

Analyst session for fiscal year 2021 third quarter financial results

Q&A

Date/Time February 9, 2022 / 18:30-19:30

Speakers

Ashwani Gupta

Director, Representative Executive Officer, COO

Stephen Ma

Executive Officer, CFO

Questions & Answers

Question 1:

In Q3, on a consolidated basis, you have delivered great results. But when it comes to the automotive business, it seems like you are still making losses. What are the issues?

Answer 1:

Ma: Auto profit is still negative. We have done more than expected in terms of cost reduction to build a good solid foundation, and our breakeven point is much improved. The main issue for us right now is we don't have enough semiconductors to produce the cars that we want to sell. If there were no semiconductor supply shortages, we would be close to breakeven or better.

The quarterly auto loss has been reduced at least by half versus last year, despite lower volumes. You can see the improvement in the fundamentals of the auto business profit. It's just a matter of time before we get the volume that we need to sell, and then the auto business profit should be positive.

Gupta: As a result of the actions taken under Nissan NEXT, our breakeven point has gone down below 4 million. Since last year, we have improved our auto profit on a YTD basis. We would have been auto profit breakeven if we would have done the same production and wholesale. The foundation which we wanted has been done and now we just need the volume to move forward.

Question 2:

Why is the negative impact of raw materials expected to increase so significantly in Q4?

Answer 2:

Ma: We had a negative impact of JPY81 billion from raw materials in Q3 YTD versus FY20 Q3 YTD. That implies Q4 will be roughly a negative JPY90 billion versus FY20 Q4. We have been purchasing the parts and raw materials at the contracted volume and contracted price early in the year. This is one of the reasons why working capital was negative, because we had built up inventory we could not use because we didn't have semiconductors.

On the other side, because they were bought at lower prices early in the year, we were able to avoid some of the price increases. We were able to consume more of the lower-priced inventory. Now, some of the pricing impact is hitting and coming through in terms of our cost of goods sold. It may not be as bad in Q4. But the point is that the raw material price hike will definitely come in 2022, as it's impacting all the OEMs.

Question 3:

How do you see logistics costs with the increase in the vessel rates?

Answer 3:

Gupta: This year, it is not impacting because we have annual contracts. For next year, we will definitely see that because the rates are going high. We see the headwinds on raw materials, energy and logistics. On the other side, we see the tailwinds when it comes to net revenue per unit and volumes. We have to wait until we have full visibility on FY2022.

Question 4:

Where are you today in terms of visibility of semiconductors and production? The retail volume remains unchanged for the full year projection.

Answer 4:

Gupta: We are working closely with our suppliers to make precise forecasts. While the dependence of semiconductor suppliers in the automotive sector is small, nobody can predict what will be the semiconductor usage for the nonautomotive industry. While the situation is getting better, I think that the demand and supply gap will still remain in 2022. This also means we will have the opportunity to still keep lean inventories with the increase in net revenue with reduced incentives. We will have to run 2022 in the same way which we are running 2021.

We originally announced 4.4 million units accounting for the semiconductor situation but we are now forecasting 3.8 million units of retail. This means we lost 600,000 units. But maybe because of our strong customer acceptance of our products, we could have done more than 4.4 million units, so we are not able to count the lost opportunity.

Question 5:

While you are making a steady progress in delivering better results towards the 5% operating margin target for Nissan NEXT, headwinds must be more challenging compared to two years ago. Do you think you need additional actions?

Answer 5:

Gupta: We are done with our fixed cost rationalization, and we don't want to do more because we don't want to impact our future growth potential. Moving forward, volume is the only answer to justify the existing capacity, which we have, and the investment, which we have done in the product and technology.

Question 6:

Please comment on the media report on the suspension of the engine development.

Answer 6:

Gupta: In Europe, at the time of Euro 7, we will stop all the new, stand-alone gasoline engines. We believe that the total cost of ownership of electrified cars will be more competitive than the ICE car because of the technology and precious metals required for the ICE car to meet CO2 regulations.

On the other side, there are markets where the total cost of ownership for ICE is better, where the customer aspiration is still for ICE engines. We will continue to do that. We announced in Ambition 2030, we are going to invest JPY2 trillion in the next five years in electrification, which is not an add-on. It includes the shift of resources from ICE to electrification.

Question 7:

For minicar or kei, what is the cause and impact of the quality issue? Please also tell us your expectation for the kei EV.

Ma: We lost some sales for Roox, but we are restarting the sale fairly soon. In total, for the Japan market volume, we just reallocated the chips to other vehicles.

Gupta: Regarding our strategy for the kei EV, we are going to pioneer this market. And thanks to the government of Japan's subsidies on electric vehicles, our total cost of ownership from the customer viewpoint of the kei EV will be very close to be on par with the ICE. Moving forward, seeing how the kei EV is performing, we will have to redefine our kei strategy in Japan if the market is naturally shifting towards the kei EV.

Question 8:

Please explain the underlying volume assumptions for Q4 net revenue forecast.

Answer 8:

Ma: It's a minor update and it's only a 1% adjustment to our previous forecast. There is a model mix or country mix impact resulting from semiconductor allocation.

The retail volume is slightly lower or almost flat versus Q3. The wholesale number and delivery were slightly adjusted. In the previous outlook, we had assumed a little bit faster recovery than we are actually seeing in terms of supply of semiconductors. Now we only have two months left to year-end, we're updating the assumptions.

Question 9:

What is the calendar year 2022 plan for sales volume or profit projection in China? And what's the plan for introduction of electrified vehicles in China?

Answer 9:

Gupta: In China, we are focusing on two pillars in terms of the electrification strategy, the e-POWER and BEV.

On the e-POWER, in future, we believe that we will introduce e-POWER for each of the core models starting from Sylphy. On the BEV, we will introduce the Ariya, and then we will see the shift towards the BEV. The only trigger which we are waiting today for the shift to BEV in China is the China 7. As we move forward, the regulations will become clearer. We will then decide our next step of the electrification strategy.

Ma: For the BEV, under the Nissan brand, the new introduction is Ariya. We have other EVs including Venucia, which is our local brand in the market. We will come back at a later time and show you our China ambitions.

Gupta: For the calendar year 2022, we have to see how many semiconductors we can get but our plan is 1.6 million units.

Question 10:

Was there a one-off positive or negative factor behind the Q3 profit of JPY50 billion?

Answer 10:

Ma: On the Q3 profit, there are some one-time factors, but not to the same extent that we had in the first half because it's leveled out now. We had some remarketing good news and sales finance credit loss provision releases, which was roughly a positive JPY20 billion in the JPY52 million.

We had some cost increases at product enrichment or other costs that net off to be almost zero. We booked some quality provision under the normal course of business.

Question 11:

Based on your Q3 results for automotive free cash flow, what are your prospects with regards to resumption of the dividend?

Answer 11:

Gupta: Q3 free cash flow was breakeven. Q4 free cash flow should be positive, which means the second half of 2021 should be positive. In order to consider resumption of dividend, we have said that operating profit and net income should be positive, automotive free cash flow should also be positive and we should have a healthy level of net cash, and all the numbers are moving in the right direction. Having said that, we want to wait until we will announce the annual financial results of FY2021 with the forecast of FY2022, when we will be deciding about the dividend.

Question 12:

The production of products with high unit price, such as the Pathfinder, Patrol and QX60, have decreased in November and December, and I am concerned about deterioration in product mix. Is the situation improving?

Answer 12:

Gupta: For the Pathfinder, Patrol, and the QX60, they use big navigation screens and the semiconductor was short for this specific big screen. The situation is getting better in Q4 but supply is still limited based on the demand we have for these vehicles.

Question 13:

In Q4, R&D expenses, Capex and depreciation costs are expected to increase significantly. Are you sure that these costs will increase so much in Q4?

Answer 13:

Ma: It is increasing from Q3 to Q4 because we expected it to happen in Q3, but it got shifted in terms of timing. We have not reduced the investment in vehicles.

Question 14:

Can you share your views on margins, as they are important to investors?

Ma: Margins are very important to me and the major milestones under Nissan NEXT. First and foremost, we have to get back to proper margins for our business. In order to improve the margin, the best way is to reduce fixed costs, lower the breakeven point and increase revenue. That's what we're doing. We have done more than expected in terms of fixed cost reductions, as well as the new product offensive.

I want to invest so we can achieve higher margins for the future. We want to invest in the technology and the vehicles that bring value to customers with a healthy balance between cost control and cash flow. I believe we have been managing prudently to secure a healthy, sustainable foundation going forward.

Question 15:

Is there any color on the Sylphy e-POWER in China?

Answer 15:

Ma: We have not yet started sales of Sylphy e-POWER in China. We unveiled it in April at the Shanghai Motor Show. We will start sales in a few months.

Gupta: We just produced 6,000 units and we are ready to launch in the market.

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