*Our researchers are undertaking research into new types of surfactants.
Chapter 3

Mid- to Long-term Strategies

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Kao encourages each of its employees to continuously make efforts to contribute to the future of Kao. We work toward cultivating such human capital and establishing corporate culture.

Akio Matsui
Executive Officer
Senior Vice President, Human Capital Development, Global

Basic Philosophy

Through Yoki-Monozukuri, Kao has gathered together a group of employees who are passionate about contributing to society. With this group of employees, we have established an organization that, as a corporate citizen, place emphasis on a right-minded corporate culture represented by the Kao Way. While passing on our founding spirit, our senior management, managers and those on the frontlines have come together to discuss the future vision for Kao in these times of change. By proactively transforming work-styles, encouraging individuals to challenge themselves, offering fair rewards for business performance and growth, we have established a vibrant organization that is highly adaptable to change.

Among trends that include the digital revolution represented by coexistence with AI, ESG management promotion and the arrival of a super-aging society in some countries, we recognize that the most important asset is our human capital, and discuss and promote hiring and cultivating human capital that will nurture the Kao’s sustainable growth, effective company management, and optimal personnel allocation, in a personnel committee where senior management participate as members. Moreover, by appropriately giving back generated added value to our employees (human investment), we are mapping out a positive growth cycle toward creating future added value, K20, and our vision by 2030.

Human Capital Development System

We promote the Guidelines for Human Capital Development which states points 1) pursuing effectiveness and efficiency, 2) respecting human nature, 3) making efforts toward integration, which acts as the basis of Kao’s human capital development, on a global basis.

In order to promote company-wide activities in line with our basic policy throughout the entire group, we are introducing and utilizing global common frameworks. These include, for example, managing personnel and personnel cost and utilizing human resources data through the global human capital information system, enhancing organizational capabilities through the employee opinion survey “FIND”, and strengthening human capital management and cultivation through the global common ranking system, evaluation system, education system and reward policy.

Additionally, based on the perception that health is not only the foundation of employee’s personal life, but an asset of the company and the source of its growth, we encourage and actively support voluntary health promotion among our employees. While working in cooperation with the Human Capital Development Division at each of our group companies, we are promoting these activities on a global basis.
Cultivating Unique Human Capital and Establishing Corporate Culture

The feature of our organizational management is its matrix management of business and functions. Matrix management eliminates rigid organizational management and offers value to changing consumers while enabling a flexible response to society. With the expansion of global business and the additional axes in such as countries and regions, a more sophisticated management style is needed. In terms of human capital development, in conjunction with mid- and long-term business strategies, we are nurturing business leaders and introducing flexible personnel capital for growing business. At our functional axis, we are working toward strengthening the expertise of our human capital and pursuing effectiveness and efficiency of business support. At country and region axes, we are improving the quality of our employment policies as well as strengthening the capabilities of each employee.

In addition to fostering and implementing corporate culture based on the Kao Way, we are actively working to create an environment that leverages autonomy and diversity of our employees and allows them to work energetically.

Our cross-organizational activities, based on free and open-minded communication, are an indispensable element in revitalizing our organization, creating opportunities to pursue new challenges and creating a corporate culture for nurturing our employees. Kao is continually promoting innovation and improvement activities through cross-divisional projects.

Furthermore, our senior management and employees are engaged in passionate and open-minded discussions on the present and future state of the company in places for direct dialogue, such as the Kao Forum.

Cultivation of Leaders who Realize the Vision by 2030 and Lead the Way in Changes

In these times of turbulent change, cultivating leaders who promote creative innovation is essential. We have established leadership values as behavior guide required for leadership, and use these values to carry out evaluations, cultivation and promotions. We conduct 360-degree evaluations based on these leadership values as an opportunity for leadership development. Moreover, during training we emphasize opportunities to learn about business environmental changes as well as rules and principals. To this end, we implement the Global Leadership Development Program, which aims to use the latest external knowledge and fusion of participants’ wisdom. And for leaders who will lead the next generation, in collaboration with business schools globally, we aim to provide a place to explore their own nature and deeply consider their own leadership through discussions with leading experts in various fields as well as with business leaders from all over the world, and to create awareness for leading changes.
Kao’s Compliance Activities

**Plan**
- Propose plans for appropriate and effective activities based on the following two points:
  - Feedback and evaluations received from check items on the right.
  - Social expectations and trends.

**Action**
- Examine and address issues that need to be improved upon based on feedback from check items on the right and evaluations, etc.

**Check**
- Respond to revisions made to BCG and other guidelines and implement training based on action plans/appropriately operate compliance hotlines.

- Internal checks
  - Issues discovered through feedback received from the Board of Directors as well as through reports and compliance hotlines.
  - Investigations by the Department of Internal Audit.
  - Feedback from roundtable discussions and activities to solicit employee opinions.

- External checks
  - Third-party evaluations, response to outside evaluating institutions, feedback from this response.

**Do**

Taking the recent cases of Kao and other companies, we aim for a more open culture and friendly workplace through our compliance activities.

Yoshihiro Hasebe
Representative Director, Senior Managing Executive Officer
Senior Vice President, Research and Development, Global
Senior Vice President, Strategic Innovative Technology, Global
Responsible for Compliance

Basic Views
Kao regards Integrity, the value inherited from its founders, as the starting point of its compliance activities. We strategically strive to thoroughly ensure compliance mainly by instilling the Kao Business Conduct Guidelines (BCG), which is our code of conduct. We regard fostering compliance awareness by each of our employees as the key to the company’s management foundation. Creating a corporate culture which not only prevents law and regulation violations, but is open enough that offenses are immediately reported and rectified, and a friendly workplace where human capital is maximized, is indispensable for K20 and our vision by 2030. Through these activities, by fostering and establishing compliance awareness, we aim to maintain and make necessary improvements for a sound corporate culture.

Compliance Promotion Structure
We have a group-wide structure that ensures the implementation of PDCA. To begin with, we have established the Compliance Committee, chaired by a Representative Director and made up of representatives from each relevant division and affiliated company. Based on the mid- to long-term and annual activity plans reviewed by the committee, the committee works to implement 1) the establishment and revision of not only BCG, but internal rules pertaining to anti-bribery, avoiding conflicts of interest, corporate entertainment, gifts, and celebration or condolence packages, 2) education activities inside and outside of Japan and 3) appropriate responses to compliance reports and consultations. Furthermore, it is committed to improving its activities through periodic reports presented to the management, the board of directors and so on.
Working toward Profitable Growth

While focusing on reducing serious compliance risks to achieve K20 success, through cooperation with related departments in each of our group companies, including legal affairs, human capital development, corporate culture and literature, crisis management and Kao Global Internal Audit, we carry out the following activities.

1. Thorough Permeation Activity based on PDCA Activity

- We regularly hold study sessions, led by external instructors, for our executives.
- Through divisional training lectured by each executive officer, we strive to create compliance awareness not only in each executive, but in each employee.
- We regularly make revisions to respond to changes in international affairs and social environments, along with SDGs and other societal expectations and carefully conduct education and permeation activities aimed at our group employees.

2. Activities Focused on Reducing Serious Compliance Risks

- We focus on preventing compliance violations, through training, making case studies available internally and so on that cover topics for which we have received many reports.
- We promote activities for compliance with laws and regulations by clearly defining which departments are responsible for relevant laws and regulations. Regarding important laws and regulations, we engage in monitoring the implementation status of annual action plans by each responsible department.
- Our activities to reduce risk include implementing countermeasures against possible business risks regarding social media, data tampering, etc., which have been designated serious compliance risks in a risk survey.
- These activities have been put into practice by the group within Japan and are being developed for enactment by the group as a whole in the future.

3. Monitoring

- We share issues identified from analysis of compliance reports and consultations with the management and corporate auditors every quarter and address them in future activities.
- Through employee opinion and compliance awareness surveys conducted biannually, we collect information on on-site issues and concerns, and plan and implement improvement measures from a compliance perspective.
- We get feedback on our compliance activities and take them into consideration for future activities.
- We use responses to CSR surveys from external evaluation institutions and our business partners as opportunities to confirm whether our activities are appropriate in light of societal expectations, and for deciding on future activities.

Thirteen consecutive years on the “World’s Most Ethical Companies®” list

We regard the World’s Most Ethical Companies® as an important indicator of compliance activity success. This award is an element of the evaluation process of our executive officers. We regard it as an indicator regarding whether Kao’s compliance activities meet the societal expectations. Taking advantage of our continuous selection for this prestigious award. We will continue to strategically strengthen our compliance activities.

* “World’s Most Ethical Companies®” and “Ethisphere” names and marks are registered trademarks of Ethisphere LLC.
Risk and Crisis Management Strategy

Strategic management of significant risks and crises enables Kao’s sustainable growth.

Shigeru Ueyama
Managing Executive Officer
Senior Vice President, Corporate Strategy, Global

Basic Views

Kao regards the potential negative impact on the achievement of its management targets and business activities as a “risk” and the materialization of such risk as a “crisis.” We appropriately manage the various risks and crises that can occur throughout its overall business activities in accordance with the response priority detailed in the Kao Risk and Crisis Management Policy (1. Protection of human lives 2. Environmental conservation 3. Continuation of operation 4. Protection of assets).

To promote K20 and achieve our vision by 2030, we are stepping up our risk and crisis management through the following measures.

1. Clarifying significant risks to be handled by management and building a corresponding response structure

We designated risks that would particularly have a significant impact on our management and which we need to strengthen our response to, as “corporate risks.” Executive officers are responsible for handling these risks.

2. Expanding the scope of target risks

Risk management, which has mainly focused on operational management risks, has been expanded to strategic and reputation risks* from 2015, and we are promoting our responses to them.

* Risks that inflict loss on a company from decline in corporate trust and brand value due to the spread of critical evaluations and rumors against the company.

3. Strengthening response to the materialization of risks

Taking it for granted that risks are revealed, even if they should become apparent, we are strengthening our response structure in times of crisis so that we are able to take prompt and appropriate measures.

In line with the direction of strengthening this structure, we establish main themes each year and conduct related activities. In FY2018, we steadily implemented priority measures aimed at strengthening our practical ability to respond to corporate risks, strengthening management of significant risks at our operations outside Japan, and increasing employees’ awareness of risks among other measures to strengthen the Kao Group’s overall management of risks and crises.

Risk and Crisis Management System

The Risk and Crisis Management Committee, held 4 times a year, chaired by an executive officer in charge of risk and crisis management, establishes a system and operating plans for risk management. Each division, subsidiary and affiliated company ascertains and evaluates risk based on these operating plans and conducts risk management by formulating and implementing appropriate countermeasures.
In addition, we have established the Risk and Crisis Management Promotion Council, held once a month as a subordinate organization of the committee, which discusses proposals with the committee and promotes committee decisions.

Furthermore, themes and persons in charge of material risks (corporate risks) to be managed by management are decided through the approval of the Management Committee, based on interviews with management, internal risk surveys (conducted for each division and subsidiary), and others.

Executive officers who are responsible for corporate risks organize response teams, formulate and implement countermeasures, and strive to comprehensively strengthen risk response. The progress of corporate risk activities is reviewed by the Risk and Crisis Management Committee, and is reported or discussed at the meetings of the Management Committee or the Board of Directors on a regular basis (once a year) as well as in a timely fashion.

Corporate Risks

Anxieties over climate change, natural disasters, water depletion and biodiversity have caused a rise in awareness among consumers and customers and tightened environmental regulations. Additionally, with the development of information and communications technology and the widespread use of smartphones in society in recent years, social media usage has prevailed and e-commerce business has rapidly grown, making great changes in the way people communicate and in their purchasing behaviors.

Based on these changes in business environment, we select themes of corporate risk and review them annually. In FY2018, we further strengthened our practical ability to respond to risks by upgrading our response structure and conducting response drills for the following corporate risk themes.

- Large-scale earthquakes and other natural disasters
- Personal information protection
- Pandemics
- Exchange rate fluctuations
- Reputation
- Response to product quality issues
- Change in structures of sales channel
- Risks associated with the use of digital media
- Risks related to business in Asia etc.

Strengthening Significant Risk Management at Overseas Bases

Regarding risk management at the subsidiaries outside Japan, their management is promoting risk management by selecting significant risks and examining countermeasures against them.

In FY2018, we established PDCA cycle for risk management and strengthened response through coordinating risk management at each of our subsidiaries with activities regarding corporate risks and our responsible department in Japan.

Emerging Risks

In order to contribute to sustainability of the world, we are pushing forward measures on resource circulation, climate change and chemical substances. Due to the ocean plastic waste problem in recent years, global monitoring the use of plastics in products, product containers and packaging have been intensified, and regulations in each country on the use and disposal of plastics have been tightened. Moreover, international trade conflicts have also developed in other fields including technology, and are now more complex.

Accordingly, it is now necessary to pay attention to its impact on business activities not only as a result of increasing raw material costs, but tightening regulations.

We are making more efforts to respond to these changes in terms of both opportunity and risk.
Overview of Kao’s Business

Consumer Products Business

Cosmetics Business

In order to respond to the diverse beauty values of each consumer, Kao is refining the characteristics of our brands and delivering skin care and make-up products to consumers all over the world.

Main brands sold in Japan include those centered around Skin care products like est, Sofina ip, Curél, freeplus. Brands focusing on make-up products include RMK, SUQQU, Primavista, COFFRET D’OR, and KATE. Additionally, high-prestige brands like SENSAI and Molton Brown in Europe, or freeplus in China, are widely used by many consumers world wide.

Skin Care and Hair Care Business

Kao delivers Skin care products like facial cleanser, body cleanser, sunscreen, and body lotion as well as Hair care products such as shampoo, conditioner, styling products, Hair coloring products, others to people all over the world so that they are able to express their desired personalities. By these products, we contribute to the realization of truly healthy, beautiful skin and hair. Our major brands include the Skin care products like Bioré and Jergens, along with Hair care products like Merit, Essential, Liese, Cape, Rerise, John Frieda, and Success. Our brands for Hair salons include Goldwell, Oribe and KMS.

Chemical Business

The Chemical Business globally offers a wide range of Chemical products, including Oleo chemicals made from natural fat and oil, Performance chemicals such as surfactants, and Specialty chemicals including toner and toner binders for copies and printers. In addition, with the environment as one of our business themes, we aim to contribute to a sustainable society through two approaches, “green innovation” and “eco technological solution.” “Green innovation” is developing unique alcohol derivatives, secondary derivatives, as well as biochemicals made by biorefineries as a growth engine. “Eco technological solution” is developing environmentally conscious innovations in ink and solutions in response to the environment, environment-
Human Health Care Business

Kao delivers Sanitary products which are gentle on the skin because they are generated from Kao’s unique nonwoven fabrics and processing technology, along with functional beverage promoting new health values and products that support healthier and more comfortable daily lifestyles including toothpaste and bath additives.

Major brands include Laurier sanitary napkins, Merries baby diapers, Relief adult diapers, Healthya functional beverage, Clear Clean, PureOra, and Deep Clean toothpastes, toothbrushes and mouthwash, Bub bath additives, and MegRhythm, thermo products.

Fabric and Home Care Business

Based on quality and function founded on essential research, Kao creates and markets products in response to changing consumer values and strive to create moments in everyday life that embody a feeling of cleanliness and beauty for as many people as possible. Major brands include laundry detergents Attack, Newbeads and Emal, fabric softener like Humming and Flair Fragrance, Haiter bleach, CuCute dishwashing detergent, Magiclean household cleaners, Quickle Wiper household wipers and Resesh clothing fabric and air refresher.

friendly solutions in the fields of electronic materials and infrastructure as a growth engine.

Additionally, these products contribute to enriching the lives of people in a wide range of industrial fields such as household and personal care, pharmaceuticals, information materials, electronics, and civil engineering and construction.
Consumer Products Business

With a sincere approach to our consumers, the creation of products that are truly needed by society enables Kao to create value and achieve profitable growth.

Tomoharu Matsuda
Director, Managing Executive Officer
President, Consumer Products, Global

The Social Situation Surrounding the Kao’s Business and Consumer Trends

In FY2018, the Japanese market faced severe heat waves and numerous disasters, but both markets for household and personal care and cosmetics grew year on year, and have remained solid.

Due to uncertainty about the economy’s future in light of influence by international trade conflicts, Asia faced a weak currency exchange, which is slowing down its growth rate even though the market is experiencing growth. In the skin and hair care markets in the Americas and Europe, because of the natural and organic boom, the number of products with high unit prices has increased, leading to market growth.

Future concerns over climate change and an aging society will continue to increase, and thus the demand for secure and safe products is growing. Furthermore, aspirations toward sustainability have taken root.

As digitalization advances continue, consumers have come to search for and transmit information themselves, invest aggressively in themselves and aim for self-actualization.

As the use of SNS has spread and communication method leadership has shifted drastically from manufacturers to consumers, there has been a continuing shift toward diversified and high-value-added products.

In the purchasing, e-commerce enables consumers to purchase the amount they want whenever they want when searching for products. In physical stores, they have made service function enhancements, such as offering product experiences, cashless shopping and speedy delivery and challenging new sales methods as the speed of consumer purchasing behavior changes continues to accelerate.

Trends in Net Sales and Operating Income

<table>
<thead>
<tr>
<th>Net Sales</th>
<th>1,232.9 billion yen (+1.4% year-on-year/+1.6% on a like-for-like basis*)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Income</td>
<td>175.7 billion yen (+2.7 billion yen year-on-year**)</td>
</tr>
<tr>
<td>Operating Margin</td>
<td>14.3% (+0.1 percentage points year-on-year)</td>
</tr>
</tbody>
</table>

*1 Like-for-like growth rates exclude the effect of translation of local currencies into Japanese yen.
*2 The sales organization of Kao’s Consumer Products Business in Japan was reorganized from FY2018. The operating income for FY2017 was restated accordingly.
Opportunities Taking Advantage of Kao’s Strengths and Response to Risk

**FY2018 Results and Issues**

With the new global brand portfolio strategy in the Cosmetics Business, Kao’s business direction was set, and with efficient management the year showed much improvement regarding profits.

The Cosmetics Business in Greater China proved to be very strong in sales, and sales of freeplus, Sofina makeup base and UV care products, as well as Curél increased significantly. In addition, due to the severe heat waves in Japan, the Skin care products in Japan grew sharply, mainly led by seasonal products. Much like within Japan, Bioré UV has expanded even further in other parts of Asia where needs for products capable of blocking ultraviolet rays are rising.

On the other hand, following the price decline of parallel import goods, sales of Merries slowed down in the Chinese e-commerce channels, resulting in a decline in sales in Japan and Asia. Moreover, the Fabric care products faced struggles due to rising raw material costs and drop in retail price.

In FY2018, we actively proposed high-value-added products for small-mass markets. We accelerated our global asset utilization strategy by launching Rerise, the innovative next generation of gray hair care, in Japan and elsewhere, along with Jergens US hand and body lotion, US Bioré facial cleanser and Guhl hair care line, which has a long history in Germany.

In the Consumer Products Business in the Americas and Europe, though Jergens remained solid, products similar to Bioré pore cleansers were launched one after another, affecting sales. In the hair care market, the launch of small-mass brands in last fiscal year was also remarkable, further promoting market segmentation.

In order to strengthen US business in the future, we welcomed the high-prestige brand Oribe in salon business domain and Washing Systems, LLC into the group in Professional-use laundry business domain.

**Taking Advantage of Kao’s Strengths**

With Kao’s technology innovation capabilities as its core, we are revitalizing our Yoki-Monozukuri and making valuable product offerings that are truly useful for consumers.

In 2019, as needs for blocking ultraviolet grow year after year, we launched a revolutionary UV care products that thoroughly protects skin by blocking ultraviolet rays up to the micro level. At the same time, we launched high-value-added UV care products that are able to offer great protection even under high temperature and humid environments in East Asia.

In April 2019, changing our views regarding laundry detergent thus far, we made an innovative proposal named “zero clean”, where neither dirt, detergent residue, nor smells would be left on clothing.

**Offerings on Social Issues**

Based on our ESG activities in 2018, especially regarding plastics waste problems, we are strongly promoting Monozukuri from a 4R-focused (reduce, replace, reuse, recycle) perspective. Especially when it comes to the challenge of considerably reducing amount of plastic containers, we offered the Raku-raku Eco Pack Refill and a cartridge-type Smart Holder instead of conventional refill containers, and will continue to make more advanced offerings in the future.

We will continue to strengthen ESG management through each brand, and through new marketing efforts to consumers in the digital age, we are working to ensure customer satisfaction with the innovative value created by Yoki-Monozukuri.
Offering Solutions to Social Issues

Through beauty, the Cosmetics Business engages in social value creation with the ability to offer moments of joy in daily life. By managing our business with an ESG focus, Kao is contributing to realizing a society in which fulfilling lives are possible for all, throughout the world.

In promoting the use of environmentally conscious, renewable resources in our ingredients, containers, and packaging, the use of renewable energy in production and distribution processes, and waste reduction in the use stage by consumer, Kao makes contributions to the sustainability of the world across the value chain.

Toward 2020 and beyond

While offering products that combine our proven quality, made possible by our industry-leading expertise in the area of skin science and beauty-enhancing qualities with emotional and sensory appeal, we aim to build on the distinctive identities of each of our brands and create a global presence for our businesses. We will engage in creation of strong brands by continuing to offer consumers exciting brand experiences. At the same time, Kao will seek out various growth opportunities from the increasing cross-border exchanges of people and information as well as new digital technology to lead cutting-edge business operations.

Strategy

Establishment of the New Global Portfolio

Kao established the New Global Portfolio, consisting of five businesses in the Cosmetics Business, in May 2018.

For the 11 brands selected as global strategic brands (G11), Kao will actively pursue expansion of the areas in which they are offered. Meanwhile, by also strengthening our travel retail business, Kao will accelerate their development in Japan and elsewhere in Asia and in Europe. Kao has designated eight regional brands (R8) for priority development mainly in Japan and will concentrate investment in them to support their development.

Reorganization of counseling and self-selection brands

In Japan, Kao will drive creation of strong brands with clearly redefined brand positioning. Kao will reorganize its existing brands into counseling brands, which are sold via beauty consultants who have received specialized education, and self-selection brands, and revise how the brands are produced and sold.

Management system reform

Kao is introducing a brand team system to better respond to the fast pace of change in the business environment. The brand teams will implement the Plan, Do, Check, Action (PDCA) cycle in more adoptable and fast cycles. Authority will be delegated to brand team leaders, who will conduct target marketing at a brisk pace.
Offering Solutions to Social Issues

The impact on the global environment of the excessive use of plastic is a source of concern. Kao has developed the new Raku-raku Eco Pack Refill container as well as the Smart Holder, which allows consumers to insert a pump directly into Raku-raku Eco Pack Refill products and use them, with considerations for both the environment and ease of use. These innovations are designed to reduce plastic use, reduce CO₂ emissions across the lifecycle from production to disposal, and reduce waste of residual product in containers to contribute to the sustainability of society.

Strategy

Skin Care Business
Kao will strive to expand our business fields with bold moves via development of new technology to address environmental stressors that affect skin, centered on UV care and deodorant, and to meet needs in the field of hygiene in addition to reinforcing our unique positioning and further enhancing our high-value-added offerings in our core businesses based on cleaning.

Hair Care Business
In addition to universal hair care needs, Kao will revitalize our mass brands by offering value propositions for daily life that precisely target the trends of the times, make new value creation offerings that meet personalized needs, and actively pursue development of high-value-added products. In our hair salon business, Kao intends to accelerate business growth through differentiation based on original Kao technologies and expansion of its brand portfolio.

Business area expansion
The global skin care brands Biore and Jergens will evolve to facilitate their global growth as Kao develops their product lines to drive expansion into the countries in which they are not offered. While maintaining the high growth of Oribe, which Kao acquired in FY2018, in the premium segment, Kao will achieve synergies between Goldwell and Oribe to accelerate their global development.

Toward 2020 and beyond

Kao will develop unique products with high-value-added to drive our global expansion as a highly profitable business. With a sharp focus on consumers’ sense of toward beauty and changes in lifestyle habits, Kao will lead market invigoration by accelerating the shift toward delivering high-value-added products and making distinctive and attractive offerings unique to the Kao. Specifically, Kao will launch and develop distinctive, appealing new products that are a half step ahead of the times and engage in marketing activities that stay ahead of consumers’ changing purchasing behavior. Kao will also implement reforms to its sales methods to advance its business operations.
Offering Solutions to Social Issues

Kao will support people around the world to enjoy improved health through activities focused on mothers and infants in maternity wards, first menstrual education in elementary schools, and enlightenment on adult diapers and oral care in hospitals and nursing home. We will also strive to have communities and our employees enjoy improved health through efforts that partner with government agencies and other companies.

Strategy

Strive to strengthen people's vitality by offering advanced, high-value-added products on an ongoing basis.

With the aim to be the most “gentle on the skin” diaper in the world, Merries contributes to the healthy physical and emotional development of babies. We aim to help solve health and wellness challenges at each life stage with products such as MegRhythm, which uses original Kao thermo technology, Healthya products contributing to wellness for people with visceral fat and high blood pressure issues and advanced Oral care products contributing to a lifetime of teeth and gum health.

Kao is accelerating our global expansion with evidence-based, high-value-added products offering unique health care propositions. First, led by our Merries, Laurier and MegRhythm brands, Kao intends to offer products with greater customization to fit local health care needs while collaborating with and creating a network of universities, health care professionals and other experts in each country.

Based on consumption patterns and distribution conditions in countries, Kao will work to expand its offered products and the countries where they are offered through strategic use of distributors and growing e-commerce channels.
Offering Solutions to Social Issues

Some countries and regions are projected to face future challenges including falling birth rates, aging populations, and population declines. Kao believes it is its mission to accurately understand consumers’ changing attitude and habits in the area of laundry, cleaning, and other housework, and to take the lead in helping to solve various social issues. Kao has to date taken actions to reduce our environmental impact at each stage of the product lifecycle, such as by making products more concentrated so that their containers can be more compact and by increasing the use of refill and replacement products. Kao will contribute to the sustainability of the world with the goal of further reducing the amount of plastic Kao uses.

Toward 2020 and beyond

People’s attitude and habits on the housework such as laundry and cleaning are undergoing major transformation due to the greater diversity of living environments and lifestyles as well as other social factors. Countries and regions also have a range of emerging needs as standards of living improve. While staying attuned to what different consumers want in life, we will use the insights we gain from them to take the lead in activities to solve various social issues. By offering products and solutions with high-value-added that enable anyone around the world to live each day in greater cleanliness and comfort, we contribute to realizing greater contentment in daily life.

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Some countries and regions are projected to face future challenges including falling birth rates, aging populations, and population declines. Kao believes it is its mission to accurately understand consumers’ changing attitude and habits in the area of laundry, cleaning, and other housework, and to take the lead in helping to solve various social issues. Kao has to date taken actions to reduce our environmental impact at each stage of the product lifecycle, such as by making products more concentrated so that their containers can be more compact and by increasing the use of refill and replacement products. Kao will contribute to the sustainability of the world with the goal of further reducing the amount of plastic Kao uses.

Toward 2020 and beyond

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Sales Strategy

Viewing changing circumstances surrounding our business as growth opportunities, build a new sales structure and sales channels aiming to achieve further growth.

Toshiaki Takeuchi
Representative Director, Senior Managing Executive Officer
Representative Director, President, Kao Group Customer Marketing Co., Ltd.

Sales Structure Innovation

The environment in which the Sales Division operates has experienced major changes over the last several years. In the retail industry, market domination by leading mass retail chains has grown stronger in part through M&A, and more companies are structuring their business operations to be led by the chain headquarters. Consumers’ purchasing behavior has also shifted sharply to digital platforms as mobile devices have become ubiquitous. Distribution channels have seen major growth in e-commerce, which is also influencing the store and product strategies of companies in the retail industry. For instance, many companies that operate physical stores have recently been implementing strategies to differentiate themselves from their competitors, including by developing stores specializing in beauty products and by reinforcing their private brands.

The Sales Division has traditionally covered all areas of Japan using a business model that provides products for store display and attentive follow-up at individual stores of retail companies, and has leveraged this business model in the so-called mass marketing sector. We are now adjusting this business model in light of the changes that are taking place today.

While adapting to these changes and earning the support of consumers, we will build a new business model that enables continuous growth at retailers and at Kao.

E-commerce Strategy

As a new initiative for the e-commerce business, in FY2017, we started having retailers solely engaged in e-commerce carry our Cosmetics products. Going forward, we will actively provide products, services and information desired by e-commerce users, purposefully developing exclusive online product offerings in larger sizes corresponding to internet user preferences to purchase large and bulky items. We will also generate interest online by releasing information before launching products designed for niche markets that are better able to capitalize on the strengths of e-commerce, such as personal Skin care and Hair care products.

We will implement a similar strategy outside Japan as well. The Chinese market, in particular, is undergoing major transformations in consumer purchasing behavior and its distribution structure as e-commerce expands and the economy becomes increasingly cashless. E-commerce is also receiving more attention across Asia. Along with moves by leading Chinese e-commerce platforms to expand their regions of business, companies based in the Americas and Europe, including local companies in various countries are enjoying brisk e-commerce business conditions throughout Asia.

We are building out our sales structure using
the Chinese subsidiary and moving quickly to adapt all of our brands to the e-commerce platform and develop digital marketing activities. We will also fully undertake export sales for China using cross-border e-commerce to provide opportunities to purchase baby diapers with peace of mind. In addition, we are preparing sales structure and products to capitalize on e-commerce growth as a new growth opportunity for local companies in other Asian countries going forward. We will do this by adding new products to our portfolio and by drawing on our e-commerce experience in China and Japan.

Sales Strategy in Physical Store Channels

In addition to e-commerce, we will also further deepen cooperation with retailers whose main business consists of brick-and-mortar stores. The environment in which retailers operate is changing. Viewing these changes as opportunities, we will mobilize the comprehensive strengths and specialized capabilities of the Kao Group to propose campaigns and in-store activities customized to their specific needs. This will serve to resolve issues and attract consumers through collaboration and co-creation with retailers.

Although e-commerce is predicted to continue growing, circumstances in Japan are also said to be more amenable than in other countries to consumers buying products in brick-and-mortar stores. Consumers also have needs that are still difficult to satisfy via e-commerce. In the cosmetics field for example, consumers like to purchase products after testing them on their skin and checking the color in person.

There are also more efforts to connect online and in-store experiences instead of keeping them separate, for example campaigns that link in-store promotions with online activities, and pop-up stores that give consumers in-person product and brand experiences. Going forward, we believe that there will be more of these new ways to enhance the consumer experience and optimize business operations that cross boundaries between the real and virtual worlds.

While the means may differ, the principle of listening to consumer feedback remains the same for both our online and in-store sales strategies. We have proposed sales floor designs conducive to product selection and sales methods designed for consumers after gaining a scientifically based understanding of consumer purchasing behavior and preferences. By creating new strengths adapted to the changing market without losing our Consumer-Driven approach, which forms part of our corporate philosophy, we will continue building a business model that allows us to harness synergies between online and brick-and-mortar commerce.
Maximizing use of our environmentally conscious technologies, we will continue contributing solutions to social issues toward realizing a sustainable society while achieving profitable growth.

Masahiro Katayose
Executive Officer
President, Chemical Business, Global

The Social Circumstances and Customer Trends Affecting Business

In the short term, changes in social circumstances surrounding the Chemical Business include increased trade friction and tighter environmental regulations in China. While fully recognizing both the positive and negative aspects of these changes and monitoring trends, it is essential that we adapt to these changes appropriately.

In the mid- to long-term, various changes in the global environment related to climate change, water resource depletion, and biodiversity, as well as tighter environmental regulations to address them that demand an ESG approach by companies, will take on greater scope globally.

For instance, customers will also want to use sustainable palm oil produced with consideration for biodiversity and human rights. At Kao, we already use RSPO-certified oil for the palm oil and fat used as raw materials in fatty alcohols we manufacture and use. We are also working to ensure traceability of the oil. In consideration of the impact of using edible materials for industrial purposes, we are also conducting research on manufacturing fatty alcohols using inedible algae as the raw material.

Furthermore, besides our core technology in surface science, we have technologies for catalysts that are key to manufacturing natural fat and oil derivatives, for enzymes used in manufacturing biochemicals, and for polymer design and surface control necessary in solutions offering reduced environmental impact. As such, we believe that heightened environmental awareness in the international society will facilitate expansion of our business.
Opportunities taking advantage of Kao’s strengths and risk response

The Chemical Business possesses one of the largest production scales in the world for natural alcohol, and broadly conducts business focused on natural alcohols and their derivatives as well as a wide range of surfactants for global customers and industries. Meanwhile, we also offer customized products to meet customer needs and resolve issues in the information materials fields, leading examples of which are the toners and toner binders for copiers and printers. The Oleo chemical business, whose main ingredients are natural fats and oils, has become increasingly commodified after the participation of plantation companies. Sharp fluctuations in the price of natural oils and fats have increased the risk of volatility in business profitability to the point where stable growth is an issue. Keeping in mind our ESG approach, we have therefore diversified the oil and fat raw materials upstream while building up the development and production of distinctive oil derivatives and surfactants downstream. In addition, we will expand the fields of our technical development and use biorefinery technology to conduct new material development using renewable biomass resources as raw materials. And in the information materials and Performance chemicals, we will offer solutions leading to increased customer value after understanding their needs and issues from the standpoint of reducing environmental impact, and develop innovative products together with customers that offer greater customization.

Chemical Business Strategy

Focusing primarily on the environment part of ESG, the Chemical Business seeks to provide solutions to issues that customers and industries are facing by actively investing in technology innovations and M&A. We have achieved profitable growth as a result, and define our basic strategy as contributing to the sustainability of the world. Specifically, we will increase our ratio of environment-related products among total sales from the current 70% to 80% or more using two approaches.

The first approach is Green Innovation. In addition to standard development, we are conducting development to manufacture the world’s first green derivatives with new functions as well as world-first biochemical development.

The second approach is Eco Technological Solutions. Using Kao’s expertise in surface science, we are focusing on innovative product development offering reduced environmental impact. An example of this is water-based pigment inkjet inks that use our pigment nano dispersion technology. This enables high-resolution printing with water-based ink on plastic film, which in the past had been difficult to realize. Because solvents are not used, the inks produce almost no volatile organic compounds (VOCs), which also greatly reduce negative impact in work environments. The Consumer Products Business also uses the inks, enabling synergies to be generated between the Chemical and Consumer Products Businesses as well. With environmentally conscious solutions in the electronic materials and infrastructure fields also serving as growth engines, we will increase the presence of the Chemical Business by making contributions to solving issues faced by society, customers, and industries.
Creating Strong and Distinctive Brands

The growth of the Cosmetics Business is crucial to achieving K20 and the vision of the Kao Group beyond that. We are undertaking an ongoing series of structural reforms aiming to achieve further growth in Asia and Europe.

The Cosmetics Business has so far been divided into five businesses (Kanebo Cosmetics, Sofina, Curél, e’quipe and Molton Brown), each with independently-run business operations. This has now resulted in 49 different brands at the beginning of 2018, and strategic brand growth has emerged as an issue. Taking a broad view of the business, each brand’s role and growth prioritization has become vague, and brands are not able to fully capitalize on the comprehensive strengths of the Kao Group.

New Global Portfolio

The New Global Portfolio concentrates management resources in selected strategic brands to refine them into strong and distinctive brands. We will capture cosmetics demand in rapidly expanding Asian markets, develop the brands to be globally competitive, and build momentum for their global development.

Specifically, we have defined 11 global strategic brands “G11,” which include a new brand scheduled for launch in 2020, and 8 regional strategic brands “R8.” We will focus on global development for the G11 and development primarily in Japan for the R8.

The G11 were selected for their current brand power and profitability as well as their potential for...
global growth. In the challenging prestige segment, accelerated global development of the SENSAI brand is major pillar of our strategy. The SENSAI brand is available in more than 40 countries and regions, many in Europe, and combines refined Japan’s sense of delicate harmony with the latest dermatological science from Japan. The brand epitomizes the future vision for the Cosmetics Business.

The RMK and SUQQU brands mainly focused on makeup products are achieving success in the prestige market, and developing strong prestige skin care brands will be key to the future growth of the Cosmetics Business. We are planning the groundwork for this major growth by launching SENSAI in Asia, continuing the shift to high-value-added offerings for the est and KANEBO brands and

expanding the countries in which they are offered, and strengthening the travel retail business. Approaches to the rapidly expanding middle class in Asia will be the largest driver of growth. We will leverage the Curél, KATE and freeplus brands to capture this demand.

In our business in Japan, we will revise our existing brand development strategy implemented for individual distribution channels such as department stores, specialty stores, and drugstores and reorganize the brands into the two groups of “counseling brands” purchased after receiving a consultation and “self-selection brands” that consumers select and purchase by themselves. Through this, we will be able to better highlight the distinctive identities of each brand and make them stand out.

In our organization, we have also reformed management system and introduced brand team system for each brand and speed up the decision-making process to quickly respond to the changes of the times and realize a Cosmetics Business with a distinctive global presence.
**Special Feature**

**Advanced Technology Strategy**

**Digital Transformation**

The Strategic Innovative Technology Team (SIT) was established in April 2018 to promote a strategic digital transformation (DX) and to realize business transformation and enhancement of operational efficiency through the effective utilization of cutting-edge technology. The essential value of AI- and IoT-based digital environments is their ability to connect to anyone, anywhere and anytime, at ultra-low cost and ultra-high speed. We will fully utilize Kao AI (i-Kao), which takes computers equipped with artificial intelligence (AI) capable of learning has them learn from the big data we possess, to realize discontinuous improvement of company productivity (value-added/labor time). The nine target DX fields are management, business, sales, research, supply chain management, logistics, finance, human capital and corporate identity (CI). The following four groups in SIT are implementing Kao DX.

**Efficient Utilization Group**

Leveraging digital technologies, this group plans and implements strategy and tactics to fundamentally improve efficiency in work processes. Existing data is integrated after formatting to improve its usability, and is converted into high-value-added information using advanced technology.

**Information Group**

This group proposes strategy and tactics from a comprehensive approach including real-world experiences in addition to using digital technologies to innovate communications with stakeholders (employees, customers, shareholders, society) inside and outside the group. It is forging relationships with and creating a network of outside content partners to develop information content aligned with the strategy and tactics.

**Business and Sales Group**

This group uses digital technologies to propose new businesses and new business models, and establishes faster product development processes suited to the business model.

**Monitoring**

This group is rebuilding our information system platform and introducing and implementing advanced information technology for the digital transformation. This will support the activities of the other three teams. By combining our core value of Yoki-Monozukuri with advanced technologies, we aim to enhance the level of our value propositions to all stakeholders and, in the long term, continue being a company where employees find fulfillment in their work and from whom outside groups anticipate good things.
Specific Examples

Efficient utilization field

In the research field, at the end of last year we began operation of a system that uses AI to conduct searches more efficiently. This system captures not only reports, patents, formulations, and trial results but also unstructured data, namely product information including pharmaceutical affairs and information related to consumer consultations, to retrieve comprehensive information needed for development at one time. This has greatly reduced the time taken by routine tasks and dramatically increased the speed of development.

Related to human capital, we are in the process of building a new integrated system that will centralize a number of currently decentralized systems for performance evaluations, salary calculations, work attendance management and others, allowing them to be viewed and managed in one place. This will make promotions, which in the past have been decided based in part on personal judgments, to be based on objective standards that will better serve to promote diverse human capital.

Information utilization field

The way information has been communicated in the past has been independently managed by business divisions, as has app provision, and cooperation and cross-use by other divisions have at times been lacking. We intend to consolidate our systems for customer relationship management (CRM) that have been implemented individually in this way into one system able to customize information received from and sent to individual stakeholders so that only the information that is truly needed is communicated.

Business and sales fields

Using AI, we will redesign how we conduct market research, product development and sales leveraging online sales and social networks. We will also strengthen our digital advertising not only to communicate product information but also to precisely provide information on research leading up to product launch and details of technical development to the parties that need it. We are developing new virtual communication methods as tools to efficiently communicate product information and offer completely new and appealing product value experiences.