堺化学工業株式会社

Sakai Chemical Industry Co., Ltd.

Q2 Financial Results Briefing for the Fiscal Year Ending March 2022

November 29, 2021

Event Summary

[Company Name]	Sakai Chemical Industry Co., Ltd.	
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[Event Type]	Earnings Announcement	
[Event Name]	Q2 Financial Results Briefing for the Fiscal Year Ending March 2022	
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[Time]	15:30 – 16:27 (Total: 57 minutes, Presentation: 29 minutes, Q&A: 28 minutes)	
[Venue]	Webcast	
[Venue Size]		
[Number of Speakers]	2	
	Masaaki Yabe	President, Representative Director, Executive Officer
	Atsuya Nakanishi	Managing Director, Executive Officer

Presentation

Moderator: Thank you very much for taking time out of your busy schedule to join us today for the briefing on Sakai Chemical Industry Co., Ltd.'s 2Q Financial Results Briefing for the Fiscal Year Ending March 2022.

The time has arrived, so we will now begin the briefing session. My name is Moderator, and I will be the moderator for today's session. I'd like to thank you for your cooperation. This year's briefing will also be conducted through a live stream on the web.

As for today's schedule, President, Representative Director, & Executive Officer Yabe will begin by explaining the situation after the explosion and fire at the Yumoto Plant that occurred on May 11 this year.

Explosion and Fire Accident at the Yumoto Factory

1. Date and location of occurrence

May 11, 2021, Yumoto Factory zinc dust manufacturing plant

2. Casualties

4 workers of a subcontractor
seriously or lightly injured ⇒All have been discharged from hospital

3. Progress of the investigation by the Accident Investigation Committee

Established on June 5 with 3 experts invited from outside the Accident Investigation Committee has met 5 times to date.

The cause will be determined and a report compiled by the end of this year. We expect to announce it by the end of January next year.

4. Withdrawal from the zinc dust business

Annual sales of zinc dust for the fiscal year ended March 2021: Approximately 1.3 billion yen

5. Impact on consolidated financial results for the full year ending March 2022 (earnings before tax)

Expected to be approximately 300 million yen

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Yabe: My name is Yabe, the President. Thank you for your cooperation today.

We would like to express our sincere apologies to our shareholders and other stakeholders for the inconvenience and concern caused by the explosion and fire that occurred at our Yumoto Plant on May 11, 2021.

It has been about 6 months since the accident occurred, and I would like to briefly explain the progress that has been made since then. One injured person who was hospitalized has already been discharged and is on the mend.

In order to investigate the cause of the accident, an accident investigation committee was established on June 5 by inviting 3 outside experts, and the committee has held 5 meetings to date. We expect to be able to investigate the cause and compile a report by the end of this year and report it in January next year.

The amount of loss due to this matter is not expected to change significantly from the initially announced amount of approximately JPY300 million. We would like to ask for your understanding in this matter as we will continue to strengthen our safety management. That's all.

Key Points of This Briefing

■ Summary of Interim Financial Results for the Fiscal Year Ending March 2022

→ In terms of sales, each business, especially electronic materials, performed well. However, the revenue declined due to the application of new revenue recognition standards.

→ Operating income increased significantly due to strong performance, particularly in the electronic materials and organic chemicals fields.

→ Sales of cosmetics materials were weaker than in the same period of the previous fiscal year due to the continued impact of voluntary restraint on going out due to the spread of COVID-19.

■ Forecast for the Fiscal Year Ending March 2022

→ Electronic materials and titanium dioxide are expected to continue to perform well. At this point, we expect the results to be in line with the upward revision made in November of the current fiscal year.

→ We plan to pay an annual dividend of 70 yen per share. (Interim: 35 yen, Year-end: 35 yen)

* The interim dividend for the previous term was only 15 yen

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Moderator: Now, let's move on to the financial results briefing. As you can see on the slide, there are 3 points in the summary of financial results and 2 points in the earnings forecast for today's presentation.

Managing Director & Executive Officer Nakanishi, who is in charge of investor relations, will explain the details, and then President Yabe will explain the recent topics.

At the end of the session, there will be a question and answer period, and we will use the raise hand feature of the Zoom webinar to take your questions. Detailed instructions will be provided at the beginning of the question and answer session.

The meeting is scheduled to end at 4:30 PM.

Now, Executive Director Nakanishi, please.

Summary of Interim Earnings for the Fiscal Year Ending March, 2022 (YoY)

Monetary units: million yen

	2021.3 2Q		2022.3 2Q		Increase/decrease	
		Net Sales Ratio		Net Sales Ratio		
Net Sales	40,244	—	39,905	—	▲ 338	▲0.8%
Operating Income	1,597	4.0%	4,356	10.9%	2,759	172.8%
Ordinary Income	1,219	3.0%	4,599	11.5%	3,380	277.2%
Profit (loss) attributable to owners of parent	558	1.4%	3,180	8.0%	2,622	469.8%

◆ Sales

Sales increased, particularly in electronic materials.
However, the revenue declined due to the application of new revenue standards.

* Before the application of new revenue recognition standards: 47,484 million yen

◆ Operating income

Profits increased in every field other than hygienic products, led by electronic materials, resulting in a year-on-year increase of 172.8%.

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Nakanishi: My name is Nakanishi and I am in charge of investor relations. I'm looking forward to working with you.

First, I would like to provide an overview of our business results for the first half of FY2022. Sales for the period under review totaled JPY39.905 billion, down JPY338 million YoY, or 0.8%. However, this figure is based on the new revenue recognition standards, so under the old standards up until last year, the sales were JPY47.484 billion, or an increase of JPY7.240 billion, which is an 18% real increase.

Operating income was JPY4.356 billion, a significant increase of JPY2.759 billion, or 172.8%, YoY. Ordinary income was JPY4.599 billion, an increase of JPY3.380 billion, or 277.2%, YoY. Net income attributable to shareholders of the parent company was JPY3.180 billion, an increase of JPY2.622 billion, or 469.8%, YoY.

Net Sales and Operating Income by business

Monetary units: million yen

		2021.3 2Q	2022.3 2Q	Increase/decrease	
Chemical Business	Net Sales	36,299	35,809	▲ 490	▲1.4%
	Operating Income	2,290	5,101	2,811	122.7%
Medical Business	Net Sales	3,945	4,096	151	3.8%
	Operating Income	242	233	▲ 9	▲4.0%
Company-wide Expenses	Net Sales	—	—	—	—
	Head Office Expens	▲ 936	▲ 977	—	—
Total	Net Sales	40,244	39,905	▲ 339	▲0.8%
	Operating Income	1,597	4,356	2,759	172.8%

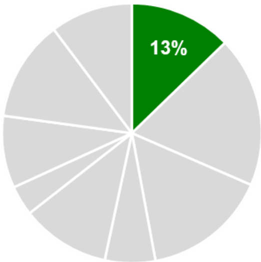
Next, I will explain sales and operating income by business segment.

YoY sales in the chemical business were JPY35.809 billion, a decrease of JPY490 million, or 1.4%. This is also due to the impact of the new revenue recognition standard, as I mentioned earlier. However, operating income increased by JPY5.101 billion, or 122.7%, or JPY2.811 billion.

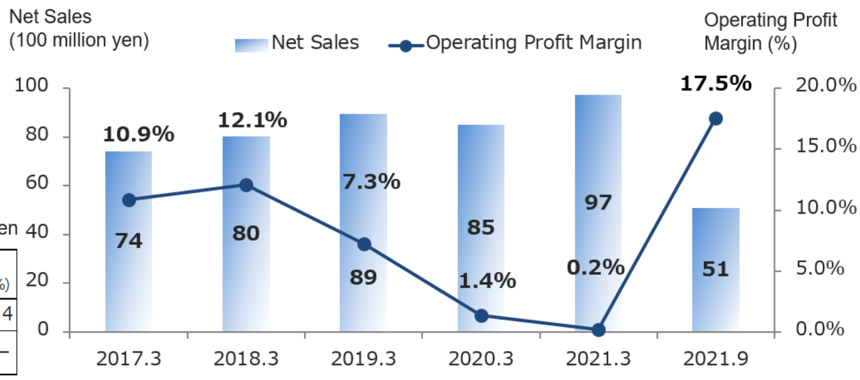
In the pharmaceutical business, as I will explain later, sales for the previous fiscal year were JPY4.096 billion, an increase of JPY151 million or 3.8%. Operating income was JPY233 billion, a decrease of JPY9 million, or 4%.

As for the head office department expenses, there was a slight increase in expenses to JPY977 million, or plus JPY41 million. This increase was mainly due to transportation costs associated with the increase in sales, but the increase was kept to a minimum by controlling travel and transportation expenses and other costs.

Chemicals



Electronic materials



Monetary units: million yen

	2020.9	2021.9	Increase Decrease(%)
Net Sales	4,525	5,086	12.4
Operating Income	▲ 117	892	–

Key points for the first half of the fiscal year ending March 2022

* Sales decreased by 1,022 million yen due to the application of the new revenue recognition standards.

- Both dielectrics (barium titanate) and dielectric materials (high-purity barium carbonate) for laminated ceramic capacitors for use in vehicles, 5G base stations, and telecommunications equipment performed well in general, and both sales and operating income increased.
- **Compared to the previous fiscal year, net sales increased by 561 million yen (+12.45%), while o perating income increased by 1,009 million yen.**

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I would now like to report on the performance of each sub-segment. The first one is electronic materials.

Continuing the strong performance from 4Q of the previous fiscal year, both dielectrics and dielectric materials performed well. Both sales and profits increased.

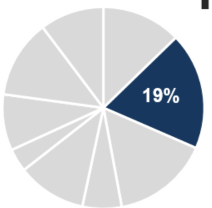
Before the new revenue recognition standard, sales increased by 35% YoY, which was strong across almost all end products, from automotive and 5G base station applications to general purpose consumer products, driving the Group's strong performance.

Compared to the same period of the previous year, sales increased by JPY5.086 billion, or 12.4%, plus JPY561 million, and operating income was JPY892 million, a significant turnaround. This is an increase of JPY1.009 billion.

Existing facilities are almost at full capacity, and the large drop in fixed costs per unit is the source of the V-shaped recovery in operating income.

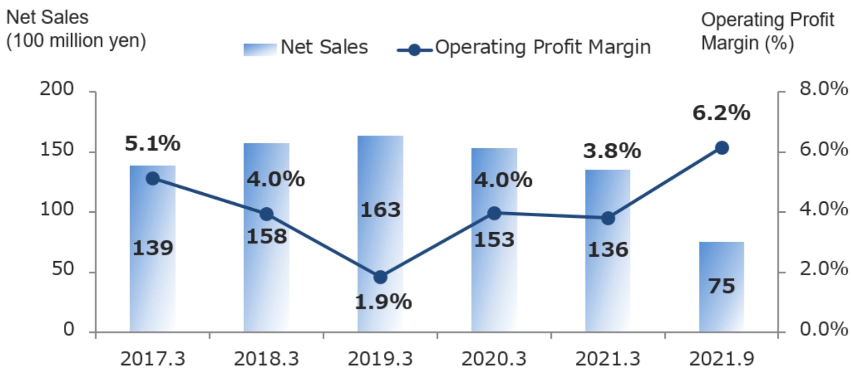
Titanium dioxide and zinc products

Chemicals



Monetary units: million yen

	2020.9	2021.9	Increase Decrease(%)
Net Sales	6,229	7,491	20.3
Operating Income	239	461	92.9



Key points for the first half of the fiscal year ending March 2022

*** Sales decreased by 87 million yen due to the application of the new revenue recognition standards.**

- Sales and profits of titanium dioxide increased due to strong sales for various applications, particularly for gravure inks used for food packaging.
- Sales and profits of zinc products increased due to strong sales of zinc oxide for tire applications, together with a sharp rise in the price of zinc.
- Sales and profits of ultra-fine titanium dioxide and zinc oxide for use in cosmetics decreased due to a drop in demand for cosmetics and sunscreens caused by city lock-downs and people staying at home overseas.
- **Compared to the previous fiscal year, net sales increased by 1,262 million yen (+20.3%), while operating income increased by 222 million yen (+92.9%).**

* Expenses related to the explosion at the zinc dust manufacturing plant: an extraordinary loss of 143 million yen has already been recorded

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Next, titanium dioxide and zinc products.

Sales of titanium dioxide, mainly for use in gravure inks, were steady throughout the period. The main reasons for this were that there were no major equipment problems and production was stable, and that the price hike implemented since early spring was absorbed in the latter half of the term, contributing to higher unit prices.

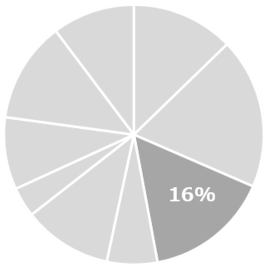
Sales of zinc products are almost exclusively zinc oxide due to the explosion and fire accident at the Yumoto Plant. Sales increased by JPY1.262 billion, or 20.3% YoY to JPY7.491 billion, due to higher zinc prices and increased volume of zinc oxide for tires, despite the absence in sales of zinc dust.

Regarding zinc dust, operating income in the sub-segment almost doubled to JPY461 million, plus JPY222 million or 92.9%, due in part to an extraordinary loss of JPY143 million for expenses related to the accident.

As for cosmetics applications, demand continues to decline due to the effects of COVID-19, and recovery is expected to take more time. However, from the second half of the fiscal year, sales to Europe and the United States have started to pick up slightly, and since we have almost completed the establishment of a system to increase production, we are in a position to adequately respond to future increases in demand.

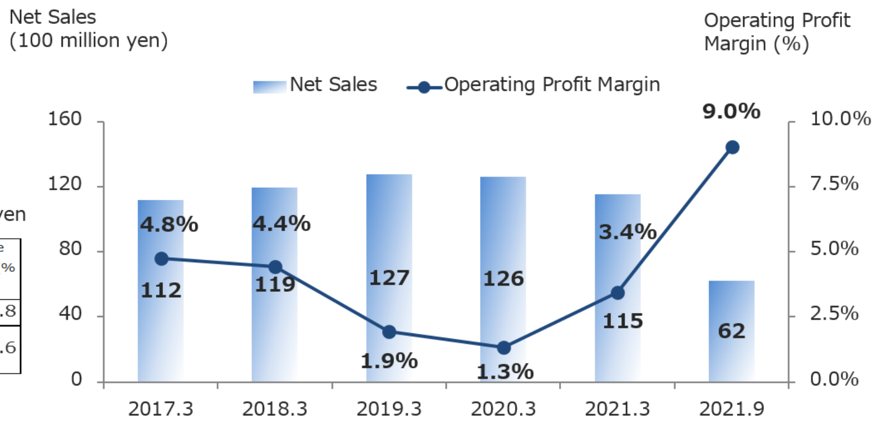
Chemicals

Plastic additives



Monetary units: million yen

	2020.9	2021.9	Increase Decrease(%)
Net Sales	5,315	6,209	16.8
Operating Income	28	561	1903.6



Key points for the first half of the fiscal year ending March 2022

*** Sales decreased by 402 million yen due to the application of the new revenue recognition standards.**

- In the domestic market, sales and profits increased due to strong sales in general, including those for housing, automobiles, and industrial plates for IT-related equipment.
- In overseas markets, sales and profits both increased due to strong sales of PVC stabilizers for automotive applications and hydrotalcite used in agricultural sheets.
- **Compared to the previous fiscal year, net sales increased by 894 million yen (+16.8%), while operating income increased by 533 million yen (+1903.6%).**

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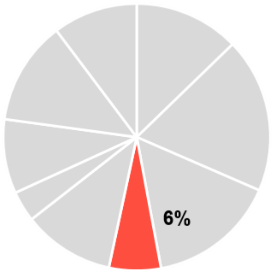
Next, there are plastic additives.

In the area of plastic additives, domestic demand continued to be strong for PVC stabilizers in a wide range of fields, including housing, automobiles, and industrial plates for IT-related equipment. Overseas, our subsidiaries in Vietnam and Thailand performed well. Sales of hydrotalcite for PVC stabilizer applications in China and for agricultural sheets were strong, contributing to higher earnings.

As a result, sales increased by JPY894 million, or 16.8%, to JPY6.209 billion. Operating income increased significantly to JPY561 million, an increase of JPY533 million or 1,903.6%.

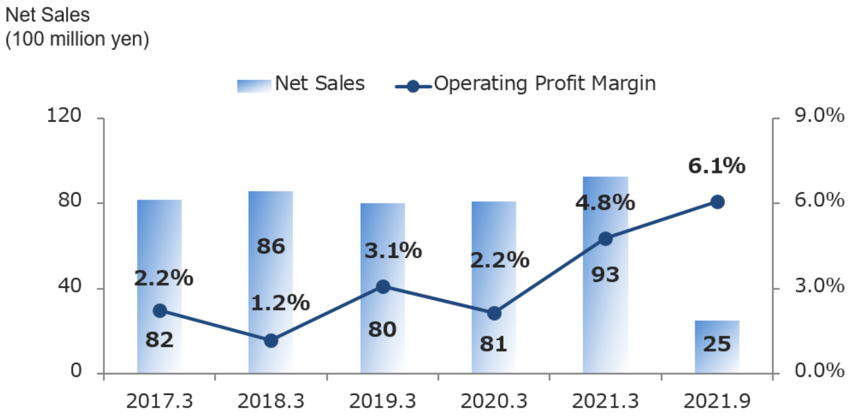
Chemicals

Hygienic products



Monetary unit: million yen

	2020.9	2021.9	Increase Decrease(%)
Net Sales	4,748	2,506	▲ 47.2
Operating I	212	152	▲ 28.3



Key points for the first half of the fiscal year ending 2022

*** Sales decreased by 2,055 million yen due to the application of the new revenue recognition standards**

- Sales decreased significantly due to the application of new revenue recognition standards.
- Although the manufacturing and sales business at the local subsidiary in Indonesia remained strong, profits decreased because there was no special demand for non-woven fabric related to the COVID-19 in the current fiscal year, which existed in the same period of the previous fiscal year.
- **Compared to the previous fiscal year, net sales increased by 2,242 million yen (+47.2%), while operating income increased by 60 million yen (+28.3%).**

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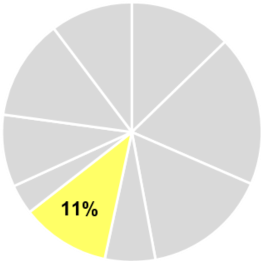
Next are hygienic products.

The impact of the new revenue recognition standard was noticeable in this segment. In addition, both sales and profits decreased compared to the same period last year due to the absence of the pandemic-related special demand in the previous fiscal year at the Indonesian subsidiary.

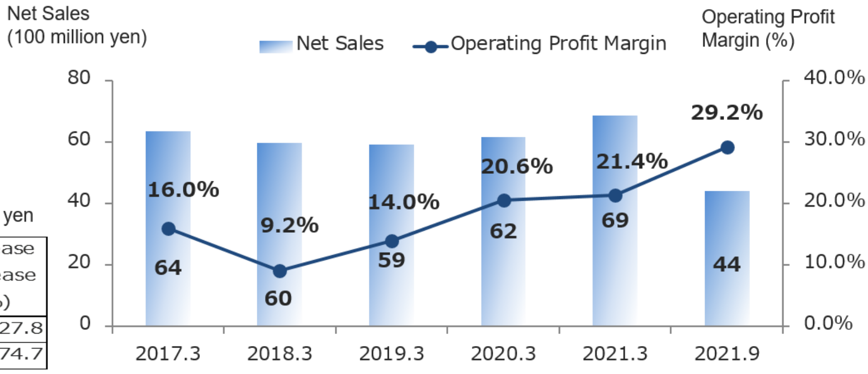
Sales were JPY2.506 billion, down JPY2.242 billion or 47.2%. Operating income decreased by JPY60 million, or 28.3%, to JPY152 million.

However, as a base, this segment has remained strong. Our local subsidiary in Indonesia has been operating at almost full production.



Organic chemicals

Chemicals



Monetary units: million yen

	2020.9	2021.9	Increase decrease (%)
Net Sales	3,461	4,422	27.8
Operating	739	1,291	74.7

Key points for the first half of the fiscal year ending March 2022

*** Sales decreased by 18 million yen due to the application of the new revenue recognition standards.**

- Sales and profits of thio products increased due to strong sales of products used in plastic lenses and phosphorus products for use as lubricant additives in the manufacture of automobiles and various parts.
- Sales and profits of contract production of bulk pharmaceutical products and intermediates increased, partly due to the concentration of shipment volume of mainstay intermediates during the first half of the current fiscal year.
- **Compared to the previous fiscal year, net sales increased by 961 million yen (+27.8%), while operating income increased by 552 million yen (+74.7%).**

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Next, we will look at organic chemicals.

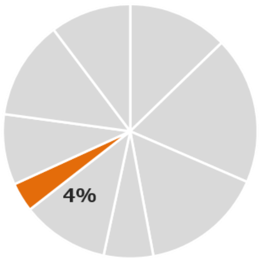
Sales of thio products, mainly for plastic lenses, and active pharmaceutical ingredients and intermediates were strong. Particularly in the area of pharmaceutical contract manufacturing, commercial shipments were concentrated in the first half of the fiscal year, driving a significant increase in both sales and profits.

Sales were JPY4.422 billion, an increase of JPY961 million, or 27.8%. Operating income was JPY1.291 billion, an increase of JPY552 million, or 74.7%.

In the second half of the year, however, sales of major products will be down due to regular repairs at major customers, and the profit margin of contract manufacturing of pharmaceuticals will be lower due to the concentration of low-margin development shipments in the second half. The performance of this segment is expected to slow down in the second half compared to the first half.

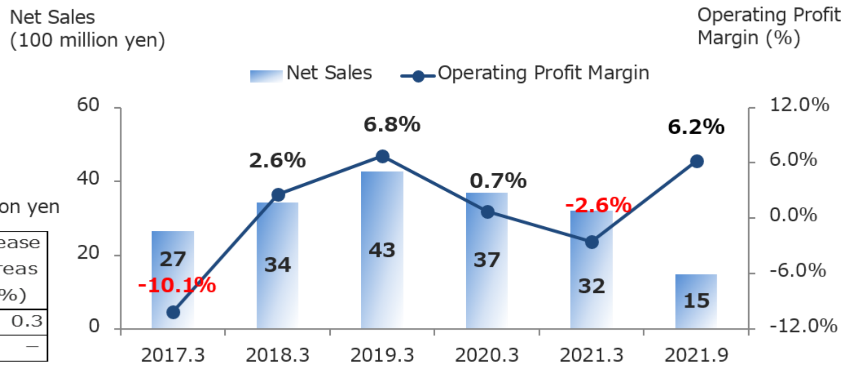
Catalysts

Chemicals



Monetary units: million yen

	2020.9	2021.9	Increase decrease (%)
Net Sales	1,482	1,486	0.3
Operating I	▲ 66	92	–



Key points for the first half of the fiscal year ending 2022

*** Sales decreased by 254 million yen due to the application of the new revenue recognition standards.**

- Sales of nickel catalysts used in the resin hydrogenation process decreased due to the postponement of deliveries to major customers.
- Sales and profit of de-NOx catalysts used in thermal power plants and waste incineration facilities increased due to the start of large-scale shipments to overseas customers.
- **Compared to the previous fiscal year, net sales increased by 4 million yen (+0.3%), while operating income increased by 158 million yen.**

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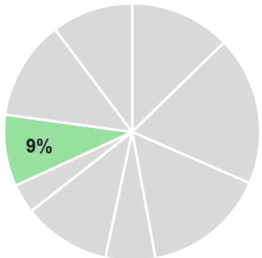
Next are the catalysts.

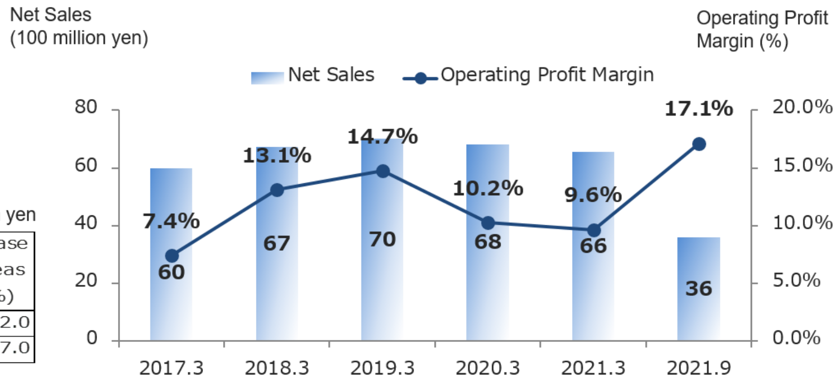
Sales of nickel catalysts decreased due to delays in the start-up of new facilities at major customers. Meanwhile, sales of deNOx catalysts were supported by the contribution of large-scale projects in China throughout the year. As a result, we returned to profitability.

Sales were JPY1.486 million, plus JPY4 million, or 0.3%, YoY. Operating income was JPY92 million, an increase of JPY158 million.



Contract processing

Chemicals



Monetary units: million yen

	2020.9	2021.9	Increase decrease (%)
Net Sales	2,942	3,589	22.0
Operating I	249	615	147.0

Key points for the first half of the fiscal year ending March 2022

*** Sales decreased by 250 million yen due to the application of the new revenue recognition standards.**

- Sales and profits of processed pigments increased due to strong sales for use in automobiles and daily supplies.
- Sales and profits of contracted processes such as calcination, mixing, and drying increased due to an increase in highly profitable contracted products.
- **Compared to the previous fiscal year, net sales increased by 647 million yen (+22.0%), while operating income increased by 366 million yen (+147%).**

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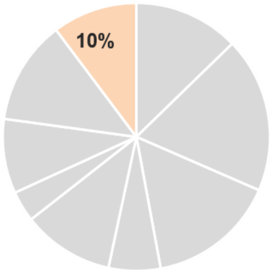
Next, there is contract processing.

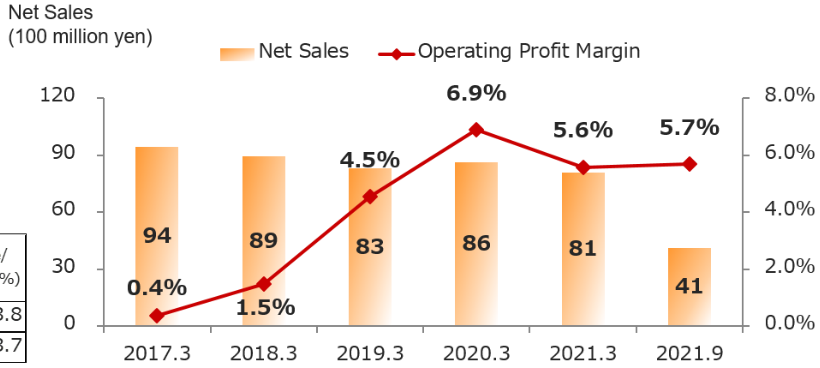
Business conditions for processed pigments recovered, especially for automotive applications. In the contract manufacturing business, both sales and profits increased significantly due to stable orders for high-profit projects throughout the first half of the fiscal year.

Sales were JPY3.598 billion, an increase of JPY647 million, or 22%. Operating income increased to JPY615 million, plus JPY366 million, or 147%.



Medical Business

Medica



Monetary units: million yen

	2020.9	2021.9	increase/ decrease(%)
Net Sales	3,945	4,096	3.8
Operating Income	242	233	▲ 3.7

Key points for the first half of the fiscal year ending March2022

*** Sales decreased by 38 million yen due to the application of the new revenue recognition standards.**

- Sales and profits of barium contrast media increased due to growth in exports, mainly to South Korea, despite the impact of the decline in health checkups under the COVID-19 pandemic that has continued since last year.
- Sales of Alloid G increased despite the impact of drug price reductions, as COVID-19 did not affect sales.
- Sales volume of medical equipment recovered, resulting in increased sales and profits.
- Sales and profits of OTC drugs such as Kaigen, a cold remedy, decreased due to the absence of special demand under COVID-19 in the same period of the previous year and the absence of a cold epidemic due to thorough prevention of COVID-19 infection.
- **Compared to the previous fiscal year, net sales increased by 151 million yen (+3.8%), while operating income decreased by 9 million yen (-3.7%).**

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Next is the medical business.

This segment is the one that is most affected by the pandemic. We managed to secure sales by exporting barium contrast media, expanding sales of prescription drugs such as Alloid G and endoscope cleaning machines, resulting in a YoY increase in sales.

Sales were JPY4.096 billion, an increase of JPY151 million, or 3.8%. On the profit front, however, operating income decreased by JPY9 million, or 3.7%, to JPY233 million due in part to the reduction of drug prices.

Cash Flow

Units: million yen

	2021.3 2Q	2022.3 2Q	Increase/decrease
Cash at Beginning of Period	9,148	11,153	2,004
Profit (loss) Before Income Taxes	1,286	4,537	3,251
Depreciation	2,024	2,260	235
Other	873	▲ 1,414	▲ 2,287
Cash Flow From Operating Activities (Operating CF)	4,183	5,383	1,199
Purchase of property, plant and equipment	▲ 5,118	▲ 3,837	▲ 1,280
Other	236	19	▲ 217
Cash Flow From Investing Activities (Investment CF)	▲ 4,882	▲ 3,818	1,064
Cash Flow from Financing Activities (Financial CF)	1,836	▲ 1,025	▲ 2,861
Cash at End of Period	10,248	11,774	1,526

◆ Operating CF

Operating cash flow increased, mainly due to strong business performance.

◆ Investment CF

Investment cash flow decreased because capital expenditures were limited to the maintenance and renewal of existing facilities, and spending for the acquisition of tangible fixed assets was cut down.

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Next, I would like to explain about cash flow.

Cash flow used in operating activities was JPY1.4 billion due to an increase in accounts receivable and inventories resulting from increased sales, which are included in other items. However, due to high performance, operating cash flow was JPY5.4 billion, an increase of JPY1.2 billion YoY.

Cash outflows from investing activities decreased due to the peak out of capital investment. As for cash flow from financing activities, cash decreased as debt repayments exceeded.

As a result of all these factors, cash inflows exceeded cash outflows, resulting in a JPY1.5 billion increase in cash at the end of the period.

Trends and Forecasts for Major Items

Monetary units: million yen

	2017.3	2018.3	2019.3	2020.3	2021.3	2021.9	2022.3
Net Sales	83,938	87,223	89,541	87,177	84,918	39,905	**80,000**
Operating Income	4,551	4,690	4,404	4,015	4,304	4,356	**7,000**
Ordinary Income	4,290	4,279	4,553	4,208	4,012	4,599	**7,200**
Profit (loss) attributable to owners of parent	2,037	2,329	3,606	2,535	▲ 2,803	3,180	**5,300**

Capital Investment	4,636	3,771	6,891	8,403	9,567	3,837	**5,000**
Depreciation	2,877	3,005	3,189	3,686	4,243	2,260	**4,100**
Research and Development Expenses	2,909	3,217	2,951	2,898	2,487	1,168	**2,500**

Next, I would like to explain our earnings forecast for FY2022.

The sales forecast for the current fiscal year on the far right is JPY80 billion, which is a decrease due to the application of the new revenue recognition standard, but in light of the old standard, we expect a significant increase in sales, exceeding JPY90 billion.

Operating income is expected to increase by 62.6% YoY to JPY7 billion, ordinary income by 79.4% to JPY7.2 billion, and net income attributable to shareholders of the parent company by a large margin from the negative figure of last fiscal year to JPY5.3 billion.

Capital investment totaled JPY5 billion, peaking out from the large investments made in the previous fiscal year. Depreciation was JPY4.1 billion, a slight decrease from the previous fiscal year, partly due to the impairment loss at the end of the previous fiscal year. R&D expenses are planned to be JPY2.5 billion, almost unchanged from the previous fiscal year.

Forecast for the Fiscal Year Ending March2022

Monetary units: million yen

	2021.3		2022.3					
	Full-year Results		First-half Results		Second-half Forecast		Full-year Forecast	
		Change From the Previous Year		Change From the Previous Year		Change From the Previous Year		Change From the Previous Year
Net Sales	84,918	—	39,905	—	40,095	—	80,000	—
Operating Income	4,304	5.10%	4,356	10.9%	2,644	6.6%	7,000	8.8%
Ordinary Income	4,012	4.70%	4,599	11.5%	2,601	6.5%	7,200	9.0%
Profit (loss) attributable to owners of parent	▲ 2,803	▲3.3%	3,180	8.0%	2,120	5.3%	5,300	6.6%

- Chemical Business:
  ⇒ It is expected to remain strong, particularly electronic materials and titanium dioxide.
  As for organic chemicals, shipments were concentrated in the first half of the year and will not grow significantly in the second half.
  Sales of cosmetics materials have been recovering since the second half of the year, mainly in Europe and the United States.
  We expect a recovery in the next fiscal year.
- Medical Business
  ⇒ Although sales are expected to increase from the previous year, profits are expected to decrease slightly.
- The extraordinary loss due to the explosion and fire at the zinc dust manufacturing plant is expected to be 300 million yen, in line with initial estimates.

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Next, I would like to explain in some detail the comparison between the first half and the second half of this fiscal year's forecast.

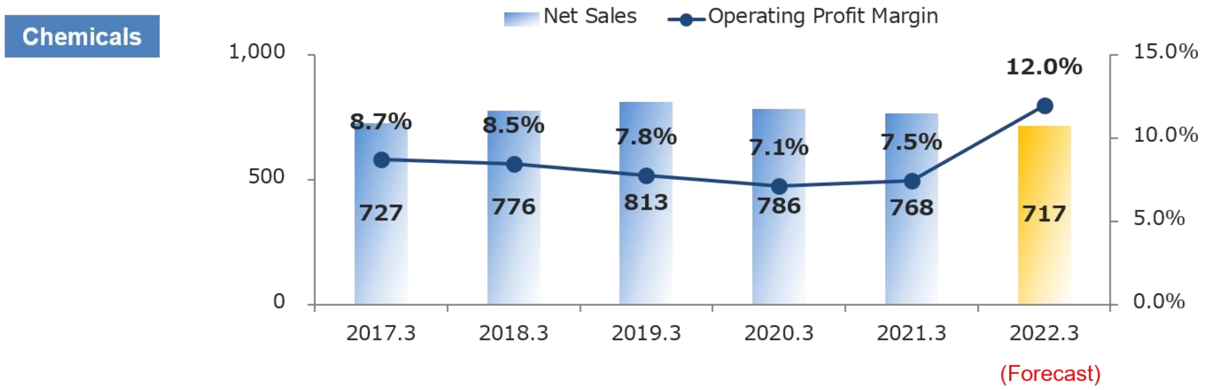
Comparing the first and second half of the fiscal year, sales are expected to be almost the same level. However, as you can see, there will be a difference of approximately JPY1.7 billion in operating income between the first and second half.

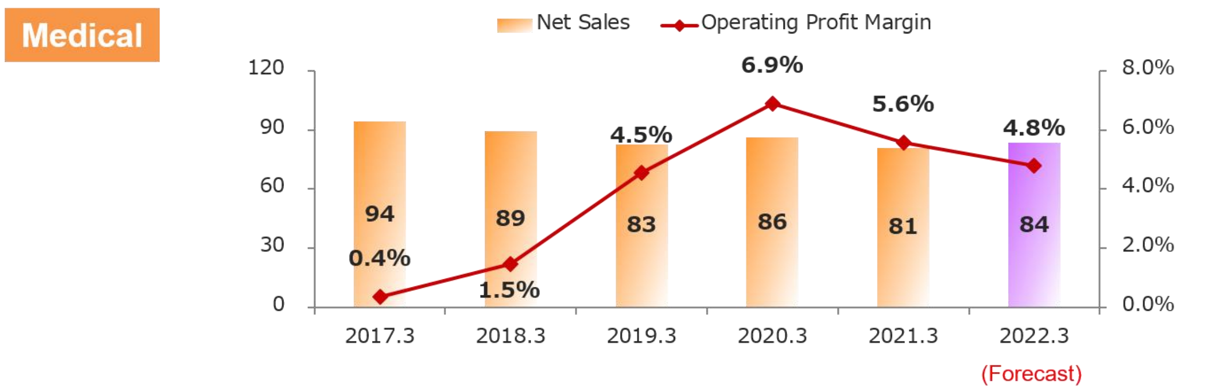
This is due to the fact that, as mentioned earlier, the sales of commercial products of Active pharmaceutical ingredient and intermediates, i.e. products that generate a lot of revenue, are concentrated in the first half of the fiscal year, while the second half of the fiscal year is dominated by sales of development products, which are less profitable.

Since Kaigen's medical business has a bias toward the first half of the year, the difference between the first and second half of the year is approximately JPY1 billion due to the impact of these 2 companies. In addition, we are forecasting higher raw material and fuel prices in the second half of the fiscal year in other segments as well and have made slightly conservative estimates based on the assumption that this will put some pressure on gross profit margins.

Although it looks as if the business performance will slow down a little in the second half, we forecast that the strong trend of the first half will continue in the second half, mainly in electronic materials, if we omit these special factors.

Earnings Forecast for the Fiscal Year Ending March 2022





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Lastly, I would like to explain our forecast by segment.

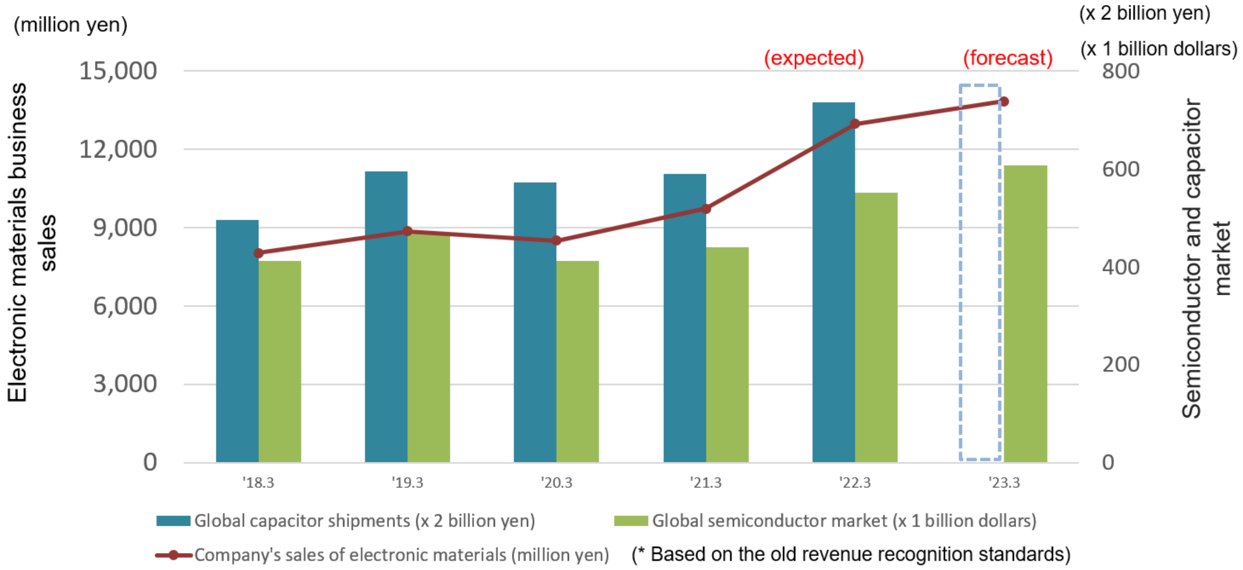
Although it is assumed that the pandemic will calm down, the performance of the chemicals segment is expected to be solid, especially in the electronic materials business, and the operating income ratio is expected to increase significantly from the past level, despite a decrease in revenue due to the impact of the new revenue recognition standards.

In the medical segment, as I explained earlier, we expect sales to increase slightly from the previous fiscal year due to the planned reduction of NHI drug prices, but the operating margin is expected to decline, and the recovery of business performance will be limited.

This is the end of the explanation of our business performance.

Moderator: Thank you very much. Next, President Yabe, please continue.

Forecast for the electronic materials business and the capacitor and semiconductor market Value basis



Our electronic materials business is expected to grow in line with trends in the capacitor and semiconductor markets.

* Sources
Global semiconductor market: WSTS (World Semiconductor Trade Statistics)
Global shipment value of capacitors: JEITA (Japan Electronics and Information Technology Industries Association) statistics

Yabe: I will now explain the topics. First of all, I would like to explain the outlook for the electronic materials segment.

In this graph, the green bars indicate the semiconductor market, and the blue bars indicate the shipment value of capacitors. The units are different for each of them, so it may be difficult to understand, but basically, the number of units is increasing steadily.

On the other hand, the red line graph shows the projected sales forecast for our electronic materials segment. For this, we have used the old revenue standard.

In FY2021, our sales in the electronic materials segment were approximately JPY9.7 billion. In contrast, for FY2022, we expect sales of approximately JPY13 billion for the current fiscal year and approximately JPY14 billion for the next fiscal year, assuming that there will be no major adjustments.

ESG Initiatives

■ Our Materiality

	Making people happy		Solving social challenges through manufacturing
1	Fostering an environment that enables the development and growth of human resources	7	Creating products and services that help solve environmental and social issues
2	Creating a comfortable working environment	8	Promoting responsible procurement
3	Contributing to local communities		
	Protecting the global environment		**Building a transparent and sound management system**
4	Managing chemical substances appropriately, reducing environmental impact, and improving product safety	9	Increasing the effectiveness of the Board of Directors
5	Reducing industrial waste emissions	10	Understanding risks and taking countermeasures
6	Giving consideration to biodiversity	11	Timely and appropriate information disclosure

We established the Sustainability Committee in September this year and are currently working on setting KPIs to achieve the above tasks and to be able to disclose information based on TCFD.

<Major initiatives to date>

- August 2005: Fuel conversion to LNG at the Sakai Manufacturing Site and Semboku Factory
- June 2016: Fuel conversion to LNG at the Onahama Manufacturing Site
- April 2020: Began use of carbon neutral LNG (CNL)
- March 2021: Awarded EcoVadis Gold Medal for our CSR platform
- June 2021: Introduction of executive officer system
- September 2021: Establishment of human resource development policy and reform of personnel system
- October 2021: Completion of RSPO membership registration

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Next, I would like to briefly explain our approach to ESG strategies.

We have formulated 11 key issues, or materialities, from the following 4 areas. To make people happy, to solve social issues through manufacturing, to protect the global environment, and to build a transparent and strong management system.

In September of this year, we established the Sustainability Committee, which has set KPIs for each materiality and is promoting initiatives.

We have already been implementing initiatives to reduce our environmental impact in the past and have already converted fuel from heavy oil to LNG in the Sakai area in 2005 and in the Onahama area, which consumes the largest amount of fuel, in 2016.

Last year, we adopted carbon-neutral LNG at our cosmetics materials manufacturing plant. In addition, EcoVadis, CSR platform, awarded us the Gold Medal in FY2020.

In terms of governance, we have increased the number of outside directors and introduced an executive officer system this year to clearly distinguish between management execution and supervision, as well as reformed the personnel system to strengthen human resource development.

Offering of Shares & Acquisition of Treasury Stock

<Purpose of the offering>

As a company aiming to be listed on the Prime Market, we will further promote the elimination of cross-shareholdings, increase liquidity, and engage in constructive dialog with as many investors as possible to increase our corporate value.

- Announced on October 12, 2021
- October 27, 2021: 2,269 thousand shares traded

  (＊13.3% of the total number of shares issued, including the over-allotment portion)

<Purpose of the treasury stock acquisition>

To strengthen shareholder returns and mitigate the impact of the offering on stock supply and demand

- Commenced the treasury stock acquisition on October 28, 2021

  Maximum number: 900,000 shares; maximum amount: 1,500 million yen

<Future challenges>

Formulate and execute management strategies to enhance corporate value in a variety of areas, including capital policy, business strategy, and ESG.

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Next, I would like to explain the secondary offering of shares and share repurchase.

As you may know, we conducted a secondary offering of shares in October. This was approximately 2.27 million shares, or 13.3% of the total number of shares issued.

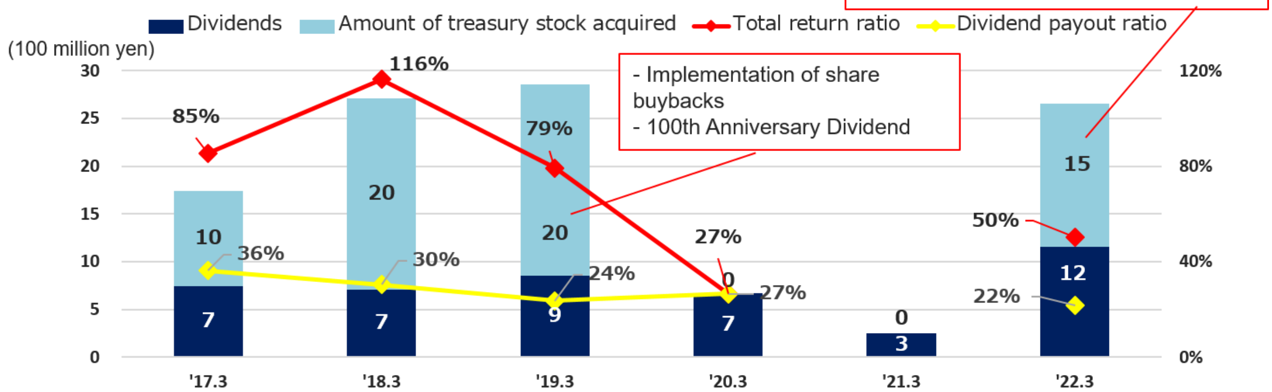
As our company aims to be listed on the Prime Market, we will further promote the elimination of cross-shareholdings, increase the volume of shares in circulation, have a large number of investors hold our shares, and grow through constructive dialogue. We are determined to make further efforts to improve our corporate value with a sense of urgency.

In conjunction with the secondary offering, the Company will also repurchase its own shares. The maximum number of shares is 900,000 and the maximum amount is JPY1.5 billion. The purpose is to enhance shareholder returns and to mitigate the impact of the secondary offering on demand for shares.

As for future tasks, we would like to swiftly formulate and implement management strategies to improve our corporate value in the future, including capital policies and ESG.

Shareholder Return

■ Changes in the total dividend payout ratio



Concerning surplus dividend, the Company considers the stable return of profits to shareholders to be one of our most important management issues, and aims to strengthen our financial position and increase the internal reserves necessary to actively grow the business. At the same time our basic policy is to pay dividends twice a year, taking into account profit trends and the business environment.

In our mid-term management plan, SAKAINNOVATION 2023, we are working to achieve a total payout ratio of 30% or more.

For the fiscal year ending March 2022, we plan to return 70 yen per share: 35 yen for the interim period and 35 yen at the end of the term.

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Lastly, I would like to explain about stock returns.

In our current mid-term management plan, SAKAINNOVATION 2023, we are targeting a total return ratio of 30% or more.

For the current fiscal year, we plan to pay an interim dividend of JPY35 and a year-end dividend of JPY35, for a total of JPY70, and after taking into account the share buyback explained earlier, the total return ratio is expected to be 50%.

The dividend payout ratio, excluding share buybacks, is expected to be around 22%.

The above is a brief explanation. I'm looking forward to working with you.

Moderator: Thank you very much.

Question & Answer

Moderator: We will now move on to the question and answer session.

If you would like to ask a question, please click the raise hand button at the bottom of the viewing screen. Those who raised their hands, I will nominate them in turn. When your turn comes, we will unmute you, so please ask your questions verbally. If it is difficult to ask your question in audio, please write your question in the question & answer section. After the question and answer session via audio, I will answer a selection of the questions that have been submitted via text.

Now, since 2 of you have already raised your hands, I would like to begin with Mr. Questioner1

Questioner1: I'm looking forward to working with you. I would like to ask you 3 questions.

The first is about electronic materials. The operating income margin for the first half was 17.5%, which is very high, but then the audio was cut off in the middle of the presentation. You might have explained it already. What is the reason for this? Also, is it sustainable in the future?

Also, in terms of electronic materials, sales for the first half were JPY5.1 billion when applying the new standard. If we combine it with the figures in the back, it looks like you are expecting about JPY6.5 billion in the second half. What can you say about the sales in the second half for electronic materials?

Yabe: This is Yabe. We are now looking at annual sales of about JPY13 billion under the old standards. If we convert that into the new standard that I mentioned earlier, it would be about JPY2 billion less, so JPY11 billion.

Questioner1: I see.

Yabe: In the first half of the year.

Questioner1: What about the JPY5.1 billion?

Nakanishi: Under the old standards, it was about JPY6.1 billion, and under the new standards, it is JPY5 billion.

Yabe: So, under the new standards, the second half of the year will be about JPY6 billion.

Questioner1: I see. I understand. I think it will be about JPY1 billion more in the second half versus the first half. I understand.

Yabe: Also, in terms of profits, although we would naturally like them to be a little higher, we are gradually seeing the fruits of our efforts.

We haven't said much about the impairment yet, but we believe that we will be able to increase profits by investing in equipment that will be sold in the future and increasing production and sales, because the depreciation will be reduced.

Questioner1: In that case, the profit margin, which is more than 10% now and at highest level ever, can generally be maintained at the current level, although it may drop a little in the second half of the fiscal year. Is that correct?

Yabe: Yes. That's what I'm thinking at the moment.

Questioner1: I understand. Thank you. The second is about the raw materials for cosmetics. In addition, there are some concerns about the new variants that are coming from South Africa.

However, if things go normally, I think we will see a lot of movement in the next fiscal year. Some people have commented that we are seeing movement in Europe and the United States, but I would like to know what the situation is now.

Also, I believe that the original growth story was about a shift away from so-called oil-based products, but what is the current situation and outlook for this?

Yabe: You're right, there is a new virus variant from South Africa. Before we received this information, we were in a situation where orders from overseas were coming back quite a bit due to the fact that we were on a recovery trend, especially in Europe and the United States. Therefore, we expect a recovery to some extent in the second half of the fiscal year.

However, we don't yet know what the impact will be in the future, so we need to consider the possibility of such risks.

In addition, we are aware that the trend of shifting from organic to inorganic materials has not basically changed.

Questioner1: Excuse me. What is the scale of sales in the first half of this fiscal year compared with the level before COVID-19? If you exclude South Africa, how far did you envision it recovering in, say, the second half of this fiscal year and beyond, if at all possible?

Nakanishi: In terms of sales, it is almost the same as the first half of the previous fiscal year, since the previous fiscal year was mostly affected by COVID-19 as well. However, in terms of revenue, it has been reduced by half because we have made some investments to our facilities. That is, when compared to the first half of the previous fiscal year.

Questioner1: Operating income was reduced by half.

Nakanishi: I see. On an operating income basis, the figure was halved.

Questioner1: I see. What is your sense of the level of sales compared to before COVID-19?

Nakanishi: Compared to before COVID-19, it's less than half.

Questioner1: Less than half. If it had not been for South Africa, how would you have anticipated the degree of recovery?

Yabe: To put it bluntly, I thought it would be the same as before the pandemic, and in some cases even slightly better.

Questioner1: I see. I understand. Thank you. I'm sorry, but I have a third and final point.

I wonder if you could comment on the synergy between Sakai Trading and other companies, or how you are thinking about that in the future. That's all. I mean synergies, or capital relationships.

Nakanishi: One of the things that Sakai Trading does is to procure almost all of our electronic materials, especially raw materials, which I mentioned are driving our business performance.

In that sense, our relationship is characterized through a very important partnership, rather than a synergy.

Also, in terms of sales, Sakai Trading functions as a sales agent for Sakai Chemical Industry for a large number of customers in the electronic materials field.

Questioner1: I see. I understand. Thank you very much. That's all.

Moderator: Thank you very much. Next, Mr. Questioner2, please join us.

Questioner2:I also have 3 points, though.

One is the electronic materials business, which can be broadly divided into dielectrics and dielectric materials. I wonder if you could elaborate a little on the growth rate of each of these, how they differ from each other, and whether the impact on operating income is also quite different.

Nakanishi: In terms of the growth rate, both dielectrics and dielectric materials show a similar trend. In that sense, we are not particularly biased in terms of profits.

Questioner2: In the mid-term plan, I think you were planning to make a rather large investment. Now that you are almost at full operation, what is your next investment going to be?

Nakanishi: When we say full operation, we mean the facilities that were present before the capital investment of 2 to 3 years ago. These are now almost at full operation.

In the past 2 to 3 years, we have made quite some impairment losses, but those were capital investments towards the new demand in the future. In particular, the last plant for dielectric materials has not yet been put into operation.

In the area of dielectrics, we are gradually starting to operate a factory for high-end products. In that sense, the almost full operation that we mentioned applies to existing facilities. We still have the capacity to operate the facilities related to this large investment.

In that sense, I think that the additional investment you just mentioned will come a little further down the road while we consider the operational status of the new facilities.

Questioner2: I see. For the time being, the already completed investments would be sufficient.

Nakanishi: I see.

Questioner2: In that case, is it correct to expect that the profit margin will remain the same, even though amortization will increase?

Yabe: As I mentioned earlier, we took an impairment loss of JPY7 billion, but the reason why we said that there is still capacity in the future is because most of that capacity has been impaired, so in that sense there is no increase in the cost of depreciation.

We are aware that there will be almost no increase in fixed costs even though the system is up and running.

Questioner2: That's what I mean.

Yabe: At this point, we believe that the difference compared to the variable costs will contribute to profits.

Questioner2: I understand. The second point is about the titanium dioxide and zinc products. There are titanium dioxide, zinc oxide, and cosmetic materials in each sub-segment.

As for the cosmetics materials, you commented that they are not contributing much to your performance. If we look at titanium dioxide and zinc oxide separately, a major point is the increase in sales and profits of titanium dioxide, right?

Nakanishi: I see. You are right.

Questioner2: Now, it seems that the price of raw materials such as ore is going up even more. Do you think that the price hikes you are currently implementing will be enough to compensate this in the second half and beyond?

Yabe: The first round of price hikes is almost over, and now the price of ores, the weak yen, and the high price of heavy oil are also factors. We are now in the process of negotiating for the second round of price increase, which is scheduled for January of next year.

Questioner2: So, do you feel that it will be difficult to make up for it in the second half of the year?

Yabe: In the second half of the fiscal year, we already have enough ore in stock, so there will be no price increase for that amount. However, there is a possibility that the heavy oil part will have some effects. It remains to be seen whether this will be a positive or negative situation. We believe that we can still maintain a profit margin for the rest of the year.

Questioner2: I see. In terms of demand, is it correct to say that the situation in the first half will continue in the second half for both titanium dioxide and zinc oxide?

Yabe: Yes. As for zinc oxide, it is mainly used for tires, so there is some conflict with automobile production, but we think there will be no major adjustments at present.

Questioner2: I understand. My third point is about other businesses in general. I think the profit margins have risen to a level that we have not seen in the past, but what are the main factors behind this?

Nakanishi: In that sense, plastic additives have picked up a lot in those 2 years. In particular, there was a slight indication that it would go up from last year. Particularly in the current fiscal year, domestic demand has been very strong, and we have also been able to raise the prices of general-purpose products, which our customers have been willing to tolerate.

Overseas, there are a few bumps in the road, but in general, we are doing well. One major factor is that stabilizers for local markets overseas in particular continue to be very profitable.

Questioner2: Regarding overseas, is it correct to assume that there will be no particular impact from the COVID-19 in the second half?

Nakanishi: Vietnam, in particular, has been on lockdown for a very long time, and this September, October, and November have been a little tough. In the second half of the year, I think we will be able to persist somehow if we can get this under control, but I'm not sure how the situation with COVID-19 will turn out.

Questioner2: One more thing: I think catalysts are also making a big recovery. What are the factors behind this?

Yabe: In the current fiscal year, we have started to ship large deNOx catalysts to China, and the contribution to profits from this is larger than last year.

Also, the start-up of the nickel catalyst business has been delayed due to a delay in the launch of a large-lot customer that we had planned, so we are facing some difficulties in terms of sales, but profits have improved somewhat.

Questioner2: Do you think there will be continuity in large-scale properties for China? Or is it like a more of a temporary thing?

Yabe: We have already finalized everything for the second half of the current fiscal year, as well as up to March of next year. After April, we will be finished with the property.

Questioner2: I understand. As for the large-scale project of the nickel catalyst hydrogenator, we are having the briefing today at the same time.

We are planning to increase depreciation substantially from the second half of the year, which will reduce profits. Thus, we think if it will establish itself gradually. That's all.

Yabe: Thank you very much.

Questioner2: Thank you very much.

Nakanishi: Thank you very much.

Moderator: Thank you very much. Do you have any other questions? Well, we have some questions for you in the chat room. Now, I will read each of them out loud.

First, the first question. If we divide the factors behind the increase in profit for this fiscal year into external & internal factors, what do you think the ratio will be? Regarding the internal factors, what other efforts are besides the price pass-through?

Yabe: As for internal efforts, I'm sure it's the same for all companies, but we've been able to reduce SG&A expenses, travel expenses, etc.

As for the business itself, as Nakanishi mentioned earlier, we have already done everything we can to reduce the cost of plastic additives that we produce domestically, and I believe that this has contributed to our profits.

In the electronic materials business, the fact that we are finally able to ship developed products to customers on a full-scale basis is also a major factor in the increase in profits.

Moderator: Now, let's move on to the next question.

We would appreciate any updates to the release on September 3 in which you confirmed that zinc oxide reduces COVID-19 infections.

Even if there is no update, we would appreciate your comments on our stance and future direction.

Yabe: We are currently conducting a survey to determine what kind of applications we can develop for this, and we are also sending out various samples.

There are also various film-related and liquid coating materials. In addition, silver is often used as an antibacterial agent, but I think there may be a way to develop a partial substitute for silver.

Anyway, we are currently responding to samples from various customers and industries, and we would like to explore what kind of areas are promising in the future and make further progress.

Moderator: That is our response to your question. Now, the third question.

You have recently announced a price increase for titanium dioxide, but do you think that this price increase is sufficient? Also, are there any other chemical products that you would consider raising prices on?

Yabe: I see, this is about the second price increase for titanium dioxide. As we have just announced, we hope to achieve it somehow. After considering how the price of raw materials and fuel will rise, we will determine whether or not there will be any other products.

Also, in terms of plastic additives, there are a lot of raw materials that we buy from China. Due to the shortage of electricity, it has become difficult for goods to come in.

In that sense, we are naturally passing on the price of those items that have increased in price, mainly those items that are not included in the price list. As Nakanishi mentioned earlier, we are doing this quite forcefully.

Moderator: Now, I would like to continue with the fourth question.

What is your medium-term policy for businesses with operating margins that remain in the low range? Especially in terms of titanium dioxide, zinc products, and the catalyst segment.

Yabe: With regard to titanium dioxide, the market environment has improved, and we are now able to make a certain level of profit.

As for what we will do in the future, since it is the core business of our Onahama office, we are still in the stage of carefully considering various things, so we cannot say exactly what we will do yet. Anyway, our main focus is to reduce costs.

As for zinc products, there was an explosion of zinc dust, which was very unprofitable, so we are now withdrawing from this business.

As for zinc oxide, we would like to increase the profit margin by developing applications for antibacterial and antiviral products, as you mentioned earlier.

In the catalyst segment, nickel is not profitable, but we are planning to improve the profit margin by consolidating and closing plants. That's all.

Moderator: That is our response to your question.

The last question, which is somewhat similar to a previous question: I would like to ask you whether it is correct to assume that the profit margin for electronic materials could be even higher than the 17% in the first half of the fiscal year when the new facilities that have been impaired are fully operational.

Yabe: Indeed. That's what I meant when I answered the previous question.

Moderator: Well, these were all the answers to your questions. It seems that all your questions have been received. The scheduled time of 4:30 PM has arrived, so we will now conclude the question and answer session.

This concludes the 2Q Financial Results Briefing of Sakai Chemical Industry Co., Ltd. Thank you very much for joining us today.

Thank you for your continued support. Now, if you'll excuse me.

Yabe: Thank you very much.

[END]

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