Kao Corporation: Announcement of Consolidated Business Results for the Nine Months Ended December 31, 2008

Transcript of Teleconference Presentation

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I am Shinichi Mita, Vice President and Executive Officer in charge of Global Accounting and Finance. I will explain the "Summary of Consolidated Business Results for the Nine Months Ended December 31, 2008 and Forecast for the Year Ending March 31, 2009."

1. Summary of Consolidated Business Results for the Nine Months Ended December 31, 2008

Compared with the same period a year earlier, consolidated results were as follows:

Net Sales	1,004.1 billion yen	+0.4%	+3.9 billion yen
Operating Income	91.4 billion yen	-4.9%	-4.7 billion yen
Ordinary Income	90.7 billion yen	-4.9%	-4.7 billion yen
Net Income	54.2 billion yen	+1.0%	+0.5 billion yen

2. Operating Environment

- Regarding the Japanese market environment in the Consumer Products Business, consumer sentiment cooled due to the uncertainty about the economic outlook and the scale of the cosmetics market was unchanged compared with the period from October to December a year earlier. Please see the charts on pages 3 and 4 of “Supplemental Information on Revision of FY2008 Consolidated Forecast.” As shown in the charts, the scale of the household and personal care products market also remained near the level of the period from October to December a year earlier, with a decrease of one percent. Moreover, average consumer purchase prices in major categories of the household and personal care products market were near the level of the same period a year earlier (Source: SRI POS data).

In North America and Europe, markets cooled notably due to the economic slowdown.

- Regarding the market environment in the Chemical Products Business, sales volume began to drop sharply in Japan from fall 2008 due to the impact of a decrease in demand from customer industries.

3. Overview of Consolidated Business Results

Now, I would like to give an overview of the Kao Group’s consolidated business results.

- Consolidated net sales increased 0.4%, or 3.9 billion yen, driven by the Consumer Products Business in Asia and Oceania and the Chemical Business. Excluding the negative effect of currency translation totaling 19.8 billion yen, net sales would have increased 2.4%.

  Sales in the Consumer Products Business decreased 1.0% compared with the same period a year earlier. Excluding the effect of currency translation, sales would have increased 0.6%. In Japan, sales increased 0.2% compared with the same period a year earlier to 669.8 billion yen and the Kao Group expanded its share of the household and personal care products market and worked to invigorate the cosmetics market by energetically launching new products. Sales in Asia and Oceania increased 10.5% on a local currency basis. However, sales in North America and Europe decreased as business operations in the United States faced difficult conditions with the impact of a cooling market and intensifying competition due to the economic slowdown.

Although the Kao Group undertook initiatives such as launching high-value-added products, strengthening sales activities and raising marketing cost efficiency, operating income decreased 6.5 billion yen to 73.5 billion yen due to the impact of the rising cost of raw materials.

- The Chemical Business has been focusing on adjusting selling prices in response to substantial increases in raw material prices, and as a result sales increased 8.5% compared with the same period a year earlier. However, sales volume began to decrease due to the global economic slowdown in the third quarter.

Operating income increased 2.1 billion yen to 17.8 billion yen.

- As of October 2008, the Kao Group assumed the impact of an increase of 36.0 billion yen in raw material prices for the year ending March 2009. During the first nine months of the fiscal year, the cost of raw materials had increased 32.0 billion yen.
- In order to absorb these increased costs, the Consumer Products Business worked to improve profitability by raising the level of customer satisfaction with high-value-added product launches while adjusting product content per package. In addition, the Chemical Business focused on adjusting sales prices, but falling raw material prices in the market in the third quarter and

onward caused downward pressure on sales prices to intensify in Japan. The Kao Group continued its Total Cost Reduction (TCR) activities, and achieved approximately 6.0 billion yen in cost reductions during the nine-month period.

- Selling, general and administrative expenses decreased 13.0 billion yen, which included a decrease of about 8.0 billion yen due to the impact of currency translation.
- As a result of the above, operating income decreased 4.7 billion yen compared with the same period a year earlier to 91.4 billion yen.
- Equity in earnings of nonconsolidated subsidiaries and affiliates included in non-operating income increased by approximately 0.8 billion yen. However, the foreign currency exchange gain of the same period a year earlier changed to a loss. As a result, ordinary income decreased 4.7 billion yen compared with the same period a year earlier to 90.7 billion yen.
- Net income increased 0.5 billion yen from the same period a year earlier to 54.2 billion yen. Factors included a decline in deferred income taxes related to undistributed foreign earnings due to the stronger yen.

4. Overview of Balance Sheets

Next, I would like to cover the main changes in the balance sheets.

- Total assets decreased 29.7 billion yen from the previous fiscal year-end to 1,202.8 billion yen, reflecting the amortization of goodwill and other intangible assets.
- Interest-bearing debt including borrowings and bonds decreased 22.2 billion yen from the previous fiscal year-end to 291.4 billion yen.

5. Forecast of Consolidated Results for the Year Ending March 31, 2009

Finally, I would like to cover the consolidated forecast of full-year results.

- The financial crisis that started in the United States has spread quickly, causing a downturn in the global economy, and consumer sentiment is cooling further.
- With regard to the Consumer Products Business, the household and personal care products market in Japan has begun to contract year on year, and is gradually becoming more challenging. Outside Japan, the appreciation of the yen is reducing sales growth even though operations in Asia remain solid. Foreign currency translation and worsening economic conditions are impacting operations in North America and Europe.
- Economic conditions are rapidly worsening in the Chemical Business. Customers are cutting back production and sales volume has begun falling short of the Company's plan.
- As a reflection of the currency translation impact resulting from the sharp appreciation of the yen since fall 2008, in addition to the abovementioned falling sales volume associated with weakening market conditions, the Kao Group has revised its forecast for net sales for the year ending March 31, 2009 to 1,285.0 billion yen, a decrease of 45.0 billion yen from the forecast issued in October 2008.
- Please see page 5 of the supplemental information. The Kao Group also forecasts that operating income will decrease approximately 15.0 billion yen due to the decline in sales discussed earlier. The prices of natural oils and fats and crude oil have been falling significantly since peaking in July 2008. However, raw material costs will not fully reflect these decreases until the next fiscal year ending March 31, 2010. As a result, the Kao Group projects that raw material costs for the year ending March 31, 2009 will increase by

approximately 35.0 billion yen, even though the impact will decrease 1.0 billion yen from the forecast issued in October 2008. Price adjustments in response to rising raw material prices will increase 1.0 billion yen from the previous forecast to approximately 23.0 billion yen. The effect of Total Cost Reduction (TCR) activities will remain unchanged at 8.0 billion yen. Amid the challenging business environment, the Kao Group will take additional countermeasures including improvement of the efficiency of advertising expenses, reduction of sales promotion materials and selective capital expenditures. These are projected to increase income approximately 3.0 billion yen. Given these conditions, the Kao Group has revised its full-year forecast for operating income downward by 14.0 billion yen compared with its October 2008 announcement, to 103.0 billion yen.

- In summary, as shown on page 7 of the supplemental information, the Kao Group has reduced its October 2008 full-year forecasts for net sales by 45.0 billion yen to 1,285.0 billion yen, for operating income by 14.0 billion yen to 103.0 billion yen, for ordinary income by 15.0 billion yen to 100.0 billion yen, and for net income by 9.0 billion yen to 60.0 billion yen.
- The Kao Group believes that stable, continuous dividends are important. As announced at the beginning of the fiscal year, the Kao Group projects a 1.00 yen per share increase in its year-end cash dividend to 28.00 yen per share, for cash dividends per share for the fiscal year totaling 56.00 yen. As a result, the payout ratio for the year ending March 31, 2009 is projected to be approximately 50%.
- Finally, please see page 8 of the supplemental information. A Kao Group survey of consumer sentiment indicates that consumers have a highly frugal mindset but want to use products that they like even if those products are more expensive. The Kao Group will continue to aim for profitable growth by developing products that offer high added value from the perspective of consumers.

- In addition, the Kao Group is working to further enhance its proposal-based sales capabilities and in-store merchandising activities to increase market share in Japan. In overseas businesses, the Kao Group is aiming for profitable growth through further promotion of the integration of business operations in Asia, including Japan.

This concludes my remarks. Thank you for your interest and attention.

** This teleconference presentation was held for institutional investors and analysts following the announcement of consolidated business results for the nine months ended December 31, 2008.*