the Ministry of Land, Infrastructure and Transport's "Unit Price for Design Outsourcing Engineers"?

The unit price of orders for design work is expected to rise by about 5% in conjunction with the unit price of engineers. On the other hand, in the case of order placement based on the proposal method, the unit price of engineers is not directly linked to the unit price of orders. So, it's hard to gauge the impact.

Do you expect SG & A expenses in the second half to increase at the same rate as in the second quarter?

We do not currently anticipate an increase in SG & A expenses in the second half.

The explanation is that both Sales and working hours per an employee have decreased as a result of the reduction of the labor load, but from the viewpoint of production efficiency, it is rather declining. This is an issue that should be discussed on a different axis.

The explanation is that as a result of reducing the workload, both Sales Amounts and working hours per employee are decreasing. But from a productivity point of view, I would rather say that it is declining. This is an issue that should be discussed on a different axis. You're right. Originally, it is recognized that the reduction of working hours and the improvement of productivity should be realized by both wheels.

At present, as a short-term measure, it is taking measures to increase human resources and reduce the load. In the mid-to long-term, it is a policy to improve productivity per person by AI utilization and project management.