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Asahi Kasei Corporation

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Presentation

Hamamoto: Good afternoon, ladies and gentlemen. My name is Futoshi Hamamoto from Investor Relations, serving as the moderator. I thank you very much for joining us in the briefing on fiscal 2019 Q2 financial results of Asahi Kasei Corporation, despite your busy schedule.

Today's participants are: Yutaka Shibata, CFO; Yozo Sato, Corporate Accounting & Control; Toshiyasu Horie, Basic Materials Strategic Business Unit, or SBU; Yukifumi Kuwaba, Performance Products SBU; Hiroaki Sugiyama, Specialty Solutions SBU; Akira Fukuda, Separator Adminisration, Specialty Solutions SBU; Izumi Kawata, Asahi Kasei Microdevices Corp.; Kensuke Sakai, Asahi Kasei Homes Corp.; and Masato Kashiwagi, Asahi Kasei Pharma Corp.

We will begin with a presentation from Yutaka Shibata, the CFO.

P. 2 Focus of H1 2019 results and H2 2019 forecast

Shibata: My name is Shibata, CFO. I will explain referring to the presentation material slides. Please look at slide 2. Here you can see key points regarding the results for H1 and the full-year forecast, focusing on operating income.

First, H1 results. Operating income totaled ¥101.7 billion, exceeding the forecast of ¥94.5 billion as revised in August. Two background factors are cited on the slide. First, the Material segment performed in line with the forecast made in August. When we made a downward revision in August, we referred to the slowdown in the Chinese economy and the slowdown in the automobile-related markets. That situation continued, and the result was as is described on the slide.

The Homes and Health Care segments both exceeded the forecast made in August. Part of this was due to the fact that some profit planned for H2 materialized earlier in H1. Each business made a firm progress as planned. It is not that there are major changes taking place in the business environment between H1 and H2, but rather, as will be explained later, there was some impact of the consumption tax increase and a shift in some fixed costs mainly in R&D from H1 to H2.

Accordingly, the operating income forecast for the full year has been revised downward by ¥12 billion from the May announcement to ¥193.0 billion, reflecting the current economic environment.

More specifically, forecast for the Material segment has been revised downward. Back in May, we assumed that, while H1 would continue to feel the impact of the US-China trade war and the slowdown in the automobile-related markets that continued from H2 of last year, recovery could be expected during H2. However, given the current situation, we now feel that no dramatic change or recovery in the environment is likely, and thus the revised forecast reflecting that.

Two major background reasons are described here. First is Performance Products. As described here, major products in fibers, engineering plastics, and synthetic rubbers were affected by the slowdown in the Chinese economy and the slowdown in the automobile-related markets.

Another is that in Specialty Solutions. We revisited volume forecast for the LIB separators. Particularly regarding a demand for ESS, energy storage system, applications in South Korea, there were several fire incidents last year, and due to the impact, several customers resorted to production adjustment for a while. In Q2 of this year, shipment volume temporarily recovered, but then at the end of H1, there were ESS fire incidents again in Korea. Because another fire broke out, production is now being adjusted again. So we took account of the resulting uncertainty for H2.

Forecast for automotive applications has also been revised in terms of growth rate. Demand for automotive applications is strong overall, and we have been increasing production capacity to meet this demand. Initially at the beginning of the fiscal year, we made a rather aggressive sales volume forecast. But then we took a closer look at the timing of the launch of new projects and others, and slightly revised the growth rate.

For Homes and Health Care, the forecast for the full year remains almost the same, but some profits shifted from H2 to H1, due to several factors. One is the last-minute demand surge ahead of the consumption tax hike. Another factor is fixed costs. Especially in the Health Care area, there are always a fairly large R&D cost. And this year, some of that shifted to H2. In addition, there was a shift in some sales from H2 to H1, partly due to reasons on the part of some customers. As a combined result of these various factors, profit shifted from H2 to H1. In that sense, we expect some decline in profit from H1 to H2, particularly for Health Care, but it's not that there has been a significant change in operating environment on half-yearly basis.

P. 5 Summary of financial results

Slide 5 shows the results for H1 and the main figures. Net Sales totaled ¥1,068.6 billion, almost the same as in the August forecast. Operating income was ¥101.7 billion, as mentioned earlier. Net sales, which increased by ¥27.2 billion, were the highest ever for H1. The acquisition of Sage Automotive Interiors, Inc. contributed to sales. Operating income, ordinary income, and net income attributable to owners of the parent also recorded the second-highest amounts, to follow the record highs set in the same period last year.

Compared to the previous year, Material felt a significant effect of maintenance shutdown of naphtha cracker and plants for derivatives this year. In addition, as I mentioned earlier, market prices deteriorated, the Chinese economy slowed down, and the market for automobiles and smartphones slowed down compared to the previous year, which had an effect.

Interim dividend for H1 is ¥18 per share, in line with the August forecast.

P. 6 Statements of income

Slide 6 shows consolidated profit and loss. I have already discussed net sales. Gross margin was almost the same as the same period previous year. SG&A increased year-on-year by ¥12.1 billion, due to IT-related investments and increased amortization of goodwill associated with the acquisition of Sage.

There is a year-on-year decline in the net of non-operating items. The decline mostly comes from equity in earnings or losses of affiliates, as MMA operations at PTT Asahi Chemical Company Ltd. in Thailand suffered from a decline in market prices.

Net of extraordinary items came to an income of ¥5.5 billion, thanks to gain on sale of investment securities as a result of reducing strategic shareholdings.

Profit for the period attributable to owners of the parent came to ¥77.9 billion, down ¥1.1 billion, year-on-year.

P. 7 Balance sheets

Slide 7 shows the balance sheet. Total assets increased by ¥15.4 billion from the end of March to the end of September. The increase comes from inventories and non-current assets. Inventories increased for Homes and for ZOLL, on the back of strong business performance. Non-current assets increased in relation to M&A and capex.

To the right side of the table for liabilities and net assets. Non-current liabilities increased due to a ¥36.7 billion increase in interest-bearing debt. With regard to net assets, retained earnings after dividend payment increased, but the share repurchase and retirement had a negative impact. In addition, the stronger yen compared to end of March pushed down foreign currency translation adjustments, which is part of accumulated other comprehensive income.

In the lower left-hand corner, we show goodwill, interest-bearing debt, and the D/E ratio. Goodwill increased after closing the acquisition of Cardiac Science Corp. in August. Interest-bearing debt increased by ¥36.7 billion to ¥461.2 billion. The D/E ratio at the end of September came to 0.33, up 0.02 from the end of March.

P. 8 Cash flows

Slide 8 shows cash flows. Cash flows from operating activities was a net inflow of ¥77.8 billion. Net income was slightly down, but goodwill and capex–related depreciation and amortization increased from the same period previous year.

Cash flows from investment activities was a net cash outflow of ¥73.8 billion. Last year, we had a major cash outflow for the Sage acquisition, but such was not the case this year.

The resulting free cash flow was a net inflow of ¥4 billion.

With regard to cash flow from financing activities, we increased debt to finance the acquisition of Cardiac Sciences and the share repurchase.

Cash and cash equivalents at the end of September stood at ¥185.5 billion.

P. 9 Sales and operating income increase/decrease by segment

Slide 9 describes H1 results and the differences from the equivalent period last year.

Material was down year-on-year for both net sales and operating income. Shipments decreased. We went through maintenance shutdown of naphtha cracker and plants for derivatives. Market prices deteriorated, the Chinese economy slowed down, and there was sluggishness in automotive and smartphone–related markets. All had negative impacts.

Homes and Health Care were up year-on-year for both net sales and operating income.

For Homes, sales and income growth was driven mostly by order-built homes, thanks to increased deliveries and higher average unit prices due to increased contribution from larger homes. There was a slight rush demand ahead of the consumption tax hike. Both net sales and operating income were highest ever for H1.

Health Care results came in higher than the August forecast. Some fixed costs were pushed back into H2, such as R&D spending for pharmaceuticals, and we booked some sales earlier than expected.

P. 11 Consolidated operating performance forecast

Slide 11 shows the full-year forecast. We have revised the full-year forecast that was announced in May. The new forecast is ¥2,221 billion in net sales, and ¥193 billion in operating income.

Homes and Health Care performance is expected to continue strong. On the other hand, Material is downward revised, as we do not expect rapid recovery during H2 with regard to conditions that prevailed in H1 such as weak market prices, the slowdown in the Chinese economy, and sluggishness in automotive-related markets.

The revised forecast for net profit attributable to owners of the parents is ¥143 billion. The forecast assumes exchange rates of ¥110 to the US dollar and ¥120 to the euro.

Planned dividend remains unchanged at ¥36 per share over the full year, but the final decision will depend on actual full-year results.

P. 12 Sales and operating income forecast by segment

Slide 12 shows the breakdown of the latest forecast by segment. Please look at the right-most column, which shows the difference from the forecast announced in May.

We have downward revised the full-year net sales forecast by ¥47 billion. Material is downward revised by ¥58 billion, while Health Care is upward revised by ¥12 billion, including the effect of the acquisition of Cardiac Science.

With regard to operating income, Material is downward revised by ¥14 billion, while Homes and Health Care are upward revised by ¥500 million each, and corporate expense and eliminations also upward revised by ¥1 billion. Total consolidated operating income is downward revised by ¥12 billion.

This concludes my presentation. Thank you for your kind attention.

<u>Question and Answer Session</u>

Hamamoto: We will now take questions.

Mr. Watabe: Watabe from Morgan Stanley MUFG Securities. My first question is on Basic Materials. From Q1 to Q2, there were such positives as the absence of maintenance shutdowns. At the same time, the price spread of acrylonitrile, or AN, obviously narrowed. Will you comment on how the profit or loss for this business category changed from Q1 to Q2, and also your outlook on AN for H2, please?

Horie: Horie from Basic Materials SBU. First of all, regarding your first question, the absence of maintenance shutdown of the naphtha cracker and the turnaround of our derivative products in Q2 did have a positive effect quarter-on-quarter, as you have correctly described. The spread of AN narrowed somewhat, but it was not a big drop. The rest was the combined effect of individual factors such as those related to polystyrene and polyethylene. Basically, the quarter-on-quarter change was in line with the forecast.

You also asked about the projection on AN for H2. First of all, looking back on H1, regarding demand we had had concerns that the ABS resin manufacturer's operating rate might be affected by the US-China trade friction, but it actually turned out to be relatively steady. As for H2, we have a slightly cautious outlook. As China's home appliance products production began to fall towards the end of H1, we anticipate that the demand might be somewhat weaker.

In terms of supply, as you know, some new plants of Chinese AN manufacturers started operations in September to October, while there was an announcement of a plant closure in the UK. Overall, supply is likely to increase a little, so we foresee that the supply and demand balance will ease toward January to March. That is the basis of our earnings forecast.

Mr. Watabe: What about the market prices and price spread specifically?

Horie: Our assumptions for H2 are; the AN market price $1,450 per ton, and propylene $900 per ton, for a spread of $550 per ton.

From April to June, the spread was $943 and the AN market price was $1,833. And from July to September, the spread was $815 and the AN price was $1,761.

Mr. Watabe: I see. My second question is on Specialty Solutions, especially LIB separators, for which you made a slight downward revision. Is it primarily related to the dry-process or is the wet-process included as well? I wasn't very sure about automotive applications. What were the changes from Q1 to Q2, and what's your projection for H2? And what about sales volume metrics?

Fukuda: Fukuda from Specialty Solutions SBU. First, from Q1 to Q2, LIB separators actually increased in volume, including those for ESS. Following the release of the Korean government's investigation report on the ESS fires in June, shipments were steadily recovering in July and August. However, as you are aware, there was another fire at the end of August, and shipments turned sluggish again in September. So, as far as Q2 is concerned, the volume increased over Q1. Also, the wet-process saw a demand increase from Q1 to Q2 thanks to the typical seasonal factors in relation to consumer electronics. So overall, the total volume increased, resulting in higher sales and profit.

Regarding the changes from H1 to H2, the capacity expansion of the wet-process is expected to contribute, so we are projecting increased sales mainly in automotive applications. So, separators expect sales and profit to increase from H1 to H2. At the same time, we expect uncertainly over ESS to continue.

Mr. Watabe: Did the separators account for the rather sizeable recovery in operating income for Specialty Solutions from Q1 to Q2?

Sugiyama: Sugiyama from Specialty Solutions SBU. The separators were a big reason, but there were others. Smartphone-related products in electronic devices improved slightly toward Q2, and shipments of ion-exchange membranes and other products also concentrated in Q2. In total, an improvement of about ¥4 billion coming from all these factors.

Mr. Watabe: I see. Thank you.

Mr. Yamada: Yamada from Mizuho Securities. My first question is on Health Care. The effect of the acquisition of Cardiac Science seems to contribute ¥12 billion in sales in Critical Care in H2. What about the impact on the operating income? And how about the next year? I also have a question on Teribone osteoporosis drug, which remains strong in the Health Care business category. But wouldn't it be regarded inferior in the face of the competition from sclerostin monoclonal antibody? Also, isn't there any risk of Teribone's market share being eroded by abaloparatide currently under clinical studies, and the like?

Shibata: First, I, Shibata, will talk about the ZOLL question, and then ask Kashiwagi to talk about pharmaceuticals. While Cardiac Science does not account for all of the ¥12 billion upward revision of full-year forecast, most is in fact Cardiac Science. The amount of goodwill has not been fixed yet, and so we are using a provisional amount. The burden of goodwill is heavy, and we had yet to feel the full benefit of synergy at the time of closing. But going forward, synergy should be felt and contribution should realize. I think that will be for the next fiscal year onward. Resuscitation is making a steady growth.

Kashiwagi: Kashiwagi from Asahi Kasei Pharma. Teribone twice-weekly self-administered auto injector formulation has been approved, but the drug price has yet to be listed. Anti-sclerostin antibody was launched in March of this year. While the mechanism of action is different, it is intended for patients with a high risk of fractures, so it is true that it is affecting the sales of Teribone. However, the autoinjector formulation that's been approved is scheduled to be released later this year, and it is indeed a very compelling, easy-to-use formulation.

Mr. Yamada: Is it fair to say that you are confident that, with the new formulation, Teribone can successfully compete against the anti-sclerostin antibodies and abaloparatide, and expand sales?

Kashiwagi: Yes, you can say that.

Mr. Yamada: Thank you. My second question is on Performance Products. I think the situation in the automobile-related markets is quite uncertain, not clear. I believe Performance Products has rather high exposure to automobile-related markets. So will you comment on the current situation related to automobile-related markets and the outlook for H2? Also, what actions do you have in mind in the face of this sluggishness in the final product markets? Can you also give us an update on the progress of post-merger integration related to Sage?

Kuwaba: Kuwaba from Performance Products SBU. As you pointed out, the automobile-related markets are highly uncertain. First, in terms of outlook for H2, we expect profit level to remain flat from H1 to H2.

Performance Products include consumables such as Saran Wrap cling film for the Japanese market, for which there basically was a surge in demand in H1 ahead of the consumption tax hike, and so it is expected that profit will decline slightly in H2. Engineering plastics and synthetic rubber are expected to see an increase in volume, resulting in higher profit.

For Fibers, some are doing better than others. Lamous artificial suede is growing in automotive interiors applications, while Bemliese continuous-filament cellulose nonwoven is struggling somewhat. Overall, we expect the fibers to remain unchanged.

As for Sage, H1 results were close to the initial forecast. H2 might turn out to be more challenging in terms of sales volume compared to the initial forecast.

Mr. Yamada: Other than engineering plastics and synthetic rubber, I really don't see much reason for growth in H2. And given that engineering plastics and synthetic rubber are quite dependent on the automobile-related markets, I think there is a downside risk. Or are you not concerned because you already have secured expanded adoptions by the automotive OEMs of your S-SBR, solution-polymerized styrene-butadiene rubber, engineering plastics, and compounds?

Kuwaba: Yes, as you described, our forecast is based on the adoptions in new car programs and the like, so we doubt there will be a major slip.

Mr. Yamada: I see. Thank you.

Mr. Ikeda: Ikeda from Citigroup Global Markets Japan. May I ask you to again tell us about the growth rate in the volume of LIB separators of the Specialty Solutions, for H1 and the full-year outlook. I think the risk of price erosion for the separators is emerging, with some Chinese manufacturers turning more aggressive regarding European automakers. What is your take on this? Can you also give us an update on the medium- to long-term outlook.

Fukuda: Fukuda from Specialty Solutions. First, overall sales volume of LIB separators in H1 dropped 14% compared to the same period of the previous year. This was largely due to the fact that, while the wet-process separators saw an increase coming from capacity expansion, the dry-process separators were reduced by half, year-on-year, due to the stagnant Korean ESS market as mentioned earlier. Accordingly, in terms of shipment volume index, it was 353 in H1 of FY 2018, 311 in H2, and 303 in this past H1.

As for the full-year outlook, we expect greater contribution from the capacity expansion of wet-process separators in H2, so the wet-process separators are projected to grow by more than 20% year-on-year. The dry-process separators depend on the ESS situation, and we expect the challenging situation to continue in H2.

Mr. Ikeda: I see. What about price projection. While prices overall are trending downward, wouldn't your policy of staying outside of the price war entail a downward risk in terms of volume over a medium term?

Fukuda: The price pressure is always strong especially in automotive applications. We are told that more recently some of Chinese competitors are offering customers fairly low prices. But still, the switch or replacement has not occurred. As far as we are concerned, we strive to contribute to reducing battery costs overall by eliminating waste throughout the supply chain. The cost benefit resulting from internal streamlining efforts can be shared with our customers. We are making such offers to our customers. Therefore, we don't believe there is big collapse in the market price.

As for the future developments, with the expectation that Europe will become a big market, we have assigned a dedicated personnel in the Düsseldorf office of Asahi Kasei Europe since October. We have had a sales person in Europe for dry-process separators, but now we have this full-time dedicated sales person to engage in the marketing for dry-process and wet-process separators together, and make preparations for production increase which may be deemed necessary in the future.

Mr. Ikeda: I would like to ask about the medium-term view on AN, in terms of supply and demand, and your thoughts on the business itself. A Chinese manufacturer has announced a capacity expansion of 520,000 tons. What is the impact of this on your business? Should we assume that the way you position the business will not change? Also, can you comment on the level of profitability you assume for this business.

Horie: Horie speaking. As you are aware, China is still a net importer of AN, so, as long as the importer position continues, there certainly will be capacity expansions. That is our long-term forecast. Regarding the large capacity expansion that's been announced, although we don't know exactly when, we are developing our business plan on the premise that it will materialize sooner or later.

The important considerations for us in doing this are how to build a more stable profit structure in the volatile market, and what part of the market we are to focus in our AN business. For example, in Europe, with the plant closure in the UK, we are receiving an increasing number of inquiries from our customers. In that sense, we are now examining whether we can develop a business view that can be expanded reliably and stably.

Mr. Ikeda: I see. Thank you.

Mr. Takeuchi: Takeuchi from SMBC Nikko Securities. My first question is on Critical Care. On slide 29, the performance of the business is shown in US dollars, and there was year-on-year growth in H1. I understand that this includes the impact of M&As, but can you give us the breakdown between LifeVest wearable defibrillators and other defibrillators? How was business growth momentum during H1?

Shibata: Shibata speaking. There is not much change from what we have been saying in recent briefings. Defibrillators are continuing steady growth, centered around North America and particularly those for professional use. With regard to LifeVest, now that the size of business is much larger than before, the percentage growth rate may have slightly moderated, but year-on-year growth in Q2 was the high single digit. Going forward, the next challenge would be to achieve synergy from the acquisition of Cardiac Science in the AED, automated external defibrillator business.

Mr. Takeuchi: Still on defibrillators. The effect of the issue at a competitor must be mostly gone by now. So, is it correct to understand that your growth is outpacing the market because you are gaining share? And would the LifeVest growth, which you mentioned is in high single digit, gradually settle down to cruising speed? Or would you invest more resources so as to boost the growth rate back into double digits? I would like to get a feel for the LifeVest business growth going forward.

Shibata: LifeVest has more potential to grow, as there are still untapped markets. According to some calculations, we are only serving one third of the potential US market. But now that the business has a much larger geographical reach, SG&A expenses are also increasing. Therefore, our marketing policy of expanding the sales network with a focus on efficiency remains unchanged. The business is transitioning from short-term, explosive growth into longer-term, stable growth, which is exactly what we want.

With regard to defibrillators, including those for professional use, as well as AEDs, we are gaining market share. In fact, it is a major contributor to the increase in the consolidated overseas sales ratio. As the product offering has now been extended by the acquisition of Cardiac Science, ZOLL has access to new market channels. We intend to optimize the product offering to make the most of the opportunities still out there.

Mr. Takeuchi: Thank you. My next question is on Homes. On slide 24, it says that value of new orders in H2 is to decline by 3.9% year-on-year. Can you tell us what led to the downward revision of H2 forecast and your view on the market condition after the consumption tax hike, please?

Sakai: Sakai from Asahi Kasei Homes. With regard to the impact of the consumption tax hike, our initial expectation was that unit homes would not be affected too much, given government support measures, whereas multi-dwelling homes which are not covered by government support programs may be slightly down. In H1, however, the situation was totally opposite. Among order-built homes, newly-built homes were not so affected, but rebuilding was affected.

Taking that into account, and given that H2 orders were very strong in FY 2018, our forecast now expects H2 orders to be down year-on-year at the same rate as H1.

Mr. Takeuchi: Does that mean the current forecast is more reasonable than the initial one which seemed rather challenging?

Sakai: Yes, you could say that. In H2, we will focus our efforts to boost orders, particularly for rebuilding, through various training programs for our salesforce and promotion campaigns for potential customers.

Mr. Takeuchi: Would the order backlog at the end of the year be large enough so that neither sales nor operating income would be significantly down in FY 2020? Can I take it that your order book is sufficiently large to ensure that?

Sakai: That would depend on orders in H2.

Mr. Takeuchi: Thank you very much.

Mr. Umebayashi: Umebayashi from Daiwa Securities. I also have a question regarding Homes. According to slides 17 and 18, if you compare H2 figures year-on-year, you are forecasting sales to be up ¥30 billion, while operating income is to be down by more than ¥1 billion. And you are maintaining the full-year forecast.

Now, at the beginning of the financial year, you were expecting an increase in fixed costs. Judging from year-on-year comparison of H1 operating income, it appears that fixed costs did not increase significantly. So the question is, would that expected increase all happen in H2, so that operating income would be in line with the forecast? Or, could fixed cost be pushed further down into FY 2020, meaning upside potential for FY 2019?

Sakai: Sakai speaking again. Much of the fixed costs that did not happen in H1 are simply pushed back into H2. Actually, the delayed expenses were mostly related to advertisement. So, in Q3, we are executing major sales promotion campaigns to boost orders, with an expanded budget.

Mr. Umebayashi: Does that mean total fixed costs over the full year would be pretty much in line with initial expectation?

Sakai: Yes, that is correct.

Mr. Umebayashi: Thank you. And perhaps related to that, have your sales activities or deliveries been affected by the recent typhoons and floods that hit the Kanto region?

Sakai: I do not think there is any direct effect on deliveries. There may be some impact going forward, as there may be increased demand for post-disaster reconstruction leading to competition over manpower. The effect may be about availability or higher labor costs. But at this point in time, we do not expect a major impact. With regard to orders, visitor count to model homes were affected, as a number of typhoon approaches coincided with weekends.

Mr. Umebayashi: Thank you. My next question is on separators, the dry-process separators in particular. Earlier you mentioned that shipments of dry-process separators in H1 was only half that of the same period previous year. That drop sounds overly large. When we visited your production site in the US, we heard that the dry-process separator business was half for ESS and half for automotive. Does that mean shipments for ESS almost came to a standstill, or did shipments for automotive also decline year-on-year?

Fukuda: Fukuda for separators. With regard to the ESS business of dry-process separators, back when we were budgeting for the current financial year, we expected the South Korean government to release results of the investigation into the first fire incident sometime around March, so that business would be back to usual from April. However, the investigation report only came out in June. As a result, there was very little shipment for ESS in Q1.

In addition, there was disturbance in the market for automotive due to Chinese government policy, which resulted in reduced shipments to China. When you all came over for the plant tour in September, capacity utilization was still high, but shipments fell just after that, and the environment remains very challenging.

Mr. Umebayashi: Would that have an impact on your capacity expansion plans? Any delays?

Fukuda: With regard to the dry-process capacity, we commissioned part of the additional capacity in FY 2018 as planned. With the dry-process, you can increase capacity in increments. After the ESS-related fire incidents and slower-than-anticipated demand growth, we adjusted both the commissioning schedule for new capacity and utilization levels of existing capacity. Full commissioning of the planned additional capacity would be delayed by roughly a year.

Mr. Umebayashi: Thank you very much.

Mr. Miyamoto: Miyamoto from UBS Securities Japan. I also have a question regarding separators. Earlier you mentioned that dry-process separator shipments were down by half from the previous year. Is it possible to boost capacity utilization by selling more separators elsewhere, such as for use in EVs in developed countries? And, are more separator users transitioning from single-source procuring to multiple source procuring?

Can you also give us an idea about the trend in sales prices? I understand you cannot be too specific. But for example, if you look at slide 15 and the operating income difference for specialty solutions, the difference due to sales prices minus the impact of foreign exchange is a positive impact of ¥400 million.

I guess part of this would be due to sales mix difference, but can you explain this positive impact? Did electronic device prices rise, while separator prices fell? And if so, was there any difference between the wet-process and dry-process separators?

Fukuda: Fukuda from separators. With regard to the first part of your question, separators for automotive use are not general-purpose commodities, and they need to be evaluated and qualified by each customer before full-scale production, and that process takes time. It is not simply about switching a shipment from one destination to another.

With regard to sales price changes, as far as we are concerned, there is not much difference between the dry-process and the wet-process. Our separators are tailored to specific customers and specific applications. Obviously, there is competition, on price and/or performance to win business with any customer, but that has always been the case, and I do not think there has been any substantial change.

Sugiyama: Sugiyama from Specialty Solutions. With regard to the positive impact of sales prices when excluding the exchange rate effect, it includes prices raised to reflect higher feedstock prices, although the extent differs by product. Therefore, the net impact, when you look at spreads, is limited. Such price adjustments happened for performance materials, but they certainly do not represent any rising trend in sales prices.

Mr. Miyamoto: Are you saying that separator prices are coming down, but only at a similar pace as before?

Fukuda: Fukuda speaking. In the case of separators, especially for those for automotive use, when sales volume grows, we can produce in larger batches and reduce changeovers, which has significant cost benefit. Part of such benefit is shared with customers in the form of reduced sales prices.

Mr. Miyamoto: Are more dry-process separator users switching from single-supplier sourcing to multi-sourcing?

Fukuda: Yes, and it is not only dry-process separator users, but wet-process separator users as well. Therefore, where we are a sole supplier, we work hard to keep it that way. Where we do not supply yet, we try to become a second supplier.

Mr. Miyamoto: From the outsider's point of view, your efforts appear to be quite successful.

Fukuda: Well, thank you. We cannot comment on specific customers and contracts, but the reality is that we are sometimes successful, but sometimes not.

Mr. Miyamoto: Thank you for that. Now on Basic Materials. Can you provide more detail about the difference in operating income between H1 and H2, please? On slide 18, for example, H1 operating income was ¥20.1 billion and H2 forecast is ¥13.4 billion. I understand that AN is a big factor for this decline, since you discussed spreads earlier, but wouldn't there be other factors, too?

Horie: Horie from Basic Materials. Other than AN spread, MMA is also a big negative factor for H2. There is a maintenance turnaround, and prices are very challenged now. There are other smaller factors as well, such as slower shipments of polyethylene, as well as for polystyrene, whose domestic demand has been slowing down since August. They may be minor in size, but do have an impact, when combined.

Mr. Miyamoto: Can you tell us about capacity utilization, please?

Horie: With regard to AN, our current plan is to continue running at 80 to 90% capacity, while monitoring the supply-demand balance. The naphtha cracker is running at full capacity. Derivatives will also be running at near-full capacity after the maintenance turnaround in H1.

Mr. Miyamoto: Was AN capacity running at 80 to 90% capacity in Q2, too?

Horie: Actually, just for Q2, utilization was very high and sometimes near full capacity.

Mr. Miyamoto: Thank you very much.

Hamamoto: With that, we would like to close today's earnings briefing. Thank you very much for joining us.