

# Highlights for the 1<sup>st</sup> Half of FY2015

(Ended June 30, 2015)

**Kao Corporation**

July 28, 2015

**Michitaka Sawada**

**President and CEO**



**Kao**

Enriching lives, in harmony with nature.

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[http://www.kao.com/jp/en/corp\\_ir/presentations.html](http://www.kao.com/jp/en/corp_ir/presentations.html)

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

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 1<sup>st</sup> Half of FY2015**
- **Kao Group Mid-term Plan 2015 (K15)  
and Summary of FY2015 Forecast**
- **The Kao Group's Sustainable Growth  
and Corporate Value Creation**

# Summary of the 1<sup>st</sup> Half of FY2015

# Financial Overview – 1<sup>st</sup> Half of FY2015

		<u>Year-on-year growth</u>	<u>Forecast<sup>2</sup></u>
<b>Net sales</b>	<b>¥695.2 billion</b>	+4.4%	¥700.0 billion
<b>EBITA<sup>1</sup></b> [% of sales]	<b>¥73.3 billion</b> [10.5%]	+16.8%	-
<b>Operating income</b> [% of sales]	<b>¥60.1 billion</b> [8.6%]	+21.8%	¥50.0 billion
<b>Net income</b> [% of sales]	<b>¥34.0 billion</b> [4.9%]	+7.6%	¥26.0 billion
<b>Net income per share</b>	<b>¥67.92</b>	+10.0%	¥51.87
<b>Shareholder returns</b>			
<b>Cash dividends per share</b>	<b>¥38</b>	+¥4	¥38

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

2. Forecast announced on April 23, 2015

# Executive Summary (1)

- **Aiming to achieve the forecast of FY2015, the final year of K15, Kao exceeded the forecast\* of the 1st half of FY2015 for profits, even though net sales were slightly below the forecast**
- **Growth model for exiting deflation with proactive investment worked favorably**
  - Continued investment in capital that included capacity expansion of sanitary products such as baby diapers and in marketing
  - Continued high-value offerings with new and improved products
- **Key points regarding year-on-year growth of net sales and operating income**
  - Consumer Products Business in Japan
    - Market share excluding cosmetics expanded through proactive initiatives
    - Overall results excluding cosmetics were solid with strong performance by sanitary products. Fabric care products began to recover supported by new and improved products launched from the end of June
    - Cosmetics underperformed the market, even though Kanebo Cosmetics captured some inbound demand (demand from visitors to Japan)
  - Consumer Products Business in Asia
    - Overall, sales and profits increased strongly
    - Sales of products targeting the middle-class consumer segment are expanding steadily in China, Indonesia and Vietnam

\* Forecast announced on April 23, 2015

# Executive Summary (2)

## ■ Shareholder returns

- Cash dividends per share at end of the 1st half of FY2015 are 38 yen, an increase of 4 yen year on year

## ■ Corporate governance

- Kao systematically organized its corporate governance activities and disclosed the implementation status of each principle stated in the Corporate Governance Code on July 1, 2015

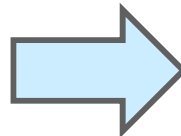
# Response to Changes in the Consumer Products Market in Japan

## • Changes in the market

- Innovative offerings in response to the demands of the times
- New value offerings based on essential research

### ● Shampoos/conditioners

Boom of non-silicone type products and cosmetics-like products has dissipated

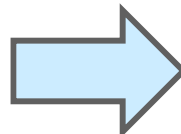


- High-value-added offerings based on essential research on hair



### ● Fabric softeners

Change in preference for strong lingering scent

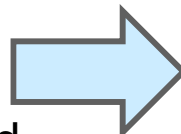


- Softness, water absorbability, 24-hour deodorization, dry effect



### ● Laundry detergents

Greater-than-expected shrinkage of the powder detergent market and expansion of liquid detergent market

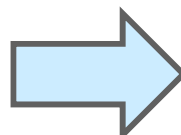


- Upgrade of functionality of liquid laundry detergents based on essential research on mold and biofilm



### ● Beverage (FOSHU\* drinks)

Impact from Food with Nutrient Function Claims



- Differentiation by emphasizing FOSHU claims that are not allowed for Food with Nutrient Functions Claims (body fat utilization)



\* Food for Specified Health Uses

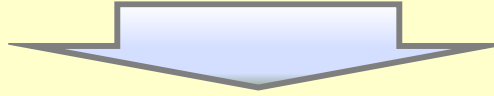
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# Consumer Products Business in Asia

**Sales growth in the 1<sup>st</sup> half of FY2015: +21.7%\***



**Aiming for 5% operating margin for FY2015, while expanding sales**

## China

- Continued strong sales of baby diapers manufactured in Japan and locally
- Sanitary napkins also performed well
- Contributed to the profit of the Consumer Products Business in Asia

## Indonesia

- Steady performance toward sales and market share expansion with baby diapers and laundry detergents targeting the middle-class consumer segment along with existing products

## Thailand

- Steady profit generation in spite of impact caused by the economic slowdown and price competition in laundry detergents

## Mature markets

- Taiwan, Hong Kong, Singapore
- High-value-added products contributed to sales and profit

\* Excludes the effect of currency translation

# Kao Group Mid-term Plan 2015 (K15) and Summary of FY2015 Forecast

# Kao Group Mid-term Plan 2015 (K15)

**Target 1: Break previous records for net sales and profits**

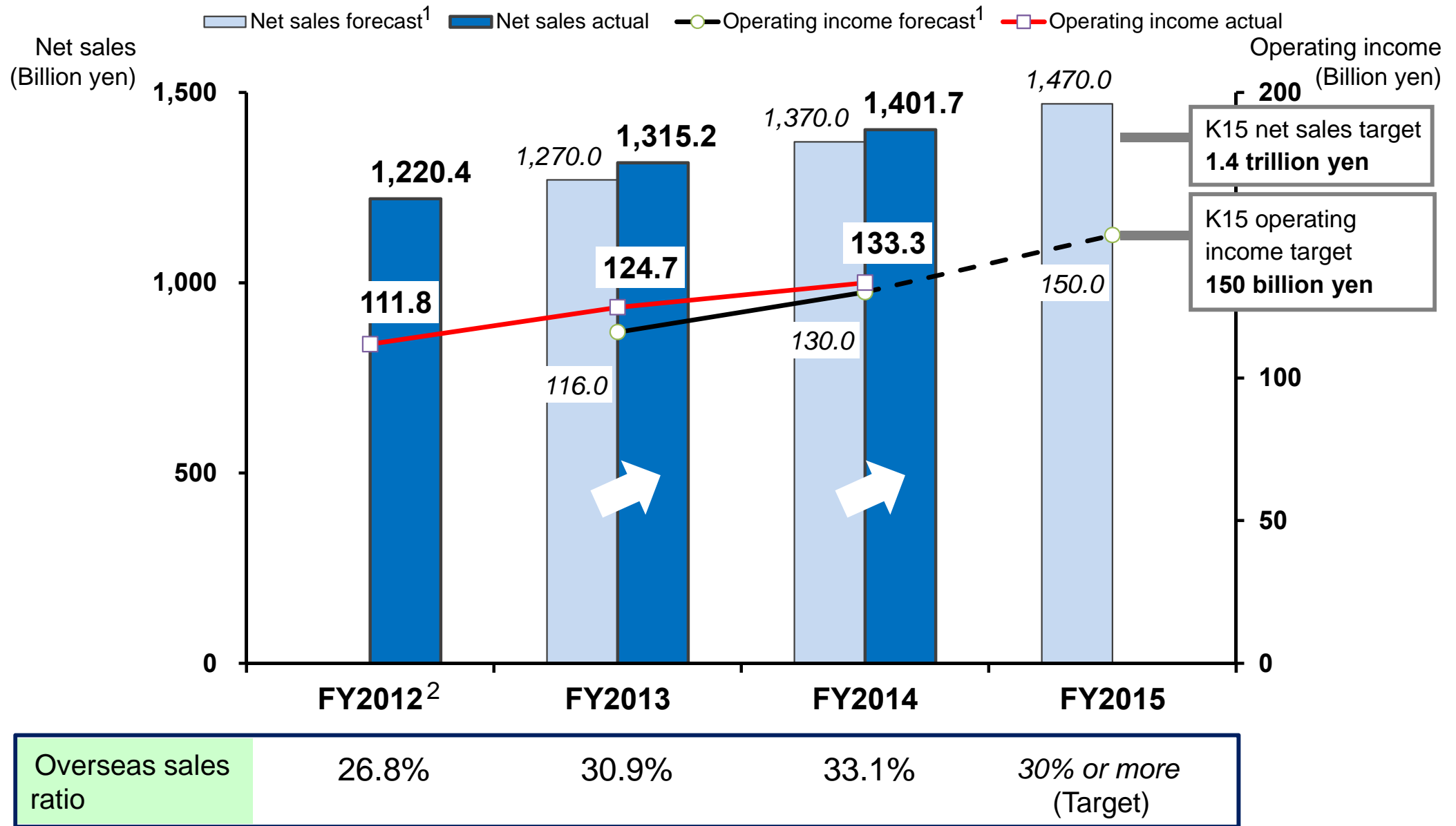
**Target 2: Achieve numerical management targets for FY2015**

## **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



1. Forecast at the beginning of each fiscal year, except FY2015 forecast announced on July 28, 2015
2. 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

# Focal Points in the 2<sup>nd</sup> Half of FY2015

**Aiming for operating income of 150 billion yen in FY2015, while investing proactively for sustainable growth beyond FY2016**

## Consumer Products Business in Japan

- Generate planned operating income, while launching new and improved products as planned and making proactive marketing investments
- Minimize negative impact from weak performance of cosmetics and beverages in the 1<sup>st</sup> half of FY2015
- Restore fabric care by nurturing and reinforcing new and improved products

## Consumer Products Business in Asia

- Nurture and enhance high-value-added products in the premium-priced segment
- Enhance consumer products business targeting the growing middle-class consumer segment

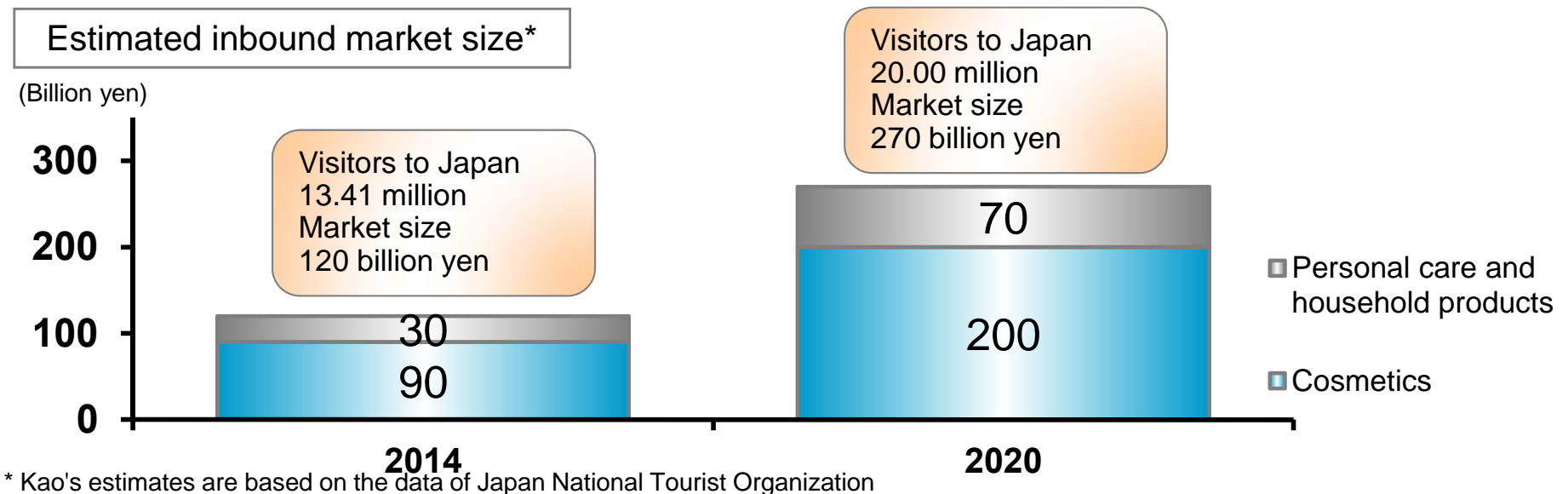
## Chemical Business

- Generate operating income steadily with high-value-added products despite difficulty in sales due to selling price adjustments in response to fluctuations in raw material prices

# Issues to Address in the 2<sup>nd</sup> Half of FY2015

## Proactively capture inbound demand<sup>1</sup>

- Attractive value offerings to visitors to Japan
- In-store display proposals that make purchase and selection easy
- Product information in English and Chinese on website



## Value communication of *Healthya* functional drinks

- Emphasize characteristics and uniqueness of *Healthya* amid numerous FOSHU<sup>2</sup> drinks
- Differentiate from Food with Nutrient Function Claims

1. Demand from visitors to Japan  
2. Food for Specified Health Uses

# New Targets to Address Starting in the 2<sup>nd</sup> Half of FY2015

## First stage of the major reform of cosmetics – Kao Sofina

- Reform whose effect continues for 20 to 30 years
- Transform to “holistic beauty,” a concept of which beauty stems from outside and inside of the body, while using concept of evidence oriented cosmetics based on skin-science as existing assets
- Further enhance counseling quality

## New business related to food and beverages

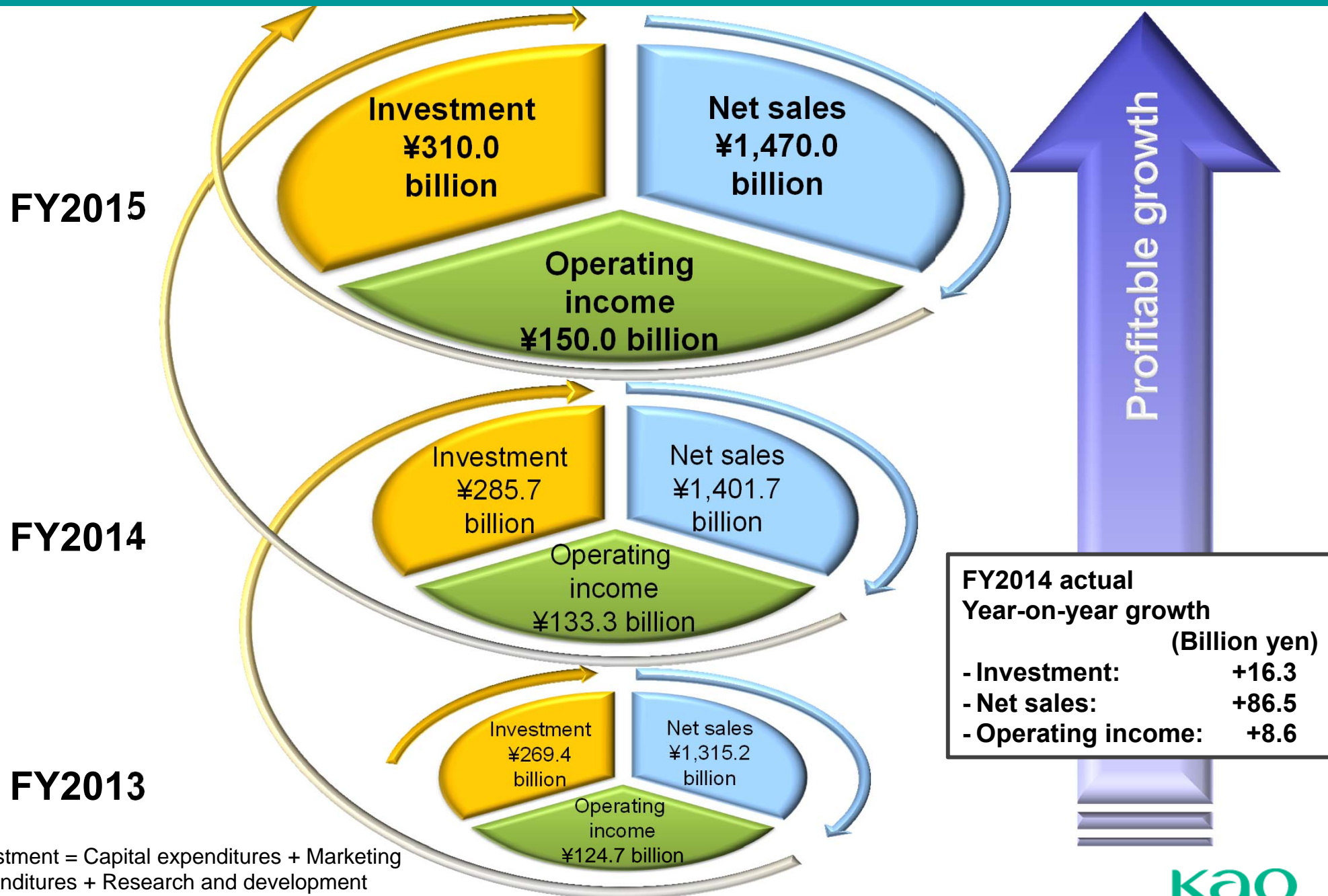
- Aim for a health solution business
- Expand the scope to include locomotive syndrome in addition to metabolic syndrome

## Maximize use of Kao Group assets through sponsorship at Tokyo Disneyland® and Tokyo DisneySea®

- Kao's unique offerings related to hygiene and cleanliness
- Attract more children and young families so that they turn into Kao fans



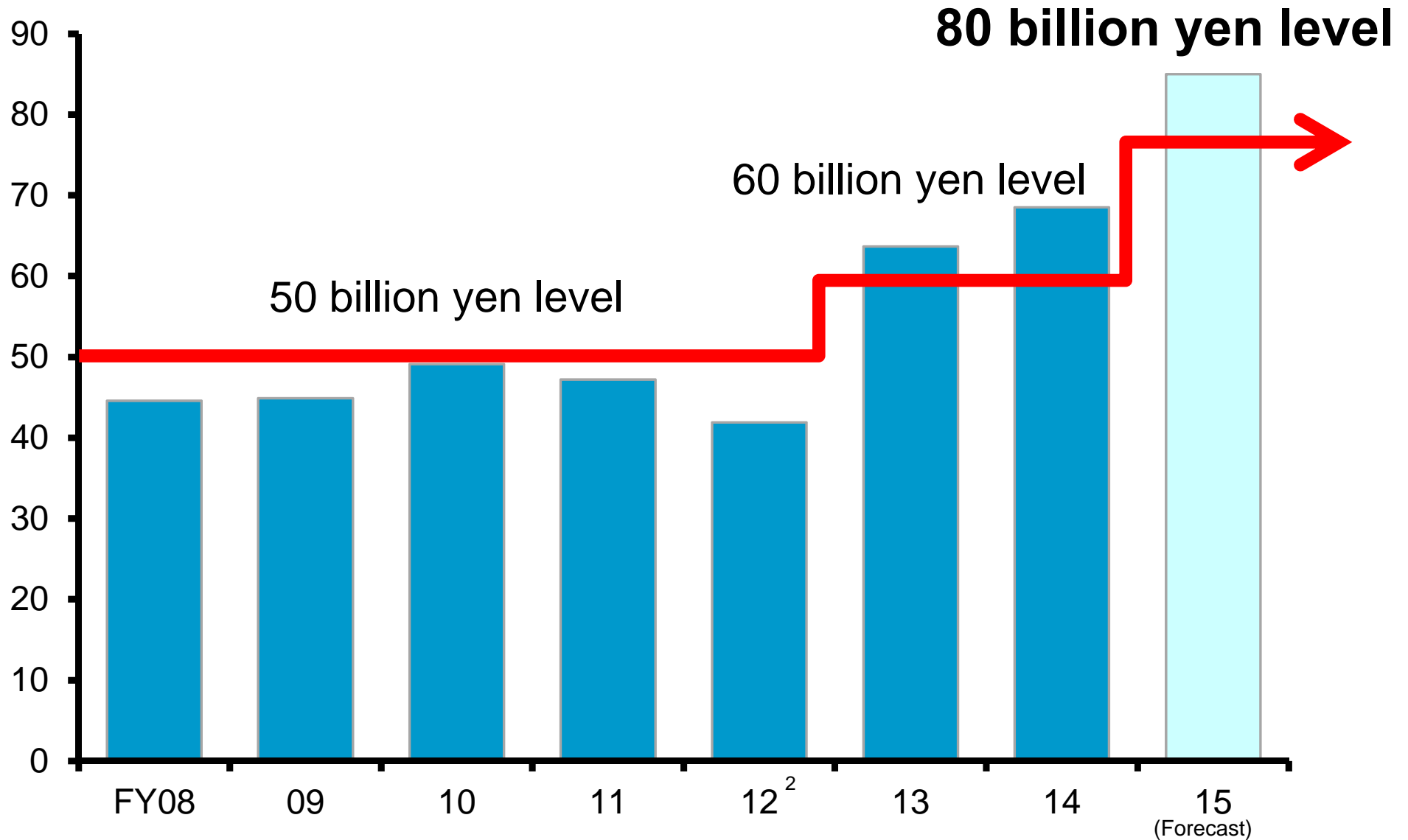
# Growth Model for Exiting Deflation with Proactive Investment\*



\* Investment = Capital expenditures + Marketing expenditures + Research and development expenditures

# Proactive Capital Expenditures<sup>1</sup> to Accelerate Global Growth

(Billion yen)



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.)

# Summary of FY2015 Forecast

		<u>Year-on-year growth</u>
<b>Net sales</b>	<b>¥1,470.0 billion</b>	<b>+4.9%</b>
<b>EBITA*</b> [% of sales]	<b>¥176.3 billion</b> [12.0%]	<b>+8.8%</b>
<b>Operating income</b> [% of sales]	<b>¥150.0 billion</b> [10.2%]	<b>+12.6%</b>
<b>Net income</b> [% of sales]	<b>¥87.0 billion</b> [5.9%]	<b>+9.3%</b>
<b>Net income per share</b>	<b>¥173.52</b>	<b>+10.9%</b>
<b>ROE</b>	<b>12.7%</b>	<b>+30 bps</b>
<b>Shareholder returns</b>		
<b>Cash dividends per share</b>	<b>¥76</b>	<b>+¥6</b>
<b>Consolidated payout ratio</b>	<b>43.8%</b>	

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

# The Kao Group's Sustainable Growth and Corporate Value Creation

# The 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**

# Use of Cash Flow\* and Shareholder Returns

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

1. Investment for future growth  
(capital expenditures, M&A, etc.)

2. Steady and continuous cash dividends

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

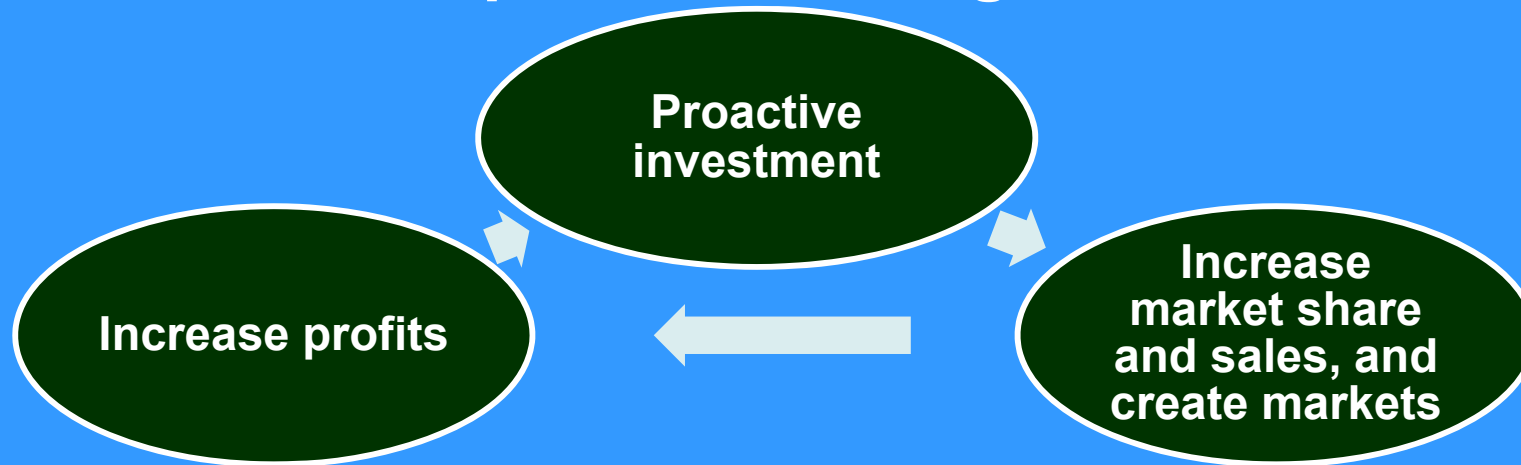
\* Net cash provided by operating activities

# Appendices

# Targeted Sustainable Growth Model

Profitable growth

Establish a post-deflation growth model

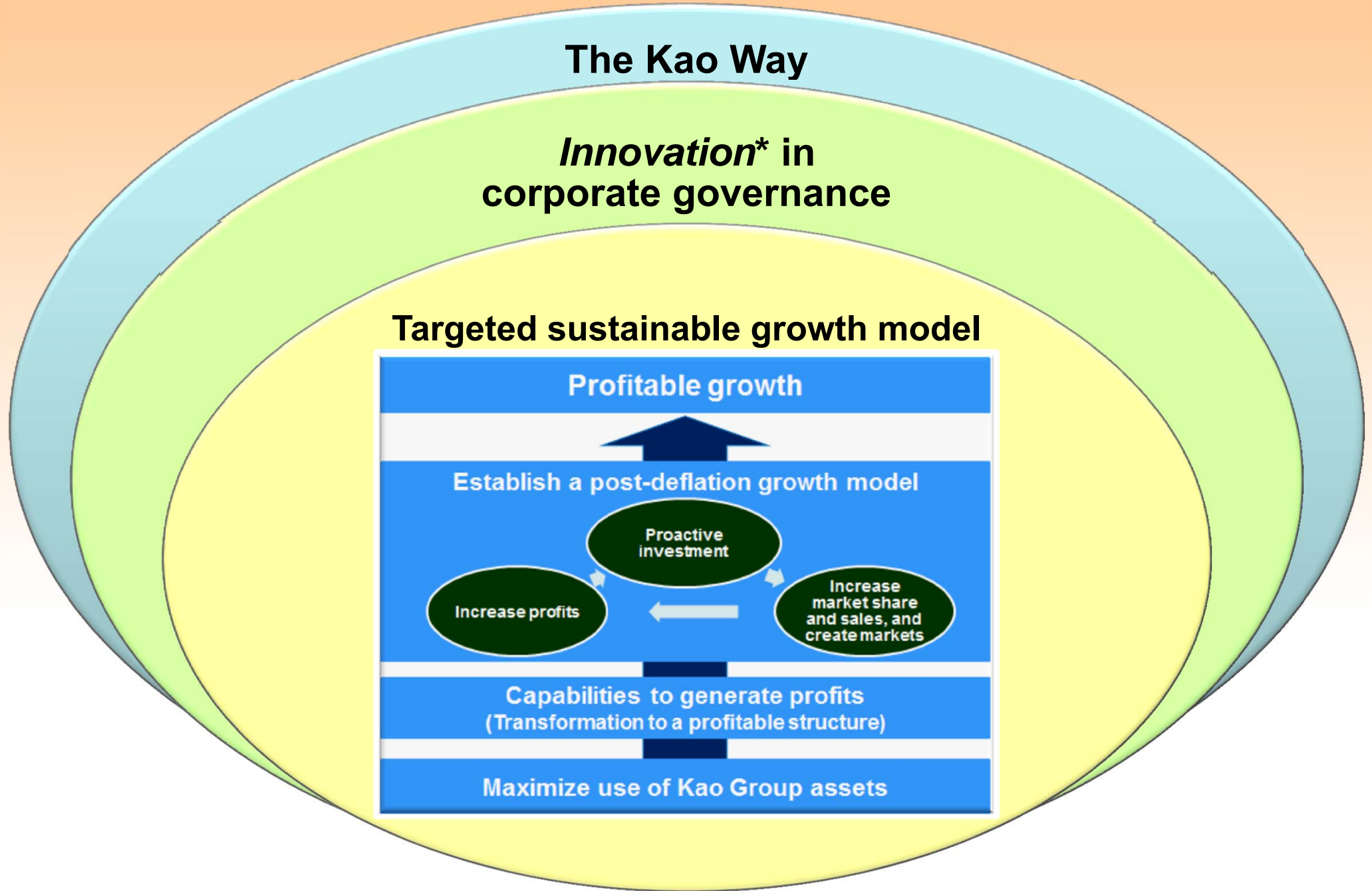


Capabilities to generate profits  
(Transformation to a profitable structure)

Maximize use of Kao Group assets



# Profitable Growth and Corporate Governance



\* Innovation is one of the values of The Kao Way, the corporate philosophy of the Kao Group.

# 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 the environment, health, the aging society, hygiene, 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

# Business Segments and Main Product Categories

Consumer Products  
Business

## Beauty Care

1H/FY2015 sales: ¥287.5 billion

[Growth: +1.4% / Share of net sales: 41.4%]

Professional hair care products  
Cosmetics  
Skin care (mass products)  
Hair care (mass products)



Consumer Products  
Business

## Fabric and Home Care

1H/FY2015 sales: ¥149.1 billion

[Growth: +0.7% / Share of net sales: 21.5%]

Laundry detergents and fabric treatments  
Products for kitchen, bath, toilet and living room care



Consumer  
driven

## Human Health Care

1H/FY2015 sales: ¥132.9 billion

[Growth: +21.2% / Share of net sales: 19.0%]

Beverages  
Oral care  
Blood circulation enhancement products  
(incl. bath additives and thermal pads)  
Sanitary products



Consumer Products  
Business

## Chemical

1H/FY2015 sales: ¥143.8 billion

[Growth: -1.0% / Share of net sales: 18.1%]

Oleo chemicals  
Performance chemicals  
Specialty chemicals



Chemical Business

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

# 1H/FY2015 Breakdown of Beauty Care Business

		Billion yen	Increase/decrease
<b>Beauty Care</b>	Net sales	287.5	+1.4% <sup>1</sup>
	Operating income <sup>2</sup>	4.6	-1.9 billion yen
	Operating margin	1.6%	-70 bps
<b>Cosmetics</b>	Net sales	114.7	-6.7% <sup>1</sup>
	Operating income <sup>2</sup>	-15.4	-5.7 billion yen
	Operating margin	-13.4%	-550 bps
<b>Skin care/hair care (mass products) and professional hair care products</b>	Net sales	172.8	+7.6%
	Operating income <sup>2</sup>	19.9	+3.8 billion yen
	Operating margin	11.5%	+150 bps

## Kanebo Cosmetics

- Net sales:  
Approx. ¥80 billion  
(1H/FY2014: Slightly more than ¥80 billion)
- Profit as a % of sales<sup>3</sup>:  
Slightly less than 2%  
(1H/FY2014: Approx. 4%)

3. Operating margin before deduction of royalties

1. Increase/decrease excluding the impact of the revision of the sales system for Kao Sofina:  
Beauty Care +2.6%, Cosmetics -3.9%
2. Includes amortization of goodwill and intellectual property rights related to M&A
  - Beauty Care: ¥13.2 billion
  - Cosmetics: ¥12.7 billion
  - Skin care/hair care (mass products) and professional hair care products: ¥0.5 billion

# Cosmetics in Japan – 1<sup>st</sup> Half of FY2015

## Cosmetics market in Japan

[Year-on-year growth on a value (yen) basis]      Jan. - Jun. 15      Jan. - Dec. 14

**Total market**

**-6.2%**

**-0.2%**

**High-priced segment (over ¥5,000):**

**-4.9%**

**+0.1%**

**Mid-priced segment (¥2,000- ¥5,000):**

**-7.0%**

**+0.3%**

**Low-priced segment (below ¥2,000):**

**-6.7%**

**-1.2%**

**Kao Group total (Kanebo Cosmetics + Kao Sofina)**

**-7.2%**

**-0.5%**

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

# ROE Enhancement

## ■ Operating margin improvement

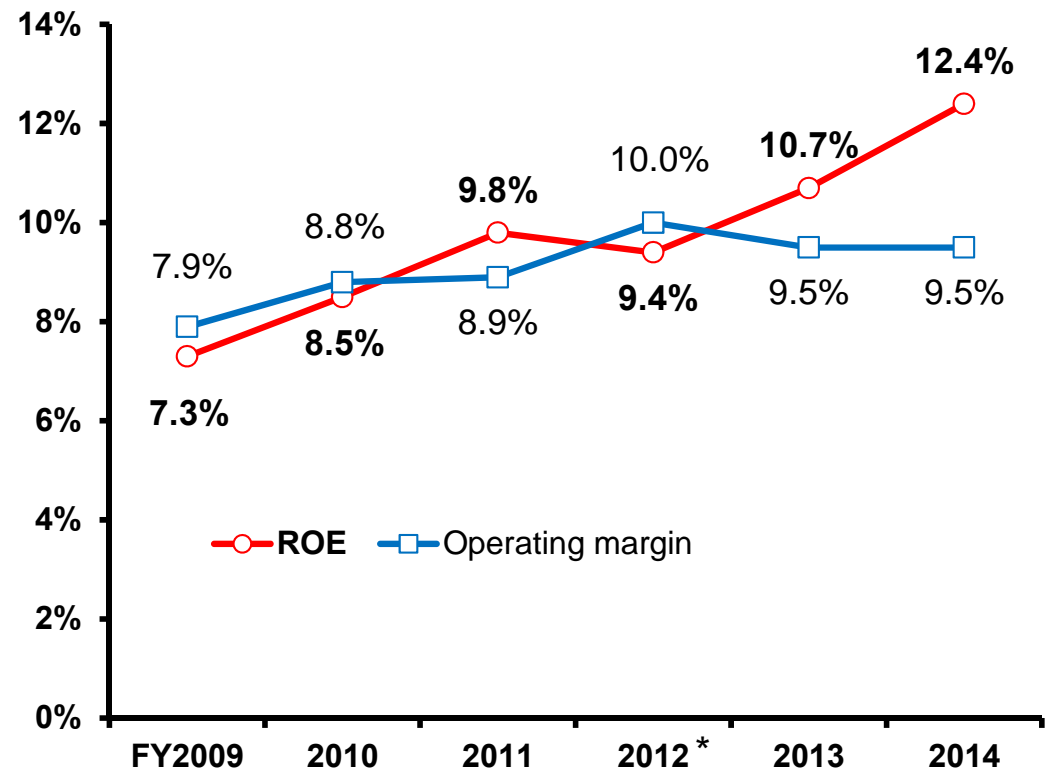
- Improve operating margin while increasing operating income

## ■ EVA perspective

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

## ■ Shareholder returns as a use of cash flow

- Steady and continuous cash dividends (25<sup>th</sup> consecutive fiscal year of increases in cash dividends in FY2014)
- Share repurchases



\* 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.



# SRI Indexes and External CSR Evaluations

## SRI indexes for which Kao has been selected

MEMBER OF

**Dow Jones  
Sustainability Indices**

In Collaboration with RobecoSAM



FTSE4Good



## CSR-related evaluations from external organizations



Kao Corporation also received Gold Class 2015 and Industry Mover 2015



(As of July 28, 2015)

CSR: Corporate Social Responsibility  
SRI: Socially Responsible Investment

**Kao**

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The logo for Kao, featuring the word "Kao" in a bold, sans-serif font. The letter "K" is a dark blue, while "a" and "o" are a lighter blue. The letters are closely spaced and have a clean, modern design.

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