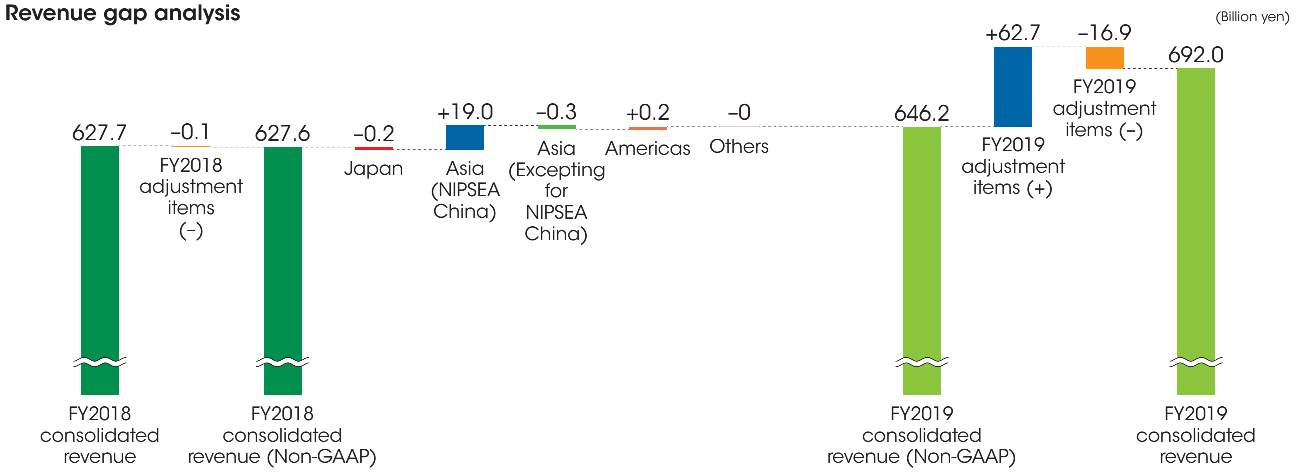
Analysis of Operating Results

Overview of consolidated financial results

During the fiscal year ended December 31, 2019, consolidated revenue of NPHD and its group companies (collectively, "the Group") increased by 10.3% from the previous year to ¥692,009 million due to the strong performance of the decorative paints business and industrial coatings business in Japan as well as the decorative paints business in China, and the acquisition of ownership of Australian paint manufacturer DuluxGroup Limited and Turkish paint manufacturer Betek Boya ve Kimya Sanayi Anonim Sirketi, despite the effects of the yen's appreciation. Consolidated operating profit decreased by 9.8% from the previous year to ¥78,060 million due to the recording of share acquisition-related expenses associated with corporate acquisition in Japan and an impairment loss on the Europe automotive business group and an Indian automotive business company, despite a significant profit increase in China resulting from low raw material prices. Consolidated profit before tax decreased by 10.7% from the previous year to ¥79,518 million, and profit attributable to owners of the parent decreased by 19.0% from the previous year to ¥36,717 million. Factors for changes in non-GAAP results are as shown in the following figures.

Revenue gap analysis

(Billion yen)

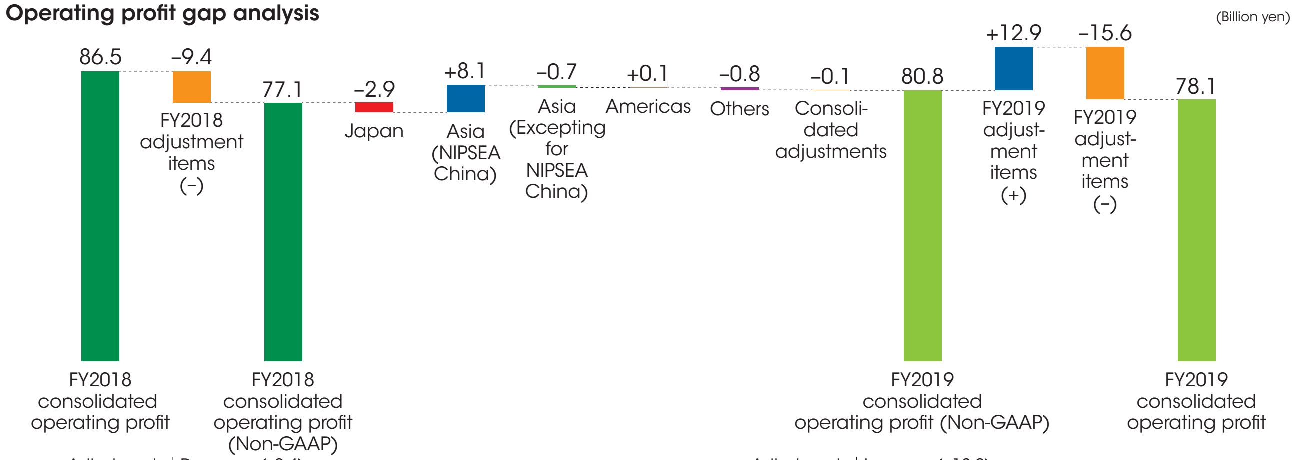


Adjustments | Decrease (−0.1)
Effects of exchange rate fluctuations

Adjustments | Increase (+62.7)
New consolidation (DuluxGroup +47.6, Betek Boya +15.1)
Decrease (−16.9)
Effects of exchange rate fluctuations

Operating profit gap analysis

(Billion yen)



Adjustments | Decrease (−9.4)
Sale of Neyagawa Office (−2.3)
Subsidy income in China (−3.7)
Gain on sale of fixed assets in China (−3.4)

Adjustments | Increase (+12.9)
New consolidation (DuluxGroup +5.9, Betek Boya +2.2),
Insurance income in Japan (+2.0), subsidy income in China (+1.5), gain on sale of fixed assets in China (+1.3)
Decrease (−15.6)
Effects of exchange rate fluctuations (−2.1)
Impairment loss (−11.3), M&A related costs (−2.2)

Status of assets, liabilities and net assets

Total assets at the end of the fiscal year ended December 31, 2019, increased by ¥524,657 million from the end of the previous fiscal year to ¥1,478,646 million. Current assets increased by ¥63,001 million from the end of the previous fiscal year, mainly due to increases in trade and other receivables of ¥33,575 million, and inventories of ¥27,052 million, despite a decrease in cash and cash equivalents of ¥6,333 million. Non-current assets increased by ¥461,656 million from the end of the previous fiscal year. The increase was primarily attributable to factors such as an increase in property, plants and equipment of ¥32,974 million following the application of IFRS 16 Leases and increases in property, plants and equipment of ¥62,376 million, intangible assets of ¥133,726 million, and goodwill of ¥215,763 million resulting from the acquisition of DuluxGroup Limited and Betek Boya ve Kimya Sanayi Anonim Sirketi.

Liabilities increased by ¥484,297 million from the end of the previous fiscal year to ¥790,667 million, mainly due to an increase in borrowings of ¥320,852 million due to the acquisition of DuluxGroup Limited and Betek Boya ve Kimya Sanayi Anonim Sirketi and an increase of liabilities of ¥177,163 million associated with the addition of new companies to the scope of consolidation.

Equity increased by ¥40,360 million from the end of the previous fiscal year to ¥687,979 million. This was mainly attributable to an increase in foreign currency translation adjustments and an increase in retained earnings due to the recording of profit attributable to owners of parent. As a result, equity attributable to owners of parent to total assets fell from 54.5% at the end of the previous fiscal year to 37.4%. Also, goodwill to equity attributable to owners of parent increased from 39.2% to 77.2% due to an increase in goodwill in relation to the acquisition of DuluxGroup Limited and Betek Boya ve Kimya Sanayi Anonim Sirketi.

Status of cash flows

Status of cash flows

In the fiscal year ended December 31, 2019, operating activities generated an influx of ¥92,076 million, investing activities resulted in an outflow of ¥352,769 million, and financing activities delivered an inflow of ¥254,018 million, resulting in cash and cash equivalents (hereinafter "cash") of ¥123,300 million, a decrease of ¥6,333 million compared to the end of the previous fiscal year.

Cash flows from operating activities

Net cash provided by operating activities increased by ¥30,542 million from the previous fiscal year to ¥92,076 million. Primary factors include a cash inflow (excluding increases and decreases in operating capital) of ¥113,112 million, mainly reflecting non-cash expenses such as depreciation and amortization on profit before tax, and a cash increase of ¥1,813 million due to a decrease in operating capital and income taxes paid of ¥22,849 million.

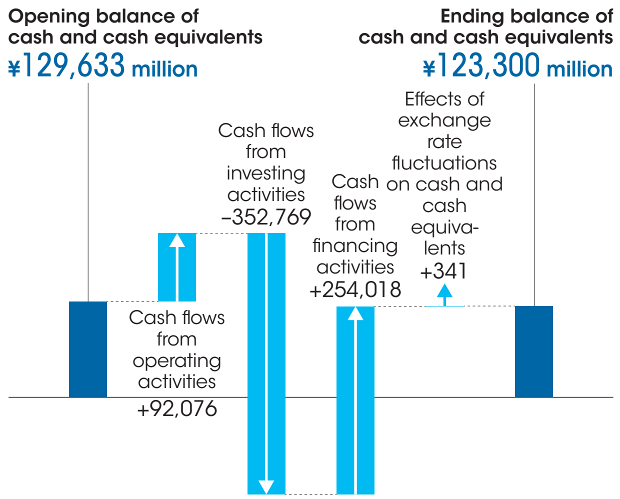
Cash flows from investing activities

Net cash used in investing activities increased by ¥315,329 million from the previous fiscal year to ¥352,769 million. This was mainly attributable to an outflow of ¥318,655 million due to the acquisition of shares of subsidiaries and an outflow of ¥22,764 million due to the purchase of property, plant and equipment.

Cash flows from financing activities

Net cash provided by financing activities increased by ¥247,789 million from the end of the previous fiscal year to ¥254,018 million. Primary factors include an inflow of ¥301,178 million due to an increase in short-term borrowings, an outflow of ¥21,209 million due to repayments of long-term borrowings, and an outflow of ¥26,743 million due to dividends paid.

Cash flow analysis



Analysis of Operating Results

Sources of equity and liquidity of funds

The Group uses earnings from operating activities as the financial source for business activities and appropriates them for capital expenditure, R&D investment, operating capital, payment of dividends, and repayment of borrowings. To meet funding requirements necessary for strategic investment to achieve sustainable growth, we procure funds externally with consideration given to our earnings outlook, overall funding requirements, and repayment capacity, while maintaining financial discipline. During the fiscal year ended December 31, 2019, we made borrowings of ¥320,852 million to execute M&A transactions. As a result, the balance of bonds and borrowings at the end of the fiscal year ended December 31, 2019, stood at ¥338,854 million for NPHD and ¥103,342 million for its consolidated subsidiaries. The Group had operating capital of ¥152,427 million at the end of the fiscal year ended December 31, 2019. The balance of cash and deposits of the Group at the end of the fiscal year ended December 31, 2019, was ¥123,300 million, the breakdown of which is as follows: the balance of cash and deposits of NPHD amounting to ¥40,751 million, the balance of cash and deposits of domestic subsidiaries of ¥2,875 million, and cash and deposits and marketable securities with high liquidity totaling ¥79,673 million held by overseas subsidiaries. Cash and deposits of domestic subsidiaries are centrally managed by NPHD using the cash management system (CMS). Cash and deposits owned (and held) by overseas subsidiaries are mainly used for expanded reproduction at local production bases, and any surplus cash generated is collected separately from ordinary dividends, as special dividends. The Group currently holds sufficient cash on hand to smoothly maintain its business activities, and we have little concern about a shortage of funds for meeting future fund requirements.

Financial results by segment

The status of each segment is as follows. "Oceania" has been added as a reportable segment as of the third quarter ended September 30, 2019.

Japan

Revenue for automotive coatings was at the same level as the previous year in an environment where the number of automobiles manufactured remained solid, despite the effects of the Consumption Tax increase and a decrease in the export of products. As for industrial coatings, revenue was at the same level as the previous year, impacted by a decline in market conditions resulting from natural disasters that occurred in the fourth quarter of the fiscal year under review and a tax increase, despite an increase in demand for the fiscal year under review due to restoration works following the natural disasters that occurred in the previous year. As for decorative paints, revenue was higher than the previous year under solid market conditions due to factors such as efforts to expand sales in the retail sector.

As a result, consolidated revenue for the Japan segment decreased by 0.1% from the previous year to ¥182,585 million. Consolidated operating profit decreased by 15.2% from the previous year to ¥36,990 million due to factors such as the recording of share acquisition-related expenses associated with the corporate acquisition announced in April 2019. The consolidated operating profit includes ¥13,585 million of dividend income from overseas group companies (¥14,012 million in the previous year). All of this dividend income is eliminated under intersegment eliminations and other adjustments as it is an internal transaction.

Asia

Revenue for automotive coatings was lower than the previous year due to a decrease in the number of automobiles manufactured in China, India, and Thailand from the previous year. As for decorative paints, our primary business in Asia, revenue was higher than the previous year as a result of focusing on sales promotion activities for mainstay interior residential paints and achieving favorable sales of decorative paints for exteriors in China, in spite of stagnant market conditions in Singapore, etc.

As a result, consolidated revenue for the Asia segment increased by 1.0% from the previous year to ¥359,213 million. Consolidated operating profit decreased by 3.1% from the previous year to ¥50,769 million due to the effects of the yen's appreciation, an absence of the subsidy income related to the removal of factories resulting from environmental regulations in China recorded in the previous year, and the recording of an impairment loss on an Indian automotive business company, despite a decline in raw material prices.

Oceania

The profit and/or loss of DuluxGroup Limited since September 2019 has been reflected in the Group's consolidated financial results. The decorative paints business and the paint related business remained solid by virtue of sales promotion activities and a share increase under weak new housing market conditions in Australia.

As a result, consolidated revenue for the Oceania segment was ¥47,578 million, and consolidated operating profit was ¥5,861 million.

Americas

Revenue for automotive coatings decreased from the previous year due to factors such as the sluggish production of automobiles in the United States, the core region. In decorative paints, revenue increased from the previous year due to the sales expansion of high value-added products and an increase in the number of shops.

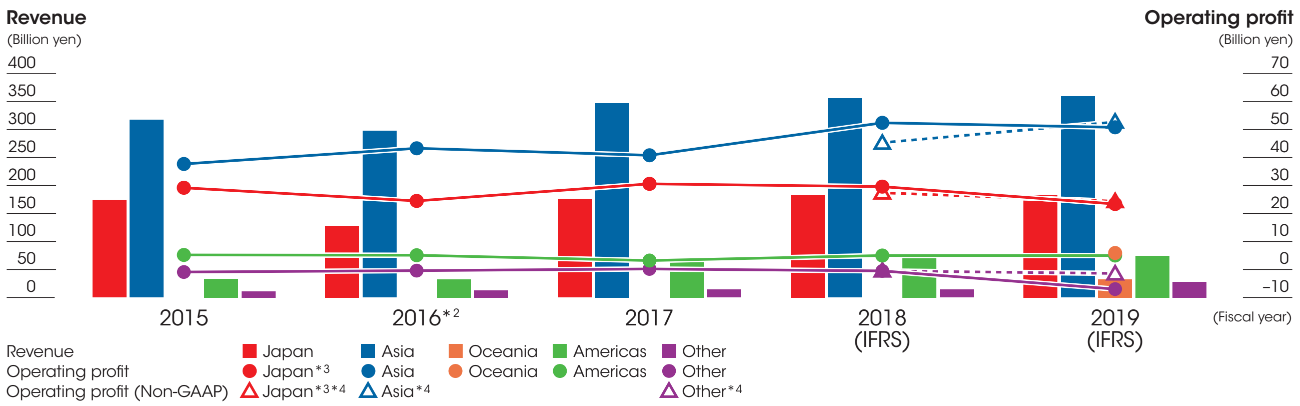
As a result, consolidated revenue for the Americas segment decreased by 0.8% from the previous year to ¥74,618 million. Consolidated operating profit increased by 0.4% from the previous year to ¥5,010 million due to factors such as an improved product mix for decorative paints.

Other

Revenue for automotive coatings decreased from the previous year due to the yen's appreciation and sluggish production of automobiles in our operating regions. The financial results of Betek Boya ve Kimya Sanayi Anonim Sirketi, whose profit and/or loss since July 2019 is reflected in the Group's consolidated financial results, remained solid.

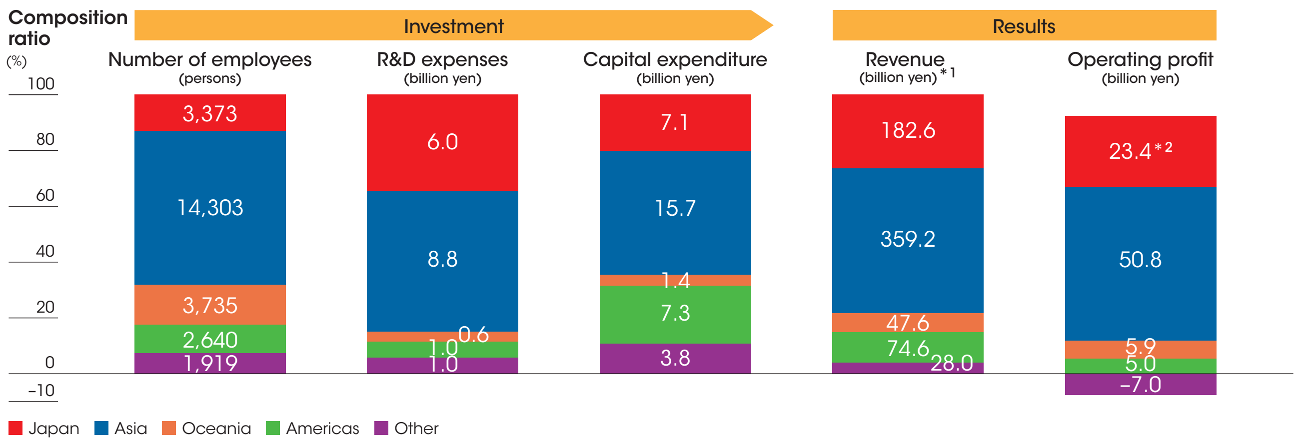
As a result, consolidated revenue for the segment increased by 101.5% from the previous year to ¥28,012 million, and consolidated operating loss was ¥6,972 million, compared to an operating loss of ¥529 million in the previous year, due to the recording of an impairment loss on the Europe automotive business group.

Revenue & operating profit transition by segment



*1 Revenue excludes intersegment revenue.
*2 Revenue for the Japan segment for the fiscal year ended December 31, 2016, covers nine months from April 1 to December 31 due to a change in the accounting period.
*3 Operating profit for the Japan segment excludes dividends from overseas group companies.
*4 Non-GAAP adjusts for F/X, subsidy, M&A related costs, and impairment loss.

Investment results by segment



*1 Revenue excludes intersegment revenue.
*2 Operating profit for the Japan segment excludes dividends from overseas group companies.