

Date and time:

Wednesday, August 3, 2022, 17:00-18:50 (JST)

Respondents:

Yoshihiro Hasebe, Representative Director, President and Chief Executive Officer

Tomoharu Matsuda, Representative Director, Senior Managing Executive Officer

Masakazu Negoro, Managing Executive Officer

Mitsuhiro Watanabe, Vice President, Investor Relations

---

- 1. To achieve the operating income forecast for FY2022, operating income for the second half must increase by about 25% or a little less than 20 billion yen year-on-year. I believe management initiatives will be important for the achievement. How will you increase operating income by 16 billion yen through cost structure reforms, in particular?**

The operating income forecast of 91.3 billion yen for the second half is an increase in operating income of 18.3 billion yen year-on-year. When 22.0 billion yen due to hikes in raw material prices is added to the figure, operating income must increase by approximately 40.0 billion yen. Meanwhile, when approximately 7.0 billion yen of the cost of structural reforms including the impairment loss on the facilities of the baby diapers posted in FY2021 is taken into account, operating income must increase by 33.0 billion yen as a result. We expect to offset about 40% of the amount by increasing sales and about 60% of the amount through Total Cost Reduction (TCR) activities and cost structure reforms. The cost structure reforms are related to fixed costs, and consist of the following three areas: analog cost reductions through digitalization, thorough shift to in-house operations from outsourcing, and restructuring of unprofitable operations.

- 2. You explained that half the impact of hikes in raw material prices will be absorbed by conducting strategic price increases in the Household and Personal Care (H&PC) business in Japan. However, since the price increase is proceeding smoothly, I expect that more impact will be absorbed by the price increases. Are there any issues such as the industry environment and other factors?**

The strategic price increases are increasingly more effective month by month, with a total of 2 billion yen in the first half. As shown on slide 25 of the presentation material (Consolidated Financial Results for the Six Months Ended June 30, 2022 and FY2022 Forecast), among 10 major retailers, those in which the average shipping price and market share increased through strengthening initiatives constitute 65% of sales, other retailers in which the average shipping price decreased and market share increased constitute 20% of sales. The other retailers in which the market share decreased due to price increases constitute 15% of sales. However, the decrease in the market share was smaller than we anticipated. We will carefully work on this strategy to add up the effects of price increases while ascertaining which of the

procedures, specifically, streamlining of sales promotion expenses, simple price increases, adding higher value, and reducing product contents will suit the situation of each retailer. Going forward, we will implement price increases in cosmetics as well.

**Amid ongoing trade-down in the United States, how do you consider the risk of increasing market share of retailers which offer discounts?**

Currently, e-commerce is growing. The Kao Group has been working on a shift to digital technology, which will act as a tailwind. It would be possible for us to shift to retailers that are beneficial to consumers rather than merely reducing selling prices.

**3. Under the structural reform policy for the baby diaper business, when will new ESG-oriented products be launched and what type of marketing tactics will be taken? And what time frame are you thinking about?**

Sales of *Merries* baby diapers made in China is gradually growing due to the longer time that the baby can feel comfortable because it can be used for long hours after the baby urinating. There are few companies which have this technology even globally. In addition, *Merries* made in China is almost complete as a thin and compact diaper, and so changing its design will not require a large capital expenditure. It reduces raw materials to be disposed of and, moreover, its wastes can be turned into chemical products that are useful for society by utilizing the technology of the Chemical Business.

While improving communication, we plan to launch the next generation of new baby diapers by 2025.

**Is there any possibility of lowering the prices of baby diapers that have been increased once?**

Since the prices of baby diapers sold in Japan are lower than the global level, we hope we will be able to establish the current price level as the standard. We would like to increase prices, return the profits to shareholders and employees, and thereby significantly change the market in Japan.

**4. Is my understanding correct that since the impact of hikes in raw material prices is within the estimated range, the primary factors for the recent downward revision of the forecast for FY2022 are the increase in logistics expenses, lockdowns in China, changes in the sales plans, and so on? For which businesses have the plans been changed after the announcement of the financial results for the first quarter?**

Although there were some remarks at the time of the announcement of the financial results for

---

the first quarter that the forecast should be revised downward, we were unable to adequately predict the impact of the Russia-Ukraine crisis and lockdowns in China. Also, we were unable to anticipate the impact of Japan's seventh wave of COVID-19. When it has almost been confirmed that the impact of hikes in raw material prices will continue in June, which will not be absorbed with only the measures that have been developed, we revised the forecast downward. Note that there is already a good prospect for half of the 16 billion yen in cost structure reforms.

From the overall situation regarding our H&PC market share in Japan as shown on slide 27 of the presentation material, our Category-Leading brands in which we make marketing investments and work on the shift to digitalization are winning the competition. The skin care business also has the No. 1 share in sight. In addition, due to the low hurdle year-on-year comparison for the second half, a heat wave, and shift to the normalization of daily life, which are supplying a nice tailwind, we expect the business environment will turn around and consider the second half to be the time to go on the offensive.

**Is Cosmetics Business the primary factor for the minus 6 billion yen for changes in sales plans, etc. as shown on slide 18 of the presentation material?**

The recovery of the cosmetics market in Japan is half a year to one year behind expectations.

5. **The 7 billion yen as the effect of strategic price increases in the second half looks almost equal to the increase in sales in the Hygiene and Living Care Business and the Health and Beauty Care Business. Since it is said that your market share of UV care and other products is growing, I think the sales forecast is modest. What kind of risks in H&PC market in Japan are you anticipating?**

The sales forecast for the second half is more aggressive than that for the first half. Although Reborn Kao focuses on the fabric care, home care, and cosmetics businesses, we will also strengthen the categories whose market share is decreasing. We will enhance the personal health business in the Stable Earnings Area, skin care business in the Growth Driver Area, and the R8 brands in the cosmetics business. In the hair care business in the Business Transformation Area, products focused on digital technology will increase the market share, and we will also reinforce the high price range in the sanitary business. While enhancing the categories that are growing, we will implement measures to boost categories with declining market share at the same time.

**I suppose your sales forecast for the Cosmetics Business for the second half is +11%, which I think looks aggressive. On the other hand, your sales growth forecast for the H&PC business remains equivalent to the portion of price increases, which I think looks moderate. What are their primary factors?**

For the H&PC business, we are trying to grow the sales volume. On the other hand, due to inventory control by demand forecasting, some H&PC products may be out of stock. For the Cosmetics Business, we have won approximately 70 best cosmetics awards and have come to be top class in the cosmetics industry in Japan. New products are also scheduled to be launched. The point would be high value-added offerings to address the heat wave or adapt to the increased opportunities to remove face masks.

**6. What are your price assumptions for natural fats and oils and petrochemical raw materials in the second half?**

The assumed price for crude oil is 110 US dollars per barrel, while the assumed price for lauric oils and fats is 1,100 to 1,300 US dollars per ton. At the time of the announcement of the financial results for the first quarter, we assumed the price of lauric oils and fats to be 2,300 US dollars per ton. The reason why the impact of hikes in raw material prices will not reduce even if the market price will decrease in the second half is because there will be a significant effect of the yen's weakening.

**7. Can you explain the probability of achieving the downward revised operating income forecast for FY2022 of 145.0 billion yen and risks of not achieving it?**

On the assumption of a gradual market recovery from the impact of the COVID-19 pandemic, we will implement measures, including new and improved product launches. The forecast of 145.0 billion yen is a level that is achievable by bearing various positive and negative factors in mind.

We have prepared a wide range of measures to achieve the forecast operating income. Although there are variable factors, including raw material market conditions and market environment for the business, we aim to achieve the figure by implementing such various measures as planned.

**8. Over the last several years, you have repeatedly been revising downward in the first half while expressing your belief and then failing to achieve the figure at the end of year. What is different this fiscal year compared to the previous years? In addition, will you explain your growth policy for the next and subsequent fiscal years in relation to the Kao Group Mid-term Plan 2025 "K25"?**

We regret that we have been unable to achieve the announced forecast for four consecutive years. In this fiscal year, the Kao Group has been doing everything within its power to achieve the announced forecast amid the impact of the unprecedented level of hikes in raw material prices. Although we cannot guarantee that we will achieve the forecast no matter what unexpected event may occur, we will do our best to achieve the forecast with the concerted efforts of employees so as not to lose trust. I would appreciate it if you could read through

the Integrated Report issued in June, which describes how we will become a company with a solid business structure and profitable development through Reborn Kao and Another Kao.

- 9. Although the sales growth rate of the Cosmetics Business in Japan for the first half was about 2%, which was at the market level, sales growth for the second half is forecast to be +11%. Can you explain the reason behind the sales growth?**

Although we plan the same level of sales in amount in Japan for the third quarter as that of the second quarter, the growth will be a double-digit rate. We believe we have been acquiring digital communication capabilities thanks to investment in digital transformation (DX). While maintaining the strongly growing G11 brands, we will strengthen the R8 brands, with which we have been struggling a little, by utilizing digital technology.

- 10. The categories in the priority area of H&PC business in Japan have been improving. Is this due to your own efforts or to external factors including changes in the competitive environment?**

There were no significant changes with regard to cosmetics and H&PC markets in Japan for the first half of FY2022. As immediate changes, home care-related markets will weaken due to people who had been spending time at home starting to go outside. On the other hand, some categories will boom as a result of increased opportunities for people to go outside. Such categories include cosmetics, hair care products, wet wipes and other products. In addition, categories in which Kao can demonstrate its superiority amid a heat wave include UV care products, which can be differentiated with the comfort of applying products. Some categories will increase sales as a result of the expansion of the market, while other categories will increase sales as the market share increases.

**Is my understanding correct that competition from peer companies remains unchanged with regard to laundry detergents and fabric softeners, but factors such as climate and recovery from the COVID-19 pandemic have a positive effect on sales?**

That's correct.

**Does the revised sales forecast for H&PC business in Japan take into account the underperformed results in the first half, revision of figures for the second half, and the impact of Japan's seventh wave of COVID-19?**

That's correct.

- 11. From Kao's recent TV commercial in Japan, I can see a change of marketing from the conventional promotion of functionality to a consumer-oriented one. Can you explain**
-

**your marketing policy?**

We have been enhancing marketing in terms of the following three points:

- (1) Life Value Solution Marketing: In addition to offering functional value based on evidence, which has always been one of the strengths of Kao, life value is offered after carefully considering emotional value as well as social value.
- (2) Decisive brand and business management
- (3) Stimulation of DX

**The regional portfolio of each business is unbalanced. Will you explain your policy of correcting such a situation?**

As the basic approach, we have been developing a wide range of categories for which the Kao Group can apply its superior and characteristic approaches in the respective regions. We will carefully develop a model for each area so that it can earn profits as soon as we enter the market. We are not thinking about forcibly correcting such unbalance.

Although profit margins are declining in Japan, we have thoroughly analyzed ways of competing without being affected by the market or market conditions. The operating margin of products for hair salons, which was previously 3 to 5%, has improved to close to 10% by shifting the products to a premium range using digital technology. We will apply the same approach to competing for sanitary napkins as that used for baby diapers.

**Can you explain the progress of Precision Life Care?**

We plan to collaborate with companies in the same industry, competitors, and others in diverse categories, implement in FY2023 and significantly contribute to the profits from FY2024. We believe you will be able to see this plan realized at an early stage in FY2023.

**Note**

The content presented in this document is the opinion of the Company. The content is a summary of questions and answers in the earnings conference. 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.