Date and time:
Wednesday, February 7, 2024, 17:00-18:30 (JST)

Respondents:
Yoshihiro Hasebe, Representative Director, President and Chief Executive Officer
Masakazu Negoro, Representative Director, Senior Managing Executive Officer
Toru Nishiguchi, Director, Senior Managing Executive Officer

1. **Core operating income for FY2023 was 114.7 billion yen, lower than the announced 120.0 billion yen, with SG&A expenses increasing during the fourth quarter of FY2023 compared to the first nine months. Has the increase in marketing expenses affected the result?**

   It is true that we had larger marketing expenses during the fourth quarter of FY2023. However, sales of cosmetics in China decreased more than expected, and a drop in sales of cosmetics in Japan also affected the result. Some other expenses were also recorded in the fourth quarter. Although we were unable to achieve the 120.0-billion-yen target, we believe the result is within our expectations, excluding the impact of local reaction to Japan's discharge into the ocean of water treated using the Advanced Liquid Processing System (ALPS) from the Fukushima Daiichi Nuclear Power Station. We could not have anticipated that the impact in association with ALPS treated water would be so significant, but we allocated marketing expenses for cosmetics in Japan to compensate for it. This has contributed to this year's good start.

   Does the increase in SG&A expenses of 17.0 billion yen for FY2024 include the profit improvement effect of 18.0 billion yen due to structural reforms? Will you explain the breakdown of the 17.0 billion yen?

   We expect a profit improvement effect of 18.0 billion yen in FY2024 from structural reforms. The profit improvement is expected to come 50% from (1) conducting a drastic strategic review and reorganization of inefficient businesses and (2) promoting structural reform of human capital; and 50% from (3) reforming earning power. Items (1) and (2) are included in the change in SG&A expenses (-17.0 billion yen), and item (3) is included in price increases (+10.0 billion yen) and volume, etc. (+15.0 billion yen) in the Consumer Products Business as it contributes to improved gross profit. In addition, the profit improvement effect from (2) in FY2024 will only show up for half a year.

2. **What investments were made in the Cosmetics Business in Japan during the fourth quarter of FY2023? And what are your assumptions for the Cosmetics Business in Japan and China in FY2024?**

   In the fourth quarter of FY2023, we made marketing investments in *KATE* and *KANEBO*, which are selling well, as well as investments in the improved *Sofina iP*.
   Regarding the forecast for FY2024, it is based on the assumption that the negative impact in the market in China in association with ALPS treated water will remain during the first half of the year, but will

gradually recover starting in the second half of the year. The market in Japan is steady. We will focus on the five brands taken up in the Global Sharp Top Strategy: *KATE*, *KANEBO*, *Curél*, *SENSAI*, and *Molton Brown*.

3. **Why does the effect of the strategic price increases in consumer products for FY2024 remain at 10.0 billion yen, slowing down from FY2023? Also, can you share the categories that are subject to price increases?**

   Kao has been ahead of the industry in promoting strategic price increases. As a basic premise, we will continue this policy. As for the 10.0-billion-yen price increase effect for consumer products, we have set this as the minimum number necessary to continue the strategic price increases. As a breakdown, fabric care and sanitary products are the most significantly affected by the price increases. In beauty care products, we will also continue our activities to raise prices in general by launching new products.

   Your plan is based on the idea that price increases will have a negative impact on the volume, but you will still continue the strategic price increases or maintain the increased price. Is my understanding correct?

   Kao handles a wide range of product categories, and it is difficult to continue increasing prices based solely on corporate circumstances. We will set prices in dialogue with consumers while taking into account our brand strength and level of necessity.

4. **What were the sales of cosmetics in China in the fourth quarter (Oct. to Dec.) of FY2023? How do you see the sales of cosmetics in China in FY2024 and how do you factor this into your forecast?**

   Sales of cosmetics during the fourth quarter of FY2023 were tougher than expected. This situation in the fourth quarter is expected to continue during the first half of FY2024 and recover to some extent from the second half onward. The impact in association with ALPS treated water has changed consumers' awareness and the way they judge a good product. From the latter part of the first half of FY2024 to the second half of the year, Kao will launch new products, including locally produced products developed mainly by local team members in China, with a greater number of items than previously planned and at an accelerated pace.

   Are you assuming that a similar decrease in sales during the fourth quarter of FY2023 will continue through to the first half of FY2024?

   In the first quarter of FY2023, there were curbs on shipments of *freeplus* ahead of its rebranding. Based on this fact, we do not expect there to be a decrease similar to the fourth quarter.

What is the level of inventory adjustment in China, including Hainan Island?

Inventory adjustments are expected to be completed during the first half of FY2024. Regarding Hainan Island, inventory adjustments there will not have a significant impact on the entire company as the scale of Kao's business there is not large.

5. **How will each business area contribute toward achieving the ROIC target of 11% under the Kao Group Mid-term Plan 2027 (K27) in the future? Also, how do you use ROIC in making decisions regarding investment in and divestment from businesses?**

Business transformation: We will raise the target to 7%. We are making steady progress due to the transfer of businesses and other efforts.
Stable earnings: We are aiming for over 20%. In the fourth quarter of FY2023, the core operating margin for fabric and home care products increased up to 19.7%. Since we have made no significant capital investment, we expect to approach the target by the end of FY2024.
Growth driver: This is the business area that needs to grow the most. Since we are increasing invested capital such as for goodwill in cosmetics, the acquisition of Bondi Sands, and capital investment in the Chemical Business, the key point is how to increase profit.

We will regularly review the business portfolio and make improvements in businesses with low ROIC. We have also set guidelines and believe that the 11% target can be achieved by strengthening our business portfolio management.

How do you view the macro environment of Kao's businesses from a long-term perspective? Is the current resource allocation optimal with respect to that?

Kao has been too focused on Japan until now. Going forward, it is important to change the way we do business outside Japan and develop more essential, high-value-added products. The basic principle is to determine our operation areas after considering where Kao's technologies will be most beneficial for consumers. Brazil and Europe are the leading regions for Kao in relation to this principle. Despite being areas that have been considered very difficult, we are confident that if we develop high-value-added products like *Bioré*, consumers will accept them. There are a wide range of areas where Kao's business can contribute, including the Americas and Europe. Under the Global Sharp Top Strategy, we consider areas for expansion with this in mind. It is a big change from the past approach, but we have established a system that allows us to make decisions in an agile manner, and so we will speed up the process.

6. **Will you explain the decrease in sales within the Cosmetics Business in Japan in the fourth quarter of FY2023, breaking it down into factors such as the impact in association with ALPS**

treated water and brand portfolio review?

Sales have dropped significantly due to returns as a result of cosmetics brand consolidation and to a decrease in travel retail sales in Korea and cross-border e-commerce sales owing to the impact in association with ALPS treated water. Excluding these impacts, sales decreased about 4% on a shipment basis, partly due to the significant success of *KATE*'s *Lip Monster* in 2022.

7. **With the profit improvement effect by structural reforms of 18.0 billion yen to be expected in FY2024, is the operating income forecast of 130.0 billion yen for FY2024 not conservative?**

The operating income forecast of 130.0 billion yen is a must-achieve target. While the contribution of structural reforms is significant, when we take on new initiatives such as launching new products that we count on for success and major business reforms, we will make solid investments including marketing investments to achieve growth.

Will you explain the operating income forecast of 130.0 billion yen, including how you view raw material prices and the Chemical Business?

We expect raw material prices to increase by 1.0 billion yen year-on-year, but there are also risks such as the situation in the Middle East. Even if that amount were to increase further, we would offset it by increasing the prices of consumer products.
As for marginal income in the Chemical Business, the market for tertiary amines and synthetic aroma chemicals has a very high barrier to entry, and Kao is the number one globally. They are highly profitable products, and we are going to expand sales mainly in Europe by making capital investment. In addition, we plan to grow sales of performance chemical products, and so an increase in marginal profit of 11.0 billion yen is not that difficult to achieve.
In the Consumer Products Business, considering the additional profit from Bondi Sands and the creation of synergy with existing businesses, the 15.0-billion-yen increase in relation to volume increase is a hurdle that must be overcome.
Furthermore, the profit improvement effects of structural reforms will also be showing up. The effects of fixed cost reduction are also included in the change in SG&A expenses, and there is an offset here which results in a 17.0-billion-yen increase in SG&A expenses. An operating income of 130.0 billion yen is not an easy figure, but we will work to further increase it.