

Date and time:

Wednesday, February 3, 2021, 17:00-19:00 (JST)

Respondents:

Yoshihiro Hasebe	Representative Director, President and CEO
Toshiaki Takeuchi	Representative Director, Senior Managing Executive Officer Representative Director, President, Kao Group Customer Marketing Co., Ltd.
Tomoharu Matsuda	Director, Managing Executive Officer President, Consumer Products, Global
Yoshihiro Murakami	Managing Executive Officer President, Consumer Products - Cosmetics Business, Global Senior Vice President, Consumer Products – DX Co-Creation, Global Representative Director, President, Kanebo Cosmetics Inc.
Kenichi Yamauchi	Executive Officer Senior Vice President, Accounting & Finance, Global

---

**1. What are your expectations for operating income growth in fiscal 2021, fiscal 2022 and beyond?**

To achieve a 48.0 billion yen year-on-year increase in sales in fiscal 2021, we will increase marketing and digital-related investment by 15.0 billion yen each for a total increase of 30.0 billion yen in strategic investments. We will continue making these investments for about two years, but results could begin to appear as early as the second half of the current fiscal year. For future growth in operating income, we believe it will be important to first establish core sales over the next two years.

**What exactly does “digital-related investment” mean?**

To build our Precision Healthcare digital platform, we will be collecting data, improving its precision, analyzing it, and connecting data. To do all that, we will need software and the skills of people, including people from outside the Kao Group. We call these expenses digital-related investment. Our returns from each business will vary significantly depending on the results of this investment, so we consider it very important.

**2. The operating margin of the Cosmetics Business was 1.1% in fiscal 2020. What is your target for the future and what are your strategies to achieve it?**

To achieve the Kao Group Mid-term Plan 2025 “K25” (hereafter, “K25”), the strategy for the Cosmetics Business is to proceed with the following four-point plan, which is already under way. (1) is an initiative to further accelerate the growth strategy started in 2018, and (2), (3) and (4) are initiatives to resolve the Kao Group issues that the COVID-19 pandemic has brought to the fore.

(1) Accelerate the development of strong brands

- Enhance the brands specified in the growth strategy announced in 2018 into purpose-driven brands that are even more useful to consumers
- Expedite brand strategies by restructuring in January 2021 into three groups (global prestige brands, global masstige self-selection brands and regional brands mainly for Japan)
- Fully utilize RNA monitoring technology for skin care offerings that are unique to Kao
- Provide useful technologies and products for consumers that demonstrate an extremely high level of performance close to plastic surgery, such as the new makeup technology announced in November 2020 that smoothens nasolabial folds inconspicuously through a simple application

(2) Transition to a robust business structure by accelerating structural reforms

- Merge the two beauty counseling companies on April 1, 2021. Ramp up activities to communicate the images and values of brands and to maintain and increase the number of loyal users, and work to generate synergies by improving beauty advisor productivity and deploying staff appropriately.
- Transform the business model for makeup products (consolidate brands, launch new colors in limited quantities)

(3) Expand the e-commerce business by promoting DX/transformation into a customer retention model

- Accelerate D2C initiatives with a department to promote DX (digital transformation) that was newly established on January 1, 2021 in the organization that supervises the entire Consumer Products Business
- Work to evolve and improve UX (user experience) using digital technology, such as the "MAKEUP LAB." for the *KATE* makeup brand, announced on February 1, 2021 in Japan

(4) Maximize demand from Chinese consumers

- Continue to ramp up initiatives with e-commerce platforms and begin social commerce in fiscal 2021
- Start transactions with a Hainan duty-free store in the first half of fiscal 2021
- Make a full-scale entry into the C2C (consumer-to-consumer) market and work on new business models

**What is your targeted operating margin for the Cosmetics Business?**

The operating margin in fiscal 2019 was 14%. Inbound sales were high then, so we were able to save marketing expenses. Excluding these factors, operating margin was about 12-13%. We are now formulating a business plan to return the margin to the level of fiscal 2019 by fiscal 2025 and then achieve our initial target of 15%.

**3. Although the Kao Group has excellent technologies, I feel that it is slow to roll them out in growing markets outside Japan. How will that change under K25? Does your ambitious plan to increase investment by 30.0 billion yen-on-year in fiscal 2021 include expenses for accelerating business outside Japan? Please explain, area by area.**

Going forward, we would like to use our Precision Healthcare digital platform to compete head to head with retailers and e-commerce platforms. The way we compete will change because we will be conducting data-driven operations globally, rather than our traditional approach of launching new products in Japan first. It is difficult to explain this new approach area by area. For example, the genetic-level and virus-level data that Precision Healthcare compiles from information in the Hygiene and Living Care Business on bacteria and viruses that people come in contact with in their daily lives will be easier to utilize in other businesses and areas. In the digital age, it will be an advantage not to be a specialized manufacturer of household and personal care products or cosmetics. The key for digitalization is how to connect and control detailed, usable data. In other words, we believe that the way the Kao Group has deepened the way it has traditionally acquired and connected data on the broad range of businesses it conducts in household and personal care products, cosmetics and chemicals will be a more powerful advantage going forward in the digital age.

**You said that the results of the 30.0 billion yen year-on-year increase in investment could start to appear as early as the second half of fiscal 2021. If that is the case, will global sales also accelerate?**

It is likely to take a little longer for the Precision Healthcare digital platform to make a significant contribution to business performance. However, because we are going to transform our business model with digitalization, I think changes will appear a little earlier. For example, in the process of creating this platform, we have already begun communicating via digital technology and building relationships with e-commerce platforms for some mass-market beauty care products in the Americas, so results from these initiatives may start to appear as early as the second half of fiscal 2021.

**4. You said that you will continue to make ambitious additional investments of 30.0 billion yen for two years. Do you expect investment to peak in fiscal 2021 and then taper off? When do you expect to realize a return on your investment?**

Our current plan is for the highest level of investment to be in fiscal 2021. We hope to dramatically increase sales in the next year or two while using expenses efficiently to make highly competitive products. The Kao Group has confidence in its *Yoki-Monozukuri*,\* total cost reduction (TCR) activities, and creation of high added value. We intend to substantially increase the number of users and gain momentum over the next two years. In addition, in K25 we have set a net sales target of 1.8 trillion yen, but since it previously took 10 years to increase sales by about 300 billion yen, an increase of 300 billion yen in five years is a challenging. We will confront the next five years head on, while boldly considering joint ventures and M&A.

*\* The Kao Group defines Yoki-Monozukuri as a strong commitment by all members to provide products and brands of excellent value for consumer satisfaction. In Japanese, Yoki literally means "good/excellent," and Monozukuri means "development/manufacturing of products."*

**5. How will you secure human resources for digital development?**

Kao used to be in the information technology business, so we have many employees from that time who have high-level IT skills. Those individuals will grow the business through linkages with external companies that have outstanding, cutting-edge technologies. In other words, we are not a group of amateurs trying to somehow get ahead by enlisting the help of companies with digital technologies. Rather, we already have in-house IT professionals familiar with the Kao Group's manufacturing and businesses who will form linkages with external companies possessing cutting-edge technologies to build a new digital platform.

**It is hard to picture your Precision Healthcare digital platform. How will it increase sales? Collecting data is easy in the Cosmetics Business, but isn't it difficult to do so for household and personal care products?**

I realize that Precision Healthcare is difficult to grasp. However, creating a platform that is easy for everyone to understand means that it winds up being something that anyone could think of. Consequently, Precision Healthcare is often considered hard to understand.

To make it easier to picture, I will give you the following example. Suppose that in the Hygiene and Living Care Business, the Kao Group has technology to identify what kinds of bacteria and viruses are present and to specify their coordinates at the genetic level. Suppose those technologies enable monitoring of the transmission routes of those bacteria and viruses when they enter the human body, and how they can be blocked. Also, picture something like a PCR test that can be done at home.

Infectious and intractable diseases can be dealt with in various ways if intervention is early, but if that is not possible, patients must rely on medical treatment. Therefore, if the Kao Group can establish a platform that serves as a network of information on how to prevent

such diseases, it will be able to provide data required by hospitals and pharmaceutical companies, as well as by hair salons and restaurants that many people visit. We believe the creation of Precision Healthcare will enable us to conduct research to gain an accurate understanding of the things that cause harm, the essential causes of harm and comprehensive knowledge on all matters surrounding them.

This is a new business model. With it, there is no need for the marketing we have traditionally conducted, and this model could also be utilized in existing businesses. We have conceived this digital platform with the intention of openly collaborating with various parties to deliver the best to consumers on a digital basis. We intend to change the way we compete globally based on variable and predictive data rather than data on the current situation.

**6. Life Care Business sales are expected to be 58.0 billion yen in fiscal 2021. Will the nearly 150.0 billion yen in sales from Another Kao you are planning for fiscal 2025 all come from the Life Care Business? Or does Another Kao encompass contributions from other segments? What kind of profit margins do you envision between now and fiscal 2025?**

The Hygiene and Living Care Business accounts for the largest share of sales by far in the fiscal 2021 forecast, and we are aiming for substantial, balanced growth in this business through effectively focused investments. In the Health and Beauty Care business, we expect a downturn in comparison with fiscal 2020's substantial increase in demand for hygiene-related products, but we will continue working to achieve higher sales from value offerings that are useful to consumers. The Cosmetics Business will be our next growth driver.

The Life Care Business will be the core business of Another Kao. In order to grow it into a business with sales exceeding 100 billion yen, we intend to give it a boost by introducing a new structure for business in the medical field, rather than just growing organically. In addition to these four businesses, we intend to increase the scale of sales in the Chemical Business from 300 billion yen to 500 billion yen going forward.

**Do you envision sales in the medical field to start increasing after four or five years? I think this is a field that companies from other industries can enter, so how do you plan to build a sales channel?**

We are not thinking about creating a medical sales channel. We envision Another Kao as the expansion of our existing business domain that we will reinforce by forming a new structure, while we view Reborn Kao as the creation of a stronger platform through further expansion.

**7. You said you want to make effectively focused investments in the Hygiene and Living Care Business. How will you do that?**

Currently, the Kao Group has just under 50 mass-market brands of household and personal care products. We have divided them into three segments. We have designated 16 category-leading brands and six life design brands that we will strengthen across respective business divisions. The remainder are all edgy niche segment brands. Until now, we have been investing in omnidirectional marketing, but we will add balance by selecting priority brands for cultivation and varying investment while using digital technologies.

**What are the assumptions behind your forecast of 3.8% growth in Cosmetics Business sales in Japan for fiscal 2021?**

Although inbound demand recovery will be limited and wearing a mask will remain common practice, strict restrictions on going outside are not expected, so the cosmetics market in

---

Japan is expected to grow by about 4% compared with the previous fiscal year. Looking at fiscal 2021 sales by quarter, the first quarter is a challenging because there was no impact from COVID-19 in January and February 2020. Growth is therefore expected to be around negative 10% compared with the same period a year earlier. Growth between 10% and 20% is expected in the second, third, and fourth quarters. However, first-quarter growth has been about 10 percentage points lower than originally expected due to the recent declaration of a state of emergency.

The Kao Group will continue to conduct various structural reforms, including utilizing digital technology and ramping up e-commerce, as it increases sales centered on the eleven global strategy brands (G11) with the aim of achieving a growth rate roughly on par with the market.

**Will sales at a Hainan duty-free store start with *freeplus*?**

We will start with the prestige brands *SENSAI* and *est*. The store will also sell products with Fine Fiber technology. Local sales of the mass-market brands *Curél* and *freeplus* are very strong in China, so we are currently in no hurry to sell them at the Hainan duty-free store.

**8. Do you have any plans to sell *KANEBO* at the Hainan duty-free store? How many counters are open and what is your target for sales in the first year?**

For a product to be sold at Hainan duty-free stores, its ingredients must be approved by the Chinese authorities. *SENSAI* and *est* will be cleared during fiscal 2021, but *KANEBO* and *SUQQU* are currently undergoing the approval process. As for our store plan, one counter is scheduled to open in the second quarter of fiscal 2021. New duty-free stores are opening one after another, but we want to proceed strategically instead of just opening counters randomly. The scale of sales is not being disclosed, but we hope to get on track as soon as possible.

**What caused the improvement in the operating margin for the Cosmetics Business in the fourth quarter of fiscal 2020? Can we expect that momentum to continue in the first quarter of fiscal 2021 ?**

In the fourth quarter of fiscal 2020, sales in China were strong, mainly on Singles' Day. In Japan, performance was strong for products such as *Milano Collection* base makeup and body care, which have large-scale sales, and market conditions also improved slightly, so profits improved. However, because the Cosmetics Business has high fixed costs, it does not turn a profit until sales exceed a certain level. Sales in the first quarter of the year are always lower, and a state of emergency has been declared in Japan in 2021, so the operating margin in the first quarter of fiscal 2021 is expected to be very weak.

**9. You have already explained your income and cash flow statements, but I would like an additional explanation of the effects of your business investments in connection with the balance sheet in your communications with investors. You have changed your business segments as of fiscal 2021, but what are the key points for deciding whether to continue a business? How do you use EVA internally? How do you view the returns on your investments?**

We will not discontinue any businesses that only the Kao Group can conduct successfully. Nor will we terminate any business if we can help to resolve issues by engaging in it. Our approach to our businesses is to make a profit as we accomplish these goals and, if possible, use those businesses as a growth engine. On the other hand, if we judge that we cannot

---

improve a business or its category even if we make investments, we decide to terminate it. We withdrew from the information technology business in 1999, even though we had grown it to the number-one position globally in sales, because we realized that we were lagging behind the pace of change, with offerings that were likely to get more and more out of touch with the trends of the times. Going forward, we intend to maintain an ESG perspective in deciding whether to continue or withdraw from businesses. In addition, we have always used EVA when assessing the capital efficiency of the entire Kao Group, as well as in deciding on capital investment and environmental investment. We set aside a little time after investments to review the results, especially for unprofitable businesses.

**So, the Kao Group places a high priority on ROE targets and overall profitability in management?**

Exactly. Especially given the various changes recently, we feel that it has become difficult to recover investments within one year. Therefore, key factors will be the extent to which we can deal with matters from an ESG perspective and our predictions of the future. We want to make anticipatory investments aimed at being the central player in businesses by the time they have become large. Time spans will be a little longer, but the Kao Group's stance is to grow by increasing EVA through recovery of its investments.

**10. You said that the Kao Group will enter new business categories in the future. What are the advantages and distinctive features of the Kao Group's research and development from a global perspective? Please give me some examples.**

The Kao Group conducts fundamental research on essential properties. Over the past two or three years, our researchers have had discussions with many places that conduct pathology research and with pharmaceutical manufacturers, and they have all asked them why a household and personal care products company like us would become so involved in the areas they research. To give a specific example, the VHH antibodies we announced in May 2020 neutralize viruses at an extremely high level, and we have technology for neutralization using antibodies that can be stored without special temperature controls.

In the manufacturing of medicines, even though a company might conduct research on viruses or bacteria, for example, its research is pharmacological—that is, it involves investigating how people contract a disease and what substances are effective in curing it. On the other hand, the Kao Group's research covers how a virus changes, where it is most likely to be found, how to protect those places, how to eliminate the virus when a person comes in contact with it, and how to eliminate it as quickly as possible. We steadfastly conduct such research and publish many academic papers, so we even receive requests for cooperation from the government sometimes. I think this gives you an idea of the level of our fundamental research.

By 2050, the number of deaths from antibiotic-resistant diseases are expected to exceed deaths from cancer. We believe our work in this area is a distinctive feature of our research. Because the viruses and other targets of our research will change, we want to be ready with technologies that provide the most effective methods for tackling those viruses.

**11. Isn't your net sales target of 1,430.0 billion yen for fiscal 2021 a very challenging considering your slow sales growth recently? If there are risks, what are they?**

We believe that Reborn Kao will account for most of the 1,430.0 billion yen. We intend to push toward this target by restructuring the Cosmetics Business and consolidating the business portfolio and making balanced investments. The outlook for COVID-19 is uncertain, but this figure shows the strength of our determination even under these circumstances.

---

The biggest risk is COVID-19. Conditions will be severe if hair salons and stores in the U.S. and Europe temporarily close again. There is a limit to what e-commerce and direct sales can cover. Another key issue will be the level of success of the strategies we are planning. This year, we are also planning new product launches in which we put substantial management resources into new product introductions. In fiscal 2021, we will boldly deploy marketing expenses for these launches, including for products we were unable to launch in fiscal 2020 due to the COVID-19 pandemic. There are risks, but we intend to overcome them.

**Note**

The content presented in these materials is the opinion of the Company. The content is a summary of questions and answers at an analyst meeting. The Company makes no guarantee or promise regarding the accuracy or completeness of this information, which is subject to change without notice.

Forward-looking statements such as earnings forecasts and other projections are based on information available at the time of disclosure and assumptions that management believes to be reasonable, and do not constitute guarantees of future performance. Actual results may differ materially from expectations due to various factors.