

Highlights for the 1st Half of FY2014

(Ended June 30, 2014)

July 29, 2014

Kao Corporation

Michitaka Sawada

President and CEO



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http://www.kao.com/jp/en/corp_ir/presentations.html

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Fiscal year end is December 31 from FY2012

Term of consolidation for FY2012

- Group companies whose fiscal year end was previously March 31*: April-December 2012
- Group companies whose fiscal year end was already December 31: January-December 2012

Restated FY2012

Figures for the period from January 1 to December 31, 2012 for the purpose of comparison with FY2013 (January 1 to December 31, 2013)

Adjusted growth

Comparison with restated FY2012

* Kao Corporation and certain consolidated subsidiaries with the same fiscal year end

Agenda

- **Summary of the 1st Half of FY2014**
- **Summary of FY2014 Forecast**
- **Mid-term Growth Strategies**

Summary of the 1st Half of FY2014

Financial Overview – 1st Half of FY2014

		<u>Growth</u>	<u>Forecast²</u>
Net sales	¥665.9 billion	+6.6%	¥650.0 billion
EBITA¹ [% of sales]	¥62.8 billion [9.4%]	+9.2%	-
Operating income [% of sales]	¥49.3 billion [7.4%]	+14.9%	¥43.0 billion
Net income [% of sales]	¥31.6 billion [4.8%]	+73.3%	¥26.0 billion
Net income per share	¥61.77	+74.4%	¥50.75
Shareholder returns			
Cash dividends per share	¥34	+¥2	¥34

1. Operating income before amortization of goodwill and intellectual property rights related to M&A

2. Forecast announced on April 25, 2014

Executive Summary (1)

- **Net sales and profits grew year-on-year and achieved the forecast**
- **Growth drivers of net sales and operating income for the 1st half of FY2014**
 - Consumer Products Business in Japan
 - Appropriate response to last-minute surge in demand before the consumption tax increase and pullback that followed
 - Market share expansion through proactive initiatives
 - Chemical Business
 - Operating income exceeded the forecast due to increased sales and the effect of sales price adjustments
- **The Kao Group's response to vitiligo-like symptoms experienced by some customers of Kanebo Cosmetics brightening products containing Rhododenol**
 - Execute product recall thoroughly to prevent an increase in the number of people with symptoms
 - Ensure greater safety and reliability to prevent reoccurrence
 - Respond in a sincere manner to those with vitiligo-like symptoms
 - Efforts to investigate the cause and establish therapeutic methods
 - Deal with compensation in a sincere manner

Executive Summary (2)

■ Shareholder returns

- Cash dividends per share at the end of the 1st half of FY2014 are 34 yen, an increase of 2 yen

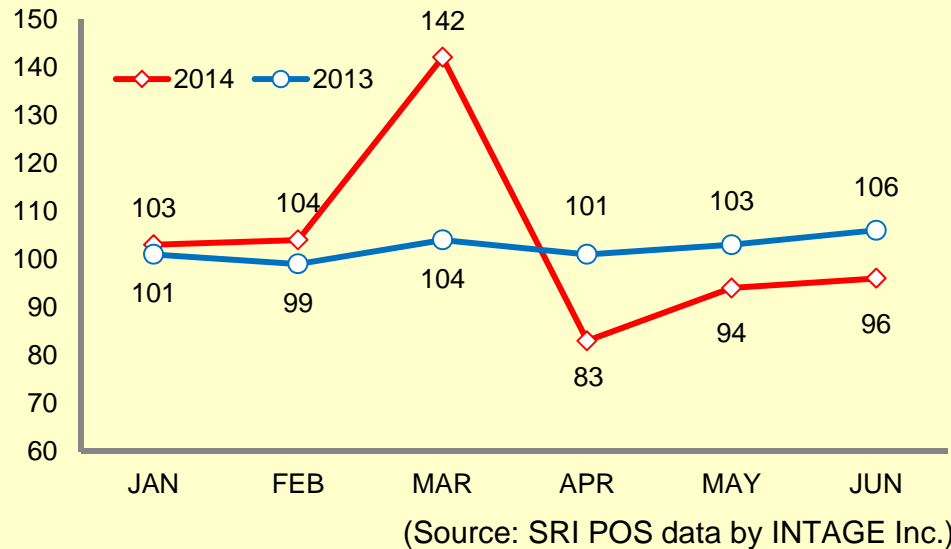
■ New corporate governance system has started

- An independent outside director has assumed the position of chairman of the Board of Directors and the number of inside directors and outside directors is equal at three each
- Enhanced corporate governance with a reorganization that incorporates even more outside perspectives (March 2014)
 - Committee for the Examination of the Nominees for the Board of Directors and Executive Officers (members: all outside directors and outside Audit & Supervisory Board members): Reorganized the former Committee for the Examination of the Nominees for the Chairman of the Board of Directors and the President and CEO and expanded the scope of examination to all nominees for the Board of Directors and executive officers
 - Compensation Advisory Committee (members: Chairman of the Board and all representative directors, outside directors and outside Audit & Supervisory Board members): Outside Audit & Supervisory Board members have been newly included in the committee

Impact of the Consumption Tax Increase* on the Japanese Market

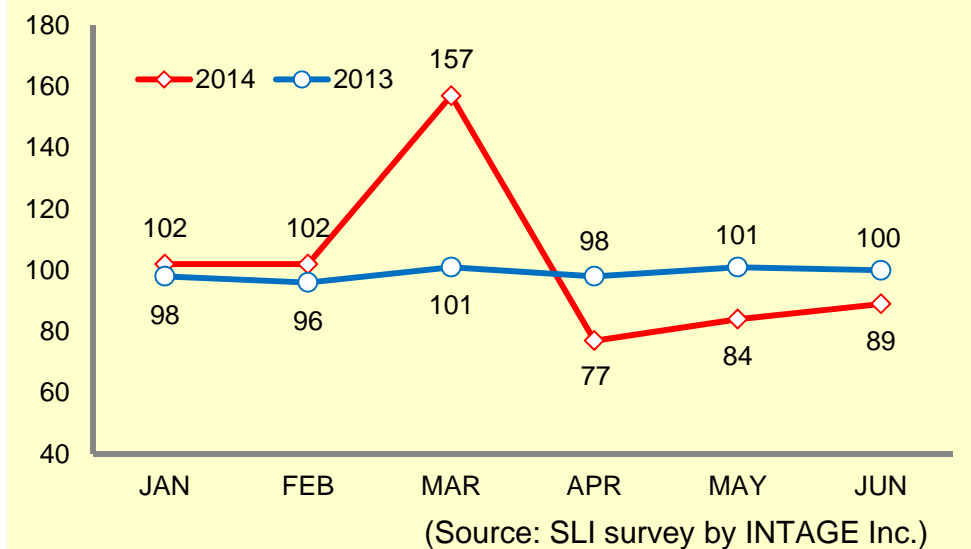
Household and personal care

79 categories; year-on-year growth rate of market size on value basis (yen)



Cosmetics

26 categories; year-on-year growth rate of market size on value basis (yen)



1st quarter

- Greater-than-expected last-minute surge in demand with a peak in March
- Response to sharp increase in demand from retailers using the strength of the Kao Group's supply chain



Impact on net sales and operating income was +25 billion yen and +15 billion yen, respectively

2nd quarter

- Initiatives in response to a pullback from last-minute surge in demand
 - Launched new and improved high-value-added products
 - Enhanced proposal-based sales activities
 - Aggressive investment in marketing

* The consumption tax rate was raised to 8% from 5% on April 1, 2014.

New and Improved Products Launched since April 2014

Beauty Care



Human Health Care



Fabric and Home Care



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Rich Pipeline of New and Improved Products for Launch in Japan in the 2nd Half of FY2014

Revitalize markets with continuous value offerings



Sales Expansion Drivers in the Growth Markets of Asia

Proactive value offerings for the growing middle-class consumer segment

■ Laundry detergents

- In China, the Kao Group launched *Attack Power Soaking* powder laundry detergent for hand washing in July 2013 and is expanding sales inland while ensuring proper communication of its distinctive features
- In Indonesia, *Attack Jaz1* powder laundry detergent for hand washing was launched at the end of June 2014. It is manufactured at the second consumer products plant, which was completed in June 2014
- In Vietnam, *Attack* powder laundry detergent for hand washing was launched in March 2014



Attack Jaz1 (Indonesia)



Attack (Vietnam)



Laurier Active Day Double Comfort (Indonesia)



Laurier Fresh & Free (Vietnam)

■ Sanitary napkins

- In China, *Laurier* gained market share (high-value-added *Laurier Slim Guard* also contributed)
- In Indonesia, innovative and easy-to-wash slim-type sanitary napkins that respond to local needs contributed to expansion of market share
- In Vietnam, *Laurier Fresh & Free* was launched in July 2013

■ Baby diapers

- In China, locally manufactured baby diapers are steadily expanding
- In Indonesia, pull-up type baby diapers, manufactured in the second plant, will be launched during 2014



Merries Shun Shuang Tou Qi (China)

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Summary of FY2014 Forecast

Key Points in FY2014 Forecast (1)

- **Aiming to achieve five consecutive fiscal years of increases in net sales and profits* and break previous records for net sales and profits**
 - **Promote a business model for exiting deflation and maximize use of Kao Group assets**

(1) Growth of the Consumer Products Business in Japan

- Accumulate successes of new and improved products launched in the 2nd half
- Partially offset rising raw material prices with higher-value-added products and cost reduction activities (TCR)

(2) Recovery of trust for Kanebo Cosmetics

- Respond in a sincere manner to those with vitiligo-like symptoms
- Operating margin before deduction of royalties
 - ◆ FY2013 actual: Slightly less than 5%
 - ◆ FY2014 forecast: Approximately 8%

(3) Contribution of the Chemical Business to profits

- Conduct price adjustments in tandem with rising raw material prices
- Further reinforce oleo chemicals
- Propose high-value-added products

(4) Operation of the Consumer Products Business in the Americas and Europe in line with the plan

(5) Steady development of business targeting the growing middle-class consumer segment in the Consumer Products Business in Asia

* Excludes the impact of the change in financial term in 2012. (Please refer to slide 2 for details.)

Key Points in FY2014 Forecast (2)

■ Enhancement of shareholder returns

- Annual cash dividends per share for FY2014 of 68 yen, an increase of 4 yen compared with the previous fiscal year (planned 25th consecutive fiscal year of increases in cash dividends)
- Share repurchase: Up to 13 million shares or ¥50.0 billion

Summary of FY2014 Forecast

		<u>Growth</u>
Net sales	¥1,390.0 billion	+5.7%
EBITA* [% of sales]	¥156.3 billion [11.2%]	+1.0%
Operating income [% of sales]	¥130.0 billion [9.4%]	+4.3%
Net income [% of sales]	¥75.0 billion [5.4%]	+15.8%
Net income per share	¥147.54	+17.1%
ROE	12.1%	+140 bps
Shareholder returns		
Cash dividends per share	¥68	+¥4
Consolidated payout ratio	46.1%	
Share repurchases	¥50.0 billion	

* Operating income before amortization of goodwill and intellectual property rights related to M&A

Mid-term Growth Strategies

Kao Group's Vision for the Future

A company with a global presence

Profitable growth

Further innovation

Contributions to sustainability of the world

Products and services that are "a half-step ahead"

Maximum use of human resources and organization

Corporate philosophy of the Kao Group (The Kao Way)

To strive for the wholehearted satisfaction and enrichment of the lives of people globally and to contribute to the sustainability of the world

Kao Sustainability Statement

Kao Group's basic direction of contribution to the sustainability of the world

Key areas

Conservation

Community

Culture

Contributions to Sustainability of the World

Contribution to society through business activities

Key areas

Conservation

Community

Culture

Fulfill our role as a public entity of society based on the Kao Way



■ Contribute to the resolution of global social issues through innovative products and services

- *Product development considering environment, health, aging society, sanitation, etc.*

■ Continue and reinforce social contribution activities as a corporate citizen

- *Collaboration with stakeholders and local communities*

■ Act on global issues

- *Participation in the United Nations' Global Compact, RSPO* membership and sustainable palm oil procurement, respect for diversity*

* RSPO: Roundtable on Sustainable Palm Oil, an international non-governmental organization that pursues solutions to issues related to palm oil production, including the destruction of ecosystems by rainforest logging and poor labor conditions for workers on plantations

Kao Group Mid-term Plan 2015 (K15)

Target 1: Break previous records for net sales and profits

Target 2: Achieve numerical management targets for FY2015

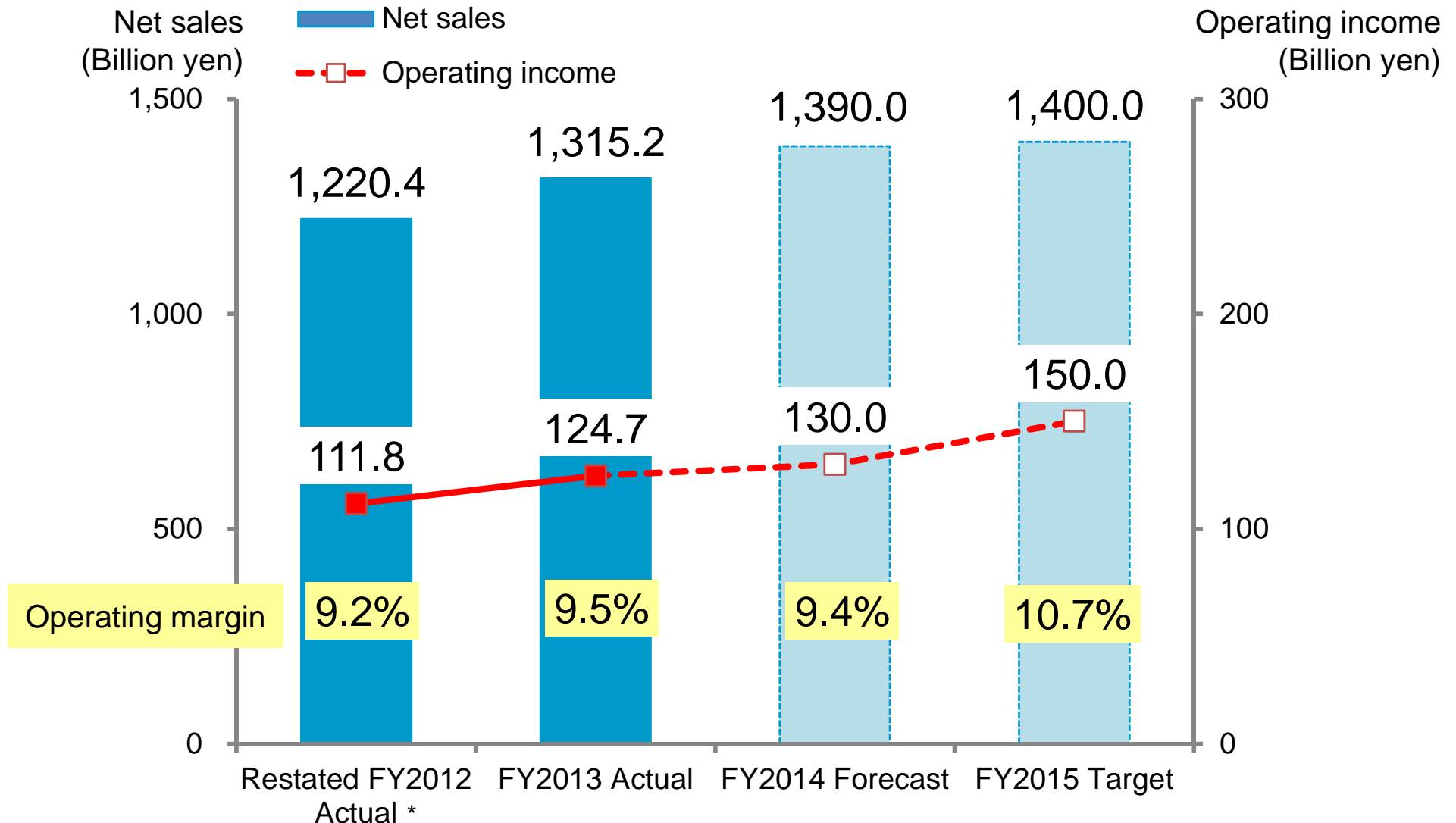
Numerical Management Targets for FY2015

- **Net sales:**
1.4 trillion yen
- **Operating income:**
150 billion yen
- **Overseas sales ratio* :**
30% or more

* Ratio of net sales to foreign customers to consolidated net sales

K15 Net Sales and Operating Income

FY2014 is an important year toward the achievement of K15



* Excludes the impact of the change in financial term in 2012. (Please refer to slide 2 for details.)

Growth Strategies to Achieve K15

1. Expand the Consumer Products Business globally

- Growth markets: Expand the business significantly by proposing products in the domain of “cleanliness” including laundry detergents, baby diapers and sanitary napkins that target the growing middle-class consumer segment
- Mature markets: Accelerate growth with high-value-added products

2. Further reinforce the Fabric and Home Care Business, and accelerate profitable growth in the Beauty Care and Human Health Care Businesses

Fabric and Home Care Business

- Maintain or capture the top share in each product category

Beauty Care Business and Human Health Care Business

- Move the cosmetics business to a phase of profitable growth
- Propose products and services through new approaches focused on health and the aging society

3. Reinforce the Chemical Business

- Promote higher added value
- Strengthen synergy with the Consumer Products Business

Key Points to Achieve K15

■ Ensure profits of the Consumer Products Business in Japan

- Deal with the consumption tax increase in October 2015
- Achieve profitable growth in the cosmetics business, especially Kanebo Cosmetics
- Make value offerings in response to social issues such as the environment, health and the aging society

■ In the Consumer Products Business, expand the business in Asia and ensure profits in the Americas and Europe

■ Stable growth of the Chemical Business in the changing global business environment

- Improve profitability of oleo chemicals
- Expand sales of high-value-added products

■ Generate profits with the Transformation for Profitable Growth (TPG) Project

- Prepare and invest for further growth beyond K15

Global Expansion Project

- FY2015 sales target of the Consumer Products Business in China: 50 billion yen
- Triple the business in Vietnam
- Operating margin target for the Consumer Products Business in Asia: 5%
- Reinforce and expand businesses in the ASEAN region including the Mekong region
- Prepare to build the foundations to tap into markets in Russia, Brazil, India, the Middle East, etc.

ROE Enhancement

Operating margin improvement

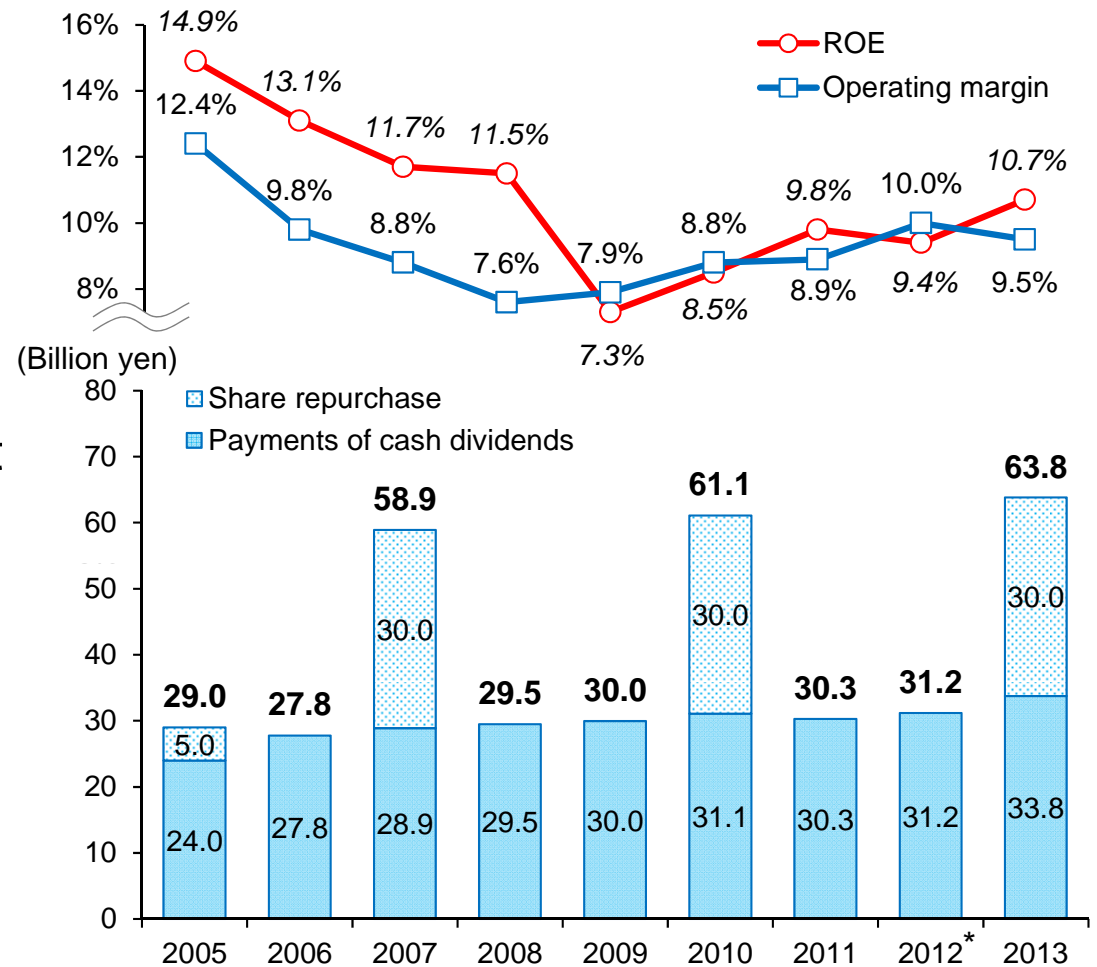
- Improve operating margin while increasing operating income

EVA perspective

- Proactive investment for growth
- Balance sheet management that considers cost of capital

Shareholder returns as a use of free cash flow

- Steady and continuous cash dividends
- Share repurchases (Aggregate from FY1999 to June 2014: 393.8 billion yen)



* Fiscal year end is December 31 from FY2012. (Please refer to slide 2 for details.) ROE of FY2012 is for the transitional period associated with the change in fiscal year end.

Use of Free Cash Flow* and Shareholder Returns

Use steadily generated free cash flow effectively in order of priority shown below from an EVA standpoint toward further growth.

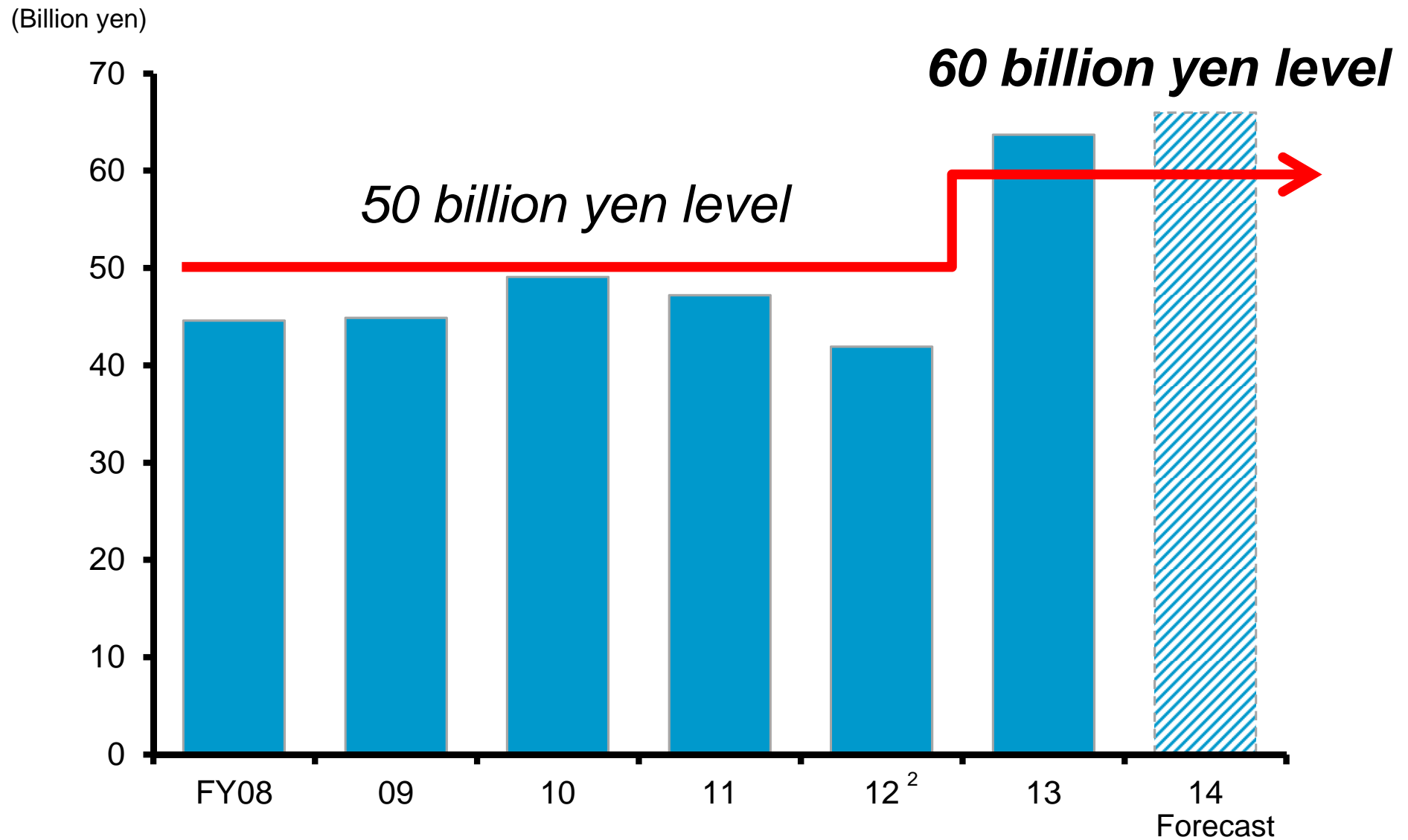
1. Capital expenditures and M&A for future growth

2. Steady and continuous cash dividends

3. Share repurchases and repayment of interest-bearing debt including borrowings

* Free cash flow = Net cash provided by operating activities + Net cash used in investing activities

Proactive Capital Expenditures¹ to Accelerate Global Growth



1 Long-term prepaid expenses are included in capital expenditures.

2 Fiscal year end is December 31 from FY2012. (Please refer to slide 2 for details.)

Appendices

Business Segments and Main Product Categories



Note: Sales include intersegment sales. Share of net sales is calculated based on sales to customers.

1H/FY2014 Breakdown of Beauty Care Business

		Billion yen	Increase/decrease
Beauty Care	Net sales	283.5	+1.8%
	Operating income ¹	6.4	+3.4 billion yen
	Operating margin	2.3%	+120bps
Cosmetics	Net sales	122.9	-2.7%
	Operating income ¹	-9.7	+4.2 billion yen
	Operating margin	-7.9%	+310bps
Skin care/hair care (mass products) and professional hair care products	Net sales	160.7	+5.5%
	Operating income ¹	16.1	-0.9 billion yen
	Operating margin	10.0%	-110bps

Kanebo Cosmetics

- Net sales:
Slightly more than ¥80 billion
(1H/FY2013: Approx. ¥90 billion)
- Profit as a % of sales²:
Approx. 4%
(1H/FY2013: Approx. 2%)

2. Operating margin before deduction of royalties

1. Includes amortization of goodwill and intellectual property rights related to M&A

- Beauty Care: ¥13.4 billion
- Cosmetics: ¥13.0 billion
- Skin care/hair care (mass products) and professional hair care products: ¥0.5 billion

Cosmetics in Japan – 1st Half of FY2014

Cosmetics market in Japan

[Year-on-year growth on a value (yen) basis] Jan. - Jun. 14 Jan. - Dec. 13

Total market

+2.4%

-1.5%

High-priced segment (over ¥5,000):

+2.3%

+0.3%

Mid-priced segment (¥2,000- ¥5,000):

+3.4%

-3.4%

Low-priced segment (below ¥2,000):

+1.1%

-0.9%

Kao Group total (Kanebo Cosmetics + Kao Sofina)

-1.9%

-3.5%

Source: SLI survey by INTAGE Inc. (Data based on tracking service of 40,060 female consumers nationwide in Japan)

SRI Indexes and External CSR Evaluation

SRI indexes for which Kao has been selected



FTSE4Good



CSR-related evaluations from external organizations



CSR: Corporate Social Responsibility
SRI: Socially Responsible Investment

(As of July 29, 2014)

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