**LIXIL Corporation**

Financial Results Briefing for the Fiscal Year Ended March 2022 for Investors and Analysts

April 28, 2022

# Event Summary

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|---|---|---|
| **[Company Name]** | LIXIL Corporation | |
| **[Company ID]** | 5938-QCODE | |
| **[Event Language]** | JPN | |
| **[Event Type]** | Earnings Announcement | |
| **[Event Name]** | Financial Results Briefing for the Fiscal Year Ended March 2022 for Investors and Analysts | |
| **[Fiscal Period]** | FY2021 Annual | |
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| **[Venue]** | Webcast | |
| **[Venue Size]** | | |
| **[Participants]** | | |
| **[Number of Speakers]** | 3 | |
| | Kinya Seto | Director, Representative Executive Officer, President, and CEO |
| | Sachio Matsumoto | Director, Representative Executive Officer, Executive Vice President, and CFO |
| | Kayo Hirano | Senior Vice President, Leader, Investor Relations Office |
| **[Analyst Names]*** | Hiroki Kawashima | SMBC Nikko Securities Inc. |
| | Sachiko Okada | Goldman Sachs Japan Co., Ltd. |
| | Masashi Miki | Citigroup Global Markets Japan Inc. |
| | Daisuke Fukushima | Nomura Securities Co., Ltd. |
| | Ryo Yagi | Mitsubishi UFJ Morgan Stanley Securities Co., Ltd. |
| | Arisa Katsuyama | Morgan Stanley MUFG Securities Co., Ltd. |

*Analysts that SCRIPTS Asia was able to identify from the audio who spoke during Q&A.

## Presentation

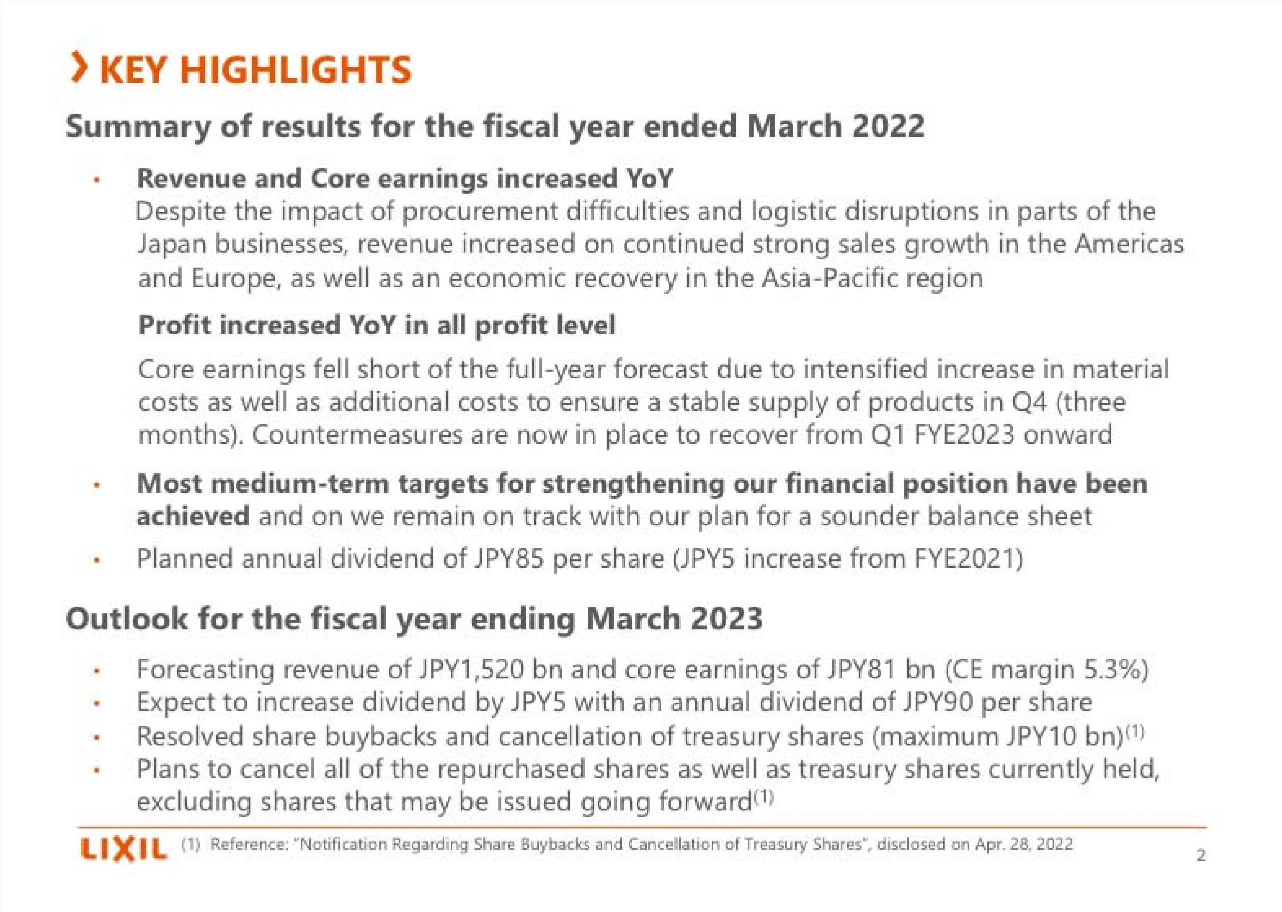
**MC:** As we have reached the appointed time, I would like to begin the financial results briefing for LIXIL Corporation for the fiscal year ended March 31, 2022. This briefing is being conducted via live Internet streaming. Thank you very much for your cooperation.

Let me begin by introducing today's presenters. Kinya Seto, Director, Representative Executive Officer, President, and CEO; Sachio Matsumoto, Director, Representative Executive Officer, Executive Vice President, and CFO; Kayo Hirano, Senior Vice President, Leader of the Investor Relations Office. My name is Fukushima, from the IR Office, and I will be the moderator for today's session.

Please refer to the presentation materials posted on the Company's website in the Investor Relations section.

Allow me to explain today's proceedings. To begin with, President Seto will explain our financial results for the fiscal year ended March 31, 2022. There will be a question and answer time afterwards. The event is scheduled to end at 6:00 PM. Please stay until the end.

Now, Mr. Seto will explain the financial results for the fiscal year ended March 31, 2022. President Seto, please go ahead.




**Seto:** Hello, everyone. I will now present the financial results for the fiscal year ended March 31, 2022. Two of the last three months were particularly difficult. There were issues like the spread of COVID-19, then Ukraine situation, then a lockdown, and many other things.

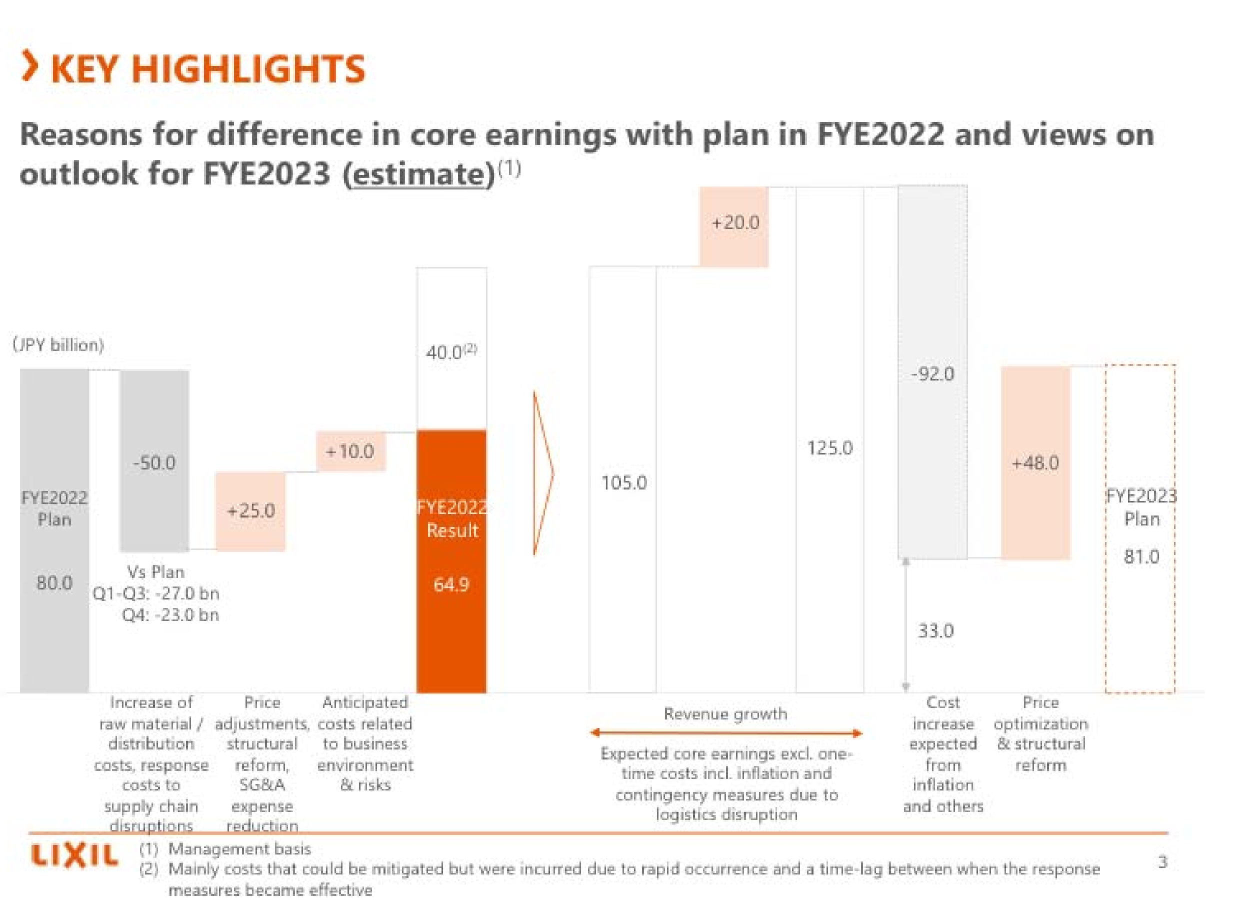
Despite that, we managed to secure an increase in revenue and profit. Unfortunately, we were not able to achieve our plan. However, the fact that we have taken measures one by one to deal with very challenging operational situation will probably result in a large potential profit margin once the problems are resolved. So, some good may come out of these difficulties.

As for financial strength, we have generally achieved our mid-term targets. We expect to increase the dividend by JPY5, to JPY85 per share.

For the current fiscal year, we forecast core earnings of JPY81 billion and a dividend of JPY90 per share, as I will explain later.

We are also considering a share buyback of up to JPY10 billion, as well as the cancellation of not only the treasury shares we have acquired, but also the cancellation of the treasury shares we originally owned. Originally, we had about 23 million shares of treasury shares in case we acquired a company in the future, but we have decided that we do not need that many shares in light of our recent strategy.

Also, the fact that we hold these shares might in itself raise questions about future capital increases, so we will cancel all of these 22,280,000 shares and the JPY10 billion amount of treasury shares acquired.




The topic that will be most central to our discussion today is this slide. We have included a simple diagram of how we have responded to the various events, as well as a summary of what this means for our future potential.

In the beginning, we had planned for JPY80 billion of core earnings. However, in the end, the figure for H2 changed due to the JPY50 billion rise in raw material costs, the rise in logistics costs, and our response to disruption of the supply chain. In our case, since we use a lot of aluminum, and faucets account for a high percentage of our international business, the increase in copper and aluminum prices has been quite a big hit on our financials.

Also, since we export products all over the world and import parts from them, the impact from the so-called container cost increase is quite significant. The more significant impact was the disruption of the supply chain. It happened a lot, especially in Q4, and to be honest, if it had happened at the same pace as the JPY27 billion in costs up to Q3, I think JPY80 billion core earnings would have been achievable in FYE2022. With almost half of it occurring in Q4, we just couldn't reach our plan.

We had anticipated about JPY10 billion of risk at the time of business planning and we managed to minimize the impact to some extent by shifting about JPY25 billion onto prices, implementing structural reforms, and by further reducing SG&A expenses. As a result, we managed to reduce the impact to some extent, but fell short by JPY15 billion to post core earnings of JPY65 billion.

I wondered how much the business performance would have been without such a large cost impact, and the result was JPY105 billion, which was obtained by adding JPY40 billion to the total. Of course, there were various problems behind the JPY50 billion. It is obvious that the JPY50 billion will not be added as is, and of course, some of the costs that were raised in response to the various costs will have to be lowered if the costs are lowered.

For example, the costs due to the supply chain disruptions that I mentioned earlier, inventory was shipped by air because no products were available. Also, for example, during a lockdown, a certain product could not be made, so we made from a mold. And this time, because there was a impact on our factory in Vietnam due to the lockdown, Maebashi factory alternatively produced the Vietnamese factory's portion.

It is natural to consider such expenses as profits if similar problems no longer occur, so if we add JPY40 billion to the total, we get JPY105 billion. If we had been able to do in FYE2022, I believe we could have reached 7% as a core earnings margin.

If we include profit growth in FYE2023, this comes to JPY125 billion. In that case, I think we would be able to achieve a figure above our original idea of 7.5% in FYE2023.

However, the three infrastructure elements I just mentioned, raw material costs, fuel costs, and costs due to supply chain disruptions, are expected to total JPY92 billion, although we will have to see whether this is correct or not. It is a huge amount.

The total amount we can handle for this year is JPY48 billion, which comes together to create JPY81 billion in core earnings. We are forecasting JPY81 billion by subtracting JPY92 billion in costs from JPY125 billion and adding JPY48 billion from response measures. Originally we had thought we could achieve JPY125 billion. In this sense, we are taking a positive view that the JPY44 billion difference between the two figures is room for growth in FYE2023 and beyond.

As I mentioned, there were three major cost factors: rising raw material and other costs, rising logistics costs, and supply chain disruptions. The last of these, the supply chain disruption, is the cost of dealing with a special situation, so if such a situation no longer occurs, I think this part of the profit will naturally increase to some extent in the future, if it does not happen as it did this time.

Meanwhile, the increase in raw material costs inevitably involves a time lag from response measures, and the difference in response costs will be the difference in the time lag. As for logistics costs, container costs are now 5 to 10 times higher than they were two years ago. There were offsets for the portion where costs are settling and for the portion where fuel costs have gone up, but we are thinking that it will probably settle down by the end of this year.

## KEY HIGHLIGHTS

### Changes of external business environment and response

| Changes in external environment | Response to the changes |
| --- | --- |
| Increase of raw materials cost | • Price adjustment and optimization<br>• Shift to mid-to-high-end price range products<br>• **Switching to alternative materials**<br>• **Shortening of time lag and digitalization** |
| Increase of distribution cost | • Building a more agile and resilient supply chain and production system<br>• **SKU reduction and increase in inventory level**<br>• Price optimization |
| Supply chain disruptions | • Long-term measures for procuring raw materials<br>• Backup production plan in case of power shortage in Germany<br>• Redundancy of supply chain<br>• Narrowing down SKUs<br>• Expanding platform production<br>• Enhancement of IT systems |
| Consumer demand | • Increase in sales of environmentally-friendly products<br>• Expansion of DIY products<br>• Accelerate digital transformation(1)<br>• Expansion of differentiated products |

LIXIL (1) Please refer to "Enhancing the customer journey with digital tools" of page 35

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First, the cost of raw materials is rising, and the best way to deal with this is to pass it on to prices. Another is to optimize the price structure itself. In other words, we will not sell at a discount. To some extent, the average unit price will naturally increase if the price structure is properly consolidated into a reasonable price.

Another approach is to shift to high value-added, high quality, differentiated products that customers will buy even if prices are raised. This is quite important.

Another area where I think we are doing quite well is in the switching to alternative materials, especially copper. We have been replacing brass, which is commonly used in Europe and the US, with zinc ever since we opened our Thai Klaeng factory in 2017.

Currently, about 20% is switched from brass to zinc, but I think it is possible to raise this ratio to 40% to 50% in the future. The cost of brass is probably about USD7,800 per ton, since brass is an alloy of copper and zinc, when copper is roughly on a base of USD10,000 per ton now. Meanwhile, the cost of zinc is in the USD3,000 range per ton at best, so less than half price can be achieved. If it could be combined with plastic, it would be even cheaper.

In Japan, as the result of long-term effort, half has already been switched to plastic. However, in Japan, the percentage of our sales of fitting products is small, so this shift to alternative materials will be most effective in international markets, such as in Europe and the Americas.

Also, as I mentioned earlier, price revisions inevitably have a time lag. Prices cannot be raised the following month just because raw material costs have gone up. Now, though, it is possible for us to do that at least twice a year, whereas we used to have to wait a year.

In international markets, we are using digital methods to make those changes more often. These efforts will allow us to reduce the time lag between the rise in cost and passing on the price, probably starting this year. As for the increase in logistics costs, we need to strengthen the system to sell products made in each region, in order to minimize these costs as much as possible.

For North America, we have factories in Mexico; for Europe, factories in Europe; for China, factories in China; and for Japan, factories in Japan. We are also making it a rule that, as a buffer, only products from factories in Southeast Asia will be sold globally.

However, even so, many of GROHE's faucet products, which have a particularly high freight burden, are exported around the world, so we are planning to address the rising freight and logistics costs by making the supply chain more robust in this area.

Then, of course, by reducing the number of SKUs (Stock Keeping Unit) or raising inventory levels, it will be easier to deal with various problems, including lockdowns, to some extent. And, of course, costs will be passed on to prices.

The disruption of the supply chain affects many areas, as I mentioned earlier. For example, airfreight, in-house production instead of buying them from suppliers, creating new partners for new production in some cases, and making things in Japanese factories that are already being made in international factories. This time, these costs were very high.

However, thanks to these initiatives, we were able to continue selling almost all of our products to customers without running out of supplies compared to other companies, which was a considerable advantage this time and will be our strength in the future.

The obvious place to start, of course, is to make a long-term allowance for raw material costs. Also, for example, fuel supplied from Russia to Europe will likely be reduced this year due to the problems in Ukraine. The most vulnerable spot for us there is the factories in Germany.

Most products at these German factories are designed to be able to be made at other factories even if the power supply is cut in half. There are also several shower and other products that cannot handle power supply cuts as much as 50%, but can maintain production at 25% lower power supply. We are going to keep trying to be able to maintain production at 50% lower power supply from the current level.

Redundancy of supply chains, narrowing down SKUs, expanding platform production, we have been doing all of these things. We are also strengthening our information systems so that we can better ascertain our vendors and where the common components of our vendors are located.

Meanwhile, changes in the world naturally reveal new demands and new markets. For example, in relation to environmental issues, what we are considering now is that almost all existing windows in Japan are not in compliance with the environmental standards of fiscal year 2016. A new product, *Replus*, was created to replace these windows with triple glazing.

We are also planning to sell products such as *Revia*, which is made from waste plastic, as a new environmentally friendly material, as I mentioned last time.

We have also established the *QuickFix* brand for DIY products, especially in Europe, where customers want products that they can install themselves without hiring plumbers. This is growing at a very fast pace and we believe it will become a major product pillar.

In addition to *QuickFix*, we also make many products that are easily supported by plumbers, such as the GROHE Professional range.

We are also expanding our digital promotions, *LIXIL-X*, *GROHE X*, and online showrooms.

Also, various differentiated products. As I mentioned earlier, if you create differentiated products, your customers will be less price-sensitive.

For example, there is a product called *KINUAMI* that we are planning to expand sales of starting after Japan's Golden Week holidays in May this year. With this product, soap foam rushes out of the shower like a fire extinguisher from the beginning and then hot water comes out when you press the switch, so the body can be washed without scrubbing. This innovative product also reduces the amount of hot water used. We have received a resounding response.

By increasing the number of such products, we intend to gain profit from areas other than just price competition.

## › PERFORMANCE HIGHLIGHTS

- **Revenue: JPY1,428.6 bn, up 4% year-on-year, Q4 (3 mon.) up 3%**
  - **Q4 (12 months) :** -2% in Japan (+1% excl. impact from divestments) and +18% in international markets
  - **Q4 (3 months):** Flat in Japan (+1% excl. impact from divestments) and +10% in international markets
- **Core earnings: JPY64.9 bn, up JPY7.6 bn year-on-year, Q4 (3 mon.) down JPY8.9 bn**
  - **Q4 (12 months):** JPY-3.2 bn in Japan, JPY+13.1 bn in international markets, and JPY-2.3 bn for consolidation adjustment/others
  - **Q4 (3months):** JPY-8.8 bn in Japan, JPY-1.3 bn in international markets, and JPY+1.2 bn for consolidation adjustment/others
- **Net profit(1): JPY48.6 bn, up JPY15.6 bn year-on-year**
  - Steady progress in profit for the year as a result of reduced volatility in business performance due to focus on core businesses and progress in structural reform
- **Year-end dividend forecast: increase by JPY5 from the previous forecast and revised it to JPY45(2)**
  - Planned annual dividend of JPY85 per share for FYE2023 with the interim dividend (FYE2021: JPY75)
  - Planned to increase dividend by JPY5 and projecting annual dividend of JPY90 per share for FYE2023

LIXIL (1) Net profit = Profit attributable to owners of the parent for the year
(2) Reference: "Announcement Regarding Revision of the Dividend Forecast (Dividend Increase) for the Fiscal Year Ended March 2022", disclosed on Apr. 28, 2022

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Unfortunately, the business environment for the just-ended term was very difficult, but we were able to increase both sales and profits by nearly approximately JPY65 billion in terms of core earnings.

Thus, when looking at the full year, in Japan, in terms of core earnings, aluminum prices rose considerably right at the end. At one point they were over USD4,000 per ton, so that's where we suffered in Q4 regarding the LHT business, but I think we would have done considerably better without it.

It is unfortunate that we could not pass the price on to the customer when the price rose so sharply. However, the very small gap between core earnings and net profit is due to the progress in structural reforms. I believe this is one result for the fact that we were able to increase profits at all levels for a net profit of JPY48.6 billion, an increase of JPY15.6 billion over the previous year.

The year-end dividend forecast has been revised to JPY45 per share, an increase of JPY5 from the previous forecast.

## › FYE2022 CONSOLIDATED BUSINESS RESULTS

| JPY billion | Q4 12 months | | | | Q4 3 months | | |
|---|---|---|---|---|---|---|---|
| | FYE2021 | FYE2022 | Increase /decrease | % | FYE2022 | Increase /decrease | % |
| Revenue | 1,378.3 | **1,428.6** | +50.3 | *+3.7%* | **354.2** | +11.4 | *+3.3%* |
| Gross Profit | 469.2 | **486.9** | +17.6 | *+3.8%* | **113.5** | -5.8 | *-4.9%* |
| (%) | *34.0%* | ***34.1%*** | +0.0pp | - | ***32.0%*** | -2.8pp | - |
| SG&A | 411.9 | **422.0** | +10.1 | *+2.4%* | **110.4** | +3.1 | *+2.9%* |
| Core Earnings(1) | 57.3 | **64.9** | +7.6 | *+13.2%* | **3.1** | -8.9 | *-74.1%* |
| (%) | *4.2%* | ***4.5%*** | +0.4pp | - | ***0.9%*** | -2.6pp | - |
| Net profit including Discontinued Operations(2) | 33.0 | **48.6** | +15.6 | *+47.1%* | **7.1** | +12.7 | - |
| EPS (Yen) | 113.92 | **167.21** | +53.29 | *+46.8%* | **24.43** | +43.85 | - |
| EBITDA(3) | 137.9 | **145.6** | +7.7 | *+5.6%* | **23.4** | -8.6 | *-26.8%* |
| (%) | *10.0%* | ***10.2%*** | +0.2pp | - | ***6.6%*** | -2.7pp | - |

- **CE margin:** Improved by 0.4pp (Gross profit margin maintained flat, SG&A ratio improved by 0.3pp)
- **Gross profit margin and core earnings margin:** Improvement driven by an increase in the sales distribution ratio of the international business with higher profit margin and benefits from structural reform in previous years as well as price optimization and SG&A expenses reduction measures
- **SG&A expenses:** SG&A expense ratio improved by 0.3pp despite the increase of JPY10.1 bn in 12 months year-on-year (Japan JPY7.6 bn decrease, International JPY17.7 bn increase) due to increase of revenue

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(1) Equivalent to "Operating profit" of JGAAP
(2) Profit for the quarter/ the year attributable to owners of the parent
(3) EBITDA=Core earnings + Depreciation + Amortization

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As you can see from the consolidated results, one point of interest is that the gross profit margin increased slightly in the fiscal year ended March 2022 compared to the fiscal year ended March 2021, although it is a subtle difference. I think we did a very good job with this. That is because costs rose so much during this period that if we had not taken any action, I think there would have been a major impact.

One thing about this section, for example, Q4, with gross profit margin at 32%, was the period when costs rose most sharply. We were able to pass on the price rises to a certain extent. However, if costs didn't rise so sharply, I think gross profit would have increased significantly this fiscal year.

I think that the fact that we were able to increase our profits including core earnings under these circumstances, despite the fact that we were not able to pass on the cost rises to pricing in time, can be said to be a potential for a large profit increase when the time comes where we would be able to pass on cost increases to pricing.

## › FYE2022 BUSINESS RESULTS BY SEGMENT

**Strong LWT business drove increase of revenue and core earnings.**
**Core earnings at LHT declined due to the impact of sharply higher raw material costs in H2, especially in Q4, which offset gains from SG&A expense reduction measures**

| | | Q4 12 months | | | Q4 3 months | |
|---|---|---|---|---|---|---|
| Segment | JPY billion | FYE2021 Results | **FYE2022 Results** | Increase/ decrease | **FYE2022 Results** | Increase/ decrease |
| LWT | Revenue | 783.8 | **862.2** | +78.4 | **215.0** | +8.5 |
| | CE | 62.1 | **76.6** | +14.5 | **12.1** | -3.7 |
| LHT | Revenue | 474.3 | **466.7** | -7.6 | **112.2** | +4.1 |
| | CE | 31.4 | **28.2** | -3.2 | **-0.9** | -6.3 |
| LBT | Revenue | 93.4 | **89.3** | -4.1 | **23.6** | +1.0 |
| | CE | 2.6 | **3.5** | +0.9 | **1.5** | -0.3 |
| H&S | Revenue | 46.6 | **30.3** | -16.3 | **7.6** | -2.1 |
| | CE | 2.1 | **-0.1** | -2.3 | **0.4** | +0.2 |
| Consolidation, adj. & other | Revenue | -19.8 | **-19.8** | -0.1 | **-4.2** | -0.1 |
| | CE | -41.0 | **-43.3** | -2.3 | **-10.1** | +1.2 |
| LIXIL | Revenue | 1,378.3 | **1,428.6** | +50.3 | **354.2** | +11.4 |
| | CE | 57.3 | **64.9** | +7.6 | **3.1** | -8.9 |

Forex impact： Q4 12 months: Revenue +25.2 billion, Core earnings +2.0 billion
Q4 3 months: Revenue +6.0 billion, Core earnings +0.1 billion

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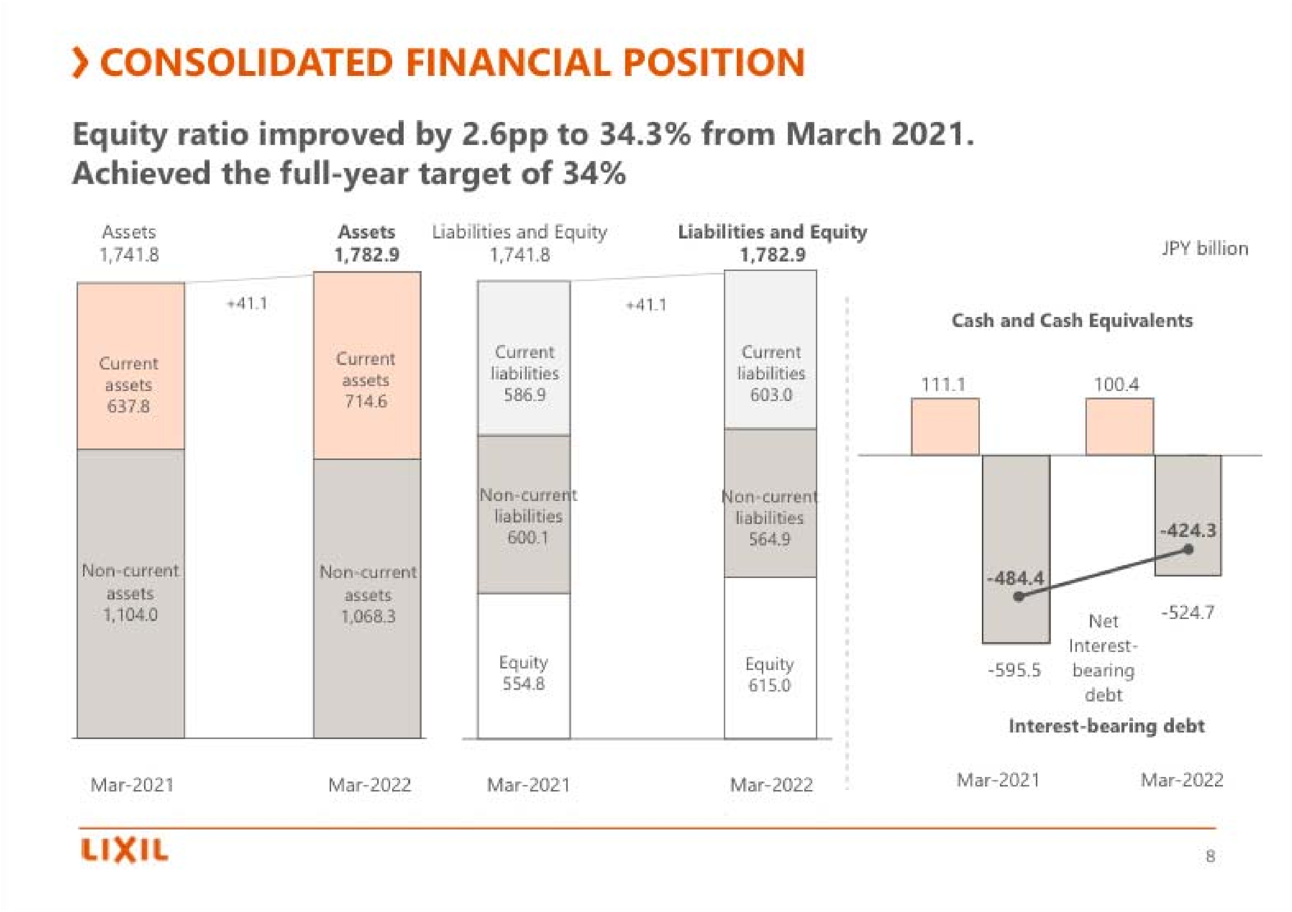
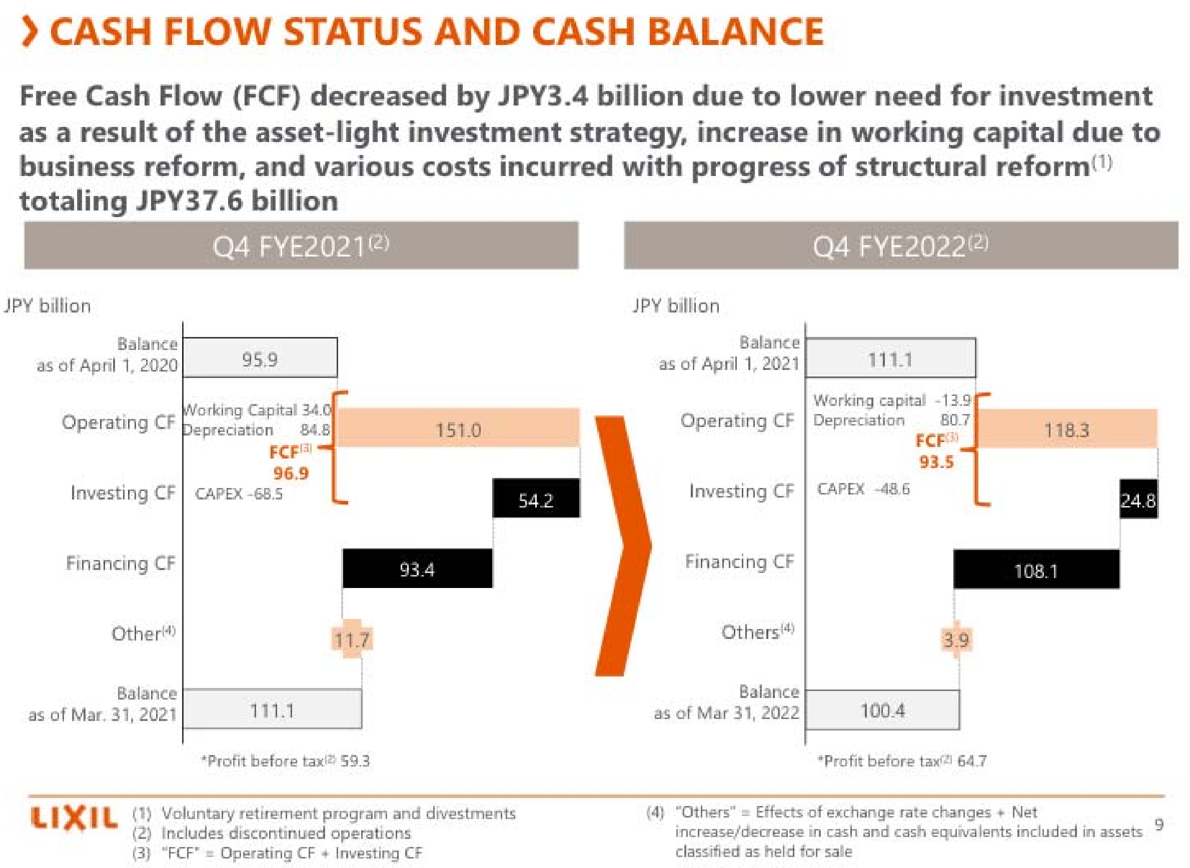
In terms of segments, LIXIL Housing Technology struggled in Q4, but I think the LIXIL Water Technology business did particularly well in international markets.




In terms of our balance sheet, due to some supply chain issues at this time, we had to increase our inventory, and accumulated some working capital. Interest-bearing debt has been steadily reduced and achieved equity ratio of 34%, which was the full-year plan, so I think we are doing as planned.




Regarding cash flow, there was some impact from slightly increasing our inventory as I mentioned earlier, but I think the result shows that, in accordance with our strategy, we are steadily transforming into a company that generates cash.

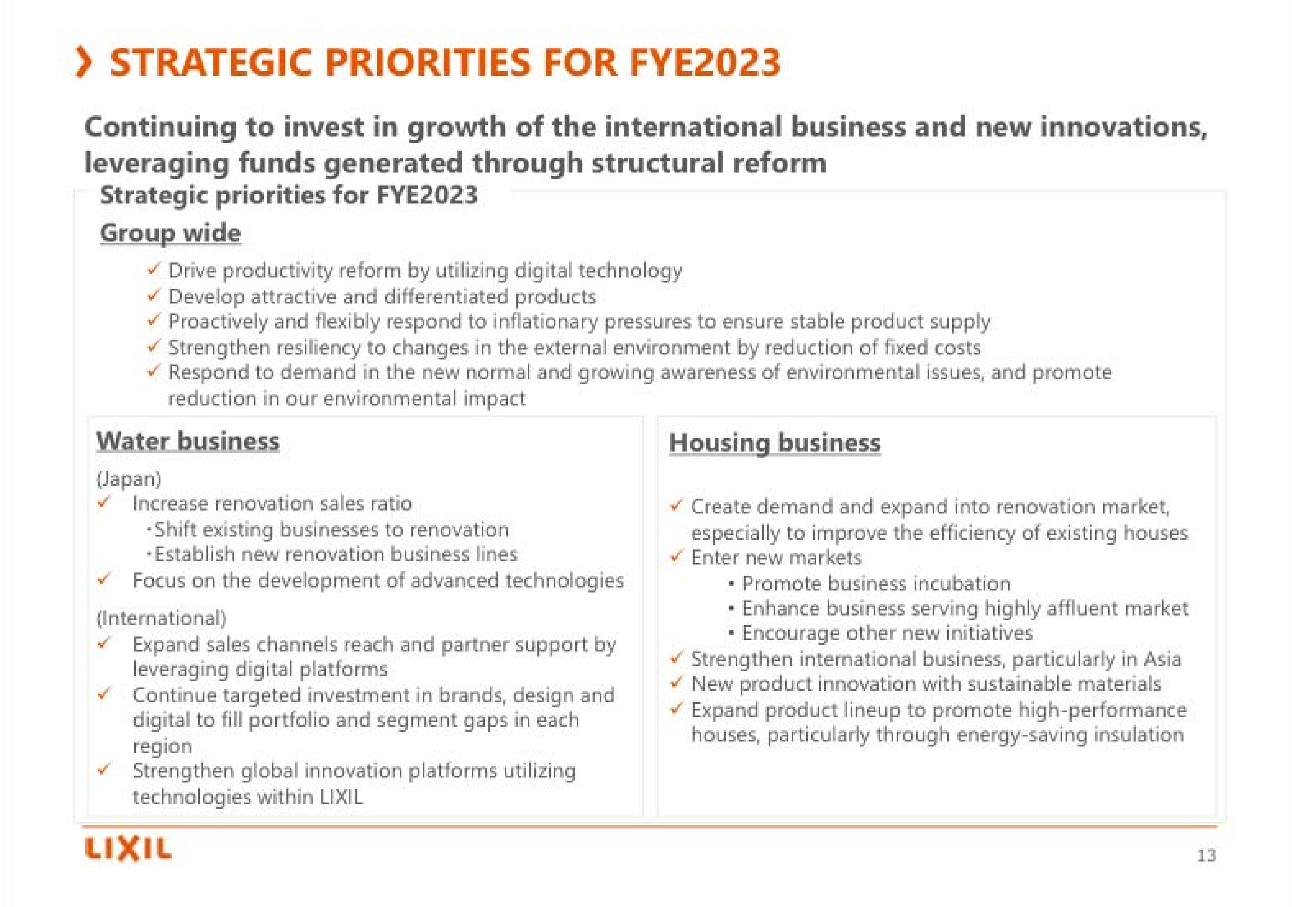

As for the management strategy, as we always say, the basic idea is to improve productivity and lower costs through platform-based production and digitalization, while changing the organizational culture to make it a more energetic company. And although we were affected by a variety of external circumstances this time, I think the fact that we were able to fight the good fight to some extent is one of the results of our past efforts.

The premise of 10% ROIC is a 10% core earnings margin, but I think we have already come close, actually. Looking at the costs, from the current surface figures, we have only made half, but as I mentioned earlier, if nothing had happened last fiscal year, I believe we would have made a core earnings margin close to 7%.

Also, this fiscal year, if there were no major impacts from rise in costs or geopolitical issues like those occurring now, we would have been able to significantly exceed the 7.5% core earnings margin target that we originally had in our medium-term management plan. So, as I mentioned earlier, I believe that the impact from the supply chain disruptions, bad as they are, will level out.

As for freight costs, I think the numbers here will settle down to some degree by the end of this year or early next year. It is unlikely that it will continue to rise at a rate of 4 times, 5 times, or 10 times. As for commodities, of course, if energy costs rise, they will rise in turn, but if we can reduce the gap and time lag to some extent, I think that this 10% figure will be realistic within two to three years. I think we can do this, since this time, the response costs for various things have become a basis of the estimate in some sense.

In that sense, we have been able to accomplish all four of these tasks in sequence, and qualitatively speaking, we believe that these four tasks are proceeding almost as planned.




In terms of priority areas for the fiscal year ending March 31, 2023, this will, in a sense, remain largely unchanged from the fiscal year ended March 31, 2022 and we will utilize digital technology. The platform-based production and digital technology, which I mentioned earlier, will improve productivity.

In addition, we will develop attractive and differentiated products. I think this is one of the bases for reducing price sensitivity and creating an environment in which we can raise prices.

Flexibility to adapt to changes in the external environment. I believe that we were able to demonstrate our resilience by maintaining a stable supply of products regardless of inflation or supply chain problems. Although it entailed some cost, our product supply did not falter.

We are also reducing fixed costs and, as new business, creating new products that can respond to the current new social norms and environmental issues. I think this will be a major growth factor for us.

## › FYE2023 FORECAST

**Projecting increase of Revenue and Profits compared to the previous year. Forecasting increased annual dividend of JPY90 per share**

| JPY billion | FYE2022 Results | FYE2023 Forecast | Change |
|---|---|---|---|
| Revenue | 1,428.6 | 1,520.0 | +91.4 |
| Core Earnings (CE) | 64.9 | 81.0 | +16.1 |
| Operating Profit (OP) | 69.5 | 78.0 | +8.5 |
| Profit before Tax | 67.3 | 76.0 | +8.7 |
| Tax expenses | -16.7 | -24.2 | -7.5 |
| Profit (loss) from discontinued operations | -1.8 | -0.6 | +1.2 |
| Net profit attributable to non-controlling interests | 0.1 | 0.2 | +0.1 |
| Net profit attributable to owners of the parent | 48.6 | 51.0 | +2.4 |
| EPS (JPY) | 167.21 | 175.42 [1] | +8.21 |
| ROE (%) | 8.3 | 8.1 [1] | -0.2pp |
| ROA (%) | 2.8 | 2.9 | +0.1pp |
| ROIC (%) | 4.5 | 5.0 | +0.5pp |
| EBITDA [2] | 145.6 | 161.0 | +15.4 |
| Net debt/EBITDA [2] | 2.9x | 2.4x | -0.5x |
| Dividend (JPY per share) | 85 | 90 | +5 |
| Payout ratio Consolidated basis | 50.8% | 51.3% [1] | - |

LIXIL (1) Calculated using the number of shares outstanding as of March 31, 2022 (excluding treasury stocks)
(2) EBITDA=Core earnings + Depreciation

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With regard to the earnings forecast, it is based on what we have just discussed.

To be honest, I am a bit unwilling to accept the JPY81 billion figure of core earnings this time, but considering the cost of responding to the current circumstances, I think it is unavoidable this time. We now plan to increase the dividend to JPY90.

## FYE2023 FORECAST – MARKET OUTLOOK & ASSUMPTIONS

### Market outlook and assumptions

| | | FYE2022 Results | FYE2023 Forecast | Difference |
|---|---|---|---|---|
| Housing starts (YoY%) | Total | 855.000(1) | 849,000/-1% | - |
| | Renovation | +5% | +2% | - |
| FX rate (Average rate) | JPY/USD | 112.86 | 115.0 | +1.9% |
| | JPY/EUR | 131.01 | 131.1 | +0.1% |
| Raw material prices (JPY/ton) | Aluminum | 305,000 | 360,000 | +55,000 |
| | Copper | 868,000 | 862,000 | -6,000 |

### Business outlook

**Group wide:**

- Mitigate the impact of significant headwinds from increased raw material and distribution/logistics costs, as well as supply chain risks through various initiatives(2) such as price adjustments and restructuring of supply chains

**Japan:**

- **New houses**: The gap between new housing starts and number of houses built in FYE2022 has been almost resolved. Forecast for new housing starts in FYE2023 is expected to decrease slightly against FYE2022, especially in H2.
- **Renovation**: Continued strong demand. However, lockdowns in China could affect supply chain and cause delays of construction.

**International:**

- **EMENA:** Moderating growth in Europe and continued strength in the Middle East
- **Americas:** Continued positive renovation demand expected despite decline in new housing demand due to rising interest rates
- **China:** Closely monitoring impact of lockdown on economic activity and supply chain
- **Asia Pacific:** Expect continued economic recovery
- Closely monitor impact from logistic disruptions and accelerated cost inflation to timely mitigate availability constraints and maintain margins

LIXIL (1) Company estimate of new housing starts for FYE2022 as of February 2022
(2) Please refer to page 4

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Business assumptions. I think it has rarely been as difficult to come up with business assumptions as it was this time. In terms of the big picture, we believe that what happened from January to March will continue for the foreseeable future.

When the cost of new construction in Japan has risen to such an extent that it is difficult to build new houses, especially low-cost new houses, I believe there is a good chance that this will lead to a shift to renovation.

As I mentioned earlier, when it comes to price optimization, the ratio of low-cost housing is declining, so I think it is a good thing for renovation to increase.

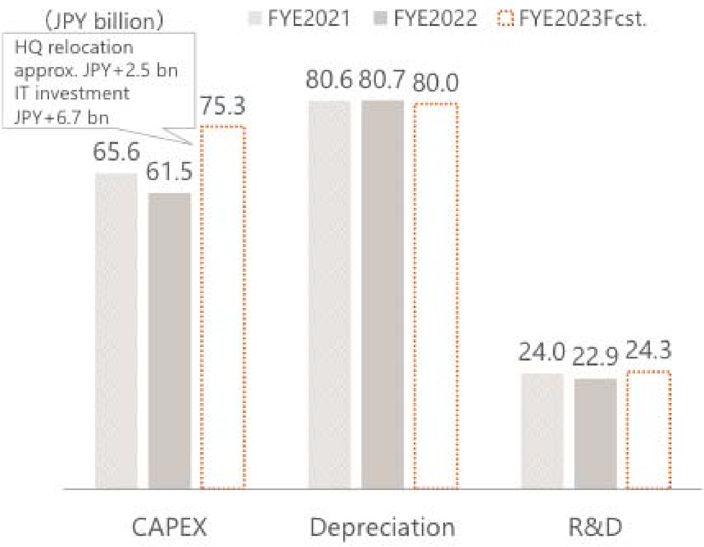
Meanwhile, I believe that many things will happen in the international businesses. Europe, certainly, is not without its concerns. However, in the Middle and Near East, various projects are returning to normal against the backdrop of rising fuel prices.

In North America, we are concerned that higher interest rates may dampen demand a bit, but for the time being, we are receiving very solid orders related to our renovation business.

China has some uncertainty going forward. With regard to Asia Pacific region, there have been lockdowns here and there for the past two years, so I think there is enough pent-up demand.

## CAPEX, DEPRECIATION, AND R&D EXPENDITURE[1]

**By setting investment efficiency and safety indicators such as Key Goal Indicator, we achieve both an improvement of financial strength and in profitability**




Breakdown of CAPEX

| JPY billion | FYE2021 Actual | FYE2022 Actual | FYE2023 Plan |
|---|---|---|---|
| IT investment | 9.8 | 10.1 | 16.8 |
| Excluding above | 55.7 | 51.4 | 58.5 |
| Total CAPEX | 65.6 | 61.5 | 75.3 |

Breakdown of Depreciation

| JPY billion | FYE2021 Actual | FYE2022 Actual | FYE2023 Plan |
|---|---|---|---|
| IT depreciation | 10.8 | 12.9 | 12.0 |
| Excluding above | 69.8 | 67.8 | 68.0 |
| Total Depreciation | 80.6 | 80.7 | 80.0 |

LIXIL (1) Excludes discontinued operations. CAPEX and Depreciation includes intangible assets and IFRS 16 lease

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As for structural investment, as I mentioned earlier, we will continue to invest in intellectual properties, design, IT, and other such areas, but we plan to limit investment in traditional facilities to a certain extent. We are working in accordance with our strategy playbook, which is LIXIL's management direction.

That concludes my explanation. I would like to continue explaining by answering your questions.

## Question & Answer

**MC [Q]:** We will now begin the question and answer session.

Let me introduce the first question. This is from Mr. Fukushima of Nomura Securities Co. I think that the price increase starting with April orders will not be sufficient, so I am sure that a second price increase is being considered somewhere down the road. On the third page of the financial results presentation, you plan JPY48 billion in price optimization and structural reform effects for the fiscal year ending March 31, 2023. If you separate by items that are largely confirmed from those that still need to be determined, what does it look like? What needs to be done going forward?

**Seto [A]:** Naturally, as I mentioned earlier, JPY23 billion of the JPY50 billion in increases of material costs and other costs were in January to March, which conversely means that it is impossible to optimize prices in April, so most of the price optimization for this portion will be in October.

In that sense, it will take six months to have effect. That time lag is one of the reasons why we were only able to accumulate about JPY48 billion of response measures against the JPY92 billion expected cost increase that I mentioned earlier.

Conversely, that gap between expected cost increase and effect from response measures will be smaller once the price optimization starting in October covers a full year. Therefore, in a sense, if the current situation continues, the period from October to March would be more profitable for us rather than the period from April to September.

The JPY48 billion strategy is almost complete. It is almost finalized. So, for example, if the October price optimization were not already almost finalized, to start on that from now would mean it would not be ready in time. Therefore, I think the difference is whether or not that can be added to if something were to happen from here on in. At this stage, this has already been done sufficiently.

**MC [Q]:** We have received one more question from Mr. Fukushima. The company has announced a share buyback, saying that it has achieved its mid-term goal of strengthening its financial position. How do you intend to position share buybacks in shareholder returns going forward? Please tell us again about your shareholder return policy, including your dividend policy.

**Seto [A]:** This is not something that can be answered only by the executive side, so I will tell you just my own thoughts. I am sure there are many opinions among the directors, of course. One thing that can be said about dividends is that we have been aiming for stable dividends for some time now, so if we gradually raise our profit level, in turn, we will be able to give return to shareholders, mainly through dividends.

On the other hand, I think there are two purposes for share buybacks in general. One is to make some plans regarding the cash we have, and to return this portion to the shareholders where we feel it is safe to return it to them now. The other is to send a message to the market when the Company's stock price is too low compared to the Company's original evaluation.

However, the latter approach is not commonly practiced in Japan, and to do it when there is not enough cash available to buy back the Company's own shares would be misleading in a sense. So, regarding share buybacks, mainly for the first approach, we have to stabilize our dividends somewhat.

On the other hand, we will set dividends conservatively, but use it in such a way that if cash remains compared to the amount of investment we plan to make in the future, it is reasonable to return it to shareholders. So, I think that, for share buybacks, it is difficult to plan when they will happen.

I think the normal practice is probably to pay dividends for the portion that can be paid out in a planned manner, and the buyback Company's own stock for the rest. But again, this is just my opinion, and it is not a policy that has been decided through discussion by the Board of Directors.

**MC [Q]:** Next, we have questions from Mr. Takegawa, of Sumitomo Mitsui Trust Asset Management. This is the first question. Can you give us some background on the period that just ended in terms of the slight underachievement of core earnings of the international business? The second question is whether or not the construction companies will be able to keep up with the price optimization in Japan? The third question is regarding the background of the revenue increase in Japan for the current period.

**Seto [A]:** I think that the rapid increase of raw material costs in Q4 was the biggest reason why we fell short of our plan, both in international market and Japan. Roughly speaking, costs have risen by JPY50 billion, JPY27 billion of which is for the first nine months. Therefore, normally, the last three months would be JPY9 billion.

But the actual cost was JPY23 billion, so the difference was JPY14 billion. The difference between JPY80 billion of initial forecast of core earnings and JPY65 billion of actual result of core earnings is JPY15 billion, so I think that pretty much explains this part. This is almost the same situation in Japan and international businesses, but I think that the major shortfall factors in Japan, especially in the housing technology business, was due to that.

Secondly, regarding if construction companies will be able to keep up with the price optimizations in Japan, basically, we have no choice but to ask them to follow us. We think that it will probably be very difficult to win market share without price optimization as material costs increased this much.

Simply put, I think that most construction companies will pass it on to the house owner if increases of material costs are reflected on product prices. What is somewhat different now, I think, is that the so-called "house manufacturers" are moving toward a more upscale approach, concentrating on houses that are somewhat expensive and have a high price per unit of area.

Power builders will continue with regard to the land they have already purchased, but it will be difficult for them to demand an unreasonable price. I don't think there are that many manufacturers who will decide to go along with this.

If we are forced to adjust our prices, it will not be a sustainable business in the long run. If we were in a position of being pushed to comply without being able to adjust prices, I think we could probably survive without doing that. Conversely, I think those portion that we don't force ourselves to take will eventually come back to us.

Last are the so-called small- and medium-sized local construction companies. They don't purchase land in advance, and their variable cost portion is relatively large, so, although they are similar to the house manufacturers I mentioned earlier, but they may decide not to go along with new housing. I believe that they would then be more likely to shift toward renovation instead.

I am not sure which part is the tipping point, but one thing I can say is that although the current number of new housing starts in Japan at annual 800,000 houses seems very low compared to the numbers of the past, but when you consider the ratio of new houses to the population of Japan with the US and Europe, it is rather high. Conversely, I believe this is because we have built a large number of houses that are not designed to be renovated.

Whether or not this will be the tipping point where the market changes in the future will be important for our business. However, in our business, when it comes to selling differentiated, high-quality products, we would like to move away from the business model of providing very inexpensive products for very inexpensive houses.

In that sense, if the purpose of your question is to ask whether we should offer a low price in order to gain market share, we would not do so, and we have been promoting platform-based production and structural reform of the Company to make that acceptable. That is also the reason we lowered fixed costs as well as organized our factories to some extent.

In terms of your third question which is the background of revenue growth in Japan, there are the renovation projects I mentioned earlier, as well as a national policy to invest in windows as an environmental measure, which is attracting a great deal of attention at the moment. We believe that it is quite probable that these and other high-end and differentiated products that we have been working on steadily will sell well.

**MC [Q]:** Next, we have received one more question from Mr. Takegawa. Regarding Housing & Services business, please tell us about the rapid recovery measures you will have to make this period.

**Seto [A]:** Until now, we have had a rather large share of the low-cost market, but we are trying to change this as well. One is to offer renovation products to customers who have already purchased from us in the past by, for example, changing exterior walls via the cover construction method or installing a better kitchen, rather than spending money on new construction. And the other thing I would like to do is to shift a little bit to luxury housing.

We have said that we do not intend to own many tangible assets, so we think it is important to change LIXIL REALTY into a service business without having many assets.

**MC [Q]:** Next, we have two questions from Mr. Kawashima of SMBC Nikko Securities. This is the first one. The current prices for aluminum and copper exceed the assumptions for the fiscal year ending March 2023, but will the increases of these costs continue in the fiscal year ending March 2024, when the hedging effect wears off, or will the October price optimization cover these impact as well?

And the second question is, you will sell your shares in EDION, but how should we understand this in terms of the strategy for the renovation sales channel? Will you also sell further holdings, such as shares in housing companies?

**Seto [A]:** As for the current price, we are planning to cover it considerably by price optimization in October, which is, of course, related to the earlier question. An October price revision, of course, would only be in effect for six months with respect to the current fiscal year, so in that sense, it is inadequate. Therefore, there is a possibility of an additional price optimization in the fiscal year ending March 2024 if this situation continues, but we are considering a large range of price revisions in October 2022, so I think we will be able to cover quite a bit.

On the other hand, as for copper prices, they have calmed down a bit. Regarding the price of copper, as I mentioned earlier, we believe that hastily switching from copper to zinc and plastic will have a large positive effect.

As for the EDION shares, when we purchased the shares of EDION Corporation, we started talking with each other about working together to expand renovation sales, and we have already achieved considerable numbers. Therefore, we decided to continue the business tie-up after reaching an agreement that both parties can work well together without holding shares in each other.

This is not a major change, but for us, selling products to retailers is a very important strategy that is easily understood by end users. We are planning to sell our products not only to EDION Corporation, but also to various other retailers.

As for the sale of shareholdings, we have been working nonchalantly to reduce our cross shareholdings. However, of course, there is a lot of past history and promises made to customers at that time, so I cannot make a blanket promise now about what will happen.

However, as you can see from our track record, over the past several years we have been gradually making changes to these cross shareholdings, for ones which are not well accepted by our shareholders.

**MC [Q]:** Next, we have two questions from Ms. Okada of Goldman Sachs. First question, in the business of the Americas, I assume that you have been passing on past increases in raw material prices and other costs, but I am not sure if the situation is such that price optimizations will be acceptable in the future. Also, what is your view on the impact of higher mortgage rates on the housing market?

Second question, regarding the China business, I think it did relatively well despite the deteriorating real estate market conditions. Can you please explain the reasons for that?

**Seto [A]:** The business of the Americas has passed on prices the most times. In that sense, the competitors have also been doing this, so I don’t think the price pass-through itself will affect demand.

However, our faucet business in the Americas is the weakest among our international operations. Our business of the Americas is very strong in ceramics, and we want to strengthen our faucet business, especially showers. In this respect, we are able to use zinc while our competitors are currently focusing on brass and copper, which, conversely, allows us to realize a cost advantage.

As for ceramics, I think that optimizing price will be done in much the same way as others do.

Meanwhile, I am sure that the housing market will probably be impacted by the mortgage rate hikes you mentioned, but it’s not always the case that it happens right away. Also, when you buy a new house, there is big demand in the US to renovate it. But even if you don’t buy a new house, what you end up doing with that money is to change your current house by improving the inside. That is a universal thing.

If the housing market itself were to decrease by 100%, would it necessarily impact our business? We don’t think that is necessarily the case.

At this point, based on the orders we are getting, we believe the situation is solid so far. Of course, with regard to the future, the part we don’t know is that now, in the US, if interest rates are raised more and more, it is obviously possible that this will change.

As for the China business, I believe there are still many risks, so we are working to reduce the size of each unit of business by changing from projects to retail, and from projects to e-commerce. As a result, I think it will be a resilient business, even though it may not grow brilliantly.

Now, the CFO also pointed out to me that another thing I can say is that GROHE’s China business is doing well. I think that GROHE is relatively well recognized in China as a good product and brand by end-users, and that the design and brand recognition are spreading. On the other hand, American Standard brand products, which has been relatively strong in project-based business, is struggling a bit.

**MC [Q]:** The next question is from Ms. Katsuyama, of Morgan Stanley MUFG Securities. With regard to geopolitical risks in Europe, I would like to know if there has been any impact on consumer sentiment and renovation demand.

**Seto [A]:** At least in Eastern Europe, we have already given up on Ukraine and Russia this year. As for Russia, I've given up for a very long time. As for Ukraine and Eastern Europe, I still think it will be tough.

In Central Europe, such as Germany and Austria, overall sentiment is deteriorating, but on the other hand, as I mentioned earlier, demand for DIY is growing at a fairly high rate. I think it is quite significant that we were able to launch *QuickFix* as a product and a brand that captures this demand.

I think we can say that the part of Eastern Europe that is worsening at the moment is covered by the EMEA, where energy prices in Gulf regions have gone up and project demand has gone up. Also, Central Europe, which includes Germany and Austria is doing relatively well.

Certainly, as Ms. Katsuyama pointed out, not just in Europe, there is a strong possibility that consumption sentiment itself will deteriorate, but one thing to keep an eye on is whether rising energy costs will be a positive or negative factor.

In general, rising energy costs are having a negative impact on the economy due to the current recession and a decrease in residential real estate purchases due to higher interest rates, but from a window manufacturer's point of view, rising energy costs are a great opportunity to expand business.

In the case of windows in Japan, it is said that there are windows for roughly 62 million houses in Japan today, and 90% of them do not comply with the environmental standards of the year 2016. About 80% of the houses have single-glass windows. It is said that just by replacing this single-glass with triple-glasses, CO2 emissions can be reduced by 14 million tons a year. It is hard to find a single product that lowers energy costs so much.

The residential sector consumes about 40% of the energy for heat in Japan, and 58% of that goes out the windows. Therefore, if we don't improve the windows, we will run out of fuel. I think this could be a tailwind for our business and we need to make the most of it.

Meanwhile, the international businesses focuses on water-related business, and we must use water efficiently. Especially in cold regions, where water is heated for use. Therefore, replacement with new faucets is required. Demand, especially with respect to shower products, tends to rise when energy costs rise.

Therefore, we can respond to inflation by determining which products are required by consumers, and what our customers are looking for, and then concentrating our efforts on supplying those products in the fewest number of SKUs possible. I think we can also better cope with inflation by moving forward more quickly with the switch from copper to zinc, as I mentioned earlier.

Everything is connected, but, of course, a crisis can lead to opportunity. It is true that the cost crisis has put pressure on our profitability, but in the mid- to long-term, I think it has created a great opportunity for us.

**MC [Q]:** I have received another question. This is from Mr. Miki, of Citigroup Global Markets. What is the progress of the sale of the head office building? Please tell us how you have factored this into your forecast for this fiscal year, whether you will be able to sell it this fiscal year, and your thoughts on how you plan to use the proceeds from the sale.

**Seto [A]:** We have almost agreed on the sale. There are some last-minute adjustments to be made on the contracts, but we can conclude the sale without any problems at all by the end of this term. As for the funds, we have not decided to use these funds for this purpose, but as I explained earlier, we will need to use funds for investing in items such as intellectual property and design. And we have a consistent policy of returning to shareholders what we do not use.

**MC [Q]:** Next, Ms. Okada from Goldman Sachs Japan, has a question about the policy for reducing head office expenses. The company's forecast for the current fiscal year is JPY45 billion for head office expenses, an increase from the previous year. Please explain the reasons for this and your policy for reducing head office expenses in the future.

**Seto [A]:** Part of it has to do with the sale of the headquarters, a period during which we have to hold both costs for the headquarters we are in now, and costs incurred from moving to a new place. After that, there are, of course, expenses for relocating the head office. Another major IT expense we are investing in is the shift to a cloud-based system.

Then there is digital education for employees. In short, we are talking about Citizen Developers, and our policy is basically to ensure that all employees have IT training and are able to improve their own work. We are currently anticipating these expenses.

**Matsumoto [A]:** The grouping of head office expenses includes, of course, costs from the usual head office departments, such as human resources, accounting, legal, as well as the costs for strategic use as mentioned earlier. The breakdown of regular headquarter department expenses will decrease compared to the previous fiscal year. The current situation is that we are reducing them through various measures initiated earlier, such as shared service centers and offshore.

**Seto [A]:** In that sense, the head office expenses, and as I mentioned earlier, IT and other expenses, as well as the shared services expenses, will decrease from next fiscal year onward on a recurring basis, even though those expenses are increasing this fiscal year.

**MC [Q]:** Here's the next question. It's from Mr. Yagi, of Mitsubishi UFJ Morgan Stanley Securities. What is LHT and LWT's approach to renovation demand in Japan? Is there a possibility that demand will decrease in the future?

**Seto [A]:** I think LHT will definitely increase because the demand for LHT renovation is low right now when compared to international, which I talked about a little earlier.

First of all, energy issues and the environment issues will certainly increase window renovation. Also, for example, since the number of natural disasters is increasing, we need shutters and shades during the summer months. The number of door renovation has also increased significantly, including doors that allow ventilation, because of the spread of COVID-19.

As for exteriors, people want to enjoy various things outside due to the spread of COVID-19, and this demand is increasing every year.

In terms of interior furnishing materials, the market as a whole is not necessarily growing, but from our own perspective, the strength of designing all products on our own has led to gradual growth, and I believe that LHT is growing significantly as a whole for renovation.

In the case of LWT and its water related products, I think it is quite possible to assume that when it becomes difficult to build low-cost houses at the current low-cost level, the trend will be toward renovation.

In reality, the demand for water related renovation is solid. I think the main reason why the demand for water related renovation is not growing sufficiently right now, including for our competitors, is the disruption of the supply chain. I am assuming that there is impact from shortage of semiconductors, connectors, and various other such products here and there that are needed to make large quantities of many products.

**MC [M]:** Well, since that seems to be all the questions we have, we will now conclude the question and answer session.

This concludes the presentation of the financial results of LIXIL Corporation for the fiscal year ended March 31, 2022. We look forward to your continued support of LIXIL. Thank you very much.

[END]

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***Document Notes***

1. *Speaker speech is classified based on whether it [Q] asks a question to the Company, [A] provides an answer from the Company, or [M] neither asks nor answers a question.*
2. *This document has been translated by SCRIPTS Asia.*

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