

November 27, 2019

FY 2019 2Q Results Briefing: Gist of Questions and Answers Session

- 1. I would like to ask regarding the sales of maintenance service. What were the factors behind the slightly weak sales of AP-related services despite the reasonable business environment? I would also like to ask about the sales of maintenance service for AP and BP.**

--> We cannot explain the details without closely examining each case, but there are also some common factors of sluggish growth of services for AP and BP. In particular, the balance of whether to allocate our capacity on product sales or on service tilted towards product sales. We can say that the manufacturing and engineering divisions could not fully support the handling of orders for service. For example, service sales which require short period from business negotiation to delivery fill the gap until a large-scale project starts. I believe the biggest factor was that it went off balance when we assigned resources to large-scale projects. However, maintenance service is an important item with high profit margin and recurring revenue model. Therefore, we plan to take measures to balance it with product sales by making overall adjustments. I would like to refrain from disclosing individual sales of AP and BP.

- 2. If it is just a problem of resource allocation, is it better to buy a machinery before having a maintenance even if a customer actually wants to have a maintenance service?**

-->There is a phase where customers consider whether to go for maintenance or machinery. However, emergency works through maintenance are at the highest priority and we have been able to respond to this needs. We sometimes have to ask our customers for compromise and slightly delay the timing when they want to boost capacity or replace machinery at a certain timing. This does not mean that service projects are stagnant or our service business has become weak. To be honest, what happened in reality is that we asked them to carry it over to the next period amid the increasing machinery demand.

- 3. Recently, I have heard from someone with another plant company that there is a risk of delaying sales due to manpower shortage. I would like to ask whether there is a risk of you finding it difficult to achieve the second half sales target due to delays in implementation or start of work, or whether the current resources would be sufficient.**

--> Our ratio of internal manufacturing is high and outsourcing ratio is very low. We manufacture almost all products in-house and we outsource the portion that overflows to companies in neighborhood with whom we have long relationships. Our rival companies only manufacture central parts and outsource all the rest. In other words, we have a system to respond to manufacturing demand through our own efforts and it is unthinkable that there would be any delay in delivery to customers (due to delay in our manufacturing). Majority of the reasons behind sales which did not grow due to carry-over in the previous term were the delays in works on our customers' side: for example, environmental assessment being postponed because of the delays

in foundation work compared with the scheduled plan. However, it is also true as a fact that sales did not reach the goal, so we are aiming to improve accuracy through measures such as compiling budget of individual cases by taking into account the possibility that sales may be delayed until the next term if the timing slightly falls behind.

4. Is it O.K. to think that there is no delay in foundation work as of now?

--> The factors behind delays in delivery also include manpower shortage, but recently there has been many natural disasters, which are also causing the delays. We need to draft business plans by taking into account the possibilities of stagnation of supplies and construction work delays due to bad weather, etc.

5. You have explained that the profitability of the BP business declined due to unprofitable projects as you took on orders for improving market share. I would like to ask the reason why you take on orders at loss to increase market share and its background.

--> There are two competing companies in the AP business and we have a market share exceeding 70%. For BP, there were about five companies until 10 years ago but currently it is a competition of three companies. The other two integrated their business with another company (transfer of business from a company that withdrew from the business). Under such circumstances, we have been making efforts to capture our competitors' market share, and our dynamic market share for last year and this year exceeds 40% giving us the top share. Although we are better in dynamic share, there is still a possibility that we are at a disadvantage when the static share takes effect (when the economy gets worse).

--> The impact of having flagship BP plant made by Nikko in each region is significant, so there are cases where we take on orders that are unprofitable. Flagship plants have large shipment volume, use large amount of consumables, and incur a high amount of maintenance fees, so we can expect to recoup that (the lack of profit from the plant sales) through the long term business in the future. If we do not capture these flagship plants, we will not be able to allocate a certain number of service personnel and this might lead to a situation where the business gradually declines. Taking into account these matters as a whole, we judge whether we should acquire the order or not, or whether we should overstrain ourselves or not.

6. In connection with this, when considering future profitability, is it more appropriate to think that you would give priority to market share and profitability would not increase? The medium-term plan shows that profitability would gradually increase in fiscal year 2021, but I would like to know if it is better to expect somewhere lower than that.

--> We take decision case by case and it is not our basic policy to go for market share while continuing to lose money. It is not that we would go for flagship plants at any cost. Customers recognizes our value as a manufacturer for our maintenance service more than the functions of the products. We allocate service personnel who engage in manufacturing and sales of both AP

and BP throughout Japan. Our competitors engage in AP but they do not do BP, so we are superior in placing sufficient service personnel throughout Japan. For this reason, we are not thinking of lowering the profitability outlook.

7. Profit of the other business is increasing. I would like to know the sales composition of crushers and waterproof boards. I would also like to know the situation of the market, as I wonder if this trend is likely to continue to a certain extent in the next term.

--> There have been a great number of changes in the natural environment as well as flood damages recently, and the waterproof board market is expanding. It is not that we started the business of waterproof boards recently, and we have a lineup of various grades of products including general household products, office products, and products for subway. We are also enhancing and strengthening our production bases so that we can respond to the market expansion, and although the sales are still small, we would like to double and triple them in the future.

--> A subsidiary with 75 years of history is in charge of crushers. Recently, there has been changes in demands from users, and we are producing results by proposing new crushers while accepting orders for crushing test over the internet and so on. For example, we are capturing new markets by conducting tests to break up panels in collaboration with manufacturers and considering how to recycle solar panels, etc., which we have never crushed before. If you look at the numbers, page 18 of the briefing session material says that sales of crushers increased 77% and waterproof boards 349%. Annual net sales of crushers were 500 million yen and waterproof boards 300 million yen, and those for waterproof boards in the first half of the current fiscal year were 360 million yen. Crushers have a high operating margin and roughly half is the profit. We have also been able to maintain a high profitability for waterproof boards.

8. How much capital investment are you going to make in the future? I would also like to know its breakdown.

--> As part of the recent work-style reform, we are making early capital investment in fields that lead to reduction of manhours. We are also replacing an existing equipment with a machinery with faster processing speed. It is not limited to manufacturing and we are also considering investing in our system which enables our sales force to share data with more options. In page 36 of the results briefing materials, we have listed the figures for capital investment, depreciation and amortization, and R&D expenses from 2011 on. We have been continuing capital investment that significantly exceeds the level of depreciation and amortization since fiscal year 2013. This is the result of proactive investment to update obsolete facilities, which had been postponed, since fiscal year 2013. In the last few years, we have also been investing for growth.

-->We had initially expected 800 million yen in capital investment for fiscal year 2019, but it is likely to double. In particular, we are currently manufacturing waterproof boards at one location,

Noda factory in Chiba Prefecture, and we plan to invest about 300 million yen in the current fiscal year to acquire a 600 tsubo (approximately 2,000 m²) plot in Akashi City taking into consideration transportation cost and production capacity given the expected demand also in western Japan. To consolidate the bases for concrete pumps, which are part of the BP business, we will purchase land in Shimonoseki City and invest in a building. In addition, investment in ERP (system investment) is expected to increase from the second half of the current fiscal year to the next fiscal year on. If we make a full-scale foray into Southeast Asia, the investment for that will also surface from the next fiscal year on. We are not thinking of investment to increase capacity of production facilities but we will actively make investment for improving efficiency. While depreciation and amortization would increase, we would like to continue to make investments that would generate profits exceeding the expenses and absorb them.

9. It is a basic question, but the Corporate Report says “Weakness in price negotiations” is the weak point in the SWOT analysis of AP. The operating margin of the AP business is about 5%, but given the high market share, wouldn’t it be possible to increase the margin?

--> We have a 70% market share in AP and it is said to be a monopoly. However, there are many customers with whom we have long-standing relationships, and there was a long period of time in which we somewhat neglected model change and renewal of technology through function enhancements (which require new negotiations for deciding price). Therefore, the situation continued where we could not convince customers with many plants to have price negotiation when they purchase the same model as before. However, more recently, we are making earnest efforts to have customers understand the value of new plants with the enhanced functions we developed. We are working hard to improve the profitability of AP through business negotiations for new plants. (As we are offering functions which our rivals do not offer,) if you wait for some time, you would probably be able to understand (as it starts showing in improvement of profitability and so on). Currently, we are not able to mark profitability that is significantly different from the existing level, but it is more likely that the profitability would improve, as the number of plants sold increases, which in turn achieves cost reduction.

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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