

August 25, 2021

## **FY 2021 1Q Results Briefing: Gist of Questions and Answers Session**

### Status of the existing businesses

- **How much was the impact of the unprofitable projects in the AP-related business on the first quarter operating income, and how much of loss from the unprofitable projects are included in order backlog?**

→ We record a provision for loss on order received at the end of each term for unprofitable projects whose estimated cost of sales exceeds sales proceeds among order projects. In the first quarter, there were two unprofitable projects and the total loss from them was 82 million yen. We were expecting a loss on these two projects as of the account settlement at the end of the previous fiscal year and we recorded 50 million yen in provision for loss on order received. However, there was a discrepancy between the estimated and actual cost of sales, and we additionally recorded a loss of 32 million yen, which is the difference, in the first quarter of the current fiscal year. Provision for loss on order received on the balance sheet as of the end of the first quarter is 74 million yen. There is some gap between the estimated and actual cost of sales, and unprofitable orders included in order backlog based on the current accounting estimate is 74 million yen.

- **The environments of other industries appears to be similar, but the business performance of AP and that of BP seem to be going in different directions. How should we view this?**

→ Regarding AP, it is time to replace the plants built in concentrated capital investment from the 1980s to mid-1990s, and we believe the business environment is good. For BP, there was a period when the unit price of ready-mixed concrete did not rise and customers continued to hold back on capital investment. However, the business environment for BP is also favorable given the relatively stable high ready-mixed concrete price in recent years and is right timing for the renewal of facilities.

→ As for the difference between the direction of business performance, it probably is an indication that there should be more domestic profits from AP. While the two unprofitable projects dragged down the profits in the first quarter, domestic sales and new orders received at the moment continue to be at high levels, so we do not think the business environment is bad. BP had been very good in the previous year and the year before that, so we did consider the possibility of a reactionary decline. Nonetheless, the start was strong and we are negotiating a large number of projects in the second quarter. So, we do not think orders would fall below last year's level, and we expect sales and profits

are performing relatively favorably.

- **It sounds a little awkward that the environment- and conveyor-related business could not carry out sales activities due to COVID-19. It seems like it is about time for a recovery. Could you please explain the monthly sales trends, at least for conveyors?**

→ Unlike AP and BP, we could not carry out sales activities for the environment- and conveyor-related business due to COVID-19 and the business has been stagnant in the previous as well as current fiscal years. That situation has not changed. Regarding whether it should be time for a recovery, the monthly figures through June were not good but it has slightly recovered in the month of July. However, it is highly likely that the fifth wave of COVID-19 would put brakes on sales activities from August on.

#### Overseas business

- **When we look at overseas expansion based on figures, the business in China is extremely strong. What are your thoughts on the expansion and strategy in Southeast Asia including Thailand?**

→ In Thailand, we established a sales subsidiary and manufacturing subsidiary in the previous fiscal year and are currently constructing a plant in a 40,000 m<sup>2</sup> plot of area. The plant was initially supposed to start operations from October 1, but the construction period was extended due to the impact of COVID-19 and the weather. We expected it to start operations in January of next year. Once the plant starts operating, we will have a business model where we can sell products that are produced locally in Thailand. We have explained that we received orders for two units of AP and have 10 more highly likely projects. Nevertheless, it is not possible to manufacture products with the same quality as the ones produced in Japan soon after a plant starts operations, so we believe we need to have a system to support it from Japan. We would like to establish a system that enables fully localized manufacturing at the Thailand plant as soon as possible.

→ We have not made any concrete decisions regarding the strategy for Southeast Asia other than Thailand, but we are looking at Indonesia, Vietnam, and other countries as next candidates. The population of Indonesia is forecast to continue growing toward 2030 to 2040 and also given its large land area, it has the potential of greatly exceeding Thailand in terms of AP market size. We would like to start sales activities in Indonesia as early as possible. Regarding whether or not to build a plant in Indonesia, given that the Thailand plant is larger than the one in China, with a production capacity of 30 units or more per year from the beginning compared with 25 units of the Chinese plant, we are thinking of making Thailand as the production base and exporting to Indonesia and Vietnam for the time being. We are also interested in other Southeast Asia countries, but we cannot

make forays into all of them at once, so we would like to expand into them gradually.

- **What kind of profitability is there for the AP projects in Thailand, China, and Taiwan? Also, what are the potential orders you are looking at in the next five years or so from the contract with the Thailand agents?**

- As for profitability in Thailand and China, there are almost no sales from maintenance service in China as we sell plants with no associated maintenance. In Thailand, we also expect to sell plants without maintenance for the time being. For this reason, we are aiming for at least 10% in gross profit ratio. We would like to proceed with similar profitability for Thailand and China. The margin is relatively high in Taiwan. Environmental restrictions in Taiwan are becoming more strict and since our environment-compatible plants have an advantage in the country, we are securing higher profitability of AP projects in Taiwan compared with Thailand, China, and Japan.
- Regarding the potential from the contract with Thailand agents for the next five years or so, we assume there are about 500 plants in Thailand. The renewal cycle of plants in Japan is 30 to 40 years, but it is thought to be 20 years or less in Thailand. Based on such, we estimate that there is demand for 25 units per year of replacement investment. Unlike Japan, Thailand is still building more roads and there are also demand for new plants, so we think it has a market scale of 30 to 40 units per year and we aim to capture 50% of that.

#### Earnings forecast for the current fiscal year

- **Cost of sales ratio was 73.1% in the first quarter and it is expected to improve to 72.5% in full year according to the plan. Is it achievable amid the rising price of raw materials? Or, do you plan to shift the cost to price? What are other measures you are taking against the high price of raw materials?**
- Currently the price of raw materials are rising, with the increase in steel prices having the largest impact. The price of steel has been gradually rising since the end of the previous fiscal year, so we have been changing the quotes for every month from the current fiscal year and negotiating with customers at the quotes that are linked to the market price. While we have been shifting cost to price, we expect some impact because of the orders we received in the past, especially given the time lag between orders and shipment of AP. The raw materials for most of the projects whose sales were recorded in the first quarter were procured before the price of raw materials rose and were used for manufacturing, so there was almost no impact. For the second quarter onwards, we think we are successfully shifting the higher cost of raw materials to the prices because we are negotiating using revised prices and the sales of maintenance services account for about 60% of both AP and BP, and the sales of products account for about 40%. Additionally, the period between receiving order and

sales for maintenance services is not too long. There is some impact to the rise in raw material prices on the full year too, but we are responding with increasing our prices, and we think it would not become a significant negative factor.

#### Carbon neutral-related initiatives

- **Regarding the movement towards trapping CO2 in concrete, the plan was moved forward since the government policy was revised in July. You are probably engaged in joint research with general contractors. If there is any favorable quantitative impact on Nikko, when do you think it is going to be?**

→ We are conducting joint research with various entities including general contractors, but we cannot discuss anything concrete because we have signed non-disclosure agreements for such research. We are actively involved in several projects regarding the move towards trapping CO2 in concrete. However, we do not know when we will start seeing favorable quantitative impact.

#### Next medium-term management plan

- **What are the differences between the current and next medium-term plans?**

→ We are currently in the midst of drawing up the framework for the next medium-term plan and cannot discuss anything concrete. We probably would not be doing anything entirely new, and it will be the third to sixth year plan based on the 10 year policy. One is to accelerate the expansion in Southeast Asia, of which is within the current overseas expansion, and we were able to implement the early start of building the base in Thailand in the current medium-term plan roughly in accordance with the plan. In the next medium-term plan, we would like to consider making forays into Indonesia and Vietnam as the next step. We are assuming that the business environment for AP in Japan would be roughly unchanged in the next three years, and under such circumstances we would like to do something related to the requirements for customer solutions that benefits both customers and us. In particular, we would like to establish a “before-maintenance” business model for the AP and BP maintenance service, currently being readied, in which customers would sign an annual fixed-rate maintenance contract and we check the plants on a regular basis and exchange parts and repair the parts that are likely to cause problems, shifting from the present “after-maintenance” business model. In particular, we would like to focus in the environment-compatible AP products. In addition, we are preparing for remote operation to solve the labor shortage at AP plants of major road builders, who are the main AP users, and we will incorporate this to a certain extent in the next medium-term plan.

- **Is it reasonable to understand that the new medium-term plan will be announced next spring?**

→ We are working on it so that we can announce it next spring and we are planning to work on the details in the second half.

#### Other business

**- The announcement on August 6 regarding the transfer of treasury stock free of charge to employees, was great for raising the motivation of employees, among other things. Could you elaborate further on its aim?**

→ We announced that we will transfer 100 shares in treasury stock for employees and carried out the transfer on August 25. In addition to raising the motivation, while the newly joined employees know that they are joining a listed company, they may not be aware that share price fluctuates every day. We would like the new employees to feel the joy from the rise in the value of their assets, which would go up along with the increase in share price, and think what they should do for the share price to rise. We would also like them to think from the same perspective as the shareholders, and this is why we decided to transfer the treasury stock to the new employees.

Two years ago, which was our 100th anniversary, we transferred the shares using the same scheme to all employees at that time. So, all employees hold Nikko shares. We would like to continue this system to maintain a situation where all employees hold Nikko shares.

**- What are the concrete measures being taken in employee education so as to bring out their best abilities?**

→ Our training concept used to be OJT, but recently we have been steadily expanding into external training, group training, and other training methods. We have been bearing full or half of the expenses for employees who wish to obtain MBAs or other qualifications. We basically provide some form of financial support for almost all employees who want to study to improve their abilities, although it incurs costs.

Note: This summary of the question and answer session was created in part to provide the information to those who did not attend the results briefing. Please note that parts of the text have been edited to improve clarity and enhance understanding.

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