Business Results Meeting for the Second Quarter of the Fiscal Year Ending March 31, 2022: Questions and Answers

[2022 Mid-term Management Plan]

General

Q1: The operating income target in Stage I of NOF VISION 2025, which is part of the mid-term management plan, is predicted to be achieved a year earlier than initially planned. Are you considering revising the operating income for FY2022, which is the final year of Stage I? Also, what is your vision for Stage II?

A1: We had a good business year in FY2021 and are likely to achieve the operating income target a year ahead of schedule. As for FY2022, which is the final year of Stage I, we will decide on the target figure after the budgeting process begins. Likewise, we will review the FY2025 target when we create the new mid-term management plan in FY2022.

Q2: What is your assessment of the progress of the various strategies, including capex, provided in the mid-term management plan?

A2: Our overall business as well as the individual strategies are producing good results. Capital expenditures are also according to plan.

Q3: You have predicted that you will achieve the operating income target a year earlier than initially planned. Is that mainly because of external factors? Or, do you think that it is because the individual strategies have achieved good results?

A3: There are doubtless external factors such as the recovery in demand, but we see this as the result of our individual strategies, such as product development that can respond to that kind of environment.

[FY2021 Business Results Forecast]

Business environment

Q4: Sales and operating income in the Functional Chemicals segment are expected to decrease in the second half of the fiscal year. How are the first half progress and the second half forecasts for your flagship products, such as cosmetic ingredients, anti-corrosion agents, and automobile-related products?

A4: In the first half of the fiscal year, online sales of cosmetic ingredients increased and are expected to maintain a recovering trend during the second half. Although the COVID-19 pandemic has impacted this area, we still think that sales will continue to recover at least for the current fiscal year.
Anti-corrosion agents and automobile-related products have been affected by the semiconductor shortages since the late first half. We predict that the impact will continue to expand during the second half, but full-year sales are estimated to exceed those of the previous year.

Q5: Please explain the situation regarding the impact of high raw materials costs and price hikes in the Functional Chemicals segment and the Life Science segment. Also, please describe how you are addressing the spike in logistics costs.

A5: In the Functional Chemicals segment, the raw materials price hikes are primarily affecting fatty acid derivatives, surfactants, and organic peroxides. In the Life Science segment as well, the price hikes are severely affecting edible oils. To address these raw materials price hikes, we revise product prices to make the business profitable, but we cannot use the product price to absorb all raw materials price increases. We will continue to work to secure profitability as we ask our customers to understand the situation.
As for logistics costs, we will ask customers to pay for this as necessary during the course of the price revision process.

Q6: Sales in the Life Science segment increased during the first half of the fiscal year, and you adjusted the full-year performance prediction upward. Please explain the reason why. My guess is that the DDS business is the main contributor, but I would still like to know the reason for the sales increase.

A6: As you correctly pointed out, the sales increase in the DDS business supported the sales increase in the Life Science segment during the first half of the fiscal year. The sales increase came from the increased demand for products related to the COVID-19 vaccines. Our prediction for the second half is that demand will settle down and sales will decrease slightly.

Costs including fixed costs

Q7: Page 13 of the "Financial Results" shows the factors that contributed to the operating income difference. Compared with the operating income for the first half results on page 5, fixed costs increased during the second half. Please explain why. Also, please explain why the inventory valuation increased.

A7: Fixed costs increased because sales activities are returning to normal, and the associated costs are expected to increase.
As for inventory valuation, we assume that the inventory level will be higher than the end of FY2020 in the Functional Chemicals segment. This has been incorporated as a positive influence.

[DDS Business]

Q8: Is your DDS being used for the purpose of the COVID-19 vaccines?

A8: We must refrain from providing details due to confidentiality obligations, but our PEG lipids are being used for COVID-19 vaccines.

Q9: What is your view of the future growth rate of the DDS business?

A9: Although it varies by fiscal year, we estimate that it will keep growing by about 10% annually.

Q10: While page 14 of "Expansion of DDS Business" states that product sales for COVID-19 vaccines are expected to decrease, the sales plan on page 23 shows a sales increase. Will there be no impact due to the decrease in product sales for COVID-19 vaccines?

A10: It is not that there will be zero impact. The relevant sales plan includes a sales increase expected to manifest when our product lineups for peptide/protein drugs, which are not for COVID-19 vaccines, are released to the market as they become ready.

Q11: Page 16 of "Expansion of DDS Business" is about ionizable lipids and PEG lipids. How much of current overall DDS business sales do sales of these lipid products account for? Also, in this document, sales of lipids for nucleic acid drugs are predicted to increase by 30% annually. Do you think that sales of the DDS business will increase accordingly?

A11: We are considering the use of ionizable lipids and PEG lipids for nucleic acid drugs, and we are planning to increase their sales. However, we cannot disclose the current sales breakdown. Please note that we expect future growth.
As for the overall DDS business, we estimate that annual sales growth will be about 10%.

Q12: I heard before that annual sales growth would be about 8%. Did anything slow down the growth, such as suspension of clients' research activities due to the COVID-19 crisis?

A12: The COVID-19 crisis has had no impact on research and development. The business is growing steadily at about 10% annually.

Q13: At present, are sales of ionizable lipids and PEG lipids small in scale?

A13: We are unable to disclose the scale of individual product sales, but we can say that PEG lipids are used for COVID-19 vaccines.

Q14: Will your business be affected by a decrease in future demand for products to be used in COVID-19 vaccines?

A14: The demand decrease will have an impact. However, we still forecast total annual sales growth of about 10% by expanding our product lineups for other nucleic acid drugs.

Q15: According to page 14 of "Expansion of DDS Business," the COVID-19 vaccine market will contract in size from 2022. Do you think that the sales volume will also decrease?

A15: The graph on page 14 of "Expansion of DDS Business" has been created by NOF based on Evaluate Pharma's data. With the emergence of oral medicine, the future market trend is uncertain. As far as FY2021 is concerned, demand for our product rapidly increased during the COVID-19 vaccine shortages.

Q16: You plan to spend over 10 billion yen to strengthen production capacity. If you have a definite figure for the increase, please provide it. I would also like to know if you have increased the investment value over the amount indicated in the initial plan.

A16: We plan to double the production capacity from the current level. The amount of investment has increased slightly from the initial plan due to consideration of the release timing of our leading products, including activated PEGs.

Q17: How do you envision the sales resulting from the investment of over 10 billion yen?

A17: We believe that the size of the resulting sales will enable us to recover the investment and to expand the business.

Q18: Have you decided when exactly you will make the investment?

A18: We are in the process of deciding when, but we plan to complete the investment of over 10 billion yen by FY2025.

Q19: Where do you think you will strengthen the manufacturing equipment for activated PEGs and ionizable lipids?

A19: We are thinking about our Aichi Works.

Q20: Did you have DDS-related manufacturing equipment at Aichi Works?

A20: We currently do not.

Q21: What are the reasons for installing the manufacturing equipment at Aichi Works?

A21: We plan to make a capital investment at Aichi Works for BCP reasons.

Q22: Does strengthening of the sales system for the DDS business include further expansion of business bases?

A22: We opened a new satellite office in Boston this September. We will consider opening other satellite offices depending on the situation.

Q23: Who are your competitors in the DDS business? What are your strengths over those competitors?

A23: We have multiple competitors in the lipid product area in Europe, the US, China, and other countries. However, we cannot disclose any of the details. As for activated PEGs, we believe we have the largest share globally.
Our strengths are our rich GMP track record, offering of products from laboratory scale to pilot or commercial scale to match clients' product development stages, advanced manufacturing techniques, and our GMP-compliant quality control system.

Q24: Where are your DDS products in terms of upstream and downstream?

A24: We provide chemicals to pharmaceutical companies as intermediate materials.

End of Q&A