Hakuhodo DY Holdings Inc.

FY2023 Consolidated Results Briefing: Q&A

Tuesday, June 4, 2024, 17:30–18:30

Presenters:
Masayuki Mizushima, Representative Director & President
Hirotake Yajima, Director & Executive Vice President
Masanori Nishioka, Representative Director & Senior Executive Corporate Officer
Akihiko Ebana, Director & Senior Executive Corporate Officer
Takeshi Tokugawa, Senior Corporate Officer

- Has the overcharging incident at Nihon Total Tele-marketing (“NTM”), which caused the delay in the announcement of financial results, affected financial results before FY2023? Might it also affect business performance in FY2024 and beyond?

NTM has had similar contracts with municipalities other than Kyoto City so we are now looking into the possibility of overbilling under those contracts. That is why we had to postpone the announcement.
Based on the findings of the internal investigation conducted by NTM, we have integrated the impact of the Kyoto City case in the financial results for FY2023 in consultation with the auditing firm.
If any new overcharging incident that would affect business performance is identified, its impact will be recorded in the financial results for FY2024.

- Have the Measures to Streamline the Balance Sheet (“B/S”) been completed with the disposal of cross-held shares in FY2023? Or are you planning to take measures under a new financial policy?
- Why does the new dividend policy use the dividend ratio over dividend on equity ratio (DOE) or total dividend payout ratio?

With regard to streamlining the B/S and dividend issues that you mentioned, we need basically to consider operating cash flow (“CF”) and the balance of its use. In the medium term, in principle we will ensure shareholder returns and business investment/CAPEX within the limits of operating CF, but we might need more cash in some of the years to finance M&A, for example. In such cases, we can secure funding through borrowings, etc. but streamlining the B/S might also be an important option.
Although we cannot determine at present to what extent we will resort to asset disposal, we are planning to make further efforts to generate cash, including by disposing cross-held shares and other assets.
Although our dividend policy has focused on “stable dividends,” shareholders and investors expressed in interviews their concern about the lack of concrete indicators, hence the inclusion of a new dividend ratio target of approximately 30%.

- What are some of the assumptions on the earnings forecast for FY2024 (e.g., trends of clients in Japan and overseas, prospects for selling, general and administrative expenses and developments in BPO business)?

Starting in FY2024, we will be reporting "adjusted" numbers," i.e., excluding the gain on disposal of Mercari, Inc. shares held by UNITED, Inc., one of our consolidated subsidiaries. The "adjusted" data indicate an increase of over 6% in billings, a slightly better growth of approximately 7% in gross profit, and a rise of 11.4% in operating income before amortization of goodwill.

We expect the Japanese advertising market to grow by approximately 1%, but our forecast indicates topline growth of 5% in anticipation of a better market share in Japan and the end of the effects of the reactionary drop after the termination of COVID-19–related BPO projects. In overseas markets, we assume double-digit growth including the positive effect of foreign exchange rates.

Although we plan to bring the pace of recruitment to the ordinary level this year, the growth of selling, general and administrative expenses in Japan will be on a par with, or slightly exceed that of gross profit due to the full-year impact of the previously hired employees on personnel cost. Unlike previous years, however, we are not planning any further increase in strategic investments. Outside Japan, we are planning for lower growth in selling, general and administrative expenses than gross profit as a result of structural reforms.

・ Please explain your ideas on cost management under the new Medium-Term Business Plan.

We believe that we have succeeded in improving our competitiveness in the marketing domain through proactive strategic investments over the past two years, which enabled us to recruit skilled workers to reinforce our infrastructure. We are hoping to translate this into improved operating margins going forward. Yet, we expect the cost to increase somewhat in the integrated marketing platform and commerce business domains. We also would like to continue investments required for scaling the growth domains, including technology and consulting.

That said, we are planning to control overall costs, making necessary investments within the limits of the growth of gross profit, with the aim of improving our operating margin.

・ What is the scale of the potential impact of NTM's overcharging incident in FY2024? Is that impact included in your earnings forecast as an extraordinary loss?

We cannot specify the exact amount but wish to note that no retroactive adjustment was deemed necessary in view of the findings of NTM's internal investigation, and in consultation with the auditing firm.

Thus, we have made no downward adjustment to the billings presented in the earnings forecast for FY2024 to reflect any impact of the overcharging incident.

・ It seems that the consulting business overseas has been slow to recover. How do you interpret this?

Despite concerns in some areas, including China, developed markets are largely stable, particularly in North America, hence our projection of around 5% growth overseas in general.

We recognize that kyu, which is mainly focused on the consulting business, is now experiencing changes in the business environment as companies discontinue or postpone consulting-related contracts.

Although we just mentioned our expectation for 5% growth overseas, the changing business situation warrants continued monitoring. Nevertheless, we believe we can return to profitability, as the structural reforms launched last year are expected to bear fruit.

- You just mentioned monitoring indicators. How about the result of the previous year and the forecast for the current year by business domain, in terms of gross profit?

As regards the new domains, we have to limit ourselves to future forecasts as it is difficult to make any comparison with the previous year's performance.

The gross profit of the marketing business in Japan is expected to grow some 4% per year, a level that we think we can achieve this year too. However, it is difficult at present for our marketing business in Japan to achieve the 15%+ target set for the operating margin before amortization of goodwill. Going forward, we aim to improve the operating margin through the effect of the IREP/DAC merger and increased back-office efficiency by establishing Hakuhodo DY Corporate Initiative. As regards digital marketing in Japan, "above-market growth" has been the target for the average annual growth of our gross profit.

For the new growth options, we aim for an average annual growth of at least 10%.

Regarding global business, we expect growth of at least 5% this year, but we need to make improvements because it would be difficult to reach organic growth of 5% excluding the effect of foreign exchange rates. Likewise, we are aware of the necessity of improving the operating margin through robust structural reforms.

- Is it possible to realize around 50% profit in the growth domains by FY2031 with the existing capabilities? Or do you need to take action to achieve stepped growth, such as large-scale M&A and structural reforms?

We are discussing new growth options with relevant Group companies. For example, some argue that it is necessary to obtain IP for content business, and new functions for commerce business. Although we have set our goal to be achieved by FY2031, we believe that CAPEX and M&A will be needed in the longer term both in Japan and overseas, on the premise that the goal is unattainable with the existing capabilities alone. We will proceed with cautious discussions over the coming three years in view of both the internal and external environments.