

Business Results Meeting for the Fiscal Year Ended March 31, 2025: Questions and Answers

[FY2025 Business Results Forecast]

Business environment (General)

Q1: Will U.S. tariff policy have a direct impact on the company? For example, you have a site in the U.S. for special anti-corrosion agents—how do you view the situation? Could you also tell us about any indirect impacts?

A1: Since sales to the U.S. are a relatively small part of our consolidated net sales, we believe the direct impact on our business will be limited. However, in some cases, the products we supply are processed for export to the U.S. by customers both in Japan and abroad, so indirect impacts on our business are possible. It is also possible that fluctuations in global economic trends, exchange rates, crude oil prices, raw material prices, and so on will have an impact on our results. With respect to special anti-corrosion agents, we intend to accelerate business development, including local procurement of raw materials and transfer of product manufacturing, by leveraging our ownership of sites in countries around the world, which is a strength of our group. However, since the situation is in constant flux, we will continue to focus attention on the direction of U.S. tariff policy from various perspectives.

Business environment (Functional Chemicals segment)

Q2: On page 6 of the presentation material, the changes in operating profit (year-on-year) attributable to sales volume for FY2024 was +7.0 billion yen (actual result), exceeding the forecast of +5.5 billion yen (made in November 2024). Could you explain the context for this? In addition, could you explain the context for why the changes in operating profit (year-on-year) attributable to sales volume for FY2025 on page 18 of the presentation material is smaller (+2.2 billion yen) than the FY2024 result (+7.0 billion yen)?

A2: The higher performance with respect to sales volume (year-on-year) in FY2024 relative to expectations was due to the strong demand of products such as cosmetics-related products, including ODM products, and special anti-corrosion agents. In FY2025, we expect these products to continue to perform well, but the change in the amount of increase in the sales volume is intended to reflect differences in how we will grow compared to the previous year.

Q3: In FY2025, will the growth in net sales for cosmetic raw materials and ODM products slow down compared to FY2024?

A3: We consider the growth in FY2024 to be extremely significant. You can understand this from the fact that our actual results were much higher than the initial forecast. We expect continued growth of the ODM business in FY2025; the details at the present time are shown on page 18 of the presentation material.

Q4: ODM products are expected show firm performance in FY2025 as well, but does this mean that you forecast an increase in the number of contracts based on products for existing customers or accelerated regional expansion? Or are you moving forward to acquire projects from new customers?

A4: With respect to ODM products, as explained on page 19 of the presentation material, we develop cosmetic raw materials as well as propose formulations and develop ODM products using our cosmetic raw materials. In this way, we develop our business through a two-pronged approach featuring both cosmetic raw materials and ODM products, and our products are used by multiple customers. With the ODM industry also performing extremely well, we aim to raise our overall performance while continuing to make proposals to customers.

Q5: For ODM products, which do you think will contribute more in FY2025: use by new customers or expansion of sales to existing customers?

A5: For ODM products, we have a lineup of products that are used on a relatively long-term basis as well as other products that are updated seasonally, so it is difficult to say with certainty, but we are always working to expand sales, which includes proposing new products.

Q6: With regard to special anti-corrosion agents, given the impact of tariffs and other factors in FY2025, is it fair to say that you do not foresee strong growth in automobile production volume?

A6: If you look at the publicly available documents regarding global automobile production volume, it is forecast to decrease compared to FY2024, but our sales will increase due to factors such as growth in market share.

Business environment (Pharmaceuticals, Medicals and Health segment)

Q7: Pages 7 and 21 of the presentation material show that fixed costs are expected to increase by 2.0 billion yen year-on-year in FY2025, compared to an increase of 0.6 billion yen year-on-year in FY2024. We believe this includes the depreciation of the LS Aichi Plant, but could you explain the main factors behind the 2.0 billion yen year-on-year increase in fixed costs?

A7: We will be proactively making strategic investments in FY2025, so we are expecting an increase in labor costs, R&D expenses, and depreciation and amortization. In addition, we are expecting increased outsourcing expenses and other costs associated with the ongoing intensification of production activities.

Q8: While sales of raw materials for DDS drug formulation will gradually recover for some customers in FY2025, bio-venture clinical development will continue to be delayed, so how do you view performance overall?

A8: Overall, we expect firm demand.

Q9: Page 22 of the presentation material indicates that with regard to the outlook for raw materials for DDS drug formulations, you have at least five products in the pipeline expected to launch in FY2025 or later. Could you say whether this is a lot or a little compared to the past? Does this mean that the pipeline's progress has returned to a level similar to the previous status quo following the temporary decrease in launches in FY2024?

A9: With regard to the pipeline of products in late-stage clinical trials reported in the presentation material, there are multiple products around Phase 3. Of course, the timings of their launches will differ based on the process of receiving approval from the authorities in the U.S. and Europe. We will verify the launch timings as appropriate while sharing information with customers. Given that these pipeline products will be launched in the future, please understand that demand will grow towards FY2030.

Q10: With respect to your supply agreements with customers, a customer has disclosed that the customer will terminate its obligation to your company in terms of minimum purchase volumes in FY2025. Could you indicate what kind of impact this will have in terms of your sales quantities and cancelation fees in FY2025?

A10: While that is the situation for a customer, the cancelation fee has been incorporated into the non-operating profit in our FY2025 plan. In terms of future sales, we will pursue business development in consideration of customers' circumstances.

Business environment (Explosives & Propulsion segment)

Q11: You mentioned three investment plans for defense-related products. We understood that you were making gunpowder, but given that the investment amount is quite large, could you explain the background and details of why the investment plans are divided among three locations, including the Aichi Works and Nippon Koki?

Also, it seems that the Kayaku Japan accident has impeded procurement of raw materials in the Explosives & Propulsion segment. Could you comment on the actual procurement situation?

A11: We are making extremely significant investments in two sites. Given the nature of the defense business, manufacturing at two sites is desirable from a BCP perspective. Therefore, in addition to the Taketoyo Plant where we are already carrying out manufacturing, we decided to construct similar facilities on the premises of our affiliate Nippon Koki's Shirakawa Plant, which has land available. Since the construction plan covers a long period, we plan to divide up the investment across several stages. With respect to the impact of the accident at a raw material supplier, supply is still stopped for some raw materials used in our products. Since FY2023, we have been handling this situation by importing from overseas the raw materials that we can no longer procure due to the accident. We will continue to pursue procurement of raw materials in a systematic manner based on our actual production situation.

Q12: Could you tell us the extent of sales you expect once you have completed the facility investment associated with rapid acquisition?

A12: Since this depends on the trends in contracts currently being undertaken and future defense budget trends, it is not possible to give a definitive answer. However, we estimate that the increase in sales related to the facility investment will amount to about 10% to 20% of the sales in the Explosives and Propulsion segment.

Management strategy

Q13: With respect to initiatives aimed at improving ROE, you have indicated that you are considering the ROE target in the next Mid-Term Plan. Along with the growth of high-profit products, could you say whether there are any businesses where it is possible to carry out business structure reforms or withdraw low-profit or unprofitable products?

A13: Generally speaking, it has become difficult to maintain businesses that have unprofitable or low-profit products, so we have made no changes to our approach, which is to assess the future, consider measures, and take the next step as a company. In the 2025 Mid-Term Plan, we are undertaking initiatives in the food business to shift toward product groups with higher added value in the form of functional foods. Please understand that we are proceeding in this way with product line reorganization for unprofitable and low-profit items.

Capital policy

Q14: We would like to ask about returning profits to shareholders, as discussed on page 38 of the presentation material. In the latest results, the total return ratio is over 80%, which is quite high and greatly exceeds the target level of around 50% in the 2025 Mid-Term Plan. Will you continue to pursue a policy of high returns? Or, since capital had become slightly too inflated, did you provide high returns this time as a temporary measure to reduce capital? Could you give us any hints about your future return policy?

A14: Generally speaking, as we are steadily pursuing strategic investments in the 2025 Mid-Term Plan, the target level for the total return ratio is set at around 50%. In FY2024, based on the net cash level, future free cash flow level, and ROE conditions, we announced that we would repurchase an additional 10 billion yen of shares in May 2025 as part of our profit return for FY2024. In FY2025, we are maintaining a target total return ratio of around 50%, but recognizing that returning profits to our shareholders is one of our most important management issues, we intend to consider agile share repurchasing aimed at improving capital efficiency.

Q15: Is the reason that you decided to repurchase 20 billion yen of shares as part of FY2024 to ensure that you would achieve the target ROE of 12% or more in the 2025 Mid-Term Plan? Could you confirm that aiming for the same level in FY2025 as FY2024 means that you are considering the same level of share repurchase?

A15: We will consider share repurchases in FY2025 as well based on the planned performance targets, total return ratio, ROE, and other factors during the period of the 2025 Mid-Term Plan. Looking ahead to the next Mid-Term Plan, please understand that we will continue to carefully examine and consider the details of the target level of returns to shareholders, based on the recognition that returning profits to our shareholders is one of our most important management issues.

Governance

Q16: In evaluating performance-linked compensation for your Directors, points are allocated based on the ROE and operating profit achievement level, but does this not provide an incentive to set a conservative ROE and operating profit targets?

A16: An ROE target is set to evaluate performance-linked compensation. Naturally, the Board of Directors discusses what form it should take. We will continue to consider this matter, including the possibility of revising the evaluation methods.