FY2020 4Q Financial Results Conference Call Q&A Summary
February 10, 2021

◆ Questions by Takashi Enomoto, BofA Securities Japan Co., Ltd.

Q1	My questions are about the earnings forecast for FY2021 on page 30 of this presentation. My analysis is that the consolidation of the Indonesia and India businesses will add approximately 12-13 billion yen in incremental operating profit in FY2021. However, your forecast projects operating profit growth of 5.1 billion yen, which implies that you forecast a decline in operating profit after adjusting for the effects of new consolidations. Please explain the reasons for this forecast. I don't think it's a matter of top-line growth because you expect revenue growth in all regions. Instead, it looks like the reason is a considerable increase in expenses in your forecast. Please give us the breakdown of the expenses.
A1	I would like to refrain from responding to your estimate of 12 billion yen in incremental operating profit. As you pointed out, we expect meaningful contributions from the new consolidations. After adjusting for Purchase Price Allocation (PPA) amortization and other expenses, you are correct that our existing businesses will achieve revenue growth of around 7% and that we will report an effective profit decrease. One of the reasons is that the ratio of raw material cost will be slightly higher in FY2021 due to the increase in prices of raw materials. In addition, we expect an increase in the cost of some variable cost items, such as logistics. We do not expect a large decrease in operating profit in any business. However, the headquarters in Japan will increase expenses for upgrading the Group's infrastructure. In addition, the Japan segment expects to incur some expenses. As I explained earlier about our capital investment plan, the increase in expenses including human capital investments will exert some pressure on profit. Our earnings forecasts have been criticized as somewhat conservative. We establish our forecasts based on the thinking that we cannot achieve sustained growth without making the necessary expenditures.

Q2	You mentioned that you expect "a slight increase" in the ratio of raw material cost. Don't you expect "that much" increase in the raw material cost in FY2021 despite current rises? Can we assume that you do not expect the cost of raw materials to increase in tens of billions of yen, for example?

A2	I will not go into the details because the perception of "that much" differs from person to person. One factor is the time lag between an increase in prices of raw materials and the impact on our procurement, manufacturing and sales operations. Prices of raw materials are rising considerably, but we also have raw materials procured in FY2020. Therefore, the ratio of raw material cost will not start increasing rapidly in FY2021. This is why I used the expression "a slight increase."

◆ Questions by Tomotaro Sano, JP Morgan Securities Co., Ltd.

Q1	My question is about the NIPSEA China business on page 24 of the presentation. It says the business achieved growth in revenue and operating profit in the 4Q of FY2020. Considering the marginal profit ratio, the profit growth in this business appears somewhat small relative to the revenue growth. I suppose this is due to marketing expenses and the growth of investments for the future. Can we assume that NIPSEA China's operating profit margin also will not increase that much in FY2021? In other words, are you planning to make upfront investments and large advertising expenditures again in FY2021? Or, do you expect some improvement in the operating profit margin in FY2021 because you expect investments in FY2020 will start producing benefits? Please tell us about the outlook for the NIPSEA China business.
A1	In our earnings forecast for FY2020, released in November 2020, we expected a decrease in the NIPSEA China operating profit margin because our revenue forecast for this business was rather conservative. However, NIPSEA China continued its strong momentum and achieved revenue and operating profit growth despite substantial sales promotion and other expenses for future growth. Regarding the outlook for FY2021 and beyond, we believe the Chinese paint market has much more breadth, as we explained on page 21 of the presentation. Based on this view, we will make substantial investments and take aggressive actions to increase our market share. We do not expect a consistent increase in the operating profit margin. Rather, we will work out strategies for growth in China while keeping the operating profit margin at the current level. We will obviously aim to increase our market share further. However, we will

	not sacrifice a large decrease in the profit margin for market share gains, as I have stated before. Let me add one more thing. NIPSEA China's decorative paints business comprises the Project business and the DIY business. In general, the Project business is B-to-B and the DIY business is B-to-C. The operating profit margin in the DIY business is higher than in the Project business. As the Project business is growing faster than the DIY business, the overall profit margin may come under downward pressure due to shift in the product mix. Nevertheless, we will aim for solid growth in FY2021 and beyond while maintaining growth in revenue and the operating profit margin.

◆ Questions by Atsushi Ikeda, Goldman Sachs Japan Co., Ltd.

Q1	My questions are about pages 21 and 32 of the presentation. Your revenue growth forecast for NIPSEA China's decorative paints business in FY2021 is around 10% for DIY and 20% for Project. I think your forecast corresponds to roughly half the forecast for growth in these two markets in FY2021, so this is a very conservative forecast. You mentioned that you will take aggressive actions to gain market share. In the meantime, the industry structure is rapidly shifting from DIY to Project, and Project demand is now estimated to account for nearly 80% of total demand in the decorative paints market. A leading competitor in the Project market has more than quadrupled its revenue over the last five years. In addition, this company has come out with a market share expansion plan including the plan to increase the workforce from less than 4,000 two years ago to around 20,000. I believe NIPSEA China has offered discounts to some customers to respond to the moves of competitors to gain market share. In a nutshell, I would like to know whether there are potential risks of a decrease in selling prices and profitability even though the market is growing very rapidly. You mentioned earlier that you are aiming for growth while maintaining the profit margin. With the market environment changing drastically, please explain your thoughts about these risks.
A1	As shown on page 32 of the presentation, we forecast revenue growth of around 10% for DIY and around 20% for Project in FY2021. On page 31, we project YoY growth for both the DIY and Project markets in FY2021. Based on these assumptions, I believe it's an exaggeration to say that the paint market composition has shifted to 80% Project and 20% DIY due to the

	transformation of the industry structure. Considering that DIY achieved 21% revenue growth YoY in the 4Q, as shown in this presentation, we see a big opportunity for growth under the market conditions expected for FY2021. I will not give you a specific growth rate, but I agree with your outlook that market growth will be focused on the Project segment. However, we are not assuming an extreme shift in market composition. As we described on page 21 of the presentation, the most important point is how we respond to changes in the market amid the drastic changes in the industry structure. We will proactively respond to the market shift without resting on our current positioning. Under the current business climate, competitors are taking aggressive actions to grow. However, I believe we have a strong business foundation that allows us to maintain a higher operating profit margin than that of competitors and achieve growth by leveraging our capital position and comprehensive capabilities. By the way, you mentioned discounts earlier. There is a possibility of a price offensive strategy in limited areas. But we do not intend to engage in an all-out price-cutting war that would erode the entire profit margin. Instead, we will run our businesses to earn solid returns from the perspective of Maximization of Shareholder Value (MSV). We cannot tell you anything further until the results come out. But these are our intentions and management approaches for increasing our share of the Chinese paint market.

Q2	Your competitors are taking actions to capture market share by increasing their workforce while drastically cutting prices. With the market increasingly shifting to an oligopoly of the market leaders, can we assume that you are safely positioned to get ahead of the competition by maintaining a balance between market share gains and profitability based on your superior financial resources?
A2	That's our goal. On the other hand, we are facing intense competition. Therefore, we will execute our strategies by responding appropriately to market conditions, rather than resting on our current positioning.

Q3	In that case, do you expect significant growth in revenue but rather slow growth in operating profit in FY2021?
A3	That is not our forecast. As I replied to the earlier question, we will aim to achieve revenue and operating profit growth despite various sources of

	pressure. And we have achieved revenue and operating profit in prior years.

◆ Questions by Tomomi Fujita, Morgan Stanley MUFG Securities Co., Ltd.

Q1	Your 4Q results for the Japan segment compare unfavorably with strong earnings at competitors despite the recovery of automobile production. Was your earnings growth slow because the increase in recruiting and other fixed costs offset the benefit of higher shipments of automotive coatings and other paint? Additionally, does the earnings forecast for FY2021 factor in the increase in fixed costs in Japan, such as for hiring more people and raising salaries? Or is the forecast a conservative estimate that factors in risk factors such as a demand decrease after the strong COVID-enhanced demand in Europe and the U.S. in FY2020? I would also like you to explain your basic thinking concerning the earnings forecast for FY2021 and the breakdown of expenses for the Japan segment.
A1	Our forecasts have been criticized as conservative. However, we are not intentionally making a conservative plan. We establish a forecast which we are confident of achieving, taking into account risk factors and the uncertainty of the business environment. Obviously, our earnings could miss the forecast as a result of changes in the business environment, such as the tightening of COVID-19 restrictions. On the other hand, an easing of COVID-19 restrictions could result in earnings above our plan. Our forecast factors in these various risk factors. Regarding the 4Q results for the Japan segment, headquarters expenses incurred globally are allocated to the Japan segment, as shown on pages 18 and 23. As a result, the expenses allocated to the Japan segment include both the expenses for operations in the Japan segment and the expenses associated with global integration of operations. This practice may hinder a clear-cut analysis of the expenses incurred in the Japan segment. As we announced on October 1, 2020, our automotive coatings business transitioned to an integrated operating structure worldwide under NPAC on January 1, 2021. Meanwhile, we continue to use segment reporting by region for accounting purposes. The headquarters in Japan handles the approval of raw materials for supplying paint and services to Japanese automakers for their global operations. Therefore, we must strengthen the operating

	infrastructure and enhance the sustainability of the Japan segment to meet the requirements of our customers operating worldwide. We believe reinforcing the sustainability of operations in the medium and long term in the Japan segment will result in the enhancement of our Group's infrastructure globally. For this purpose, we plan to increase expenses somewhat in the Japan segment. In the Japan segment, the decorative paints business will be impacted by COVID-19. In the industrial coatings business, end-user demand is expected to decrease, but not disappear. In any event, our sales will be affected by changes in customers' needs. So, we will build a foundation for capturing market share despite modest growth in total demand by implementing measures such as increasing salaries as part of our human capital investments.

Q2	According to A1, can we assume that the reason for the rather weak operating profit forecast in the Japan segment for FY2021 is the inclusion of acquisition-related expenses for accounting purposes? Can we also assume that you do not expect a slowdown in growth markets, including China and regions where your newly consolidated companies are located?
A2	Your understanding is right. We assume higher growth in the Japan segment in FY2021 than in FY2020. The reason is that we will take actions to capture the recovery in demand expected in FY2021 following the weakness in FY2020 due to COVID-19. Meanwhile, there has been strong momentum in the NIPSEA China business since the second half of FY2020, and this business is expected to continue growing in FY2021. In Asia excepting NIPSEA China, we expect growth due to the rebound from COVID-influenced weakness in FY2020. On the other hand, DuluxGroup expects a modest revenue growth in FY2021 after the larger-than-expected COVID-enhanced DIY demand in FY2020. Betek Boya also enjoyed strong growth in FY2020, but growth of 80% annually is not sustainable. So, revenue growth at Betek Boya is expected to continue in FY2021, but at a slower pace than in FY2020. As you can see, giving an overview of our outlook is difficult because the picture is mixed from region to region. The earnings forecast for FY2021 was prepared by taking into account market trends in all regions.

◆ Questions by Shigeki Okazaki, Nomura Securities Co., Ltd.

Q1	Please tell us about the competitiveness of the NIPSEA China business. On page 20, it says NIPSEA China increased its market share in the Project business in the 4Q of FY2020. Considering that the revenue growth rate of your competitors was higher than that of NIPSEA China until the 3Q, has there been a change? What is your take on this? I understand your view will be based on your estimates because your competitors have not announced their financial results yet. Regarding the DIY market, I believe your market share has not changed. Please explain the current competitive landscape.
A1	As I explained on page 21 of the presentation, the sphere of the Project market has become much larger. Major competitors in this market are primarily paint manufacturers in China. We have announced that we have a 17% share of the China DIY market. But our market share is in the high single-digits based on the new definition of the market. In other words, the remaining more than 90% share of the market is held by our competitors including leading paint manufacturers. The problem is how to view the paint market overall. We are not watching only the two major competitors. It's true that their moves are relatively easy to follow; But we are keeping an eye on the overall market including the activities of other competitors. The change in our market share is based strictly on our estimates and is not necessarily supported by official data. With our Project revenue growing by 34% YoY in the 4Q, our view is that we are one of the winners among the competitors in this market. It is possible that major competitors are winning likewise, but there are also competitors who are losing. This is our interpretation of the market situation. Regarding your question as to why we forecast no market share growth for the DIY business even though its 4Q revenue grew 21% YoY, the answer is that our competitors are also working very hard on capturing market share. Although the DIY sector was strong in the 4Q, we were unable to significantly surpass the growth of the market overall. This is a very subjective view. In reality, we are not losing against competitors' brands in the premium range. Market conditions were very favorable in FY2020 and our performance was strong. Nevertheless, due in part to local nature of the market, determining if the market overall is heading up or down is a subjective judgment. Irrespective of these factors, we do not think that our competitive position has been undermined at all.

Q2	Regarding your redefined Project market explained on page 21 of the presentation, do you have a rough estimate of the annual market growth rate for the next three to five years?
A2	We cannot tell you because the definition of the market has not been established at this time. After we finalize a definition, we will be able to estimate our market share. From a broad perspective, we estimate that demand for new construction projects will not increase much, and home renovation demand, including major renovation projects for existing housing, will increase significantly. We believe that the overall market will grow steadily. We have some internal market information, but this market is changing so fast that our market share data could change in the next quarter. Therefore, we can only give you a qualitative explanation of the market.

◆ Questions by Yoshihiro Azuma, Jeffries (Japan) Limited

Q1	Regarding the Project market in China, I believe that the new definition of the market will open up new opportunities to acquire market share. Please give us more information. I would like to know if the target market became bigger because it covers regions which have been outside your target. Or has the size of market doubled because you included small and medium-sized projects for repainting existing housing on top of large projects that have been included in your definition of the Project market?
A1	We have previously focused on the top 30 or 100 large real estate developers in the new construction project market. Condominium construction increased rapidly since around 1990 and condominiums that were built at that time are requiring major renovations now. These projects are being undertaken by builders of various sizes, from small contractors to large real estate developers. We have not necessarily focused on this segment, and we see a lot of potential for growth in this market. When houses are renovated, sometimes a tile exterior is replaced with a painted surface. We have been monitoring this trend for some time. In the second half of FY2020, we started holding discussions about how to target this new market sector. This included an assessment of the competitive landscape. We concluded that it would be misleading for investors to only look at demand for new construction projects based on the conventional definition of this

	market. This is why we announced the change in the markets that we are targeting.

Q2	When you expand the sphere of the market you are targeting, I'm sure you need to alter your strategies, including marketing methods, staffing arrangements, and use of advertising expenses. What changes do you expect over the next 10 years or so?
A2	Interior finishing work is on the DIY side and exterior finishing work is on the Project side. As we reexamine the definition of the Chinese paint market, we do not need to use a single approach for selling products to our major customers or through distribution channels. NIPSEA China's strengths lie in its ability to meet the needs of customers by responding to changes in market conditions with flexibility. The point is that we will take measures to efficiently expand our market share without aggressively cutting prices, sacrificing profit for market share or lowering our brand value.

Q3	I would like to know what kind of business opportunities you see in industrial coatings. I believe that there have been many changes in the industries that use your coatings. Where do you see business opportunities now? I understand that Nippon Paint has superiority in automotive coatings. Which areas have the greatest growth opportunities as you look ahead to changes in the industrial coatings segment over the next three years?
A3	It's difficult to give you specific opportunities. Compared with industrial coatings, decorative paints business is locally operated business. So, it would be great if we could continue using the acquisition model we used with DuluxGroup and Betek Boya. However, valuations of paint manufacturers have gone up. We cannot provide a convincing explanation to our shareholders for acquiring companies at prices above valuations. Therefore, we will only acquire companies that can definitely create value for shareholders. The same goes for the industrial coatings business. Industrial coatings manufacturers are more or less operating globally. We will also consider business expansion in various ways in other market categories such as automotive coatings, anticorrosion coatings, marine coatings, and coil coatings, if the opportunity arises. The agreement of target companies is needed to execute M&A transactions. In addition, we cannot announce a deal unless we can verify that the deal can

	deliver solid investment returns. We have no intention of pursuing acquisitions without discipline. We will consider various forms of acquisitions if the transaction can create meaningful synergies in sales channels and other aspects of our operations.

Q4	You mentioned M&A transaction valuations. Do you have the necessary PMI personnel to be prepared if you find an undervalued company?
A4	It depends on sectors. The answer is yes if we are to acquire a company in a sector in which we have strengths. Betek Boya, for instance, is a company which is very competitive on its own. NIPSEA China has strengths in decorative paints business in emerging countries. So, the collaboration between Betek Boya and NIPSEA China is working very well. That's a good example. DuluxGroup's primary business is decorative paints. However, NIPSEA China's customers are not large-scale retail stores. This creates an opportunity for DuluxGroup to leverage its unique strengths and share its best practices. We are aware of our strengths and weaknesses in other segments, and we will implement PMI by leveraging our strengths and supplementing our weaknesses.

◆ Questions by Yifan Zhang, CLSA Securities Japan Co., Ltd.

Q1	Please tell us the reasons for the relatively slow quarter-to-quarter growth in the 4Q in the Japan segment and for the significant revenue growth and lower profit in the 4Q compared with the 3Q in the Oceania and the Americas segments.
A1	Regarding your first question, we operate in a broad spectrum of segments in the Japan segment, from automotive coatings to decorative paints to industrial coatings. This segment was affected by the deterioration of market conditions caused by COVID-19. You can tell from data released by the Japan Paint Manufacturers Association that conditions in the paint market are tough. Regarding automotive coatings, we operate this business globally, but only sales in Japan and royalty income from overseas subsidiaries are counted as earnings in the Japan segment. Due to this profit structure, the earnings for the Japan segment were rather weak, although 4Q earnings picked up slightly. Regarding FY2021, we plan to take decisive actions including the use of

	antiviral products to differentiate our products. However, our performance will depend on how end-use demand is impacted by COVID-19. 4Q revenue was very strong in the Oceania and the Americas regions. On the other hand, operating profit growth was smaller than the revenue growth. This is because we made investments in the 4Q for growth, as I stated in November 2020. In Oceania, for instance, we made investments to improve our operating profit margin by streamlining operations and we expect modest revenue growth in FY2021. These investments were based on management decisions, and the lower profit growth compared with revenue growth in 4Q was within our expectations. The same goes for the Americas region.

Q2	Please tell us the expected impact of automobile production cuts due to shortages of semiconductors in FY2021.
A2	Our earnings will be affected if a shortage of semiconductors creates a bottleneck that reduces automobile production. At this time, we are basing our production on our customers' production plans. If there is a prolonged impact of a bottleneck, our business will be affected.

End