

Nippon Paint Group Medium-Term Plan (FY2021-2023)

Update Report Presentation Q&A Summary

April 7, 2023

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

Q1	Your market share in the TUC market in China has been increasing every year. Is this due to your significant market share gains in the Tier 3-6 cities? Or is your market share increasing in Tier 0-2 cities? According to the preliminary results of Nipsea China for the 1Q FY2023, TUC revenue increased 19% YoY, continuing strong revenue growth following the 28% YoY increase achieved in the 1Q of FY2022. What are reasons for this strong performance in the TUC segment?
A1	<p>Our market share has continued to increase even in the Tier 0-2 cities, where our market share is already high. However, our market share increased more prominently in FY2021 and FY2022 in Tier 3-6 cities, where there are big opportunities for market share gains. We believe that this trend will continue in FY2023.</p> <p>The preliminary results of Nipsea China for the 1Q of FY2023 were provided as an exception just for reference. I will provide more information at the 1Q FY2023 results announcement on May 15.</p>

Q2	Is your market share increasing in Tier 0-2 cities as well?
A2	We do not disclose market share details. What I can tell you is that we already have a high market share in Tier 0-2 cities, and our market share has not declined in those cities.

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

Q1	I have three questions about your M&A strategy. First, is there a possibility that a reversal of the low interest rate policy in Japan will slow down your M&A activities? Second, is the acquisition of NPT to close in the 1H of FY2023 as originally scheduled? Third, do you regard the adjacencies arena, including SAF (Sealants, Adhesives & Fillers) and CC (Construction Chemicals), as the primary acquisition target?
A1	<p>The answer to your first question is that we are pursuing an M&A strategy for achieving Maximization of Shareholder Value (MSV), and therefore there is no change in our policy to continue examining acquisition targets.</p> <p>My second answer is that there is no change at this time in the initial closing schedule for the acquisition of NPT of the first half of FY2023.</p> <p>My third answer about the M&A target is that the target area is unspecified with the sole basis of judgment being whether the acquisition will contribute to MSV. As a result, there is a possibility that an acquisition we determined to contribute to MSV happens to be in the adjacencies area. But we do not examine acquisition targets in any prespecified areas.</p>

Q2	I presume that you do not have a large interest expense because you have been financing your M&As with fixed-rate borrowings so far. Do you plan to continue to use debt finance such as bank borrowings?
A2	We believe we can retain a strong advantage because yen interest rates will continue to be relatively low. We will continue to prioritize debt financing, but equity financing remains an option. Regardless of what kind of financing method we use, our criteria for selecting M&A targets will be certainly about EPS (earnings per

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

Q1	<p>The Japan Group's operating profit margin temporarily improved by implementing the Survival Challenge program that started in FY2009. However, the operating profit margin subsequently declined to the low of 2.8% in FY2022 due to factors including a backlash from the reduction of CAPEX under the Survival Challenge, allocation of NPCS (Nippon Paint Corporate Solutions) expenses, and raw material price increases. What actions do you plan to take to improve the operating profit margin? I believe that it will be difficult to achieve a turnaround in profitability in the decorative paints business because of the current competitive climate. Although the operating profit margin in the automotive business is improving due to the Next Career Plan voluntary early retirement program, it is unlikely that the operating profit margin of the overall Japan Group will recover to 10%. Please give us an update about your progress with improving the operating profit margin.</p>
A1	<p>Under the Survival Challenge program that started in FY2009, our profitability improved significantly as a result of reducing fixed costs, which had much room for a reduction. However, we regret that we also cut investment for future growth, which affected the sustainability of our growth.</p> <p>The concept behind J-LFG, an action guideline that started in the Japan Group in FY2022, is to achieve lean growth by eliminating waste. As represented by the Okayama Plant, which was completed in February 2023, we are making investments in necessary areas while placing a premium on improving efficiency or eliminating redundancies. As the culture of J-LFG becomes established in our Group, we will identify redundancies and unnecessary tasks. Wee Siew Kim and I are determined to improve efficiency. For instance, taking actions such as breaking down organizational silos, increasing personnel with concurrent positions, and increasing people who can look at our company with a bird's eye view, have allowed us to identify inefficient operations. Constant improvement activities have resulted in a steady increase in efficiency. In addition, we launched eight task forces for improving profitability. We are focusing on eliminating inefficiencies that resulted from organizational silos created by <i>bunshaka</i> in FY2015.</p> <p>The Next Career Plan voluntary early retirement program was implemented across the Nippon Paint Group and has contributed to improving profitability in all our businesses including the automotive business. In FY2022, our sales growth was sluggish due to factors such as slow growth of automobile production in the automotive and industrial businesses caused by supply chain bottlenecks at customers. As a result, we were unable to fully offset the increase in fixed costs. In the meantime, we have successfully raised selling prices to appropriate levels, including in Japan. However, we cannot quickly return the operating profit margin to 10% by using a single action. We will build on one improvement after another in order to restore the operating profit margin to a double-digit percentage. In addition, we will aim to take our profitability to the level we achieved in FY2017 and FY2018.</p>

Q2	<p>You drastically reduced expenses under the Survival Challenge program to generate profits. Is there any room for further improving efficiency? Do you have any measures on the table that will dramatically improve profitability, such as a drastic revision of the product pricing structure and conducting M&A in Japan?</p>
A2	<p>We will examine potential M&A deals whenever we spot an opportunity. However, we will not use an M&A deal just to improve profitability in the Japan Group. There are still many areas where we can reduce expenses although they are not visible from outside our organization. We will gradually increase our profitability by steadily improving efficiency in those areas.</p>

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

Q1	In relation to the preliminary results of Nipsea China for the 1Q of FY2023, please give us more information as much as possible, such as demand trends in the TUC and TUB markets and the sustainability of Nipsea China's performance.
A1	The preliminary results in the page 35 of the presentation are local currency unaudited figures. The information is for reference only and was disclosed to the extent possible. At this time, we believe that demand is gradually recovering. The outlook for the 2Q is good, and we expect to achieve the full year guidance announced in February 2023. However, we do not anticipate an explosive post-pandemic demand recovery like the one we experienced in the 2Q of FY2022.
Q2	I figure that the TUC revenue growth of 19% YoY was driven partly by explosive demand recovery. Is the pace of demand recovery gradual both in the TUC and TUB markets?
A2	The figures on page 35 of the presentation are preliminary results. More information will be made available at the 1Q FY2023 results announcement on May 15. According to the local management in China, demand recovery in the TUB market is more gradual than in the TUC market. As a result, the recovery in the TUC market is covering the slower recovery in the TUB market.
Q3	Can we assume that the TUB market has already hit the bottom and is expected to continue its recovery?
A3	In the TUB business, revenue was down 22% YoY in the 4Q of FY2022 and up 4% in the 1Q of FY2023 according to the preliminary results. We expect steady growth that will be consistent with our full year revenue guidance of 0%-5% growth YoY.

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

Q1	DuluxGroup has aggressively executed acquisitions and Betek Boya was able to reduce its interest expenses. I am very impressed with the acquisitions of these companies as clear examples of companies generating synergies in the Nippon Paint Group. On the other hand, synergies with Nipsea China and the Americas are not visible from outside. Please tell us how each segment leverages the strengths of your balance sheet.
A1	<p>The number of M&A transactions at DuluxGroup has increased dramatically from nine over nine years since the company went public in 2010 to 23 in only three years since the company joined the Nippon Paint Group. As a result, DuluxGroup has grown to account for nearly a quarter of our Group in terms of revenue and operating profit. This demonstrates the success of M&A transactions that freed DuluxGroup from the need to worry about short-term stock price movements and enabled the company to realize its full potential by leveraging the financing capability of the huge platform of the Nippon Paint Group.</p> <p>The profitability of PT Nipsea (Indonesia) has not changed much since joining our Group because this company was already highly profitable as a NIPSEA Group company. This company is taking aggressive actions for more growth.</p> <p>Europe and the Americas have large markets for big box hardware stores and retail stores, which cater to the so-called DIY market. On the other hand, Asia and China have a different business model in which distributors are the most common channel. We are pursuing M&As with potential for long-term growth and synergies by fully examining local market characteristics.</p> <p>DuluxGroup has expertise for increasing its market share both with big box hardware stores and retail stores. Cromology had improved profitability by reducing expenses and was thinking about the next actions for growth when</p>

	<p>DuluxGroup acquired this company. DuluxGroup decided that Cromology could continue to grow by leveraging DuluxGroup's knowledge and business foundation in Europe, as well as the platform of the Nippon Paint Group. After taking these factors into consideration, we proceeded with the acquisition of Cromology by DuluxGroup.</p> <p>The acquisition of JUB was also led by DuluxGroup but the idea for this acquisition first came from Betek Boya, including the potential for business expansion in ETICS (External Thermal Insulation Composite System) sector. Considering the very large growth opportunities in the Turkish market, however, we decided to focus Betek Boya's resources on the Turkish market. Instead, we decided to have JUB and Betek Boya pursue synergies in the ETICS business.</p> <p>Owing to the many excellent and dependable management teams of our group partner companies, our Group is able to pursue long-term growth by maintaining the optimal structure for the Group while utilizing our platform.</p> <p>In the Americas market, competitors tend to be more vulnerable than us to the impact of interest rate increases and inflation. However, we will not acquire companies simply because they are financially struggling due to high interest expenses.</p> <p>The acquisition of Betek Boya was an exception. This is because Betek Boya depended heavily on debt, and we were able to determine a clear path for turning around its performance of the company by eliminating its high interest expenses.</p> <p>Market characteristics are different from region to region, and one success does not apply to all M&A deals in a one-size-fits-all manner. Therefore, we examine and make a judgment on the feasibility every time an acquisition target becomes available.</p>
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Q2	Am I correct to understand that if you spot a company, for instance, in China, you will not make a decision solely from the viewpoint of increasing market share? Instead, you will conduct an M&A transaction that will contribute to MSV in the Group as a whole. As a result, focus on some regions for M&A and not so much on others?
A2	I do not deny the possibility of an M&A transaction in China and other promising regions. We do not restrict M&A targets to specific business categories or regions. We place a premium on deals that can contribute to MSV, in particular, with prospects for EPS accretion in the first year as well with proper risk and return profile. Therefore, we place emphasis on assessing corporate value. We make a decision after closely examining all conditions involving a target company without limiting the target to China. Our goal is to build up excellent companies, management teams and brands in the growth markets of paint and adjacencies.

◆ Questions by Shigeru Tai, Nikkan Kogyo Shimbun Ltd.

Q1	Since the signing of a collaboration agreement with the University of Tokyo in 2020 Nippon Paint Group has been conducting development activities for anti-viral products. Please give your assessment of how big the business for these products has grown in order to contribute to improving profitability.
A1	<p>Our collaboration with the University of Tokyo is not limited to research and development activities for anti-viral products. For instance, we are jointly working to expand the potential of paint beyond the conventional functions of coloring and protecting objects, such as by adding value involving social issues like lowering CO₂ emissions. We will continue to collaborate in various fields, including basic research, by using resources of the University of Tokyo.</p> <p>Our sales of anti-viral products have not grown to a meaningful level in terms of disclosure. Our products use advanced technologies, such as visible-light-responsive photocatalysis, and have outstanding anti-viral efficacy. However, taking an example of anti-viral spray products, service providers, such as</p>

	<p>restaurants, need to show to customers that they clean the tables every day to provide peace of mind. Our product's anti-viral formula with one-month of protection does not translate much to sales because the efficacy is not visible to customers. Communicating the advantages of the advanced technologies and outstanding performance of our products in marketing activities is very difficult.</p> <p>By the way, our anti-viral products have an excellent reputation at nursing care facilities and hospitals because of the need to clean surfaces only once a month, which eliminates the need for daily cleaning.</p>
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Q2	Do you plan to extend the collaboration agreement with the University of Tokyo after it ends in 2025?
A2	<p>I will refrain from commenting about a specific project. Nippon Paint Group is a technology-driven group. However, there are some areas where our own resources are not enough. The CTO of the Japan Group is also the CTO of NIPSEA Group. I believe there is a good chance for us to explore collaboration with research institutions around the world, including the University of Tokyo, from a broader perspective, in order to further reinforce our strengths in order to contribute to achieving MSV.</p>

◆ Questions by Ryokichi Kondo, CoatingMedia Co., Ltd.

Q1	Regarding your sustainability strategy initiatives, please give us examples of bottom-up initiatives undertaken by Sustainable Teams.
A1	<p>We believe it is not easy for us in the Head Office in Japan to fully understand global environment and safety trends. We appointed Brad Hordern, who is the Head of Sustainability at DuluxGroup, as our Environment & Safety team leader because DuluxGroup has the most advanced sustainability systems and approaches in our Group. In addition to his duties at DuluxGroup, he is coordinating the activities of our Environment & Safety teams around the world. He is also overseeing the activities of our Environment & Safety team around the world and led the activities of our Sustainability Teams around the world by focusing on current issues of the highest importance. One accomplishment is the clarification of the purposes of information gathering and other activities in order to achieve a common understanding of goals among all Sustainability Team members worldwide.</p> <p>Social requirements differ from region to region. For instance, all countries have established carbon neutral targets for 2050, except China which is aiming to become carbon neutral by 2060. If our customers insist that they will no longer purchase our products unless our Group achieves carbon neutrality by 2050 on a consolidated basis, we will be required to take a unified step globally. If that is not the case, every member of our Group must act on its own according to the requirements of its region and markets. Then we must make the benefits readily visible on a consolidated basis, rather than the Head Office imposing a standardized approach.</p> <p>We established the Sustainable Procurement team in FY2022 because of uncertainty among the four existing teams about which one was responsible for procurement. It is not realistic to control all our suppliers from Japan. However, it is necessary at least to establish a supplier code of conduct and other guidelines and ensure that people can see that we are using ethical procurement practices. The Leader of our Sustainable Procurement team is from NIPSEA Group, which has the largest procurement volume in the Group. The Sustainable Procurement team will advance in phases to achieve both ethical and low-cost procurement based on the perspective of front line operations.</p> <p>We understand that it is not possible to have our Group operate effectively by simply giving instructions to companies worldwide from our Head Offices in Tokyo and Osaka. We believe that this bottom-up approach is working very well.</p>

Q2	Do you plan to update the progress of each Sustainability Team whenever necessary?
A2	The updates on each team are in this presentation, but I did not explain this at the update meeting. We will continue to closely examine requests from the public and customer requirements and disclose information in the Integrated Report and other documents based on the quarterly progress reports from these teams to the Co-Presidents.

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

Q1	Crude oil prices are currently rising due to a production cut by OPEC. In addition, TiO2 prices in China increased in March and April. Do you expect that profitability improvement will continue in the 2H despite the rising cost of raw materials? Also, do you think you can further increase selling prices after taking into consideration the current demand environment?
A1	<p>Raw material prices change constantly. Our analysis is that price inflation has slightly moderated from the peak levels last year. If prices start rising again, we will respond by building up some extra inventory. Even if prices start moving up again, we believe we have room for passing on higher expenses because price sensitivity of demand for our products is relatively low.</p> <p>Our performance will be impacted more by GDP growth as growth, rather than the prices of products. If economic growth slows down significantly or there is stagflation, our performance will be adversely impacted. However, demand elasticity of our products is low. As a result, we do not expect the demand for our products to decline in response to higher raw material prices.</p> <p>For instance, the cost of paint is smaller than wages of professional painters as a percentage of the total cost of renovations. At DIFM (Do-It-For-Me) projects, contractors' wages may increase. We hope that the economy will be stable and raw material prices will not increase further. However, even if prices do increase, the room for us to pass on price increases is not zero. This is our view at this time.</p>

Q2	Can we assume that raw material prices are currently significantly lower than the level you assumed?
A2	Our assumptions are roughly on the same level as recent raw material prices.

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

Q1	Please give us a qualitative explanation about the regional differences in the impact of weather and persistently high crude oil prices in regions other than China.
A1	<p>I will provide more information at the 1Q results announcement on May 15. For now, I will tell you that no region differed significantly from our assumptions. On a preliminary results basis, our profitability is improving overall, notably in Asia.</p> <p>Our performance in Türkiye was rather sluggish. The earthquake did not affect our employees and production facilities. However, it undermined consumer sentiment and is causing concerns about the possibility of slower GDP growth.</p> <p>Our performance in Australia normally falls within our assumptions. At this time, however, we still have raw materials which we purchased at a high price. As a result, operating profit margin improvement was slightly below our expectations. Management in Australia is confident that they can achieve a recovery and meet our assumptions. The management team of DuluxGroup is highly dependable, so we are not concerned about the company.</p> <p>Dunn-Edwards in the Americas is located on the US West Coast and is vulnerable to weather conditions. There were more rainy days than a year ago and blackouts in some areas on the West Coast. Considering the current residential</p>

	<p>market conditions, we expect that our performance will be slightly weak. The weather is not very good in Japan as well, which I expect is affecting construction companies.</p> <p>Although our performance will fluctuate from quarter to quarter, we expect to achieve our full-year guidance.</p>
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Q2	Am I correct that there is no significant change in your performance in Indonesia, ASEAN, and Europe in terms of demand, selling prices, and raw material prices compared to the FY2023 guidance announced in February?
A2	Our performance is weaker than the FY2023 guidance in Australia, Europe, and the Americas, and our performance is strong in Asia.

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

Q1	Considering that prices of raw materials such as propylene are decreasing, I expect that your operating profit margin will improve. You explained that the operating profit margin at Nipsea China improved by 2% or more based on the preliminary results for the 1Q of FY2023. How much improvement in operating profit margin do you expect? If the margin improvement is small, can we assume that the reason is price competition?
A1	We disclosed that the operating profit margin at Nipsea China increased by 2% or more based on the preliminary results. However, I will not comment on the degree of improvement beyond 2%. Some people believe that price competition is intense in China, but Nipsea China has been maintaining prices in the TUC segment. Nevertheless, this market is highly competitive, and our forecast is based on a conservative outlook.

Q2	Regarding the TUC market share shown on page 10 of the presentation, your DIY market share in FY2021 was 27%. Please explain the scope of the TUC market and the difference between the DIY market share of 27% in FY2021 and the TUC market share of 21% in FY2021 in this presentation.
A2	<p>The global market data, including the Chinese market data, are based on our estimates. The TUC market share was calculated with a larger denominator compared to the data disclosed previously, due to more accurate data available in Tier 3-6 cities and a broader range of products included in the scope of aggregation.</p> <p>The market share in FY2022 was 24%, which was a modest increase from FY2021. This was because demand was soft due to lockdowns in large cities, where we have an advantage. The impact of the pandemic was relatively small in Tier 3-6 cities, which we have been focusing on in recent years. We will aim to steadily increase our market share by steadily increasing sales in Tier 3-6 cities.</p>

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

Q1	Regarding the Japan Group, please give us updates on investments for upgrading aging facilities and developing new processes in the restructuring project for production bases in Japan.
A1	We do not have any large-scale restructuring plans for our production bases in Japan at this time. The projects we announced in the past and presented at the announcement of the Medium-Term Plan in March 2021 were projects to be considered or as future plans; they were not approved officially by the Board of Directors. We will continue to make investments in areas where necessary by prioritizing the upgrading of aging facilities and plants. We are making appropriate

	investments in appropriate locations, such as the Okayama Plant and the Research Institute in the Shinagawa Office. From the perspective of our BCP (Business Continuity Plan), we believe the geographical diversification of production facilities is critical with locations such as Chiba, Tochigi, Aichi, Okayama, and Osaka, and significant functions in each region.
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◆ Questions by Ryokichi Kondo, CoatingMedia Co., Ltd.

Q1	You explained that DuluxGroup has a successful business model in the adjacencies business. Are you planning to use this model in Japan too?
A1	In the adjacencies business, for instance, we are examining the feasibility of deploying the Selleys brand in Japan. The DIY market in Japan is not as large as in the US and Europe. We are currently working on determining the target market, investments required, returns, and needs of distributors.

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