SoftBank Group Corp.: FY23Q4 Global Conference Call Q&A

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Presenters:

Yoshimitsu Goto, Board Director, Corporate Officer, Senior Vice President, CFO & CISO, Head of Finance Unit & Administration Unit
Kazuko Kimiwada, Corporate Officer, Senior Vice President, Head of Accounting Unit
Reiko Kawamura, Head of Capital Market Department
Navneet Govil, CFO, SB Investment Advisers & SB Global Advisers
Jason Child, Executive Vice President and Chief Financial Officer, Arm Holdings plc

Q&A

Speaker 1
Q1:
Thank you. I have two questions. First of all, could you tell us a little bit more about the margin outlook for this year and ideally the next few years? Seems revenue is going up a lot, so to what degree should we expect margin expansion?

A1:
(Child) Sure. First, on margin expansion, by margin, I assume you mean operating margin or non-GAAP operating margin. Last year, we ended at 43.6 percent for the full year. Our expectation for this year is to grow top line; the midpoint of our guidance is about 22 percent. For bottom line, or actually for OPEX, we are going to grow our non-GAAP operating expenses by roughly 19 percent, delivering between 200 to 300 basis points of operating leverage this year. I think we have not given guidance on margins beyond this year, other than to say that our long-term target is to approach 60 percent, and that target we have said is at least five years away. If you use the current expectation for next year and the progress we will make, I would assume an increase of 200 to 300 basis points is a right trajectory for the next couple of years. The reason for this pace is because we are continuing to make pretty significant investments in our engineering headcount, specifically, or R&D. We are going to continue to make those investments specifically because we see a lot of demand for, in particular, our compute subsystems, where we are oversubscribed and we are going to need to continue to add people. We added about 1,000 people last year in R&D and expect to do the same this year. Probably that does not slow down for at least another couple of years. So, I think that a couple hundred basis points per year of expansion is the right expectation for the next year and probably for the next few years after that.

Q2:
Second question, I know Japan is not a major market perhaps for Arm, but could you talk a little bit

about the Japan market? It does seem we have seen a lot of hyperscalers talking about very big investments here, and I am sure SoftBank will help you with synergies there. Could you talk a little bit about the Japan market potential?

A2:
(Child) In terms of your question on the Japan market, we have not made any specific comments. Certainly, you are right, with the relationship with SoftBank, there is opportunity. And certainly, there has been investment from some of the fabrication companies in building capacity in Japan, which potentially could provide other opportunities and synergies. But at this point, nothing in particular to announce. I do not know, Goto-san, if there is anything in particular in Japan market that you want to comment on?

(Goto) No comments from my side. Thank you, Jason.

Speaker 2
Q1:
First question for Jason. You noted in the most recent result the FYE23 revenue gain being driven by market share gains in servers and automation. I was wondering, I think the last time we saw a market share figure for those areas was in FYE22. Do you have any color you could provide on progress made in those categories in FYE23 and what you are looking at for FYE24 potentially, even if it is just some qualitative commentary?

A1:
(Child) On market share for infrastructure specifically, the hyperscalers to cloud compute is typically where we have given estimates in the past. Last year, we ended at about 10%. We will provide an update at the end of Q1 because our royalty data is lagged by a quarter, so we do not have the final numbers yet. I think we did say that we expected to be around 15-ish percent this year, with a goal for next year, which we said at IPO, to be somewhere in the 20-ish percent range. We will provide a more detailed update when we get to the end of this quarter and can provide more specifics at that time.

Q2:
My second question is for Goto-san. Just wondering around that $5 billion strategic investment committed capital, that is specific to SBG and SVF? In other words, are there potentials for additional strategic invested capital opportunities that go beyond that?

A2:
(Goto) The $5 billion commitment is being made by SBG itself. This does not include investments from other entities. Approximately 70% of this $5 billion is committed to GreenBox, our joint venture with Symbotic. The remaining amount includes a smaller portion allocated to Wayve, the

autonomous driving venture in the UK that we introduced, along with various other minor investments.

Speaker 3

Q1:

Thanks for taking the questions. Could you remind us on FX to begin with, as the yen weakens, how that impacts the LTV? If we can have some rule of thumb potentially for how to think about that going forward, like what is the mismatch between your values and your net debt?

A1:

(Goto) Firstly, regarding the impact of exchange rates on Loan to Value (LTV), both assets and liabilities are affected. Therefore, if the yen depreciates, the valuation of dollar-denominated assets increases, and similarly, liabilities also increase. Consequently, calculations need to be adjusted according to the exchange rate at that time, affecting both the numerator and the denominator, rather than shifting in a single direction. Regarding costs, the depreciation of the yen does have some impact. While interest payments on dollar-denominated debt may increase slightly with a weaker yen, we do not anticipate this to have a significant impact.

Q2:

Also, how did that impact your cost of funding? Also, it looks like you have about 4 trillion yen of prepaid forwards related to Alibaba, which are now in short-term liabilities. Do you plan to settle those all with shares, or will you settle some with cash? Are you providing any guidance on that?

A2:

(Kawamura) For Alibaba transaction, we will determine whether we are going to settle with shares or cash when maturity comes, which will be within one or two years.

Q3:

My understanding is you are essentially saying that normally you will settle with shares or cash with regards to Alibaba. And then on the LTV, can you give us any color on, is there any mismatch in that asset value? I understand that some of your liabilities are in dollars, and some of your assets are in dollars, but are those perfectly matched, or is there a mismatch?

A3:

(Goto) Based on our current rough calculations, we estimate that the impact of yen fluctuation on LTV is limited to a change of about ±0.1% for a ¥1 change. In addition, since assets are larger than liabilities, it can be said that the effect of yen depreciation on assets is more significant.

Speaker 4

Q1:

Thank you for taking my question. I have one question, but maybe it is a little bit complicated. It has to do with Vision Fund and SoftBank Group and how the investment process works. You said before that investments that are strategic are done at the SoftBank Group level, and then investments for portfolio are done at Vision Fund. I want to understand better about how you collaborate or cooperate between SoftBank parent and Vision Fund on things like deal sourcing, managing the due diligence and execution. Is it one large investment committee? Do you have two? Can you just give us a better idea of how you manage that?

A1:

(Govil) The advantage we now have is we have a One SoftBank team. If you look at the most recent investment in Wayve Technologies, we had Kentaro Matsui and Sumer. Kentaro is both a member of SoftBank Investment Advisors, the Vision Fund team, as well as SoftBank Group. And Sumer, who is a managing partner in the Vision Fund, partnered on this investment. And Masa works with the team in SoftBank Group, as well as in the Vision Fund team on his projects that he is focused on, strategic investments, as well as the Vision Funds. The Vision Funds have an investment committee, which includes people from SoftBank Group as well. So, we are truly operating as one team. I would go back to the comments that Goto-san had made earlier, which is the big difference between whether an investment is in the Vision Funds or SoftBank Group is whether it is a strategic investment and whether or not we see a near-term exit or if the intent is to hold onto the asset for a longer time. Now, in terms of your questions about due diligence and all, it is a one-team approach to due diligence and all the analysis that goes through. So, Goto-san, anything you want to add?

(Goto) To add to Navneet's explanation, I would like to add a comment regarding the fundamental clarification once again. Investments in strategically significant companies will be made directly from SBG. Since the Vision Fund is just that—a fund—it's crucial to consider how returns will be generated from those investments. Investments with clear return strategies will be made from the Vision Fund. On the other hand, for companies where specific return strategies are not yet clear, but are strategically crucial, investments will be made directly from SBG. With this organization in mind, we aim to continue managing investments from both entities moving forward.

Q2:

I just want to confirm that what you are saying is that you now have one team at SoftBank Group that looks at all the investments in terms of sourcing all the way through execution. And somewhere within that process, a decision is made on whether the investment should be done at the SoftBank level or at the Vision Fund level.

A2:

(Govil) It is one team in the sense that they partner and work together and collaborate as one team. There are some people who are SoftBank Group employees, and there are some people who are employees of the Vision Funds or SoftBank Investment Advisors. There are some exceptions to that, like Kentaro is an employee of both, SoftBank Group as well as SBIA. I would not say it is one team per se, because some are employed by one entity and some are employed by a different entity. But under Masa's leadership, Goto-san's leadership, we all operate and collaborate as one team.

Speaker 5

Q1:

I have a question for Jason regarding GPU development. If SoftBank Group were to develop its own GPU-type chipset, would it affect the current relationship between NVIDIA and Arm? Arm so far launched Grace Hopper and Grace Blackwell. Would that kind of internal SoftBank development of GPU hurt the relationship between Arm and NVIDIA?

A1:

(Child) Interesting question. Have not heard of that one. I guess what I would say is, we certainly have general purpose compute designs for CPUs, which is what Grace, that pairs to Hopper and now to Blackwell, is. If SoftBank were to develop a server-based GPU, which we do not have such a product today, I do not think there would be a direct impact. They would be products that are different. Our relationship with NVIDIA is really pairing a general-purpose CPU via Grace, whereas a SoftBank GPU would be a different product. I cannot think of there being a direct impact, but hard to say. I guess the devil's in the details because this is a hypothetical question. Hard to say.

Q2:

You said something like, "Please look forward to Masa’s explanation at the shareholders' meeting in June." Can we expect some kind of explanation about the most important thing right now, such as the concept of business investment from SBG?

A2:

(Goto) As far as I am aware, Son-san's presentation materials for the shareholders' meeting have not yet been prepared at all, so at this stage, I cannot comment on anything. What I mentioned earlier is simply my own expectation.

Q3:

I believe that at last year's shareholders' meeting, the discussion was still at a conceptual level rather than providing detailed plans. Now that a year has passed, can we expect an update on the progress made during this time?

A3:

(Goto) I share the same expectation, but at the moment, I don't believe we're in a position to promise that. Well, let's hope together.

Speaker 6

Q1:

Thank you for taking my question. A question for Goto-san. You indicated that you plan to prioritize growth investments to expand NAV. However, over the last few years, you have invested around $4 billion, both in fiscal 2022 and fiscal 2023. It seems you have ample room to also initiate a buyback in addition to focusing on growth investments. Could you give us an update on your views on the buyback? Is that an option for fiscal 2024? What is keeping you from initiating such a program, considering that the holding discount is still above 50%?

A1:

(Goto) Share buybacks, as you rightly pointed out, are indeed a crucial theme for us and constitute a significant part of our capital allocation strategy. We have three major areas of capital demand: growth investment, shareholder returns, and financial improvement. While I always strive to maintain an optimal balance among these three themes, if I were to prioritize, I believe that growth investment should be prioritized over the other two capital uses. However, it's important to note that we have a firm financial commitment to safety within the scope of our financial policy. Regarding shareholder returns, we have yet to make a decision on whether to proceed with them in 2024. Shareholder returns are, of course, one of the themes in our capital allocation strategy. Therefore, while we will continue to address shareholder returns at the top management level in the medium to long term, we believe that there is still a need for thorough discussions on whether to pursue them this year at the short-term level.

Q2:

AI on the edge is a major topic for Arm and the entire semiconductor ecosystem. Could you give us an update on how you expect AI on the edge to drive growth for you in coming years? And to what degree have you incorporated this in your growth outlook for the coming years? You expect to grow more than 20% in fiscal 2025 to 2027. Is that already embedded in your guide, or is that really something that we will only see towards the end of the decade?

A2:

(Child) In terms of what is in our guidance right now, it really is just the contracts that have been signed for this year and the vast majority for the next couple of years based on licenses that have been signed or are very far along and close to being signed. Now, we have had some upside related to AI that we have talked about over the past three quarters in terms of licenses sold. We do expect that those licenses sold, we have said, are specifically due to AI. We have not broken down how much has been for training versus inference. And in particular, I think of AI at the edge as really being mostly an inference use case. So, to the extent that we see more push to AI at the edge, that, I guess, could potentially be upside. We do not specifically break out what is edge AI versus just refresh of devices using V9, versus customers that are now starting to adopt subsystems. I think it is pretty clear that a lot of the refreshes that are now happening at a slightly more accelerated pace are in part because of AI at the edge. So, I do think there could be possibly upside to the extent that we get a better view on exactly how quickly that is going to happen. But right now, I think there are certainly things that you have heard us talk about specifically like Windows PC is something that Arm-based chips, you will start seeing those here coming soon. And certainly, to some extent, they are being paired with other technologies from other partners that are building capabilities that can handle a more complex AI-based workload. There certainly are some things that are in our forecast, and there is also maybe more upside as we get a better handle on what unit volumes can be. Right now, we have these contracts signed. It is really about forecasting units. And so, that is the piece that I think right now we are mostly just using a lot of the industry estimates that we are seeing and from discussions with vendors. But in general, we are trying to probably take a more conservative view until we see some sort of a step change that occurs. Hopefully, that answers your question.

Q3:
It seems that the IPO environment is improving. We have seen a few very successful tech IPOs over the last two quarters. Could you give us an outlook on your pipeline of investees in the Vision Funds that are ready to IPO for the next 12 months?

A3:
(Govil) A couple of things. If you look at the momentum, the momentum has restarted in 2024. What we saw was in 2023, after Arm, Klaviyo and Instacart, we have seen a couple of IPOs across different sectors. Cybersecurity firm Rubrik, social network Reddit, rewards platform Ibotta. We feel like there should be more coming through this year. Some of our own portfolio companies have recently filed and are likely to go public. In India, for instance, FirstCry, which is India's biggest e-commerce platform for mother and baby products, has filed. Ola Electric, which is India's largest electric two-wheel player with 35% market share, they are both expected to go public in the coming months. Then Klarna has shared publicly in November 2023 that they are working towards an IPO in the next 12 to 18 months. Wellhub, which was formerly known as Gympass, is a leading corporate wellness platform, has recently announced that they are doing an IPO preparation. ShipBob, which is a leading fulfillment service provider, recently announced appointment of IPO book runners. Overall, which ones will take place in the next 12 to 24 months really depends on market conditions. But we are working with the management teams of the portfolio companies to ensure that they are ready for an IPO when the right time comes. Overall, I would say we have a long list of potential candidates, and they are about $32 billion in fair value that represents that pipeline that is ready to go public.

Speaker 7
Q1:
On the Vision Fund, particularly on the Vision Fund 2 markdown, can you give us some updates on where we stand in terms of valuation and what is the main driver of this round of markdown?

A1:

(Govil) In the fourth quarter, the markdown was what I would call noise. If you look at the full fiscal year, we had a $4.5 billion gain. You had some public companies that went up, some came down. In Fund 2, it was AutoStore and Symbotic that were down for the quarter. But for the full year, over a 12-month period, they have been up quite significantly. Our private valuations have overall seemed to have stabilized. It is primarily because most of our portfolio has pivoted to what we call capital-efficient growth. More than 90% of our portfolio companies have a cash runway of more than 12 months. So, the overall message is that the private valuations have largely stabilized over the last four quarters. In the public stocks, it is a little bit of noise, and it really depends on how the public markets are going to do in the coming quarters.

Q2:

I think you already mentioned, SoftBank's balance sheet has been very solid and probably too conservative. Just trying to understand, this year or in the next three years, what is the advance investment, what is the scale we are talking about?

A2:

(Goto) The amount of investment has been roughly at the $4 billion level for the past two years. However, last year, in addition to this, we committed to $5 billion. So, effectively, we made investments totaling $9 billion last year. This $5 billion commitment will be gradually invested over the next few years. As for this year's investment amount, we feel inclined to invest more than last year. However, it's important to maintain a rigorous selection process for investment targets, depending on the progress in exploring potential investments. To reiterate, our sentiment is to achieve a higher investment amount than last year. From a conservative standpoint, that's how we would phrase it.

Speaker 8

Q1:

I have one clarification question and another question on a different topic. As far as clarification, Goto-san, you mentioned was it 70% of $5 billion that relates to GreenBox JV, so $3.5 billion? Or is it a smaller number and just part of that $5 billion figure commitment? I just want to clarify, was GreenBox 3.5 out of 5?

A1:

(Goto) Yes, your understanding is correct. Disclosure regarding the investment in GreenBox has already been made, so you may want to verify that information.

Q2:

My second question is you got additional 49 million shares of T-Mobile late last year. So, a portion of your T-Mobile position is covered by call options from Deutsche Telekom. They expire in June.

Could you update us on your current view of T-Mobile investment? And also, if the options expire unexercised, are there some restrictions on monetizing this position after June?

A2:
(Goto) Since T-Mobile shares are publicly traded, we would like to refrain from commenting on their handling at this time.

Speaker 9
Q1:
On the $5 billion strategic investment, can you clarify how you define strategic? Because your definition you gave earlier says it is basically no exit. Why is that the case? Surely, in the end, you want to create value for SoftBank shareholders and exit the investment. That is one.

A1:
(Goto) Firstly, regarding the clarification on strategic investments, I raised a point earlier about whether the exit strategy is clear at this point. Even with strategic investments, it's not the case that we never exit. As you mentioned, we have a responsibility to eventually return the company's assets to shareholders. However, the presence of a short-term exit plan could be a factor in deciding whether to invest from the fund or from SBG.

Q2:
Can you clarify then what is the strategic valuation process? How different is that versus the SoftBank Vision Fund?

A2:
(Govil) The valuation approach, whether it is a strategic investment or an investment done by the Vision Fund is identical. There are no differences.

(Kimiwada) I'd like to provide some additional information regarding the valuation of strategic investments. While the valuation methods themselves remain the same, strategic investments may include subsidiaries. In such cases, the treatment in financial statements differs. Specifically, with investments where only a minority stake is held, there can be both upward and downward adjustments in valuation. However, with subsidiaries, impairments can occur, but there typically isn't an upward revaluation, resulting in a different presentation in financial statements.

Q3:
How do we ensure that the strategic investments do not end up being another WeWork situation, where the criteria are different, you look longer term, but ultimately it ends up being a disaster? How do we ensure that that does not occur?

A3:

(Goto) If that's the case, unfortunately, liquidation seems to be the only option.

Q4:

The report is that TSMC is saying the growth from the Chip on Wafer on Substrate (CoWoS), is going to be about 50% per annum over the next five years. Should we be thinking that is not a bad baseline for expectations for what Arm will do similarly in the same space in a sense of contribution from designs and the like for data centers?

A4:

(Child) First on the data center, interesting. Should our growth look similar to what TSMC is forecasting? It is probably reasonable. When Intel had their big announcement on the partnership they created with us, I think they mentioned part of the reason it was so important was from their analysis, 80% of all chips coming out of TSMC were Arm-based. Now, obviously that is more than just data center, but it is certainly reasonable to think that it could look like that. In terms of the mix and the royalty rates, which are somewhat different depending on who the player is, but in terms of unit volume, it is probably not a bad assumption.

Q5:

Which I asked at the results meeting, have you had any further thoughts about the smartphone mix over the next couple of years? Like what trajectory does it have? Does it keep the 35%, go down, or go up? I was wondering if you had any further thought on that outlook for the smartphone mix of the royalty revenues of Arm for the next couple of years.

A5:

(Child) On the smartphone mix, we said that it was pretty consistent with the quarter before when it was a little over a third of our royalties came from smartphones. It did tick up a little bit in this last quarter. If you go back to IPO, we had said that because of the subsystems that will come on later this year, we expect to see smartphone royalties probably grow pretty significantly over the next couple of years, because obviously we have the V8 to V9, where you have about a doubling of the royalty rate, but then when you go from V9 to subsystem, it doubles again. As a result, for the next couple of years, you should expect smartphone royalties to be growing pretty significantly, at least on a year-on-year basis. Then obviously the other aspects of client, there has been a lot of talk recently about what is going on with Windows PC, and that is probably a bigger driver next year, but we will see what happens within our ecosystem this year. There is some talk of perhaps something coming sooner. Anyway, that is our expectations right now. Certainly, on the server side, we do expect the cloud compute growth to be probably the strongest growth in terms of a percentage basis, but it is coming from a much, much smaller base than smartphone, so I do not see that getting close to the smartphone share probably anytime soon over the next couple of years.

Q6:

Just on the Windows PC comment, Taiwanese reports indicate that MediaTek is planning a product later this year, but not shipped till early 2025. Is that what you are thinking about, or someone else?

A6:

(Child) Let us see, I will just say, I think Rene mentioned last week that we expect there are probably a number of different projects in different segments of the market that will be addressed through some different players, and I expect there to be more than one.

Speaker 10

Q1:

I have a question around the refinancing strategy of the foreign currency bonds. Obviously, SBG has a lot of cash on the balance sheet, but I think for the euro and dollar bonds, you have around $1.4 billion in 2024 and probably another $2 to $3 billion in 2025. What would be the strategy for those?

A1:

(Goto) As for our debt management, especially concerning the upcoming redemptions, particularly those coming due within one year, our primary focus is to thoroughly study the feasibility of issuing new foreign bonds or rolling over existing ones. Whether to roll over foreign bonds until the last moment of redemption or switch to alternative financing, we intend to continue our internal study.

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