SoftBank Group Corp.: FY22Q4 Global Conference Call Q&A

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Presenters:
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Speaker 1
Q1:
I would like to ask about SoftBank Vision Fund 2. Now, the committed amount is 60 billion. Could you give us some background on your outlook for new investments for criteria you might consider? How should we think about the shareholder return balance compared to these investments you are planning to make?

A1:
(Govil) As you mentioned, SoftBank Group has increased the commitment to 60 billion. We have close to five billion dollars that are available to invest. In terms of the criteria, it is companies that are leveraging AI. We look specifically at the quality of the tech stack, the size of the addressable market, unit economics, and scalability.

Q2:
If that five billion is incremental, then should we expect a kind of similar amount of shareholder return? Is that the way to think about how you are going to spend your cash?

A2:
(Goto) This is the kind of concept we need to discuss at the board of directors meeting. We are always keen to discuss how we allocate the capital for the shareholder return. This is one of the most important agenda for the board. But at the same time, when you think about the market, along with new investment activities, we always like to keep the safeness of our balance sheet and then decide the next step. In the past five years, 4.5 trillion yen of share buybacks have been executed, therefore we would like to still maintain the healthiness and soundness of our balance sheet, and decide the time and also the size.

Speaker 2
Q1:
This is pertaining to the T-Mobile stock valuation. Currently, the contingent consideration is based upon the price being over 150 dollars. Currently, it is still below that. So, may I ask, how is that an accounting of gain taken on the same since the contingent consideration has not triggered yet?

A1:
(Kimiwada) As for the accounting process for the earnout, every quarter we check the valuation and record the fair value. Right now, the number we have is 6.2 billion as assets on the balance sheet.

Speaker 3
Q1:
I have two questions, and they are very different. The first one is about Fortress. I am not going to ask if you are selling it or not because I know it is not confirmed, but can you tell us, have you been receiving dividends from Fortress since you acquired that business?

A1:
(Goto) Yes, we have been receiving dividends from Fortress.

Q2:
My second question is related to Vision Fund. You talked about what would trigger you to invest with the different factors like AI and the tech stack and what not, but I'm wondering more about how you are thinking about the pace of investments going forward because you have a lot of cash. So, if you wanted to, you could do a lot of investments, but a year and a half or two years ago, it seemed that it was a little excessive. So, how are you thinking about, when markets return to normal or you feel more comfortable, how quickly you will put that money to work?

A2:
(Goto) The speed of the investment will not be the same as two years or three years ago. We will prioritize the safeness of our balance sheet, and we would like to be very selective when it comes to investment activities. Navneet, do you have any additional comments?

(Govil) I agree with Goto-san. A couple of things to keep in mind. As Goto-san said, it is not about cash. SoftBank Group has a lot of cash. But it is finding the right opportunities at the right valuation. Our core thesis is to focus on mid-to-late-stage, next-generation, AI-focused companies with high growth potential. So, even more focused than before on companies that are going to enjoy long-term, secular growth, and are going to drive and disrupt industries. But the most important thing is the right companies at the right valuations.

Q3:
That is pretty clear. Just one very quick follow-up. Do you believe you have the resources within Vision Fund to do that? Are you happy with how Vision Fund is staffed now?

A3:
(Govil) Yes, we have the resources within Vision Fund and we feel we are appropriately staffed.

Speaker 4
Q1:
In terms of how you are thinking about balance in new investments versus potential share, stock, or bond buybacks, obviously you are running now a very large cash balance and it is very important, the protection of the balance sheet, but maybe not necessarily the most efficient. So, how are you thinking about the allocation in those three main uses of capital?

A1:
(Goto) As for the balance of capital allocation, it is going to be the most important agenda for the discussion at the board of directors meeting for this fiscal year. Of course, the safeness of our balance sheet is the most important. While we are maintaining the safeness of our balance sheet, a buyback is also one option of investments. So, as the use of proceeds, new investments and buybacks of shares need to be well-balanced.
Last year, there were almost no investment activities over the year, but 4.5 trillion yen of buybacks have been done in the past five years. One of the main reasons for us to resume our investment is to watch the rapid emergence of generative AI. So, we would like to cherish the opportunities for new investment activities, but at the same time, we do not know if there will be great companies that we would like to invest in. So, we will continuously discuss whether we are going to consider a share buyback at the board of directors meeting, and once we agree on the size and amount, we may consider positively about a share buyback.

Q2:
Whether bond buybacks or reducing your gross debt is a priority?

A2:
(Goto) When it comes to gross debt, we will be keeping a positive stance for the buyback of bonds as well, but the volume that comes to the market is not enough. So, it may be difficult for us to buy back in size, but whenever we see an economic benefit, be it global bonds and domestic bonds, we would like to consider a buyback of bonds positively as well.

Speaker 5
Q1:
I have two questions. One is about Alibaba. Can you tell me, with all the derivatives or forward contracts, what is the current net exposure to Alibaba? Going forward, will you, at a certain point, sell all your stake in Alibaba's position?

A1:
(Goto) For your first question on Alibaba, as of today, regarding the shares of Alibaba, the remaining portion of our holdings has been all utilized for financing transactions. More specifically, we have a little bit remaining, but almost all of the shares have been used for financing. Those are the forward contracts, so that is going to be settled one year ahead or two years ahead.

Q2:
We talked about ChatGPT. As you mentioned, Masa and SoftBank Group have been investing in AI for quite a few years and are very focused on AI. How come Vision Fund missed the opportunities like OpenAI? What is the future for the Vision Fund investment?

A2:
(Govil) Regarding your question on OpenAI, the important thing to note is that Masa had the vision of identifying the importance of AI many, many years ago. It started before 2016 when we acquired Arm. So, it is not about missing generative AI or OpenAI.

The way we need to think about AI is we think of it in three dimensions. The first is the foundation layer. This powers the AI processing, and we have an acquisition there – Arm. Then, you have the application layer which provides platform infrastructure for widespread AI adoption. Then, finally we have the services layer that unlocks value across sectors from e-commerce to financial services. We have invested in all three of them – foundation layer, application layer, services layer.

Generative AI is just one application of that, and it is a core application platform technology like the Internet, PC browser, or smartphone, and it acts as a platform that catalyzes waves of innovation. With respect to OpenAI, I will not comment on that because a lot of it is about investing at the right valuations. So, I am not going to comment on a specific company, but we have been investors in AI from the very beginning and we are very pleased to see that it is now becoming mainstream.

Q2:
What is the playbook for Vision Fund if you have not been investing much? Are you just waiting to see the remaining portfolio go public or are you selling them? What is the roadmap for Vision Fund? Is it possible to have the next generation of Vision Fund 3 and 4 coming or not?

A2:
(Govil) We have invested in 473 companies over the last five to six years, and many of those companies leverage AI, but as Goto-san said in his main message, we continue to be in the defensive mode and are looking at companies at the right valuations.

Speaker 6

Q1:

Goto-san, as you look to compare new investments in AI via the Vision Fund and buybacks of SoftBank Group's own shares, will you do a calculation checking potential returns and risks from one versus the other? If I look at your current discount to NAV, the SoftBank Group shares could offer close to 100% upside at the current share price, and this is based on a NAV which is depressed, so arguably the upside is potentially closer to 150% if the NAV goes back to more fair value territory. It seems very hard to me that there would be investments out there that would match the upside of your own shares, especially given the risk-reward of new investments versus investments in something you know very well.

In addition, SoftBank Group is already very exposed to AI, so by buying your own stocks, you are just adding to the AI exposure, concentrating sort of the share of existing orders into this theme. I just want to understand whether you will have the debate, because if you do, it does feel as if the threshold to go into new investments will be very high and that the more likely scenario is greater buybacks than new investments. Is that the right thinking?

A1:

(Goto) Regarding how to decide on a buyback, of course a discount is always an important factor for discussion, but when it comes to a comparison between new investments and a buyback, a discount is not the only reason to decide and compare. So, even if we buy back, the value of our company will not have any additional value. Without new investment activities, we cannot have any additional value to the company. As long as we are an investment company, we have to do new investment activities. That is a necessity for us. At the same time, we consider the right timing for the buyback. So, it may not be an apples-to-apples comparison. Also, that needs to be discussed further from a different angle and judged.

Q2:

Just as a follow-up, when you have been meeting investors, Goto-san, is it your sense that the investment community trusts SoftBank Group to go back into investing mode, or do you think the investment community wants to see an improvement in the value of the SoftBank Vision Fund before it is comfortable with SoftBank Group doing more investments? What is your understanding of the new investors' kind of trust in SoftBank Group in making new investments, given the recent drawdowns in the SoftBank Vision Fund?

A2:

(Goto) Our investments are nothing special compared to others. I think we are the same as our peers. Happiness and sadness, and also the challenges we are feeling are in the same way and at the same timing. The past year has been a challenging year for us, but also for our peers as well.

Sometimes we are successful and sometimes we may not be successful when it comes to investments. That is why we do need to continuously look for opportunities, otherwise we will not be able to see the long-term success of the fund. Of course, it is important for us to improve the quality of the long-term holdings, but monitoring and advising of the existing portfolio may not be enough. So, for additional value for the company, not only advice, but we also need to consider follow-on investments on existing portfolio companies. When it comes to follow-on, I think that also needs to be discussed at the same level as new investment activities, meaning additional value of existing investees and new investment activities should be on the same concepts and the same kind of understanding when it comes to decisions on them.

Speaker 7

Q1:

The first one is on Arm. If we look at the NAV change in the fourth quarter based on the data you guys provide, the valuation was 3.99 trillion. That is up from 3.75 trillion at the end of December. Why has the Arm valuation increased for SoftBank Group?

A1:
(Govil) It is a number of things. One is the performance that Goto-san mentioned in his presentation. The revenue performance and EBITDA performance has been very, very strong, as well as royalty revenues which is part of the revenue performance.
In general, they have gotten a number of significant wins. A lot of that drove some of the valuation changes. But as Goto-san mentioned, given that they have filed for the IPO, I cannot provide too many details at this stage.

Q2:
To clarify, why would royalty revenue be an increase in valuation when royalty revenue growth stated in the release has decelerated from 20% to 9% in the last three quarters? That does not sound to me like a company that should be valued higher. What am I missing?

A2:
(Govil) It was actually 16% year-over-year of growth in FY22.

Q3:
No, quarterly growth during the year has slowed. That is what you guys reported. So, why is slowing royalty growth a justification for a higher valuation?

A3:
(Govil) As I said, it is a combination of things. It is top line and bottom line, and both top line and bottom line improved quite significantly.

Q4:
So, it is an annual review because the annual results are up? That is how you look at it, correct?

A4:
(Govil) We look at our valuations on a quarterly basis, not on an annual basis.

Q5:
To clarify, the valuation that SoftBank Group holds for Arm, is that the same valuation level as Vision Fund has for Arm for its 25% stake?

A5:
(Govil) Yes.

Q6:
On Alibaba, again in the same NAV data, it says that the adjustment for asset-backed finance is 4.13 trillion, but the number at the end of December was 2.1 trillion, so a two trillion increase in asset-backed finance was placed. If we quickly do the math in our heads, two trillion of asset-backed finance is about 15 billion U.S. dollars, but the presentation clearly states that it is 11 billion of asset-backed finance that was done in the quarter. Can you explain the difference for me? Is there a timing issue or something? I do not understand why it would be any different.

A6:
(Moderator) We will come back to you later in this call if we find the numbers.

Q7:
Perhaps a more general question for Goto-san on ByteDance. It looks likely, given we have had hearings in the United States that the U.S. in particular is looking to move towards TikTok being banned. We have seen other governments around the world who have said that employees of governments cannot use TikTok on government devices. Given this potential of TikTok being banned

in the Western markets and particularly the largest market, is SoftBank Group looking to work with other ByteDance shareholders to facilitate a resolution of this or to change the ownership of TikTok?

A7:
(Goto) We do not have any specific movements on that. Navneet, do you have any additional comments?

(Govil) No further comments on that, Goto-san.

Q8:
Just to clarify as well, is Masa still spending all his time on Arm, or is he working with ByteDance or anything of that nature?

A8:
(Goto) Masa is focusing on Arm and generative AI. But at the same time, as Group CEO, he is looking after many things for the group. I have not confirmed that he is specifically looking at ByteDance situations, but as Group CEO, he is looking at various management issues.

Speaker 8
Q1:
Just a quick question on Arm. I was looking at the EBITDA margin and it has been quite volatile. It has reached a pretty high level for this full year at 53%, but at one point it was down to 20-29%, so I was keen to understand what was driving this volatility in the EBITDA margin and whether we would see it stabilize.
Also, just on the Q4 Arm results, the pre-tax earnings actually flipped to losses, so I was keen to understand what the driver for that was as well.
Lastly, I was just keen to understand the timing of the IPO.

A1:
(Goto) For the first two questions, because we are in the preparations for the IPO, I am not allowed to make any comments on them.
For your last question of the timing of the IPO, our target is sometime this year. Then we may consider by the end of this fiscal year which is March next year, but that is also subject to the market and environment. So, we do not have any clear schedule or clear targets at this moment.

Speaker 9
Q1:
Goto-san, it seems you are doing everything possible to please the rating agencies. You have got loan-to-value now at 11% and a lot of cash on the balance sheet. I mean what are rating agencies waiting for to recognize that you are now running such a conservative balance sheet that you should be on track to get an investment-grade rating at some point?

A1:
I exactly feel the same way. What are they waiting for? The rating agencies and their committees have several opinions. The Tokyo members actually very much fully understand our safeness and conservative balance sheet.
Earlier, at the investor briefing call, in my presentation, I also listed some agenda for the discussion points with rating agencies. Mainly, the listed asset proportion is questioned by the rating agencies, out of the many agenda. That seems like the highest priority. Unfortunately, in the past year, because of the monetization of Alibaba, we have decreased the proportion of listed assets, but instead, we have increased in cash position, so the liquidity has been very much improved. But the rating agencies cannot be flexible to count on the cash, which contradicts our understanding. Therefore, for this area, we have been repeatedly explaining to the rating agencies about that point, and I

believe they have understood to some extent. However, when it comes to the global committees, I am not sure how they are going to make a judgment, which we cannot influence from here. However, we would like to stay close with the rating agencies and make good arguments against them.

Speaker 10
Q1:
I have a question to Navneet. In the third quarter, the Vision Fund's unlisted investment fair value had decreased because the business plan had been revised and the deterioration of the performance had been built in, but in this quarter, again the fair value of the unlisted securities decreased. I understand there are many indices, but the majority of them are due to the performance. That is the disclosure I see from your slides. Starting from the third quarter to the fourth quarter, the performance has deteriorated. When you look at the performance of the investees, how are they doing? Do you think this is the bottom? Because back then, in the third quarter, you had already built in the performance, but in the fourth quarter, we see the deterioration once again. So, do you think it is the bottom? How do you think?

A1:
(Govil) In the March quarter, our public assets saw a modest recovery which was in line with market changes. The majority of the losses were on the private assets. In particular, there were just a couple of assets, so it was idiosyncratic developments on just two or three assets, so it is very different from what you saw in the December quarter.

Q2:
In that case, from April to June, for the first quarter of FY23, looking at the macro-economy at this moment, do you think that you have fully built it into the fair value of the current situation?

A2:
(Govil) We are not going to predict the market. Anything can happen. As Goto-san said, there is geopolitical uncertainty. There continues to be volatility in the markets and inflation. Central banks are raising rates. So, we cannot predict what will happen, but as of the end of March, we believe we have the fair value of where we marked the assets.

Speaker 11
Q1:
A question for Navneet. The largest factor for the markdowns in Vision Fund this year was weaker performance of your portfolio companies. I was hoping you could maybe elaborate a bit on this. Is that primarily that your companies are taking a more conservative view on growth? I remember that a few quarters ago, you provided a percentage of your portfolio companies that were growing 50% or more in terms of revenues. Would you be able to give us an update on that?

A1:
(Govil) If we look at the last calendar year of 2022 and the first three months of 2023, let me tell you what happened. In the first six months of 2022, our write-downs were primarily because the multiples in the public markets had come down. So, we felt that the comparable multiples for the private companies should come down as well. Then, in the second half of 2022, what happened was that a lot of these portfolio companies started revising their forecasts because the demand had slowed down. They were seeing slower demand. When they revised their forecasts, by definition, their present value of those cash flows came down.

In the March quarter, the three months of 2023, most of the companies did very well. As I said, it was really two or three companies on the private side that had some idiosyncratic developments, and that resulted in a small loss. So, it is three different reasons for three different parts of the year – the first half of 2022, the second half of 2022, and then the first half of 2023.

Q2:
That is very helpful. An unrelated follow-up. A few quarters ago, you clearly deprioritized new investments in China. Today, I believe your exposure to China is only 14%. What is your perspective now to China when it comes to new investments? Are you still prioritizing other regions, or is your approach now a more balanced one?

A2:
(Govil) There are a number of constructive developments in China. First, they fully reopened. Travel and consumption trends continue to recover, as we have seen full-out crowds during the Labor Day Golden Week. Also, there have been supportive regulatory developments. DiDi relisted on the domestic app stores and greenlighted to expand consumer finance business. Tencent game launches. Our view on China is that we are long-term patient capital and we are insulated from short-term volatility. China is a very important market. Between China and the U.S., they are number one and two in AI. We believe there is a huge amount of innovation that is happening there, so we remain optimistic.

Speaker 12
Q1:
I have questions on valuation. Goto-san, there has been a lot of emphasis on companies trading at less than one time's price-to-book. I would like to hear your thoughts in general on what companies can do to deal with that change in focus, from particularly, I think, the TSE.

A1:
(Goto) The Tokyo Stock Exchange has their own idea, but we do not have any specific requests from them to us. It is sometimes not less than one time. It also depends on the circumstances for the respective companies, so we do not have any immediate actions for that.

When it comes to disclosures or requirements from the Tokyo Stock Exchange, our company has been addressing at the highest level. Therefore, when you compare with other public companies, I believe we have been achieving what has been required by the Tokyo Stock Exchange. When it comes to the requirements from the Tokyo Stock Exchange, at this moment, we do not see any insufficient parts that we have been requested from the Tokyo Stock Exchange.

However, when it comes to investor relations and communication with investors, I believe that we do need to keep making efforts to make investors happy. So, if there is anything that we can do better, please do let us know. We will do our best.

Q2:
Navneet, a question for you on valuation. Interest rates have been going up. If they come down, just in principle, what kind of impact would you think that would have on how you value the private companies that you own?

A2:
(Govil) Regarding interest rates and valuation, I think where you are coming from is that conventional wisdom says that longer-duration assets are hurt most by inflation just because of the present value of future cash flows, and vice versa.

Your point is, if interest rates come down, would the valuations go up? To some extent, but what is most important is the fundamental performance of the companies. Is their fundamental performance improving or not improving? What does the demand environment look like? That is where we look at the quality of the tech stack, the size of the addressable market, unit economics, scalability, and how they are doing vis-à-vis the investment case that we had underwritten originally. So, the short answer is, yes, it could have an impact, but we have to look at their fundamental performance on a sustained basis.

Speaker 13
Q1:
I have two quick follow-up questions. Number one is talking about the two or three idiosyncratic things that happened in the Vision Fund. Can you provide a little bit more details? What are the companies? What happened? Are there consequences to other companies?

A1:
(Govil) Your first question on the idiosyncratic developments. There were really three companies. There were two in the consumer sector. Basically, what we saw for these two particular companies was there were some demand-side moderations. It was very unique to these two companies and they were quite exposed to the consumer discretionary spending. The third company was in the logistics sector. This company has been doing quite well, so performance was not the issue. It was executing in line with their milestones. But what we saw were some negative developments within the peer group or the comp group. We felt it was important to take a cautious and prudent valuation markdown on that one.

Q2:
In these three companies, how much value are you talking about with the markdowns? Just these three.

A2:
(Govil) I will not get into the specifics, but it was about a billion dollars.

Q3:
Each or total?

A3:
(Govil) Total.

Q4:
The second one is about Silicon Valley Bank. What is the impact to the start-ups or companies' financing? Will that impact the valuation of Vision Fund going to the next quarter or the second quarter or the rest of the year?

A4:
(Govil) Most of our portfolio companies are not relying on debt or financing. 94% of our portfolio companies have more than 12 months of cash runway. So, financing is not an impact on a vast majority of our portfolio companies.

Speaker 14
Q1:
I had a question, Navneet, on generative AI. There has been a lot of talk about how it makes it much easier to do coding, and therefore the need for software engineers might come down. It is a nice story. Could you share if actually you are seeing that in any of your portfolio companies in terms of a big step change in their ability to progress on their products?

A1:
(Govil) At this stage, it is too early to see if it is going to lead to reductions in software engineers, but one thing is very clear. A lot of these are large language models (LLMs), and that requires a lot of computing power and processing power. That is for sure. But in terms of software engineers, it is too early to tell.

Speaker 15
Q1:
Goto-san, you have got the AGM coming up on the 21st of June, 2023. First of all, am I right in assuming that Masa-san will be at the AGM? If so, should we expect some news at the AGM about capital allocation because you said this is going to be discussed at the board meeting? So, should we have some more clarity at the AGM about how all this surplus capital will be deployed?

A1:
(Goto) As far as I understand, Masa is planning to chair the AGM and be in front of you to speak about our strategy for the business. I am not sure yet what he will be speaking about. Nobody can stop him, so he will speak as he wants. However, one thing I can say is that Masa is also a major shareholder of SoftBank Group as well, so he will be in line with your interests as well. So, I believe that he will be on the same page as you when it comes to the interest of the business.

Q2:
Does he understand that investors need more clarity on capital allocation to be comfortable with the investment going forward? Does he understand the impatience maybe of some investors towards not knowing what is coming next?

A2:
(Goto) Actually, I have not confirmed that there are many inpatient shareholders or not many. I know that there are some, but I do not know how the majority of investors feel about it. We do need to do a good analysis on that.

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