Summary of the Q&A Session
Financial Results Briefing for 2Q of the Fiscal Year Ending March 31, 2023

Date and Time: November 1 (Tue) 10:00 - 11:10

Notice: This summary is a reference designed for the convenience of those who could not attend the financial results briefing stated above. Please note that this is not a word-for-word transcript of all remarks made at that session, but is a summary prepared by Kurita Water Industries Ltd.

Q. With regard to orders from China, while the increase in the number of projects is positive, recently there has been talk that the outlook is increasingly uncertain. Given this backdrop, can you comment on customer type for the orders you have received? Are there concerns that are visible to you at this stage, such as impending export restrictions?

A. Our 1H China orders are mainly from local Chinese semiconductor manufacturers but cover a diverse array of customers, including small-scale chip makers. With ongoing local lockdowns as a result of the government's zero COVID strategy, we hadn't initially expected to make much progress on negotiations. However, the Chinese government's initiatives to strengthen the semiconductor industry kept investment appetite stronger than we had anticipated. This is our understanding of the backdrop to 1H orders.

On export restrictions, we believe a sudden deterioration in US-China relations could trigger the imposition of tighter restrictions. Based on this assumption, we are reviewing order content thoroughly before accepting orders. We already have track records for supplying facilities to many Chinese semiconductor and FPD makers. Our plan is to focus on the onsite service business as showcased today, more sophisticated management and maintenance services, and the supply of reclaimed water; our stance is to fully take into account the external environment, including US-China relations, in accepting orders.

Q. Recent news flow has included reports of production cuts and lower capacity utilization in certain subsectors of the electronics industry. It appears that this had an impact on the precision tool cleaning business in 1H. Please explain the current impact of customer production adjustments on businesses such as Ultrapure Water Supply, maintenance and precision tool cleaning, as well as the outlook going forward.

A. The business that is the most resilient in the face of lower capacity utilization at our customers' plants is the Ultrapure Water Supply business. The model is structured to generate profit even with just the basic fee. For maintenance services, there are customers that will undertake maintenance when plant operations are paused, so lower capacity utilization can actually lead to opportunities for business. The precision tool cleaning business is the most impacted by lower capacity utilization. Structurally, the domestic precision tool cleaning business tends to see more of an impact than the overseas business.

However, for the electronics industry business as a whole, our order backlog is currently at high levels and we have made progress in converting customers to service businesses. As such, we don't expect to see an immediate deterioration in profitability. For the precision tool cleaning business, we have a sense of urgency related to rising costs, given surging labor costs in the US. We are currently considering many initiatives to absorb the rising costs, such as automation.

Q. With regard to the expansion of service contract-type business for the electronics industry as highlighted on slide 23, please share your expectations for the magnitude of business growth and your targets.

A. We are currently formulating the next medium-term management plan. The electronics industry is positioned as a growth market and we are considering targets.

Q. The 2H guidance for overseas water treatment facilities' orders is 12.9 billion yen, significantly lower than the 1H results. Are you merely being conservative or do you expect the number of projects to decline in 2H? With regard to the orders expected from China and South Korea, please discuss the breakdown by customer type. Please provide color on changes you are seeing in terms of the firmness or stability of orders or changes in customer base.

A. The backdrop to our expectation for a decline in orders in 2H compared to 1H is that we saw some frontloading of orders originally expected in 2H into 1H, a reflection of customers placing orders earlier in response to longer lead times for the delivery of facilities as a result of component and materials shortages. Our impression is that up to the end of 1H, capex did not decline much compared to the fall in capacity utilization. It may well be that there will be some changes in timing but we have not heard that projects are going away. With regard to orders from China and South Korea, we expect orders in China to come from a wide array of customers, mainly in semiconductors. For Korea, we expect orders from existing semiconductor customers.

Q. Please talk about the progress you are making in raising prices by region as well as your plans for 2H.

A. We are currently executing on the second and third round of price hikes across all regions. We have had the most success in Europe where the 1H improvement in the CoGS ratio exceeded our expectations. The progress in ASEAN has been middling. Progress in China, South Korea and Japan has been challenging but we expect to see the impact from higher selling prices in 3Q and beyond. In the US, we have been proactively raising prices but it is not enough to fully cover increasing costs, such as logistics expenses. However, we continue to implement price hikes.

Also, ongoing initiatives to improve global procurement efficiency by leveraging procurement capabilities in each region have started to bear fruit. If the pricing situation for raw materials stabilizes in 2H, we would expect to see a positive impact come through. However, if prices continue to rise, it may be tough.

Q. In the analysis of the factors that impact profit, does the negative impact on the CoGS ratio include the net impact of higher selling prices?

A. We have factored in the net impact of selling price hikes, assuming that raw materials prices remain at current levels. However, we have not factored in 100% of our targeted selling price hikes; the expected contribution is based on our track record to date.

Q. Please provide the segment breakdown for the impact of the deterioration of the CoGS ratio for 1H and guidance for 2H.

A. The breakdown of the 1H business profit impact from the deterioration of the CoGS ratio is roughly evenly split between Water Treatment Chemicals and Water Treatment Facilities. In 2H, we expect the impact of the deterioration to be larger for the Water Treatment Facilities business, with only a modest impact on the Water Treatment Chemicals business.

Q. My impression is that it is relatively easy to pass along higher costs in the Water Treatment Facilities business at the time of receiving orders but the precision tool cleaning business is depressing segment margins. Do you anticipate implementing measures such as price hikes going forward?

A. For the precision tool cleaning business, we have already initiated price hikes in the US reflecting rising labor costs. We will be implementing measures for the domestic business going forward. In particular, we have seen electric power costs rise. However, the general trend suggests that it will be difficult to pass on higher costs immediately. We will need to be smart about how we address this.

Q. Please provide an update on the growth of the overseas CSV business and the revenue scale of the service contract-type business in 1H.

A. My impression is that the CSV business has finally started to grow. Over the last 2 years, progress was sluggish because of the pandemic, which prevented visits to conduct sales training and to customer sites. With restrictions lifted, we have started to see improved take-up of selling methods outside of ASEAN, such as in Europe, South Korea and China. Also, rising energy costs are a tailwind for the CSV business, as it makes the value proposition for the CSV business more attractive. We expect to see further growth in 2H and FY ending March 2024.

Non-consolidated service contract-type business sales in 1H were approximately 2.3 billion yen, up 0.6 billion yen YoY. The CSV business orders related to Water Treatment Chemicals as of 1H were 10.6 billion yen, up 2.5 billion yen YoY.

Q. You indicated that the increase in orders for the electronics industry was the result of frontloading orders owing to component shortages. Are you concerned about a potential decline in FY ending March 2024 orders because of the demand pull-forward? Or, do you expect demand to remain strong given the trend toward building out the electronics industry as social infrastructure?

A. We do not expect that the 1H level of orders can be maintained going forward but we do expect capex to continue around the world in the medium- to long-term given that the electronics industry is increasingly positioned as a key element of social infrastructure. Customers that operate globally tend not to miss the timing for investments; as such we expect our customers to continue to invest.

Q. With regard to services for general industry, progress in deploying the solution model had been slow as a result of the pandemic limiting sales activity and longer time frames for field trials. Do you feel you are now gaining traction?

A. We now have the ability to visit our customers' sites frequently and it is now possible to conduct field trials. The solution model is increasingly being embraced. We have seen the emergence of solutions, such as material yard management for the steel industry, which have applications not only for the domestic market but for other regions around the world. I believe it is important to deploy with speed, including training in sales methodology. I believe we can look forward to further growth, including the successful solutions included in 1H CSV business.

Q. This fiscal year, you expect to exceed full-year sales of 300 billion yen for the first time. Do you see the Kurita Group aiming to achieve sales of 400 or 500 billion yen in the next medium-term management plan which starts in the next fiscal year? Or, directionally, will you be more focused on improving profitability even if sales do not grow? What sort of initiatives are you considering for the next medium-term management plan that will lay the foundations for the 5-year period beyond the medium-term plan period?

A. We are still in the process of considering targets for the next medium-term management plan, but I think there are 2 vectors we could pursue.

The first would be to focus on how much we can grow the electronics industry business. As we focus on going deeper with current initiatives, I think the key point for the next 5-year plan will be to look at the business model of the Ultrapure Water Supply business, which most epitomizes our know-how and technological superiority, and to think about what we should target and how this service should evolve. During the last 2 years, the electronics industry has been extremely active. It may appear as if the business structure has reverted back to a focus on EPC but our aim is to shift to service businesses that allow us to maintain contact points with a diverse array of customers over the long-term by providing solutions to the challenges facing the electronics industry. The key for sales growth will be whether we will be able to directionally demonstrate a significant step up based on this.

The other is the general industry area. Compared to the electronics industry, the frequency and scale of capex is not that large. As such, we must identify issues specific to wider geographical areas or industries rather than focusing on individual companies. The key to growth will be creating new solutions in collaboration with local governments or corporates, by bringing to bear our base of global expertise and, in particular, the diverse service business base of the domestic business. Our aim is to deploy solutions unique to the Kurita Group where there are markets, without limiting ourselves to the electronics industry.

Through this, I believe it is possible to envision a scenario for topline growth.

Q. In precision tool cleaning, please describe the difference between the domestic Kuritec Service and the US Pentagon businesses. Is the strong performance of Pentagon the result of an increase in volume or progress in cultivating new customers?

A. Kuritec Service concentrates on the cleaning of production equipment tools at existing, operating semiconductor and FPD plants. By nature, the business tends to be impacted by customer capacity utilization. Pentagon concentrates on cleaning of SPE tools to be installed in new plants, so is strong in the cleaning of new equipment. The growth of the last 2-3 years reflects the success in winning business from new plants. I believe the combination of the strengths of both creates a strong business model, capturing capex growth and customer utilization. We are also focused on initiatives such as automation and technological differentiation.

Q. Is the business of precision tool cleaning for new equipment installation a new business for the Kurita Group?

A. Precision tool cleaning for new equipment requires certification by the SPE makers, but we did already have this service. However, Pentagon was further ahead than our domestic business.

Q. Is the growth in Pentagon's 1H sales the reflection of market share gains in new precision tool cleaning?

A. In addition to the continued increase in new tool cleaning projects, Pentagon is also leveraging the new precision tool cleaning business to subsequently capture utilization-linked business with customers. Pentagon is solidly increasing its cleaning business at customer plants.

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