Summary of Financial Results Briefing for Q2 Fiscal 2023

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Asahi Kasei Corporation

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Presentation

P. 2 Focus of H1 2023 results and FY 2023 forecast

Horie: In H1 2023, sales remained flat year-on-year, but operating income declined. Homes performed well, but Material was affected by a demand slowdown and lower market prices, and Health Care was affected by increased costs and the impact of an acquisition in the Health Care business category. However, all segments exceeded the forecast announced in August.

For FY 2023, we expect an operating income increase in all segments compared to the previous year. In Material, the business environment is expected to remain challenging, but we anticipate improved performance centered on growth businesses by enhancing marketing activities. In Health Care, Critical Care is expected to perform well. In response to rising feedstock costs, we will continue our efforts for price pass-through, manufacturing cost reductions, and inventory reductions. Meanwhile, we intend to accelerate studies on structural transformation of our business portfolio and put some of it into action.

We have not changed our policy on shareholder returns, and have set an interim dividend of 18 yen per share. The annual dividend is forecasted at 36 yen per share.

Regarding the progress of the medium-term management plan, we recently decided to add coating lines for Hipore wet-process LIB separators in the U.S., Japan, and Korea.

P. 4 Financial results for H1 2023 (consolidated)

Net sales for H1 were 1,345.9 billion yen, largely unchanged year-on-year. Operating income was 55.9 billion yen, down about 35%, and net income attributable to owners of the parent was 30.8 billion yen, down about 40%.

P. 5 Results by segment (year-on-year)

In Health Care, operating income declined by 6.0 billion yen year-on-year, with a decrease of 7.0 billion yen in the Health Care business category partly offset by an increase of 1.0 billion yen in Critical Care. Pharmaceuticals saw an increase in SG&A expenses due to the launch of new drugs in Japan, while Medical had a negative effect due to the difference in the consolidation period of Bionova, which was three months from July in H1 2022. On the other hand, Critical Care had increased operating income due to an improvement in the reimbursement status for LifeVest wearable defibrillator, higher sales prices of defibrillators, and increased AED sales volume due to improvement from difficulty in parts procurement.

Homes performed well, with operating income increasing by 1.7 billion yen. Construction Materials also had increased operating income as a result of progress in passing on increased costs.

Operating income in Material decreased by 22.9 billion yen due to lower sales volume and inventory valuation loss in Basic Materials, and lower sales volume in Life Innovation from sluggish demand.

P. 6 Results by segment (vs. H1 2023 forecast in Aug.)

Compared to the previous forecast announced in August, operating income exceeded expectations in all segments.

Health Care remained basically in line with the previous forecast, with an upward revision of 0.8 billion yen.

Homes exceeded the forecast by 4.6 billion yen due to better-than-expected progress in construction work and reduced fixed costs in order-built homes.

Material exceeded the forecast by 5.6 billion yen with better-than-expected sales of car interior material and engineering plastics in Mobility & Industrial, and inventory valuation gain in Basic Materials due to the sharp rise in naphtha prices since August.

P. 7 Results by segment (changes in quarterly operating income)

Looking at the consolidated operating income trends separately for Basic Materials and the rest of the businesses, each is on a recovery trend after bottoming out in Q4 2022, and this trend is expected to continue in H2.

P. 8 Statements of income

Net of non-operating income and expenses for H1 was expenses of 3.8 billion yen compared to income of 0.6 billion yen in the same period of the previous year. This was mainly due to a 2.3 billion yen net decline for equity in earnings/losses of affiliates due to a deterioration of earnings at PTT Asahi Chemical Company Limited in Thailand.

P. 9 Extraordinary income and loss

While extraordinary items netted a loss of 5.7 billion yen in H1 2022, this transitioned to income of 1.9 billion yen in H1 2023. A gain of 3.0 billion yen from the transfer of the pellicle business to Mitsui Chemicals, Inc. was recorded in H1 2023.

P. 10 Balance sheets

Total assets increased by 164.5 billion yen from the end of March to the end of September 2023. Current assets and noncurrent assets increased by 51.1 billion yen and 113.4 billion yen, respectively, due to an increase in the yen value of assets of overseas subsidiaries caused by exchange-rate movement. The yen value of liabilities also increased centered on overseas subsidiaries for the same reason. In net assets, accumulated other comprehensive income increased by 144.3 billion yen due to an increase in foreign currency translation adjustments, also caused by the weaker yen.

D/E ratio was 0.51, with no significant change from the end of March 2023.

P. 11 Cash flows

Operating cash flow was a net cash inflow of 133.9 billion yen, a 137.6 billion yen improvement year-on-year. A decrease in working capital due to a reduction in inventories was a major contributor.

Cash used in investing activities decreased year-on-year, due to the absence of M&A-related expenditures in H1 2023.

As a result, free cash flows were a net cash inflow of 46.4 billion yen, an improvement of 181.3 billion yen year-on-year.

P. 13 FY 2023 operating performance forecast (consolidated)

For the full year, we forecast net sales of 2,822.0 billion yen and operating income of 140.0 billion yen, up 3.5% and 9.6% from the previous year, respectively. Net income attributable to owners of the parent is expected to be 85.0 billion yen in FY 2023, in contrast to the loss of 91.9 billion yen in the previous year due to impairment on Polypore.

The forecast assumes an exchange rate of 145 yen per U.S. dollar and a domestic naphtha price of 74,000 yen per kiloliter for H2.

P. 14 FY 2023 operating performance forecast by segment (year-on-year)

Operating income for the full year is expected to increase year-on-year in all segments.

For Health Care, the forecast is for an increase of 4.5 billion yen. Although the Health Care business category is expected to see decreased operating income due to higher SG&A expenses, lower license income, and higher feedstock and fuel prices, overall operating income is expected to increase with strong performance in Critical Care.

Homes is forecasted to have operating income increase by 4.4 billion yen. While operating income in order-built homes is expected to decrease due to a decline in volume and the impact of rising material costs, it is expected to increase in real estate and overseas operations. Construction Materials is also expected to see an increase in operating income due to progress in passing on increased costs. Full-year operating income for Homes is projected to be 79.8 billion yen, a record high.

Material is forecasted to see operating income increase by 8.5 billion yen. We expect an increase in sales volume of separators and lower amortization of goodwill and other intangible assets due to the impairment on Polypore in the previous fiscal year in Environmental Solutions, and an improvement in demand and expanded adoption of electronic components and electronic materials in Digital Solutions.

P. 15 FY 2023 operating performance forecast by segment (vs. forecast in May)

The full-year operating income forecast was revised downward to 140 billion yen from the initial forecast of 160 billion yen announced in May.

Health Care is expected to remain essentially in line with the initial forecast.

Homes was revised upward by 2.1 billion yen due to strong performance in real estate and progress in passing on price increases in Construction Materials.

Material was revised downward by 16.6 billion yen. The main reasons for the downward revision are lower sales volume due to slower-than-expected demand and worsening terms of trade in Basic Materials. On the other hand, Mobility & Industrial is revised upward due to steady growth in car interior material.

P. 16 Operating performance forecast (Changes from H1 to H2 2023)

The full-year forecast assumes an operating income increase of 28.2 billion yen from H1 to H2. Of this amount, 14.0 billion yen is expected in Material, 9.1 billion yen in Homes, and 6.7 billion yen in Health Care.

In Material, we forecast an increase of 7.9 billion yen in Environmental Solutions due to nonrecurrence of the impact of the maintenance turnaround in H1, an increase in sales volume, inventory valuation gain, and the effect of efforts to improve margins in Basic Materials. In Life Innovation, we forecast an increase of 7.1 billion yen with steady growth in Digital Solutions, including new adoptions of electronic components and electronic materials.

In Homes, we forecast an increase of 10.5 billion yen in the Homes business category due to seasonal factors in order-built homes and an increase in the number of condominium units delivered in real estate.

In Health Care, we forecast an increase of 2.5 billion yen in the Health Care business category due to increased sales, and an increase of 4.3 billion yen in Critical Care due to increased sales of AEDs as a result of the improvement from difficulty in parts procurement.

P. 17 Shareholder returns

The interim dividend for FY 2023 is set at 18 yen per share. The annual dividend is expected to remain unchanged at 36 yen per share, the same as the previous year, resulting in a payout ratio of 58.7%. There are no changes to the shareholder returns policy.

P. 19 Material: Sales and operating income increase/decrease

Now I will explain the factors behind the change in H1 operating income of Material compared to the same period of the previous year. Terms of trade improved, as the negative impact of the sales prices factor was offset by the positive impact of the feedstock costs and foreign exchange factors. On the other hand, the sales volume factor was negative 9.2 billion yen due to a slowdown in demand. Due to lower capacity utilization resulting from the volume decline, as well as inventory valuation loss, the others factor was negative 21.9 billion yen. Overall, the segment posted a significant 22.9 billion yen decrease in operating income year-on-year.

P. 20 Material: Overview by business

The trends of each business from H1 to H2 are shown here.

Environmental Solutions is expected to see an increase in operating income in H2 due to a large decrease in costs, especially in Basic Materials, as well as the effect of a slight improvement in margins. Separators will remain at roughly the same level from H1 to H2.

As for Mobility & Industrial, the H2 forecast is roughly even with H1, but there is room for actual results to be slightly better than forecasted.

With regard to Life Innovation, we forecast an increase in operating income mainly because we expect steady growth in Digital Solutions, especially in areas where we have strengths.

P. 22 Material: Trends in separator business

The left graph shows the sales volume of Hipore. In recent years, the sales volume of automotive applications has exceeded that of consumer electronics applications. In H1 2023, sales volume decreased as it was a transitional period when there were changes in some of the vehicle models using our products in automotive applications. The graph on the right shows the performance of the separator business as a whole, including Hipore and Polypore businesses. Against the same background, EBITDA was at about the same level in H2 2022 and H1 2023. On the other hand, the recently announced expansion of coating capacity is expected to improve the operating rates of base film manufacturing facilities, and earnings are expected to recover going forward.

P. 23 Homes: Sales and operating income increase/decrease

Homes posted a year-on-year operating income increase of 1.7 billion yen in H1. The effect of the others factor was a positive 3.0 billion yen with increased deliveries of condominium units from large projects in real estate, as well as improved earnings in Construction Materials due to progress in passing on increased costs.

P. 24 Homes: Overview by business

Order-built homes, real estate, and overseas operations are all expected to have operating income increase from H1 to H2. In order-built homes, there is a seasonal factor with earnings skewed toward H2. In real estate, large condominium projects are scheduled to go on sale in H2. Overseas business also expects an increase in volume in North America.

P. 28 Health Care: Sales and operating income increase/decrease

H1 operating income of Health Care was down 6.0 billion yen year-on-year. The Health Care business category saw a decrease in operating income, with the others factor being significantly negative due to the difference in the consolidation period of Bionova and the increase in SG&A expenses associated with the launch of new drugs in Pharmaceuticals. The others factor for the segment as a whole was negative 9.2 billion yen.

P. 29 Health Care: Overview by business

As for the Health Care business category, operating income is expected to recover in H2 due to an increase in sales volume. As for Critical Care, we expect an increase in operating income due to higher sales centered on AEDs.

P. 35 Overseas Sales

Overseas sales accounted for 53% of total sales in H1. By region, sales in China decreased to 9.0% from 9.5% in the same period of the previous year, while sales in the Americas grew from 18.8% to 20.9%. The trend is for a general decline in Asia due to lower sales in China and nearby countries.

Questions and Answers

Questioner 1: Regarding Material, what are the demand environment and market price assumptions for petrochemicals for H2? And, while Mobility & Industrial is expected to experience sluggish growth in H2, to what extent do you anticipate an impact from the United Auto Workers of America (UAW) strike? In Digital Solutions, you expect a significant increase in operating income in H2 compared to the profit level in Q2, but what is the background to this?

In addition, you have reduced inventories considerably. Which business did you see major reduction in?

Tanaka: Let me take up acrylonitrile (AN) to explain assumptions for petrochemicals in Environmental Solutions. We expect the demand environment to remain challenging, and we have lowered our initial forecast assumption for global demand for AN in 2023 to the same level as in 2022. Our assumption of market prices and spreads for H2 are $1,250/ton for AN and $850/ton for propylene, for a spread of $400/ton, which is lower than our initial forecast assumption. Inventories in Basic Materials increased in H1 due to the maintenance turnaround, which had a considerable negative impact on operating income, but we are currently working to reduce inventories to the minimum necessary.

Questioner 1: Since the naphtha assumption for H2 is 74,000 yen/kL, is the impact of inventory valuation loss expected to improve from H1?

Tanaka: Significant improvement is expected for H2.

Moriwaki: I will answer regarding Mobility & Industrial. In H2, we expect sales of car interior material to decline due to seasonal factors such as the Christmas vacation, as well as the impact of the UAW strike in the U.S. On the other hand, sales of engineering plastics and nylon intermediates are expected to increase as automobile production recovers. In particular, for engineering plastics, sales of products for solar panel applications are firm and expected to increase further. The yen depreciation will also be a factor in operating income growth. As for performance coating materials, we expect sluggish sales in China and other markets to continue in H2.

Overall, sales are expected to increase, but operating income to remain flat, due to the relatively high profitability of car interior material. More fixed costs being incurred in H2 than in H1 is another reason why operating income is not expected to grow.

Regarding inventories, engineering plastics and performance coating materials have had a high inventory level since FY 2022, but this is being reduced in H2.

Igarashi: Regarding Digital Solutions in Life Innovation, there is a wide variety of applications, including devices such as smartphones, electric vehicles, industrial equipment such as air conditioners, and infrastructure-related equipment such as servers and switches, but overall demand is expected to recover from the decline that began in H2 2022.

In addition, we expect to see new adoption and expanded use of products that we have focused on developing and marketing. For example, we have been focusing on expanding adoption of sound management products and current sensors for automotive applications, and products for camera modules for smartphone applications, targeting existing customers in established markets, and we are seeing the results of these efforts. In addition, the server-related market is currently booming due to the increase in data transmission volume resulting from the spread of generative AI, and demand for related electronic materials is expanding significantly. The adoption of our products is also progressing, and we expect further expansion in H2.

Questioner 2: I would like to ask about the background behind the forecast of record-high profits in Homes for FY 2023. Order-built homes is expected to see a large recovery in H2. Regarding orders, while H1 was sluggish, they were firm in October, so is it safe to assume that the bottom has been reached? And is the strong performance of real estate transitory? Or will it continue in FY 2024 and beyond? In addition, please tell us how you are dealing with rising material and labor costs.

Kume: From H1 to H2, all divisions in Homes are planning to increase operating income. In order-built homes, there is a seasonal increase in volume in H2. In real estate, the number of condominium units delivered is expected to increase with large projects going on sale in H2. In overseas business, construction volume is expected to recover in North America.

Orders received in order-built homes were negative 16.4% year-on-year in Q1, but were positive in Q2 and recovered to negative 2.4% year-on-year for H1. Most recently, September and October were both positive year-on-year. In H2, we will continue to pursue our marketing strategy of larger and higher value-added products and expect to achieve +5% year-on-year for the full year.

Higher material and labor costs are putting pressure on our performance, but we will continue to make efforts such as fixed cost reductions.

Questioner 2: Homes performed well in H1 with an increase in the number of large units in order-built homes and large condominium units in real estate. Is this a structural change and can we expect a similar level of performance in FY 2024 and beyond?

Kume: In order-built homes, performance in FY 2024 and beyond will depend on the future recovery of orders, but we will continue to promote larger and higher value-added products and strive to maintain sales. In real estate, number of units of condominium units sold varies from period to period, but for FY 2024, we expect a certain amount.

Questioner 3: I would like to ask about Health Care. First, regarding Critical Care, has the parts procurement difficulty been improving steadily? Also, with regard to defibrillators for professional use, orders have been sluggish since H2 2022, but has there been any recent improvement?

Second, regarding Pharmaceuticals, your initial projection for this year’s sales growth of Envarsus XR immunosuppressant was about 30% over the previous fiscal year. Sales increased by 21% in H1, but what are the forecasts for H2 and the full year? Also, it seems that sales of a generic of Teribone osteoporosis drug have been suspended since September. Is there a possibility that sales of your lyophilized formulation will increase in H2 as an effect? And what is the progress of sales promotion of the autoinjector formulation?

Third, regarding Medical, is it correct to understand that the downward revision to the forecast of Bionova, a CDMO, is due to market factors such as the financial difficulties of biotech startups and not due to individual factors of your company?

Otsubo: To answer the first question regarding Critical Care, in FY 2022 parts procurement difficulties hindered the manufacture of various products, resulting in a decline in sales, higher procurement costs, and lower capacity utilization. However, that was mostly resolved in H1 and sales volume is increasing. We expect parts procurement costs to decline further and capacity utilization to improve in H2. The profit margin for defibrillators has also improved, due in part to our efforts to pass on higher procurement costs to selling prices.

Orders for defibrillators for professional use have been sluggish since H2 2022. In the year-on-year operating income variance shown on page 28 of the presentation materials, sales volume factor was negative in Critical Care. This is due to a change in the product mix with AEDs increasing and defibrillators for professional use decreasing. We expect defibrillators for professional use to gradually improve in H2, but we will continue to monitor the situation closely.

To answer the question about Envarsus XR, sales in the U.S. in H1 2023 were up 21% year-on-year. Q1 sales was up 32%, while Q2 was lower than that due to fewer business days in the U.S. compared to the previous year, as well as the fact that wholesalers had a large inventory of the product. However, sales have been steadily increasing, and we expect sales to grow at the initially expected level in H2.

Takahashi: I will answer about Teribone in Pharmaceuticals. With the sale of a generic of lyophilized formulation of Teribone suspended, we expect a positive impact in H2, which includes a halt in the decline in sales. However, since a certain amount of the product has already been delivered to wholesalers and medical institutions, the effect of increased sales in FY 2023 will not be that large. We expect sales increase in FY 2024 and beyond.

Although sales of the autoinjector formulation have been slower than originally planned due in part to the allocation of resources to the lyophilized formulation, we will step up promotion in H2.

Otsubo: To answer your question about Bionova, located on the West Coast of the U.S., its customers are biotech startups, whose financial situation does not seem to have improved significantly yet. Although it is difficult to foresee a short-term improvement in business performance, we believe that the market for next-generation antibody drugs will grow over the medium to long term. Watching the improvement of our clients' cash flow situation, we intend to seize the opportunity when demand returns.

Questioner 4: Critical Care increased its sales and operating income from Q1 to Q2, with a particularly large improvement in operating income. What are the factors contributing to that? Also, please explain the trends of your mainstay products such as defibrillators for professional use, AEDs, and LifeVest. Is the improvement in LifeVest's reimbursement status expected to continue through H2 and into FY 2024? As for the increase in sales volume of AEDs, is the final demand strong? Or was there pent-up demand due to parts procurement difficulties?

Otsubo: Critical Care increased its operating income by 3.4 billion yen from Q1 to Q2, largely due to an increase in the sales volume of AEDs as a result of improvement from difficulty in parts procurement.

With regard to trends in mainstay products, sales of defibrillators for professional use remained largely unchanged from Q1 to Q2. Sales of AEDs are expected to continue to increase in H2, which will be a major factor in the operating income growth. New orders have been received in addition to the backlog of orders that had not been shipped due to parts procurement difficulties, and we expect steady growth in the future. LifeVest sales remained mostly flat with a seasonal drop in demand in Q2 being offset by the positive impact of improved reimbursement status from Q1 to Q2. Volume growth is expected in H2 due to reinforcement of the salesforce, but we anticipate a slight decrease in operating income due to the upfront increase in SG&A expenses and labor costs. However, for FY 2024, we expect growth in volume with an expansion of marketing capability.

Questioner 4: Do you expect AED sales to continue to grow in FY 2024? Also, regarding the improvement in the reimbursement status of LifeVest, please tell us the expected impact in H2 and whether there will be further improvement in FY 2024.

Otsubo: New orders for AEDs have been firm, and we expect growth in FY 2024.
Regarding LifeVest, there was an improvement in reimbursement status for a major U.S. health insurance program in Q4 2022, which had a positive impact in H1 as it was applied to new patients, but the impact is not expected to be significant from H1 to H2. Reimbursement conditions are generally reviewed on a regular basis, such as once a year, and are determined by medical insurance organizations based on a variety of factors. This time, the improvement in reimbursement status was relatively large, partly due to inflation, but it is difficult to foresee what will happen next time.

Questioner 5: Digital Solutions in Material is expected to recover significantly from H1 to H2. In the past, there has been a seasonality in electronic components and electronic materials with sales declining in Q4 due to the Chinese New Year, but what specific applications are expected to grow? Is it the recovery of smartphones in China? Or the expansion of demand for AI-related servers? Also, what will be the major contributors in terms of products?

Igarashi: The impact of the Chinese New Year has eased somewhat compared to a few years ago due to recent trends of the staggering of smartphone production times and our products being used in a wider variety of models.
In electronic components, the growth area in H2 is automotive applications, such as electric vehicles, where adoption is expanding as the result of marketing activities. And in electronic materials, there are high expectations for AI-related server applications. The use of electronic materials tends to increase as substrates become larger and more multi-layered, and the use and adoption of our glass fabric, dry film photoresist, and other materials are on the rise.

Questioner 5: Do you expect a recovery in smartphone production in H2, including in China? Also, is it correct to assume that adoption of your products is progressing for large substrates for AI-related servers? Is the glass fabric business also firm?

Igarashi: Smartphones, especially high-end products, are expected to be firm, while the recovery of low-end to mid-range products in China is expected to be sluggish. Since many of our products are for high-end applications, they are expected to be firm compared to the market as a whole.
The adoption of our electronic materials for AI-related servers is as you have indicated, and it is expanding in line with the growing demand. This is a field that will continue to grow, and we plan to capture demand with certainty. Adoption of our glass fabric is also expanding, and we expect an increase in sales volume.

Questioner 6: I would like to ask about the Homes business category. The full-year operating income forecast for order-built homes has been revised downward by 900 million yen, from 34.1 billion yen to 33.2 billion yen. Considering that the H1 results were 14.9 billion yen, exceeding the initial forecast of 11.2 billion yen by 3.7 billion yen, the H2 forecast was revised downward by 4.6 billion yen. What is the background to the large downward revision in H2 compared to the strong performance in H1?

Kume: The H1 operating income results exceeded the initial forecast due to construction work progressing ahead of schedule and reduced fixed costs. On the other hand, the H2 forecast has been revised downward due to the fact that orders received in H1 were lower than initially expected.

Questioner 7: With regard to the Homes business category, is it correct to assume that the H1 results exceeded the initial forecast due in part to some profits being brought forward from H2? Also, while demand for unit homes was weak, orders in October were strong. Is there any factor unique to your company behind this? Or is there a surge in demand as interest rates are rising? With regard to condominiums in real estate, there seems to be an abundance of units until FY 2024. Is there still a possibility that more units will be added in FY 2025 and FY 2026?

Kume: The H1 results partly benefitted from the profits brought forward from H2, as well as the reduction of fixed costs. We do not believe that there has been any surge in orders. Although the environment for orders is difficult, we believe that our strategy of larger and higher value-added products is gradually gaining traction and we are on the road to recovery.

In FY 2024 and FY 2025, we expect a certain number of condominium units for sale, and we are continuing to promote the business for FY 2026 and beyond.

Otsubo: That concludes the financial results briefing. Thank you for your participation.