FY 2021 Business Summary and FY 2022 Outlook

Business overview of FY 2021

Construction investment in FY 2021 (fiscal year ended March 2022) is expected to have risen 2.6% compared to the previous fiscal year to 62.6 trillion yen. This is about 75% of the 84 trillion-yen peak recorded in FY 1992. Private construction investment, which account for 59% of the investment, is expected to have risen 3.0% to 38.1 trillion yen, while government investment, which accounts for 38%, is expected to have increased 2.1% to 24.5 trillion yen. By region, Kanto is expected to have seen a 4.7% increase in investment. It probably has gone up by 0.9% in Chubu, 5.7% in Tohoku, and 1.6% in other regions, while declining 1.3% in Kinki. While the Tohoku region had witnessed an increase in investment since FY 2011 due to the recovery and reconstruction demand for the Great East Japan Earthquake, the ratio in the Kanto region began increasing as investments grew for urban redevelopment and Tokyo Olympics-related construction. Going forward, we expect increased investment in construction related to the EXPO 2025 in Osaka, Kansai.

While construction investments grew on one hand, the number of workers in the construction industry decreased on the other by 1.4% from a year earlier to 4.92 million people in 2020, falling to 72% of the 1997 peak of 6.85 million. Of that, those above 55 years in age accounted for a record 36% (in comparison, it was 24% in 2001). With construction investment expected to remain steady, the aging of workers in the industry coupled with the labor shortage is becoming a structural issue in the medium- to long- term. We can expect increasing requirements for workstyle reforms in the construction industry as well as for automation and labor-saving in various construction equipment and plants. At the same time, we are looking at procurement difficulties and cost increases of various raw materials led by asphalt in the short term, with potential impact on not only customers but also on the supply chain and by extension on our business performance.

Business performance in FY 2021

In FY 2021, new orders remained flat at 39,852 million yen compared with a year earlier, while net sales rose 2.6% to 38,846 million yen, and BB ratio (new orders received / net sales) was 1.03 times. As a result, order backlog at the end of the fiscal year increased 14.8% to 16,490 million yen (about 5.1 months' worth of the annual sales). Despite increased revenues, operating income decreased 10.8% year on year to 2,053 million yen, and operating margin fell 0.7 pp to 5.3%. The main factors behind the decrease are the expenses of the launch of the Thailand subsidiary, increases in sales and administrative expenses such as R&D expenses, and recording of sales of unprofitable projects in the AP-related business. Ordinary income declined 23.5% from a year earlier to 2,274 million yen due to the absence of the 340 million yen in special dividends from Maeda Road Construction Co., Ltd. recorded in FY 2020. Net income attributable to owners of parent declined 20.8% from a year earlier to 1,649 million yen, partly reflecting the 326 million yen in proceeds from sale of investment securities recorded as an extraordinary income.

FY 2021 was the final fiscal year of the three-year Medium-Term Management Plan. Orders received exceeded the forecast for FY 2021 of 38,800 million yen by about 3%. While net sales exceed the medium-term plan target of 38,000 million yen, they slightly underperformed the FY 2021 forecast of 39,000 million yen. By contrast, operating income fell short of both the medium-term plan target of 3,000 million yen and the FY 2021 forecast of 2,300 million yen. It was primarily attributable to the shortfall at the AP-related business due to soaring raw material prices and recording sales of unprofitable projects. Regarding shareholder returns, the dividend of 30 yen per share (mid-term dividend of 15 yen and year-end dividend of 15 yen), which translates to a dividend payout ratio of 69.5% given the 1,649 million yen in net income attributable to owners of parent (43.16 yen per share). The payout ratio exceeded the target of 60% or higher presented in the previous medium-term plan.

Business overview by segment

In the AP-related business, new orders in FY 2021 declined 10.4% from a year earlier to 18,180 million yen, net sales fell 5.9% to 18,328 million yen, and BB ratio, derived by dividing orders with net sales, came to 0.99. Orders from overseas led by the Chinese market remained strong but were affected by delays in large-scale projects in Japan and a decline in appetite for capital investment due to surging asphalt price. Net sales also increased 27.1% overseas led by the strong Chinese market, while those in Japan declined 13.5% owing to delays in procurement of various parts. We had order backlog of 7,725 million yen (about 5.0 months worth of annual business). Operating income decreased 54.6% year on year to 562 million yen, and operating margin decreased 3.3 pp to 3.1%. The large profit decline was unavoidable both in Japan and abroad given the soaring prices of various steel materials and parts and the difficulties in obtaining them as well as the rising personnel expenses in China among other reasons.

The BP-related business recorded new orders of 12,086 million yen, up 21.3% year on year, and net sales of 10,839 million yen, up 17.7% year on year. Its BB ratio came to 1.12 times, largely exceeding 1. While the volume of ready-mixed concrete shipment is on a declining trend, the market is showing signs of recovery and users' appetite for replacement investment continues to be high. Operating income of the segment increased 27.8% year on year to 1,123 million yen, and operating margin improved 0.9 pp to 10.4%. Sales increase and cost reduction through planned production made contributions.

In the environment- and conveyor-related business, new orders increased 4.8% year on year to 3,014 million yen, net sales rose 26.3% year on year to 3,018 million yen, and order backlog at the end of the fiscal year totaled 631 million yen. Conveyors, which account for about 73% of net sales, recorded sales increase of 5.0%, and sales of large-scale projects such as circulating conveyors for bullet train ballast for the West Japan Railway Company and turbine mixer for glass manufacturing also contributed. Operating income of the segment increased 21.7% year on year to 588 million yen. Operating margin declined 0.7 pp to 19.5%, maintaining a high level.

In the other business, new orders declined 4.7% year on year to 6,572 million yen and net sales fell 1.9% to 6,660 million yen. Order backlog totaled 2,377 million yen partly due to consolidation of Ube Kohki (1,450 million yen). Sales of temporary construction materials decreased 26% as the appetite of customers such as temporary construction material rental services declined due to surging steel prices. Nevertheless, sales of waterproof boards and floodgates continued to be strong, posting a 0.3% decline, and those of the mobile plant business, where demand remains strong, grew significantly by 35.3%. Operating income of the other business decreased 8.3% year on year to 1,073 million yen, and operating margin fell 1.1 pp to 16.1%. The main factors behind the decline in profit include the worsened profitability of the mobile plant business caused by the continued deprecation in yen's value.

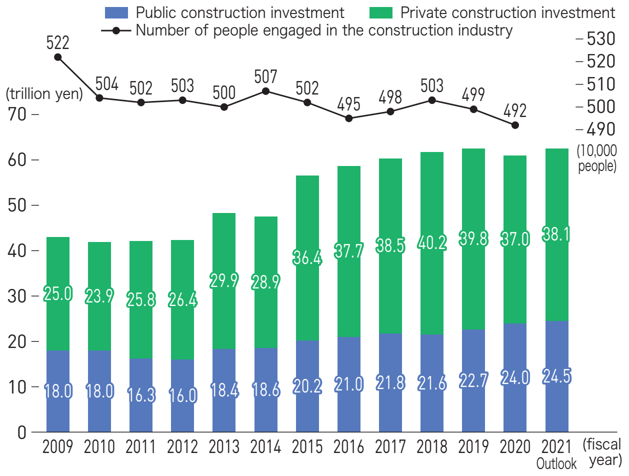
Net sales of the maintenance service business

Net sales of maintenance service of the AP- and BP-related businesses in Japan, which is one of Nikko's features, declined 2.7% year on year to 13,036 million yen. Amidst soaring asphalt prices, sales of the AP-related business declined 6.0% partly due to the postponement of capital investment, while those of the BP-related business increased 4.8%. As a result, the ratio of maintenance service to net sales of AP- and BP-businesses in Japan declined 0.4 pp to 53.8%. For FY 2022, the Group expects net sales of the maintenance service business to increase 1.6% to 13,250 million yen, boosted by new measures including flat-rate maintenance service. Its ratio to net sales is also expected to post an increase of 54.9%.

ROE and ROIC

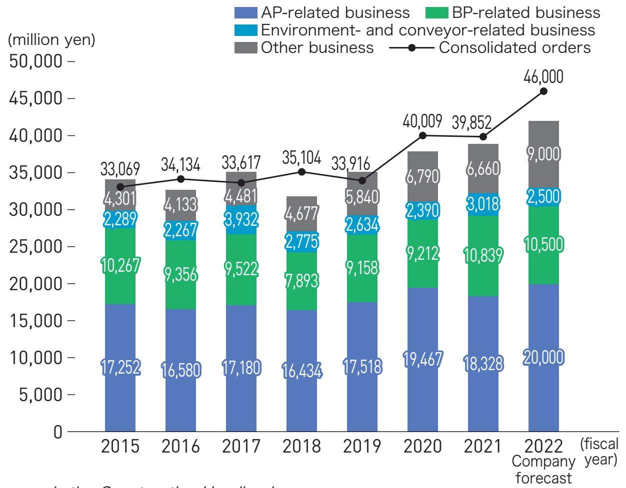
In FY 2021, ROE declined 1.6 pp to 5.2% from a year ago. The Group had aimed for 6.5% in ROE (net income attributable to owners of parent of 2,100 million yen and net asset of 32,334 million yen) in FY 2021. It succeeded in compressing net assets to 32,050 million yen through purchase of treasury shares and other means, but net income attributable to owners of parent was limited to 1,649 million yen, and ROE fell short of the target. Return on invested capital (ROIC) declined 2.3 pp to 3.6% from a year earlier. NOPAT declined 35.0% to 1,227 million yen from a year ago due to a fall in operating income and absence of the temporary dividends recorded in the previous fiscal year, while invested capital increased 5.4% to 33,900 million yen.

●Amount of construction investment and number of people engaged in the construction industry

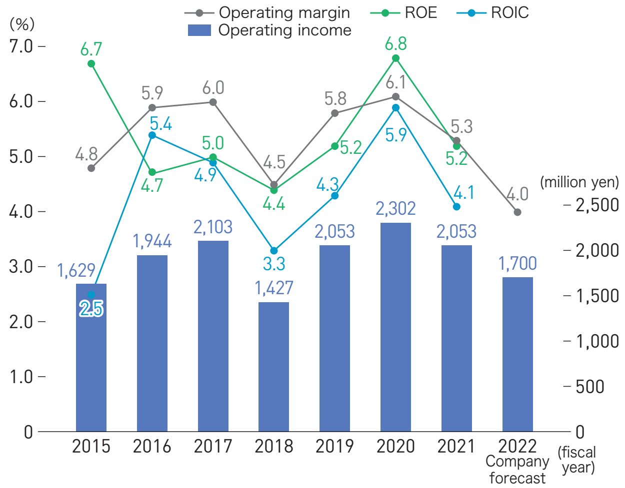


Note: The number of people engaged in the industry is on a calendar year basis and its source is the *Construction Handbook*.

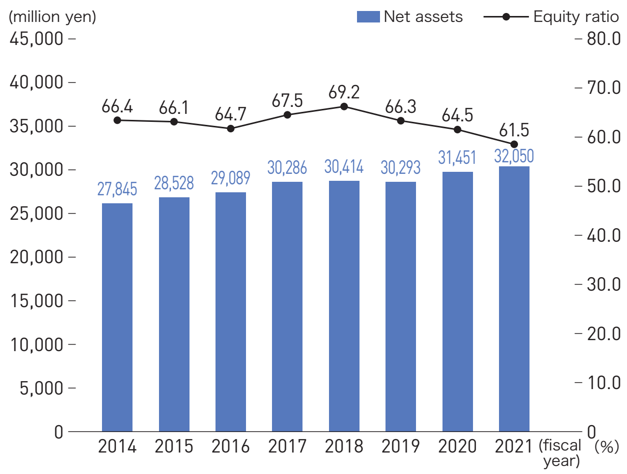
●Net sales by segment and consolidated orders



●Operating income and margin, ROE, and ROIC



●Net assets and equity ratio



Financial position

Net assets as of the end of FY 2021 increased 3,382 million yen year on year to 52,079 million yen. Net assets as of the end of FY 2021 was 32,050 million yen, and equity excluding non-controlling interests of 46 million yen was 32,003 million yen, which resulted in equity ratio of 61.5%, derived by dividing equity with total assets, down 3.0 pp from a year earlier. Equity ratio, which declined for three consecutive years after peaking at 69.2% in FY 2018, has been maintaining a high level over the past five years. Current assets came to 34,127 million yen, and non-current assets totaled 17,951 million yen. Main items that increased include inventories, which rose 3,276 million yen to 9,667 million, property, plant and equipment, which increased 1,486 million yen to 10,669 million yen, and intangible assets, which rose 376 million yen to 1,036 million yen (including 266 million yen in goodwill). Main items that decreased include notes and accounts receivable-trade (including electronically recorded monetary claims), which fell 975 million yen to 11,032 million yen, and investment securities, which declined 192 million yen to 4,336 million yen.
Current liabilities were 15,774 million yen, and non-current liabilities were 20,029 million yen. Main items that increased include newly added contract liabilities of 4,405 million yen and 1,583 million yen in long-term loans payable, which increased 1,279 million yen. Main items that recorded a decline include down payments of 17 million yen, down 2,932 million yen. Cash and cash equivalents as of the end of FY 2021 declined slightly to 12,436 million yen and net cash derived by subtracting interest-bearing debts of 3,812 million yen (1,229 million yen in short-term loans payable and 1,583 million yen in long-term loans payable) from cash and cash equivalents came to 8,624 million yen (9,999 million yen as of the end of FY 2020).

Cash flows

Cash provided by operating activities in FY 2021 decreased 560 million yen from FY 2020 to 2,224 million yen. While net income before income taxes came to 2,599 million yen, depreciation and amortization totaled 745 million yen, and trade receivables declined 1,653 million yen, contract liabilities in 1,172 million yen, inventories increased 1,583 million yen and gain on sale and valuation of investment securities came to 325 million yen.
Cash used in investing activities totaled 2,165 million yen, up 298 million yen. Main items in cash flow from investing activities include 1,697 million yen in payment for acquisition of tangible and intangible non-current assets, expenditure of 733 million yen for purchase of shares in Ube Kohki, and proceeds from sale and redemption of investment securities of 754 million yen. As a result, free cash flow derived by subtracting investing cash flow from operating cash flow came to 59 million yen, compared with 917 million yen in FY 2020.
Cash used in financing activities totaled 282 million yen. Main items included 1,099 million yen in proceeds from long-term loans payable and 1,260 million yen in cash dividends paid. The balance of cash and cash equivalents at the end of FY 2021 was 12,389 million yen, slightly less than a year ago.

Trends in capital investment, depreciation and amortization, R&D expenses

In FY 2021, the Group made capital investment of 1,907 million yen, down 841 million yen from a year earlier, and the ratio of capital investment to net sales was 4.9%. Main investments in the AP- and BP-related businesses included 798 million yen for construction of a new building of a subsidiary, expansion and renovation of factories, and acquisition and update of production facilities. Those of the other business came to 281 million yen, while purchase of computer equipment and software came to 107 million yen and acquisition of land cost 205 million yen.
Depreciation and amortization totaled 759 million yen, up 82 million yen from a year earlier, and its ratio to sales was 2.0%.
R&D expenses came to 449 million yen, up 57 million yen from a year earlier, and its ratio to net sales was 1.2%. The AP-related business spent 216 million yen and the BP-related business used 157 million yen. In the AP-related business, Nikko focused on the development of combustion burner using ammonia and hydrogen as fuel for heating and drying aggregates and improvement and commercialization of foamed asphalt generation equipment, which contributes to low-carbonization of pavement work. In the BP-related business, the Company proceeded with development of high-precision mixers in an industry-academia collaboration.
In FY 2022, the Group plans 2,000 million yen in capital investment, 800 million yen in depreciation and amortization, and 750 million yen in R&D expenses.

FY 2022 performance outlook

FY 2022 is the first fiscal year of the new Medium-Term Management Plan (FY 2022–FY 2024) with FY 2024 (fiscal year ending March 2025) as the final fiscal year. In the final fiscal year of the plan, Nikko Group expects net sales of 50,000 million yen, operating income of 3,000 million yen, and operating margin of 6.0%. For FY 2022, it expects orders to increase 11.3% from a year earlier to 46,000 million yen and net sales to rise 8.1% to 42,000 million yen. It expects operating income to decline by 17% to 1,700 million yen, operating margin of 4.0%, down 1.3 pp, ROE of 3.7%, and dividend of 30 yen per share (payout ratio of 95.6%).
When broken down, it expects net sales of 20,000 million yen in the first half and 22,000 million yen in the second half; operating income of 400 million yen in the first half (operating margin of 2.0%) and 1,300 million yen in the second half (operating margin of 5.9%). While we expect increases in raw material prices and heavy burden from personnel and R&D expenses in the first half, we anticipate impacts from product price revisions and increased sales in the second half.

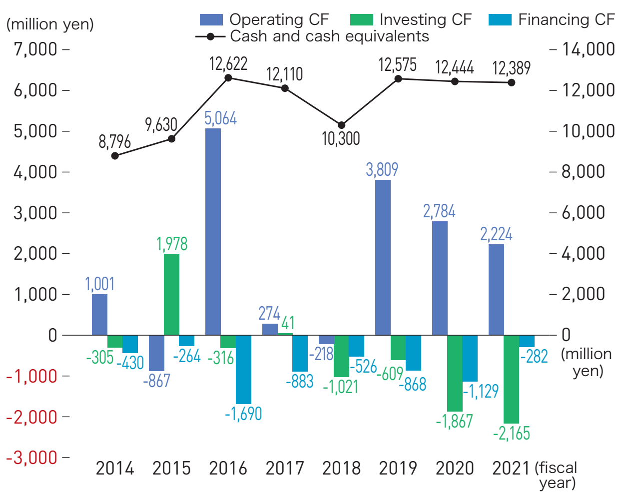
Outlook of business segments

By segment, we expect new orders for the AP-related business to increase 15.5% from a year earlier to 21,000 million yen, net sales of the segment to increase 9.1% to 20,000 yen (9,520 million yen in the first half and 10,480 million yen in the second half). Operating income is expected to increase 51% on year to 850 million yen (200 million yen in the first half and 650 million yen in the second half) with operating margin of 4.3%.
For the BP-related business, orders are expected to decline by 0.7% from a year earlier to 12,000 million yen and net sales are expected to fall 3.1% to 10,500 million yen (5,000 million yen in the first half and 5,500 million yen in the second half). The segment expects operating income to decline 6.5% to 1,050 million yen (460 million yen in the first half and 590 million yen in the second half) with operating margin of 10.0%.
The environment- and conveyor-related business expects orders to decline 0.5% from a year earlier to 3,000 million yen and net income to fall 17.2% to 2,500 million yen (1,190 million yen in the first half and 1,310 million yen in the second half). Operating income of the segment is expected to decline 15.0% to 500 million yen (220 million yen in the first half and 280 million yen in the second half).
Operating income at the other business is expected to decline 25% from a year earlier to 800 million yen (180 million yen in the first half and 620 million yen in the second half) with operating margin of 8.9%.
The Group expects consolidated operating income of 1,700 million yen by subtracting corporate expenses of 1,500 million yen from the above segment income of 3,200 million yen.

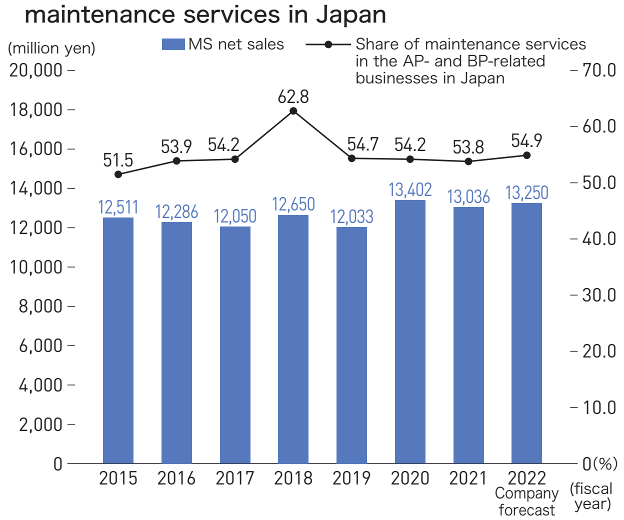
Analysis of factors contributing to changes in ordinary income

In FY 2021, ordinary income declined 699 million yen year on year to 2,274 million yen. Factors that boosted income include 264 million yen in the impact of sales increase, 381 million yen in the impact of reduced cost rate, and 20 million yen in foreign exchange gains. The decrease in income was mainly due to a rise of 336 million yen in raw material prices (including 251 million yen for steel and 57 million yen for copper wires), 558 million yen in sales and administrative expenses (including 143 million yen in personnel expenses and 76 million yen in M&A expenses), a 423 million yen decline in dividends income, and other non-operating balance worsening by 47 million yen.
For FY 2022, the Group expects operating income to decline 424 million yen to 1,850 million yen. While an 880 million yen increase in sales is expected to boost operating income, we are expecting cost rate to worsen by 525 million yen (including a 160 million yen increase in personnel expenses), a 301 million yen increase in R&D expenses, a 41 million yen rise in depreciation and amortization, and an absence of foreign exchange gains worth 77 million yen.

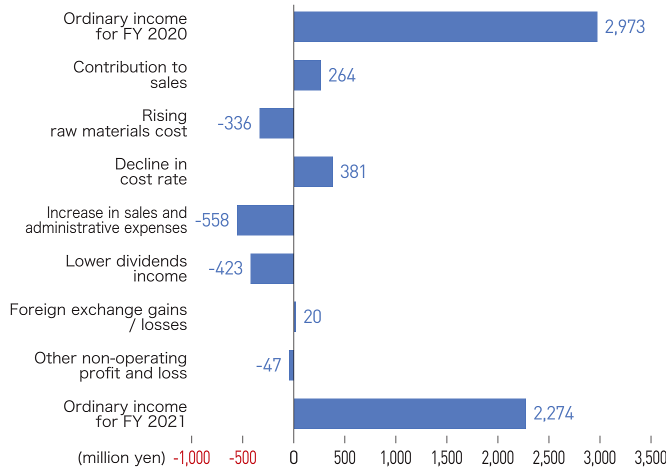
●Cash flow and cash and equivalents



●Net sales and sales share of AP and BP maintenance services in Japan



●Analysis of factors contributing to changes in ordinary income



●Dividend per share, payout ratio, total return ratio