FY2021 3Q Financial Results Conference Call Q&A Summary
(November 12, 2021)

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

Q1	The prices of raw materials are expected to continue to increase, in particular in China, through 1H of 2022. In the meantime, the market climate has been changing significantly in China, and I assume the prices of some product lines have fallen sharply. Please tell us whether or not there are obstacles to and the possibility of a change to the policy of passing on the higher raw material prices in the Chinese business.
A1	Regarding the procurement of raw materials in China, we have faced the issues involving the higher cost of raw materials and the significant availability issues of some raw materials due to the power supply shortages. Our policy is to continue measures to pass on the higher raw material prices to the extent possible based on the assumption that the raw material availability challenges will not be resolved anytime soon. If we increase selling prices in the competitive Chinese market while nobody is following suit, that would undermine our competitiveness. Therefore, we will choose the right time to increase selling prices appropriately in China. In the meantime, we need to improve our operating profit margin from the 3Q level. So there is no change to our basic policy of raising selling prices.

Q2	Do you assume that the operating profit margin in the Chinese business reached a bottom in 3Q? Or do you expect downward pressure on the operating profit margin to continue in 4Q?
A2	We are taking actions to improve the operating profit margin from the 3Q level. But we are not optimistic enough to assure you that the operating profit margin stopped falling in 3Q. We are raising selling prices in China. As a result of this, our operating profit margin may improve if the prices of some raw materials decline. But this is not our assumption at this time.

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

Q1	NIPSEA China's 3Q revenue increased 21.4% YoY on a Non-GAAP basis due to the continuing market strength and the acceptance of selling price increases. On the other hand, operating profit on a Tanshin basis declined 6.3 billion yen

	from the 3Q of 2020. Considering the marginal profit from revenue growth, I think you could have reduced the operating profit decline despite the impact of the higher cost of raw materials. What is your view of the market climate in China? Wasn't your Chinese business impacted by the financial difficulties of some real estate developers? Didn't you compete based on prices against the Chinese paint manufacturers? Please tell us about the business climate for your Chinese business including market conditions.
A1	The operating profit decrease of 6.3 billion yen from the 3Q of 2020 on a Tanshin basis includes a provision. Meanwhile, operating profit declined by 4.4 billion yen on a Non-GAAP basis. The major reason for this was the significant increase in the cost of raw materials in the 3Q this year compared to the 3Q last year. Our decorative paints revenue increased both in the Project and the DIY businesses. In particular, the DIY revenue increased 32% YoY, which was largely attributable to the increase in the sales volume. The 26% revenue growth in the Project business was mainly due to the selling price increases. In the Project business, we need to determine the right time to increase selling prices, such as when contracts are terminated or renewed and by taking into account market conditions such as the Chinese government's policy measures involving the real estate sector. As a result, the business climate is different in the DIY business and the Project business. If the selling price increases are more widely accepted based on the premise that our competitiveness will not be undermined, I believe we can secure a sufficient operating profit. In the meantime, the competitive environment in the Chinese market is far from rosy. However, we are not in a less advantageous position than our competitors. Our scale gives us a considerable advantage over our competitors in terms of the procurement of raw materials as well. Now we are firmly positioned to survive the competition.

Q2	You have just mentioned that you increased selling prices in the Project business. Did you raise prices, say, by double-digit percentages? If so, I assume you could have reduced the operating profit downturn from the 3Q of 2020 even after taking into consideration the lower prices of raw materials in 2020.
A2	We did not increase prices by double-digit percentages. Our selling price increases include effective price increases such as by reducing discounts. Our perception is that the acceptance of selling prices increases is steadily

	progressing.

Q3	Have you been able to raise selling prices in the DIY business by the same degree as in the Project business?
A3	In the DIY business, we are increasing selling prices frequently rather than increasing prices by a large amount each time. These price increases taken together will contribute considerably to our revenue growth. For your information, the DIY revenue growth was attributable more to the increase in sales volume than to the selling price increases.

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

Q1	NIPSEA China recorded a provision of 2.7 billion yen in the 3Q of 2021. You explained in the conference call for the consolidated earnings forecast revision in October that around 20% of the operating profit decline of 16.5 billion yen was attributable to one-off expenses. Based on this information, I have estimated the amount of this provision to be around 3-4 billion yen. Do you plan to record an additional provision in 4Q or thereafter? Or, will there be no provision in addition to the 2.7 billion yen recorded in 3Q? Your 26% revenue growth in the Project business without selling price increases of around double-digit percentages leads me to assume that demand has continued to grow. In the meantime, there are concerns about the slowdown in the Chinese real estate market. Please tell us your outlook for paint demand in China in 4Q and the next year onward.
A1	In the consolidated earnings revision released in October, I explained that the one-off provision would account for around 20% of the 16.5 billion yen downward revision of the operating profit forecast for NIPSEA China. That comes to 3.3 billion yen by a simple calculation, but we recorded a provision of 2.7 billion yen in 3Q. To answer your question regarding whether or not we will record an additional provision, the provision of 2.7 billion yen is our best estimate at this time. So I cannot tell you that there will be no additional provision. This is the appropriate provision for 3Q based on an agreement with our auditors. To give you the outlook for paint demand in China, I believe the DIY market has a more room for market share gains than the Project market does based on the YoY comparison. Our assumption is that new construction demand in the

	Project segment will slow down more or less, rather than remaining on the growth momentum that has been continuing since 2020. The important thing is to capture repainting demand such as large-scale renovation projects as much as possible. We expect that the overall decorative paints demand in China has room to continue growing moderately in the next year and beyond. We believe we can achieve growth that outpaces the market by capturing a greater share of the growing pie.

Q2	You expect that the new construction market in China will slow down in the near future, but the overall Project market will not shrink because the repainting market will grow. And you will increase selling prices by determining the right time by monitoring the moves of competitors and aim at expanding market share. Is my understanding correct?
A2	We may be impacted by the slowdown in the new construction market with a time lag. However, our decorative paints revenue grew in 3Q despite the severe market conditions. So our strategy will be different depending on how we see the market climate. The new construction market has room for growth in the future. But we will adopt the assumption within the Nippon Paint Group is that this market's growth will be slower than in the past. We will aim at gaining market share in the repainting market by taking actions to target the demand created by repainting properties that were constructed in the late 1990s.

◆ Questions by Atsushi Yoshida, Mizuho Securities Co., Ltd.

Q1	The operating profit margin in the Japan segment has been consistently falling since the 1Q of 2021. Operating profit in 3Q 2021 was 1.4 billion yen, which was significantly lower than in 2020. In particular, the 3Q operating profit declined considerably compared to 2Q 2021. What are the main reasons for the sharp decrease in operating profit? I expect that lower automotive coatings revenue and the higher cost of raw materials are two reasons. Please share with us the background and other reasons for the profitability decrease. Please also give us the outlook for the Japan segment including the possibility of incurring an operating loss in 4Q.
A1	As you pointed out, we see the decrease in the profitability of the Japan

	segment as an urgent matter to deal with. Under the new organizational structure that will start in January 2022 including the establishment of Nippon Paint Corporate Solutions, we will accelerate the improvement of the profitability and efficiency of the Japan segment as a whole, including partner companies and functional departments in Japan. The main reason for the decrease in the operating profit margin in 3Q both YoY and QoQ was the impact of higher raw material prices. In addition, both variable and fixed costs increased due to an increase in personnel expenses and logistics costs. We are taking various actions to mitigate the impact of higher raw material prices to improve our operating profit margin. Unfortunately, we face higher hurdles for raising selling prices in Japan than in overseas markets including China. This holds true not only for the B2B business but also for the architectural paints business due to business practices unique to Japan. This has created downward pressure on our operating profit margin. However, we are not accepting the situation as it is. We will continue to take actions such as eliminating unnecessary fixed costs and negotiating with customers for selling price increases. Regarding the increase in fixed costs, we are taking actions to prevent supply instabilities and disruptions, even if it requires additional costs, in order to fulfill our responsibility as a manufacturer to supply products. These measures are in all our operating regions, but these costs were somewhat higher than normal in the Japan segment in the 3Q of 2021. We will aim at improving our operating profit margin in 4Q and thereafter because the current profit level is far from satisfactory. The management teams of the partner companies, Co-President Wee and I have discussions on a daily basis about how we can improve profitability, and we have incorporated practical ideas into our measures.

Q2	Are you going to proceed with the investment project for updating production facilities in Japan according to the plan announced in the New Medium-Term Plan? Or, are you going to revise the plan to some degree in view of the present business climate?
A2	Today we released "Notice of a Change in the Redevelopment Project for the Tokyo Office". We are also reviewing our plan for renovating production facilities in Japan. Our initial plan was to build a new head office building, but the pandemic has changed the required functions of the head office. The

	construction of the Tokyo Office will not incur large depreciation expenses because the facilities will be built on our own premises. Our decision to revise the plan was based on the idea that building a new Research Institute, rather than a new head office building, will contribute more to our business growth. Regarding the renovation of production facilities in Japan, we will make necessary investments to clarify the accountability for profitability in our businesses in Japan as well as to improve their market share despite the challenging market conditions. We need to make wise spending decisions rather than replace all our existing equipment with the latest technologies. There will be no major change in the policy for the New Medium-Term Plan. We remain committed to building a foundation for sustainable growth in Japan. At the same time, we are more rigorously examining the cost effectiveness of capital expenditures in Japan. The change in the redevelopment project for the Tokyo Office which was announced today was the result of this cost-benefit examination. We have no additional major change in the capital expenditure plan at this time but will announce any changes if they arise.

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

Q1	I have a question about the acceptance of selling price increases. Your operating profit margin forecast for 4Q (based on figures calculated by subtracting FY2021 1Q-3Q figures from the FY2021 forecast) is 5.0%, which is lower compared to the 3Q operating profit margin. Please explain the outlook for each operating region from 3Q to 4Q and progress with the acceptance of selling price increases.
A1	The FY2021 revenue forecast of one trillion yen shown on page 25 of the presentation includes the seven months of revenue of around 18.6 billion yen from the three businesses categorized as discontinued operations. As a result, the revenue forecast is a slightly ambitious forecast. However, sales are relatively strong in all operating regions, so we do not anticipate any large gap between the forecast and the actual results. On the other hand, the profit forecast is a must-achieve goal, and we are considering by how much we can surpass the forecast. That said, we do not see any factor that would cause operating profit to exceed 80 billion yen, which is the revised forecast announced on October 12. So we must take actions such as

	increasing selling prices further to achieve the operating profit forecast. Looking at our businesses, we have appropriately increased selling prices in the decorative paints business. On the other hand, there are hurdles to raise prices in the automotive coatings and industrial coatings businesses on a timely basis. Our automotive coatings revenue is influenced by automobile production. As a result, automotive coatings revenue is slightly weaker than anticipated due mainly to a decrease in automobile production.

Q2	The selling prices of automotive coatings are generally revised at a certain time so that the impact of the higher cost of raw materials will be reflected in selling prices with a time lag of around a quarter. Is my understanding correct?
A2	The timing of revisions of selling prices depends on contracts with automobile manufacturers. We can raise prices to reflect the higher cost of naphtha and other raw materials to a certain degree. However, we cannot necessarily revise prices quickly.

◆ Questions by Yoshihiro Azuma, Jeffries (Japan) Limited

Q1	Almost all industries are being impacted by shortages of raw materials and disruptions in logistics. The paint industry is not an exception and your peer paint manufacturers have reduced their earnings forecasts due to weaker earnings prospects caused by raw material shortages. Actually, raw material availability has become a challenge faced by most companies including the Nippon Paint Group. What points such as procurement capabilities and flexibility do you see the Nippon Paint Group must strengthen in order to deal with the current unexpected circumstances?
A1	Paint manufacturers use relatively versatile raw materials and are not required to use the most advanced materials. As a result, supply disruptions were not among our top concerns. There are a few raw materials that are sourced from a single supplier. The occurrence of unexpected situations like the current one may cause force majeure that prevents the procurement of raw materials. Therefore, addressing this risk is now one of our management priorities. The Nippon Paint Group has considerable procurement capabilities and negotiation power because it procures raw materials in large volumes around the world. At the same time, we choose the optimal procurement method for

	each operating region and visualize the procurement data to monitor purchase prices of every raw material we use globally. This allows us to efficiently combine the local procurement and the global procurement of raw materials, which is a valuable strength. We believe centralized procurement management is not suitable for the paint business and are confident that our method is the best for procuring raw materials for paint. Paint manufacturers are required to obtain customer approvals for raw materials in many B2B transactions. If we cannot procure an approved raw material, there is a risk that the alternative raw material will not be approved by the customer. This may lead to an opportunity loss. This is not an issue unique to the Nippon Paint Group.

Q2	The prices of resin-based materials and naphtha are linked to crude oil prices and relatively easy to follow. So, I assume increasing selling prices to reflect changes in these raw materials is relatively easy to negotiate. On the other hand, I think changes in logistics costs are not one of the conditions that will require a price revision. I assume that logistics and other costs, which did not change much previously, are increasing. What kind of measures are you considering in Japan where deflation has been the norm?
A2	Logistics costs have increased more than you would expect. In our case, we do not have a sufficient number of truck drivers to deliver raw materials because our raw materials include hazardous substances. These supply disruptions are occurring at various places. For instance, goods are piled up at ports in the U.S. With B2B customers, we cannot easily pass on the higher cost of raw materials caused by these supply constraints. In addition, customers in Japan do not readily accept price increases in the first place. So we are considering if we can further reduce logistics costs by improving the efficiency of logistics and using the DX. At the same time, we must continue to negotiate with customers. This is where the presidents of the group partner companies in Japan can play a role, and they are making great efforts in this respect.

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

Q1	Assuming that the spot prices of raw materials remain high, the impact of automobile production cuts gradually subside, the impact of the pandemic

	passes the peak, and the Chinese real estate market slowly decelerates, please tell us the outlook for operating profit in China, Japan, Indonesia, and Oceania in FY2022.
A1	The earnings forecast for FY2022 is scheduled for release around next February, so I will not comment on our quantitative outlook. The revenue forecast for FY2021 of one trillion yen looks roughly within reach although the accomplishment of this is subject to exchange rate fluctuations. Assuming revenue of one trillion yen, a one percentage point improvement in our operating profit margin will increase operating profit by 10 billion yen. Combining 10% revenue growth with an operating profit margin of 10% will increase our operating profit by 10 billion yen. We are fully aware of our large business scale. However, the paint business is characterized by local production for local consumption. As a result, improving our operating profit margin by one percentage point is not easy and can be accomplished only through negotiations, price increases, and cost reductions in every business. For example, the New Medium-Term Plan has revenue and operating profit targets of 1,100 billion yen and 140 billion yen, respectively, for FY2023, excluding the effects of M&A such as the recent acquisition of Cromology. These targets remain a must-be-achieved goal. This plan does not assume the rapid expansion of the pandemic and sharp increases in raw material prices. However, we have no plan to withdraw the top-line target as well as the bottom-line target in the New Medium-Term Plan. We will take appropriate measures in FY2022 and FY2023 to achieve these targets. We remain confident about the strength of the Nippon Paint Group's platform (business foundation) in the medium and long-term.

Q2	The 3Q performance in Indonesia and Oceania was relatively robust, which leads me to believe that you are making progress in passing on the higher raw material prices to a certain degree. Since your market share is very high in these markets, can we assume that the operating profit in these regions will start growing again once the economy is back to normal?
A2	The 3Q performance in Indonesia was impacted by the pandemic and the higher cost of raw materials. However, we believe we can absorb these impacts because we have the top share in this market. Nevertheless, our revenue growth in Indonesia was only 6% YoY based on reference values due to the

	impact of lockdowns. Therefore, we expect that this business can grow further including the operating profit margin once the economy is back to normal. On the other hand, the Oceania business is growing steadily. In addition, DuluxGroup can pass on the higher prices of raw materials and control the supply of raw materials because they command a 50% market share in Australia and their mainstay is the decorative paints business. We do not expect the Oceania business to start growing rapidly, for instance by 15-20%, once the economy is back to normal. But this business is unlikely to experience a negative growth. Even with roughly flat market growth, we are targeting revenue growth of around 5% overall with 2-3% growth through selling price increases and 2-3% growth through volume growth. In addition, we believe the Oceania business has the potential for operating profit growth of 6-7% achieved through operating leverage. As you can see, the business climate is significantly different in Australia, Southeast Asia, and Indonesia.

Q3	The prices of some raw materials have fallen slightly. In the meantime, do you anticipate that your earnings will continue to be impacted by the challenging business climate through 1H of 2022?
A3	When the prices of raw materials are rising, actions such as selling price increases will not be reflected immediately in the operating profit margin but will be reflected with a time lag. As a result, we expect that the operating profit margin will recover starting around 1H of 2022. On the other hand, we are working on reducing the impact of higher raw material prices. Our present assumption is that the operating profit margin will improve even more if there is progress with the acceptance of selling price increases and reductions of other costs.

◆ Questions by Yang Yang, T. Rowe Price Japan, Inc.

Q1	The 3Q operating profit in NIPSEA China declined by 6.3 bn yen YoY on a Tanshin basis including a provision. According to the announcement in October 2021 of the revision of the consolidated earnings forecast for FY2021, NIPSEA China's operating profit forecast was reduced by 16.5 bn yen compared to the forecast announced in August 2021. Assuming that NIPSEA China's operating profit for FY2021 (based on the August 2021 forecast) is unchanged from the operating result for FY2020, if the 3Q operating profit declined by 6.3 bn yen,

	then the 4Q operating profit, which is calculated by subtracting the 16.5 bn yen of downward revision in operating profit from the FY2021 forecast, would be almost zero. The 3Q operating profit margin of NIPSEA China declined only by around 0.4 percentage points (excluding the impact of a provision) compared to 2Q. Could you tell us if your 4Q operating profit forecast is cautious, or is the impact of higher raw material prices is so high that NIPSEA China's operating profit could be almost zero in 4Q?
A1	We do not expect the 4Q operating profit of NIPSEA China to be zero. The 16.5 billion yen decrease in the operating profit forecast was a downward revision from the consolidated operating profit forecast of 102 bn yen announced in August 2021. I think your numerical assumptions are slightly different from ours. We are not optimistic about 4Q just as we were not in 3Q. The market will remain challenging due to the power supply restrictions and considerable supply chain constraints in China. Our forecast may prove to be cautions, but we assume that the business climate will be relatively challenging. I cannot give you specific numbers, but NIPSEA China's operating profit will be nowhere near zero.

Q2	NIPSEA China's 3Q operating profit margin, excluding the provision, declined by 0.4 percentage points from 2Q. What is your evaluation of this operating profit decrease?
A2	This decrease in the operating profit margin based on operating profit excluding the provision is roughly as expected.

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