

Q&A Summary of the IR Business Briefing of Furukawa Electric Co., Ltd.

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Contents: Communications Solutions business

Speaker:

Toshihiko Ota, Corporate Senior Vice President and General Manager of the Communications Solutions Division

Observers:

Shinji Asao, Corporate Vice President and Deputy General Manager of the Communications Solutions Division

Nobuaki Orita, General Manager of the Optical Fiber and Cable Products Division

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Jun Nishihashi, General Manager of the Broadband Solutions Division

Akihiro Fukunaga, Director, Corporate Senior Vice President and General Manager of the Finance & Accounting Division

Q: What do you believe is the reason for the slowdown in the North America optical fiber and cable market? Also, why do you expect demand to recover going forward?

A: Delays in the provision of government subsidies for FTTH, shortage of workers and reductions to customer inventories that became bloated during the COVID-19 pandemic are behind the current market slowdown. However, as a result of advances in digital services and AI, FTTH investment will increase in the medium- to long-term.

Q: What impact will the IIJA (Infrastructure Investment and Jobs Act) have?

A: Buy American could impact 20-25% of the overall market. We are currently lobbying for an exemption, and the trend will become clearer this summer.

Q: An overseas manufacturer announced the development of rollable ribbon cable. How will you respond going forward?

A: Rollable ribbon cable was jointly developed by NTT and Japanese manufacturers, and it is not easy to imitate. We will lead the expansion of the product lineup and increase sales to North America and Europe.

Q: Optical cable shipment volumes decreased in FY22 despite the strong market environment. On the other hand, in FY23, you expect shipments to increase during a market slowdown.

Also, you mentioned that you will recover the business through specialty fibers, but you are not forecasting much growth in FY23. How should I view this?

A : In FY22, much of our attention was focused on products such as rollable ribbon cable that is labor intensive products. In FY23, we will expand the product lineup in order to strengthen the rollout to regions other than North America. The business environment has been challenging recently, but we will monitor the situation going forward in regards to whether or not we will be able to achieve the indicated shipment levels (currently, shipments will likely be on par with FY22(※)). Also, concerning specialty fibers, shipments in FY23 will increase in our strong areas of submarine cable, industrial lasers and amplification fibers.

(※) Concerning North America optical cable sales (volumes), a graph that incorporates the impact of the recent market slowdown has already been announced during the 2025 Mid-term Plan briefing on May 11, 2023. Following today's briefing, the graph shown on Page 8 will be replaced taking into consideration the graph included in the briefing held on May 11.

Q : Why is the profit margin in your overall communications solutions business lower compared to other companies? How will you increase the profit margin in the future?

A : We still have commodity products and have not sufficiently focused on high value added products. From several years ago, we have increased the focus on specialty fibers and rollable ribbon cable, and we will increase our profitability going forward.

Q : What is the progress of the productivity improvements at the cable manufacturing site in North America? Also, what is your feeling in relation to increasing the ratio of high value added products, and what impact will this increase have on profits?

A : Concerning productivity, the hiring environment for operators was very challenging at the plant. We have raised wages, expanded the recruitment routes and enhanced training in order to strengthen hiring and retention, and it has been possible to achieve a certain level of improvement since last year. There is still room for improvement going forward. There is a good feeling in relation to increasing the ratio of the high value added rollable ribbon cable. Given its good workability and high density features, it will likely be adopted by telecommunications carriers in addition to data centers. Similar to Japan, demand will increase globally. Customers recognize the value, and although it is difficult to indicate quantitatively, there will be an impact on profits.

Q : Profit contributions from the FITEL business are unremarkable, but will you be able to take advantage of the technological advantages of your ITLA compared to competitors?

A : The importance of our digital coherent products, including ITLA, will increase going forward given the requirements for small size and low power consumption. Small ITLA are used for coherent light sources, and this area is one of our strengths. Optical components as a whole consistently generate billions of yen in operating income, and in the FTEL business, the profits (from optical components) are being used for industrial lasers. Optical products include the three categories of ITLA, amplifiers and DFB. We will leverage the high speed, low power consumption features of our nano-ITLA to obtain adoption for 800Gbps in 2024-2025, and we are in a good position. Also, DFB have the potential to realize increased sales for short-distance telecommunications given their overall technological capabilities, including high output features and design as an external light source.

Q : Concerning the horizontal expansion of the networking systems business, sales activities will be important, but what customer base are you aiming to acquire?

A : FEL executives have been dispatched to Europe and North America and are in the progress of developing customers and partners. The business is steadily moving forward with a focus on data centers and hospitality (hotels, hospitals, etc.). In South America, we are expanding the know-how centered on Brazil to other countries. In North America and Europe, the requests differ compared to South America, and we are responding to the product lineups and shortage of channels.

Q : To what extent do you expect industrial lasers to contribute to profits in 2025?

A : The profit contribution in FY25 will still not be sufficient, but we expect a rebound to occur from the second half of FY24. The business does not require large investments, so sales contribute directly to profits. The business is expected to contribute to profits along with the growth of the battery market (for EV).

Q : This year, how will you raise prices for existing products and incorporate the higher costs in the sales price?

A : The demand environment is different for each product, but raw material, component, energy and logistics costs are soaring, and we intend to actively adjust prices to appropriate levels while obtaining understanding from the customer.

Q : How will you achieve the FY25 targets (Net sales: JPY 230.0 billion, Operating income: JPY 11.5 billion)?

A : We are aiming to achieve results exceeding the current mid-term plan targets, and we will increase the component ratio of high value added products. In addition to rollable ribbon cable, we will also shift to high value added products in the FITELE and broadband solutions businesses. Including the discontinuation of uncompetitive products, we will restructure the business portfolio.

Q : What extent of products do you expect will be discontinued?

A : Every year, around 10-20% of products lose their appeal to the market, and we will successively discontinue such products.

Q : What is your long-term business outlook for IOWN?

A : We will build a new all-photonics network and fusion of photonics and electronics businesses. The all-photonics network business will target existing product lineups for DC, edge DC, combined wireless and wired networks and long-distance submarine cable. Also, fusion of photonics and electronics, for which there are particularly high expectations, will involve the opticalization of server CPUs, next-generation computer CPUs and GPU interfaces. We will launch a product lineup gradually from 2030 and aim to increase sales several fold during the mid-2030s. We will identify going forward when they will be realized.

Q : Generative AI will likely become important in the future. Do you currently possess any related products?

A : In relation to the Communications Solutions business, we currently do not possess any product lineups or services that contribute to generative AI. However, generative AI will likely lead to advances in edge computing, and our network routers and networking system products can contribute in this area. Also, growth of our optical fiber and cable products and optical components resulting from an increase in edge DC servers will likely contribute to profits.

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