FY2020 3Q Financial Results Conference Call Q&A Summary
November 13, 2020

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

Q1	Regarding 4Q operating profit forecast, you said the reason for forecasting lower earnings YoY is higher investments and expenses for growth in FY2021 and afterward. I think 4Q profit forecast is rather low compared to your earnings in the first three quarters. According to your projections, operating profit will decrease by around 12 billion yen QoQ from 3Q to 4Q. Does that mean expenses will increase by about 10 billion yen from 3Q to 4Q? Please explain why you are forecasting a QoQ profit decrease for 4Q.
A1	As you pointed out, YoY decrease in 4Q operating profit forecast is not because of weak performance in any particular business segments. Rather, we expect substantial expenses and investments for growth in FY2021 and beyond. On the other hand, the first three quarters of FY2020 were affected by the COVID pandemic, which caused something of a special demand. For instance, business activities in China were severely restricted temporarily until March, but our performance rebounded subsequently and remained relatively strong in 2Q and 3Q with lower promotion expenses than in a normal year. We are considering investments for future growth, including for marketing, sales promotion, and innovation, with the right timing. We expect certain expenses for these growth initiatives. The cause of the cost increase is not a jump in raw material prices but mainly an increase in SG&A expenses with stable raw materials prices overall.

Q2	Is the increase in SG&A expenses closer to 5 billion yen or 10 billion yen?
A2	We do not disclose SG&A expenses. So, please make your own estimate. To supplement my answer to your question regarding reasons for our forecast of lower operating profit for 4Q than in 3Q, seasonal characteristics are quite different between the July-September and October-December quarters. Demand is very high in September, while business activities are basically slower with fewer business days in the October-December quarter than in other quarters. This is the same in markets in the Southern Hemisphere.

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

Q1	Regarding the forecast for the DIY segment of decorative paints business at NIPSEA China on page 30 of reference material, you revised the full-year YoY growth forecast to 0%～5% growth from a 5%～10% decline in your previous forecast. This is a considerable change in assumptions from three months ago. You mentioned that your market share has not changed much. Please tell us what factors caused a big improvement in market sentiment. Do you think this change of market tone is sustainable?
A1	When we made the forecast in August, we assumed our 3Q performance would be flat from the previous year. However, as you can see in our 3Q results, our performance was much better than our forecast, with 9% YoY revenue growth. Our sales were very strong overall and did not vary across cities of different tiers. We believe the market momentum has improved significantly following an improvement in demand for repainting existing housing. This demand was declined slightly in the April-June quarter due to reasons including entry restrictions to houses for professional painters. The 4Q heat map on page 29 of reference material indicates that market conditions are projected to be almost flat compared to 4Q of FY2019. However, sales in the October-December quarter are always lower than in the July-September quarter. Even so, the market momentum is not bad at all. We constantly take actions for market share gains. At the same time, we will not make discounts indiscriminately merely in pursuit of sales volume. Instead, we will maintain a good balance between market share gain initiatives and revenue growth. This is why we upwardly revised our FY2020 forecast.

Q2	If another major outbreak of the COVID pandemic does not happen, can you expect growth to continue at a rate between a little higher than China's GDP growth rate or close to twice this rate in the China decorative paints business (DIY and Project segments) in the next fiscal year and beyond?
A2	The DIY segment has recovered, but the Project segment will certainly be the driving force behind the overall growth of the decorative paints business at NIPSEA China. I cannot give you specific figures, but your understanding is not far off the mark.

Q3	Regarding the answer to A2, can we assume that the overall decorative paints business at NIPSEA China is projected to grow at a rate a little higher than

	GDP growth?
A3	That's right. I would not talk about our growth rates in direct connection with China's GDP. However, aiming continuously for growth higher than GDP growth is consistent with our policy of consistently outperforming the growing paint market and capture market share. Our Chinese team is working very hard to accomplish this goal.

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

Q1	Regarding Europe, Betek Boya in Turkey, an emerging economy, delivered strong results with revenue growing 84% YoY. Looking at macroeconomic trends, automobile and housing sales were very strong in the July-September quarter. On the other hand, there are side effects of Turkey's monetary easing policies, i.e. devaluation of the Turkish lira and low foreign exchange reserves. As a result, macroeconomic conditions have become very unstable. You project lower revenue in 4Q at Betek Boya after strong 3Q. Do you think the condition of the economy could continue to affect performance at Betek Boya in FY2021? Or, do you think economic instability in Turkey is not a major problem?
A1	It's true that we need to look at both microeconomic and macroeconomic conditions in Turkey. As a microeconomic measure, NPHD provided financial support to Betek Boya after the acquisition more than a year ago. Betek Boya used the capital to aggressively drive sales growth, and their sales promotion activities have been very successful. Betek Boya achieved 84% YoY revenue growth in 3Q. Our forecast for lower revenue in 4Q at Betek Boya assumes a drop in revenue after the very high 3Q sales, which is less related to the macroeconomic environment. The forecast for a decrease in revenue is some repercussion from very strong first three quarters. On the other hand, in terms of macroeconomic conditions, the weak Turkish lira has both positive and negative effects. Betek Boya imports most of its raw materials and uses foreign currency for the payments. This is the same for Betek Boya's competitors. If the Turkish lira weakens, there will be discussions about price increases. Fortunately, Betek Boya is currently debt-free and changes the cash it earns into foreign currencies to purchase raw materials. Hedging functions sufficiently to reduce the risk at Betek Boya to a level that is probably lower than at its competitors.

	In addition, the collaboration for sales growth is working successfully between Betek Boya and NIPSEA Group, including for the provision of raw materials, which is giving Betek Boya an advantage over its competitors. As a result, we expect Betek Boya to gain market shares regardless of macroeconomic conditions. However, we need to pay close attention to the possibility that paint demand may decline if economic conditions change. At present, Turkey has a population of 80 million with very healthy demographics. We project that paint market will continue to grow steadily unless geopolitical risks become significant. Betek Boya is well positioned to gain market shares in this growing market.

Q2	Can we assume that there are no serious signs of an economic slowdown in Turkey or severe depreciation of lira, and Betek Boya's relative strengths can make up for even a somewhat serious downturn in economic conditions?
A2	Macroeconomic conditions are highly volatile, so we are not optimistic. But we are not particularly concerned about the current market conditions in Turkey either. Betek Boya is operated properly by an excellent management team, and we place high confidence in the company.

Q3	Macroeconomic conditions are also relatively challenging in Indonesia. What is your take on this?
A3	I will refrain from making any comments about Indonesia before our acquisition closes. After consolidation of the Indonesia business following the closing in January 2021, I will talk about market and business conditions.

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

Q1	Regarding the sales environment of NIPSEA China's Project segment, isn't there a risk of doubtful accounts because some Chinese real estate developers are now cash-strapped? In addition, payment periods for trade receivables are becoming longer. Given these circumstances, please tell us about risk involving cash flow and trade receivables collection at NIPSEA China.
A1	Some real estate developers publicly disclose information. We follow up on the status of trade receivables collections in close coordination with management in China. To give you the conclusion first, there is no need at this time to establish an

	allowance regarding trade receivables of customers. If the situation changes, we will take appropriate actions such as providing an allowance for doubtful accounts. NIPSEA China's management closely communicates with its customers on their policies for reducing debt. Management monitors the collection of trade receivables, including extensions of trade receivables payment periods, of individual receivables to manage the risk of defaults. Furthermore, the NPHD head office is closely monitoring the situation. Consequently, we believe there is no reason at this time to think receivables will become a problem. The extension of trade receivables payments has positive and negative aspects. I'm not saying that we have no trade receivables categorized as delinquent. But we will tolerate extensions of trade receivable payments as part of aggressive sales promotion measures for market share gains. Please note that we are not being forced to accept extensions.

Q2	I have heard that some companies had cash flow problems. On the other hand, can we assume that NIPSEA China has no increase in risk even with longer trade receivables payment periods and that the risk is controllable?
A2	I will not comment on individual customers. But I can tell you that we carefully monitor news reports and keep our antennas high. At NIPSEA China, sales are spread over many customers and are not concentrated on one or two customers. Naturally, we have larger sales to our largest customers. There is no ending to horror scenarios such as chain reaction bankruptcies and financial instability. However, we implement risk management with strict financial discipline.

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

Q1	Please tell us about your 4Q plans regarding investments and expenses for growth in FY2021 and beyond. Page 28 of presentation material mentions that you will increase advertising costs, sales promotion expenses and marketing expenses at NIPSEA China and DuluxGroup. Do you plan to make investments mainly in these two regions? Please also provide details about these investments.
A1	NIPSEA China and DuluxGroup have larger sales than in other regions, and accordingly they have relatively higher costs and expenses than in other

	regions. That's why we mentioned the cost increases at these companies in the presentation. Please note that page 28 also touches on the increase in headquarters expenses, which include expenses at NPHD. We will complete the acquisition of Asian JVs and consolidate the Indonesia business in the next fiscal year, and NPHD will incur some organizational development expenses. We expect a slight YoY revenue decrease at Betek Boya in 4Q, and Betek Boya also plans investments for the launch of new brands for growth in FY2021 and beyond. I'm not saying that we are already focusing only on next fiscal year. We are planning substantial sales promotion and marketing investments in almost all operating regions whilst also focusing on this year. Capital investments are depreciated over time and therefore do not result in significant expenses on a quarterly basis. Regarding activities that result in expenses, we will take many actions for growth in next year if we can make good use of our money. In doing so, I will be responsible for controlling non-urgent expenditures and spending simply to use up budgets, while maintaining the balance with revenue, to achieve our 4Q revenue and profit forecast. The reason for the operating profit decrease forecast for 4Q is not a downturn in any specific business fields. We cut back investments and expenses based on our conservative forecasts, especially for 3Q. However, our earnings were strong, and we will aggressively make investments for growth in FY2021 and beyond. This is based on the strategic direction of all group companies to pursue sustainable growth.

Q2	Regarding higher expenses planned for 4Q, can we assume that NIPSEA China plans sales promotion campaigns in 4Q and that its expenses are included in the cost increase plan?
A2	I cannot say anything about whether or not, or how many times, campaigns will be launched. We will carry out all possible activities including sales promotion campaigns. Nevertheless, these activities are mainly for growth in FY2021 and beyond and are not aimed at boosting sales this year. In other words, we will not much use price discounting sales promotion campaigns.

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

Q1	Please tell us about your marketing initiatives and capital investments. Judging from what I have heard, I assume you will increase investments this

	year because your performance is better than you expected. What are your thoughts about expenses in the next fiscal year, including marketing activities and capital investments in Aichi Plant, which is in some media reports?
A1	I will talk about our investment plans for the next fiscal year in February or later. We are now working on our new medium-term management plan. This year is the final year of our current medium-term management plan, so we are determining our goals for business activities next year. We are not talking about business activities in a single year. To achieve medium and long-term growth, we need to find the proper balance between short-term and medium- and long-term growth, although we will naturally aim for earnings growth every year. In some regions, we expect an increase in investments in businesses where we have been holding down investments. For instance, President & CEO Tanaka explained the necessity and plans for investments in the Japan segment at investor presentation in February. Numerical targets are being finalized, but the critical point is how to build a base for the sustainability and growth of business operations from a long-term perspective. To add one more point, we have positioned ESG and the SDGs as core of our management. As a result, we must carefully plan our capital investments by taking into consideration many factors, including cost effectiveness as well as the environmental impact of these investments at our operations worldwide. I cannot give you specific figures but only a big picture today.

Q2	Speaking of balance with short-term business performance, could you give us some hints about numerical targets for next year? For instance, your operating profit forecast for this year is 76 billion yen and you will aim at higher operating profit next year. Are there any possibilities, for instance, that you will incur expenses of tens of billions of yen or that a project could significantly eat into earnings?
A2	I don’t expect expenses of tens of billions of yen in a single fiscal year. The paint industry requires relatively low capital investments, and our basic policy is to pursue earnings growth. Another important subject is the starting point for the next medium-term management plan. In FY2020, COVID affected the business climate worldwide. Of course, there is no guarantee that COVID will not have a negative impact in FY2021 and beyond. This year is the final year of the

	current medium-term management plan. I believe that our performance would have been better if the COVID crisis had not happened. Consequently, we will not make FY2020 the starting point for the next medium-term management plan. We certainly have even higher aspirations. I cannot make a commitment today for growth from the operating profit forecast of 76 billion yen. But I can tell you that 76 billion yen is not a very high starting point for us.

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

Q1	You revised the full-year growth forecast for Oceania by 5 percentage points. This growth forecast is high considering GDP growth rates in this region and restrictions on immigration in countries dependent on immigrants for growth. I suppose the reasons for this revision are continuing stay-at-home demand and market share gains at DuluxGroup. Please give us updates on DuluxGroup's market shares. Also, isn't there a risk that the growth rate will start slowing down in the next fiscal year because of the front-loading of demand this year?
A1	We have stated that DuluxGroup's market share is 47%. Although we do not disclose market share figures during a fiscal year, I can say that this market share is now potentially higher. Reasons for sales increase are higher sales volumes and selling prices. DuluxGroup has grown steadily since its listing. The company's strong performance during FY2020 is driven by very high home improvement demand, which is the largest market for us, rather than a narrow stay-at-home restrictions. As I mentioned earlier, sales were strong at DuluxGroup partly because of the front-loading of demand. Therefore, I believe there is a chance that this demand will progressively normalize from 4Q of FY2020 to 2Q of FY2021. Based on this outlook, we are considering what kinds of marketing initiatives and investments will be required to achieve further market share gains in a region where growth may normalize over the next several months. With stay-at-home and other restrictions continuing in some regions because of COVID, the current booming market, due partly to the many highly appealing features of paint, is a positive surprise for us. Nevertheless, we are prepared to deal with risk factors that could affect our future business activities.

Q2	You mentioned earlier that sales growth is attributable to “higher selling prices.” Can we assume that the average unit price has increased?
A2	That’s right. Our sales do not grow this much due to higher sales volume alone. This growth is a combination of higher volumes and prices. But I cannot give you breakdown of sales growth.

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

Q1	Please explain market trends in 3Q and your 4Q outlook regarding raw materials. The prices of titanium dioxide and titanium ore, which is upstream of titanium oxide, have increased considerably, and the prices of isocyanate and propylene oxide are generally climbing. Please tell us your outlook for raw materials in 4Q.
A1	Market conditions in 3Q improved from the sharp drop in 2Q. However, overall raw material expenses at our Group, including inventories, have slightly declined because of cost reduction measures. As a result, our gross profit margin has increased slightly. For market conditions in 4Q, we are not assuming an increase in the ratio of raw materials costs at this time. But we do not expect the ratio to decline significantly either.

Q2	Can we assume that raw material prices were lower in 3Q than in 2Q and will be roughly the same in 4Q as in 3Q?
A2	The ratio of raw materials expenses varies slightly for different raw materials, but overall the ratio was lower in 3Q than in 2Q.

◆ Questions by Shuichi Nakahara, Tokai Tokyo Research Center Co., Ltd.

Q1	Please provide more details about the decorative paints business at NIPSEA China. Following a sharp decline in 1Q due to entry restrictions to buildings, revenue recovered to the prior-year level in 2Q, recovered to 9% YoY growth in 3Q and is projected to continue growing in 4Q. What is the driver of this revenue growth, sales volume or selling prices? Given that there are not many media reports of personal consumption improving considerably, are there government stimulus programs such as subsidies?

	You explained earlier that the Project segment returned to positive YoY revenue growth in 2Q and there was a large volume of new construction projects in northern and western China in 3Q, but there is not much news coverage about this. Can we assume that very aggressive investments have been continuing, whether they are backed by government's subsidies or other stimulus measures or not, and will continue in 4Q?
A1	I will use a timeline to explain the market conditions for the DIY segment. In 1Q COVID lockdowns stopped our production. However, we restarted plant operations ahead of our competitors after the Chinese New Year in February and managed to resume production in March. However, many of our employees were unable to return quickly to our production sites. In 2Q entry restrictions to buildings remained in many areas, but the situation improved gradually and was different from 1Q. In 3Q entry restrictions were lifted in many areas, and there was a recovery of demand, for instance from people who were unable to repaint their houses in 1H of this year. We are hoping that this favorable momentum will continue. As you pointed out, personal consumption is not growing explosively, as I explained in August. However, consumption is recovering slowly overall. Singles' Day retail sales were not bad, although these sales are not a direct indicator of personal consumption. Therefore, the DIY segment is recovering in terms of sales volume. We do not disclose the breakdown of sales in terms of selling prices and sales volumes. I can say that sales volumes were good overall. As you pointed out, in the Project segment we work closely with major real estate developers. We target the large number of projects of customers associated with construction activity in the real estate market overall. The issue we faced after the lifting of COVID restrictions was whether work could be restarted at construction sites. We restarted operations of most of our plants ahead of our competitors and provided production volumes and supply chains that sufficiently met our customer needs. This contributed to a quick recovery of the Project segment. However, we cannot be optimistic because our competitors have also responded appropriately to market conditions. The Project segment had a very strong 4Q in FY2019 with revenue growing 42% YoY, including last-minute demand at the end of the year. I don't know how much growth we will see in 4Q of this year, but I don't expect a major change in the current market momentum.

Q2	Can we assume that there is no overheating of public investment and investments by real estate developers and the current level of investment will continue for the time being?
A2	We are in a position to supply products that meet customer needs but not in a position to tell you about trends in public investments. So, please refer to real estate analysts for this information. However, judging from our current orders, the momentum is not negative at all.

Q3	Regarding the DIY segment, do you assume growth of 4% to 5% boosted by booming economy?
A3	No, I do not say that much. As for the DIY segment, considering its large revenue, our assumption for growth is not necessarily optimistic. In the DIY segment, however, we have a history of achieving market share gains, and will continue to aim for more gains.

Q4	So your market share has not changed as of 3Q?
A4	That's right. Our market share may have increased slightly. However, competitors' products are also selling well, so we do not think our share has necessarily increased. These are our own estimates and we do not have any objective data.

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

Q1	Page 18 of presentation material says that your market share in Japan was unchanged. However, I think you are losing out slightly to competitors in the automotive coatings sector. Is the reason changes in customers' product mix? On the other hand, based on our analysis, you are slightly capturing market share from major competitors in the decorative paints sector. This analysis is based only on sales. Please provide more information.
A1	As you pointed out, we monitor the automotive coatings business by using aggregate sales as well as sales by automakers' product line. The production volume of each line may generally be different from assumptions. We are not losing orders one after another and our market share has remained flat. Consequently, our analysis is that changes in our market share depend on the mix of vehicles produced. Our decorative paints business has many competitors. Some are direct

	competitors and others are not. The decorative paints business has the DIY segment and the Project segment. We are winning in some categories and losing in others, but overall our market share has remained roughly unchanged. This is why the heat map on page 18 has a horizontal arrow for the DIY and Project segments in the decorative paints business. As you pointed out, our market share has increased in some business segments and decreased in others. We are winning in one segment but are losing in another. Overall, however, our sales in Japan are roughly in line with the market conditions announced by the Japan Paint Manufacturers Association.

End