# Transcript of Financial Results Conference for Q1 Fiscal 2021, held on August 6, 2021

Asahi Kasei Corporation

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## Presentation

Hamamoto: Good afternoon. Thank you very much for joining the conference call on Asahi Kasei Corporation's earnings for Q1 FY 2021. This is Futoshi Hamamoto from Investor Relations. We will begin with a presentation from Koshiro Kudo, CFO. After that, we will take questions.

Other participants from Asahi Kasei are: Yozo Sato, Corporate Accounting & Control; Takuya Takahashi, Basic Materials Strategic Business Unit, or SBU; Nobuhiro Yamaguchi, Performance Products SBU; Hiroaki Sugiyama, Specialty Solutions SBU; Eiji Ishikawa, Specialty Solutions SBU, for separators; Izumi Kawata, Asahi Kasei Microdevices Corp., Kensuke Sakai, Asahi Kasei Homes Corp.; and Ryuji Kibe, Asahi Kasei Pharma Corp.

I will give the floor to Mr. Kudo now.

Kudo: Good afternoon and thank you very much for joining us for this earnings briefing.

### P. 4 Summary of financial results

Let us begin with slide 4. In Q1 of FY 2021, net sales came to ¥583.4 billion, operating income was ¥60.5 billion, ordinary income ¥65.2 billion, and net income attributable to owners of the parent came to ¥46.4 billion. All these figures are the highest ever for a Q1. In Q1 last year, earnings were significantly hit by COVID-19. This time, all 3 segments, and especially Material, posted year-on-year growth for both sales and operating income.

Starting from FY 2021, we are applying the Accounting Standard for Revenue Recognition, which means that the criteria used for recognition of net sales and cost of sales are now different for some transactions. Later, we will explain this more in detail by segment. For total consolidated results, however, the impact of this change is minor for both net sales and operating income.

## P. 5 Sales and operating income by segment

Moving on to slide 5. This shows quarterly sales and operating income by segment.

In Q1 FY 2021, for the Material segment, there was recovery in automotive-related markets. In addition, market prices for petrochemical products rose rapidly on the back of demand recovery, which resulted in inventory valuation gain by the gross average method. Sales and operating income both increased considerably.

The Homes segment benefitted from the consolidation of McDonald Jones Homes Pty Ltd., etc. and strong performance of other overseas businesses. The change in the method of revenue recognition also pushed up net sales and operating income related to order-built homes. As a result, both sales and operating income increased for the segment. In the footnotes, we describe the impact of the new revenue recognition method by segment. It pushed up operating income for the Homes segment by ¥1,751 million.

For Health Care, in Critical Care, ventilator sales are down, but the mainstay defibrillator business was strong. Pharmaceuticals and medical devices also had solid performance. As a result, both sales and operating income increased from the same period last year.

## P. 6 Statements of income

Slide 6 shows the statements of income.

Net sales for the quarter came to ¥583.4 billion, up ¥128.3 billion from the same quarter previous year. Gross profit came to ¥195.4 billion, and gross margin improved by 0.6 percentage points to 33.5%. SG&A came to ¥134.9 billion, which is an increase of ¥15.1 billion. There was an effect of newly consolidated companies such as McDonald Jones, and increased expenses for R&D and logistics.

Operating income came in at ¥60.5 billion, up ¥30.4 billion from, or almost double, the year-before figure. Operating margin came to 10.4%, up 3.8 percentage points from the same period previous year.

The net of non-operating income and expenses came to an income of ¥4.7 billion. That's up ¥4.5 billion from the same period previous year. Net equity in earnings or losses of affiliates improved by ¥3.8 billion thanks to improved performance at PTT Asahi Chemical Company Ltd. which produces AN, acrylonitrile, in Thailand.

The net of extraordinary income and loss came to an income of ¥3.2 billion. That's an improvement year-on-year by ¥8 billion. On the extraordinary income side, there was gain on sale of investment securities after unloading some strategic shareholdings, and gain on step acquisitions related to McDonald Jones. We entered a capital alliance with McDonald Jones, which is a company in Australia, back in 2017 and had since owned a 40% stake. This time we acquired an additional 40% and made it a consolidated subsidiary. Among extraordinary losses, we booked business structure improvement expenses, which is mostly related to starting up alternative production capacity after that fire at our semiconductor plant.

Income before income taxes came to ¥68.4 billion. That's up ¥42.9 billion year-on-year. Income taxes amounted to ¥21.6 billion, up ¥10.5 billion as corporate income taxes increased commensurate to pre-tax income.

Net income attributable to owners of the parent came to ¥46.4 billion, up ¥32.8 billion year-on-year.

## P. 7 Balance sheets

Slide 7 shows the consolidated balance sheets.

Total assets increased from the end of March to end of June by ¥56.8 billion. Goodwill, etc. was recorded on acquisitions including that of Respicardia, Inc. in Health Care. Property, plant and equipment increased with capex. Application of the Accounting Standard for Revenue Recognition resulted in an increase in contract assets and a decrease in inventories.

Liabilities increased from the end of March by ¥27.3 billion. Interest-bearing debt increased by ¥40.9 billion.

Net assets increased by ¥29.5 billion. Retained earnings increased thanks to net income attributable to owners of the parent of ¥46.4 billion, which more than offset the ¥23.6 billion in dividend payout. The debt-to-equity ratio came to 0.47, up 0.02 points, which is within our targeted range of around 0.5.

### P. 8 Cash flows

Slide 8 shows cash flows.

Cash flow from operating activities was a net inflow of ¥30.2 billion. Inflows included income before income taxes of ¥68.4 billion and depreciation of ¥28.7 billion. Outflows included accrued expenses coming down by ¥20.3 billion. Compared with the same period previous year, while income before income taxes increased, working capital such as trade receivables also increased as sales recovered, and the net cash inflow decreased.

The investment cash flow was a net outflow of ¥39.7 billion. Outflows included capex and acquisition of Respicardia. Compared with the same period previous year, cash outflow increased in relation to acquisitions including that of Respicardia.

Cash flow from financing activities was a net cash inflow of ¥11.6 billion. There was cash outflow due to dividend payment, but that was more than offset by the inflow from fundraising. As a result, cash and cash equivalents at the end of June came to ¥219.7 billion.

That is all for Q1 results.

### P. 10 Consolidated operating performance forecast

Moving on to page 10, operating performance forecast for H1 of FY 2021.

The forecast for net sales is ¥1,198 billion and for operating income ¥106 billion, both of which are higher than H1 of FY 2019, pre-COVID-19 level, to achieve the highest ever H1 results. We expect increased sales and profit year-on-year, on the recovery in the Material segment.

From the previous forecast announced in May, we have made upward revisions to sales and operating income forecast in all 3 segments, especially the Material segment, reflecting the strong Q1 results and changes made to the exchange rate assumptions for Q2 reflecting the depreciation of the yen.

Net income attributable to owners of the parent is expected to be ¥72 billion, a downward revision of ¥15 billion from the previous forecast in May, at which time we expected tax expenses to be reduced by about ¥24 billion this fiscal year in relation to the organizational reconfiguration at Veloxis Pharmaceuticals Inc., but due to administrative work of the Danish authorities, we rescheduled the timing of recognizing the lower tax expenses from H1 to H2, thus the downward revision. If we exclude the impact of this rescheduling, we believe that the progress of net income is also strong.

Interim dividend is forecasted to be ¥17 per share.

### P. 11 Sales and operating income forecast by segment

Next, page 11, net sales and operating income forecast by segment.

I will explain the upward revision made to the previous H1 forecast by segment. In Material, we've made upward revision in light of the strong performance in Q1, market prices of petrochemical products having risen more than expected, and firm sales expected for lithium-ion battery, or LIB, separator.

Forecast for Homes has also been revised upward, as overseas business expects firm performance.

Health Care forecast has also been revised upward with firm performance expected in the core businesses of Critical Care such as conventional defibrillators and LifeVest wearable defibrillator.

In terms of year-on-year comparison of operating income, Material expects a significant recovery, while Homes is projected to maintain the same level as in the previous year despite difficult business environment, and Health Care expects decreased profit compared to the same period of the previous year when there was special demand for ventilators, but mainstay businesses are projected to perform firmly.

### P. 13 Sales and operating income increase/decrease by segment

Page 13, breakdown of changes in net sales and operating income by segment.

The largest factor was sales volume, which contributed to an increase of ¥21.4 billion. Sales prices contributed to an increase of ¥20.6 billion, due to the rise in the petrochemical market prices, including foreign exchange rates. Others include rising feedstock prices and changes in inventory valuation gain. In summary, sales price was positive ¥20.6 billion and others was negative ¥11.6 billion, indicating improvements in terms of trade.

### P. 16 Overseas sales

Page 16, overseas sales.

Net sales in Q1 were, as mentioned earlier, ¥583.4 billion, of which overseas sales totaled ¥293 billion. The overseas sales ratio was 50.2%, exceeding 50%. Last year it was 41%. While the ratio had been around 40% in recent years, it went over 50% this year.

Of this amount, about 80% is sales at overseas subsidiaries, and the remaining 20% plus is exports from Japan. As we are proceeding with overseas M&A activities, overseas sales are increasing along with the growth of the acquired companies. We expect this trend to continue, with some possible fluctuations in the overseas sales ratio from Q1 level of over 50%.

### P. 19 Operating income forecast by business category

Page 19, operating income forecast by business category.

Operating income is projected to decrease from ¥60.5 billion in Q1 to ¥45.5 billion in Q2. During Q1 there was a profit in Basic Materials in relation to inventory valuation gain, as well as a nonrecurring gain on the accounting treatment related to the acquisition of Respicardia in Critical Care.

In Q2, we are expecting a temporary increase in fixed costs and incurring of in-licensing costs in pharmaceuticals. We thus project operating profit to decline by ¥15 billion quarter-on-quarter. But there are no concerns about demand or the business environment, including economic trends and overseas market conditions, and we consider the forecasted amount of ¥45.5 billion to be achievable.

Also, as stated in the financial statements, we have not changed the full-year forecast at this time. Toward H2, we do not have concerns regarding our business, although there are some uncertainties such as foreign exchange, the impact of COVID-19, and semiconductor shortages. We believe that currently the progress is generally in line with the May forecast.

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

## **Question and Answer Session**

Hamamoto: Let us now take questions.

Mr. Watabe: Watabe from Morgan Stanley MUFG Securities. My first question is about the Material segment. Can you provide more detail on the quarter-on-quarter difference between Q4 FY 2020 and Q1 FY 2021 for the 3 business categories, and between Q1 and Q2, please? Can you also tell us how large the inventory valuation gain impact is?

Takahashi: Takahashi speaking for Basic Materials. Could we look at slide 28, please? Quarterly operating income for Basic Materials was ¥10.1 billion in Q1, almost unchanged from ¥9.8 billion in Q4. In fact, there were a number of factors pushing operating income both upwards and downwards.

In general, demand is strong and market prices have been solid. In Q1, however, there was a maintenance turnaround at Mizushima Works which had a negative impact. On the other hand, market prices for the mainstay AN remained rather high. In addition, feedstock prices rose which resulted in inventory valuation gain. The impact of the maintenance turnaround was for about ¥3 to 4 billion, but the inventory valuation gain more than offset that.

Yamaguchi: Yamaguchi for Performance Products. Demand has been firm from Q4 FY 2020 to Q1 FY 2021 and into Q2. For automotive applications, in particular, shipments have been strong, despite some regions such as North America being affected by the shortage of semiconductors.

The improvement in operating income from Q4 to Q1 was mostly driven by terms of trade. Feedstock prices rose in Q4, but those higher prices are only reflected in sales prices with a delay. Terms of trade were therefore squeezed in Q4 but improved in Q1.

Between Q1 and Q2, terms of trade would be squeezed in Q2 as some feedstock prices are still rising quite rapidly. This is one reason for the expected decrease in operating income. In addition, more fixed expenses are to be booked in Q2, towards the end of H1. Capacity utilization will also be lower in Q2 due to maintenance turnaround. Market-wise, demand is strong for both automotive and non-automotive applications.

Sugiyama: Sugiyama for Specialty Solutions. Compared with Q4 FY 2020, Q1 net sales was down by ¥4 billion, whereas operating income was up by ¥3.3 billion. In reality, business remains firm.

With regard to net sales, separators and electronic devices were both firm and slightly up quarter-on-quarter. There were, however, one-time factors around a number of products among former performance materials. For example, we booked rather large sales for membrane-process chlor-alkali plants in Q4, but not quite so in Q1.

Thankfully, performance was firm for other products, separators in particular. And fixed costs were higher in Q4 as it was the final quarter of the financial year. Those factors drove the ¥3.3 billion quarter-on-quarter increase in operating income.

Mr. Watabe: Thank you. My next question is about business structure improvement. At the management initiative briefing in May, it was explained that 15 businesses were identified as strategy reformulation businesses. Recently you announced restructuring your spandex operations in Europe, and I believe that was the first among a series of announcements to come. Do you plan for most of such strategy reformulation for the Material segment within FY 2021? If so, are the associated expenses already budgeted?

Kudo: This is Kudo speaking. The discontinuation of production in Europe is part of the restructuring of spandex business. Among the 15 strategy reformulation businesses, for some, we may restrategize and reinforce, some we may withdraw from, and for some we may form an alliance with a partner. The time horizons, therefore, may vary. We do expect to make announcements on some businesses during the current financial year, but it may take more time for others.

Now, our next medium-term management initiative is due to start in FY 2022. When we announce the new initiative, we may provide an update with more detail.

Mr. Watabe: Thank you very much.

Mr. Yamada: Yamada from Mizuho Securities. My first question is about Health Care. Q1 results for Critical Care came in strong. Last year, from Q1 through Q3, ventilators provided a boost for earnings. How does it look like on a comparable basis, excluding that impact? What about the impact of the acquisition? Can you also explain why you expect net sales and operating income to decline from Q1 to Q2, please?

Kudo: This is Kudo speaking. With regard to Critical Care, shipments of ventilators peaked in Q2 last year, but have come down to normal levels. For Q1 this year, gain on accounting treatment related to the acquisition of Respicardia pushed up operating income. Even excluding that effect, on a comparable basis, the business is performing pretty strong, with recovery in conventional defibrillators such as AEDs and defibrillators for professional use, and LifeVest.

Now with regard to Q2, our operating income forecast is ¥7.1 billion, down from Q1. The acquisition-related accounting gain will be absent. Orders for LifeVest tend to be slow in summer. In addition, given the resurgence of COVID-19 cases, we are staying on the conservative side. Having said so, judging from results up to July, business performance is stable, and we expect the growth trend to continue for Critical Care.

Mr. Yamada: Can you tell us more about that accounting gain related to the Respicardia acquisition?

Kudo: ZOLL had extended a loan to Respicardia prior to the acquisition, and it became part of the acquisition payment. In that process, there was valuation gain.

Mr. Yamada: Is that reflected in operating income?

Sato: This is Sato from accounting. According to the US accounting standard which ZOLL uses, such valuation gain is treated as part of operating income.

Yamada: Thank you. My next question is about Homes. Back in FY 2020, Q1 and Q2 orders were very slow. Despite that, Q1 performance this year was firm. Can you tell us why? And total orders from April to July are significantly up from the same period last year. Is this better than expected?

Sakai: Sakai for Homes. In Q1, adoption of the new Accounting Standard for Revenue Recognition artificially pushed up figures. But even excluding that effect, performance was solid, partly as the average unit price rose for order-built homes with the increase in larger homes. The upward revision for H1 also reflects firm performance of overseas operations.

The value of orders received in Q1 recovered to almost the same level as Q1 FY 2019. The July figures were actually higher. This is generally as expected.

Mr. Yamada: Was the ¥2.4 billion operating income for overseas business also as expected? And could you explain the ¥5.7 billion operating income for order-built homes? I would not expect the new accounting standard to have such a significant impact, or did it?

Sakai: Overseas businesses did outperform expectations, particularly in North America. The impact of the change in revenue recognition was slightly higher than expected. As written in Slide 13, it pushed up Homes net sales by ¥7.9 billion and operating income by ¥1.8 billion.

Yamada: Does it mean you have a solid profit margin for order-built homes, in a way that allows you to stay profitable even against higher material prices?

Sakai: Yes.

Yamada: Thank you.

Mr. Miyamoto: Miyamoto from SMBC Nikko Securities. I have 2 questions. First on Specialty Solutions. You have upward revised the H1 forecast by ¥5 billion for operating income. I understand that the foreign exchange rate has a significant impact on this business category, and suspect it to be a factor, but can you tell us more about the revision?

Can you also give us an update on the separator business, which you also upward revised? On the downstream side, it appears that electric vehicles are doing very well in Europe. How does that affect you?

Sugiyama: Sugiyama speaking for Specialty Solutions. We have upward revised the net sales forecast for H1 by ¥9 billion and the operating income forecast by ¥5 billion. Basically, we expect the same factors that led to strong Q1 earnings to continue. The separator business is strong. The former performance materials businesses are also firm. In particular, with COVID-19, stay-at-home demand for IT devices have been strong, and associated demand for our products remain firm. Semiconductor-related products are doing well, too.

The foreign exchange rate also has a large impact and accounts for about half of the ¥5 billion upward revision for operating income.

Ishikawa: Ishikawa speaking for separators. We have upward revised the forecast for both net sales and operating income this time. The major driver is the wet-process separator for LIB. Demand has been strong for consumer electronics applications particularly in Q1 and continuing through H1. The same can be said for automotive-related demand, including that for Europe, too.

After that high shipment volume in Q4, we were worried that production capacity may fall short of demand, and that was reflected in our initial forecast. However, with new capacity commissioned ahead of schedule, among other things, we have now upward revised the H1 forecast.

Mr. Miyamoto: In July, a new policy was announced in Europe, recommending phasing out of internal combustion engine vehicles. Given this, do you expect further increase in LIB separator demand?

Ishikawa: This is Ishikawa for separators. We expect demand in Europe to continue to grow significantly going forward, and accordingly we feel we should consider how best to deal with it.

Mr. Miyamoto: I see, thank you. My next question is on sales of pharmaceuticals on page 25. You said previously that sales of Envarsus XR immunosuppressant drug exhibited sluggish growth in Q4 due to some temporary factors. In Q1, sales increased 26% year-on-year, indicating steady growth. Is it fair to say that the temporary factors have been resolved and Envarsus XR's sales are back on the growth trajectory? Also, do you expect the high growth to continue into Q2?

Hamamoto: Hamamoto of IR will take that question. As you have correctly indicated, the temporary factors mentioned in the briefing in May have subsided. Envarsus XR had been growing at a high growth rate until Fiscal 2020 when the impact of COVID-19 dealt a blow in the US. MR activities were restricted, which affected hospitals' adoption of Envarsus XR into new protocols. Also, conversion from other treatments remained below the previous year's level. However, since Q1 this year, the overall number of new kidney transplants has been increasing again, and the number of patients on Envarsus XR is steadily increasing as well. So, we expect steady growth in the medium to long term.

Mr. Miyamoto: I see. Can we expect high sales growth to continue toward Q2?

Hamamoto: Yes, you can expect that.

Mr. Umebayashi: Umebayashi from Daiwa Securities. I would like to ask about trends in automotive-related products, which should be mainly be the Performance Products. I see that Q1 recorded a significant increase year-on-year, but how did it compare to Q4?

I believe automotive OEMs had to cut down production due to semiconductor shortages, but it appears that auto parts and component material suppliers, including your competitors, are not affected much, looking at the level of shipments. Now, you are expecting a slight decline in profit of the Performance Products for Q2. So, I'm wondering whether this means you are expecting a reactionary decline in Q2 following a slight oversell in Q1. Can you comment on the trends of automotive-related products from Q4 to Q1, and then into Q2?

Yamaguchi: Yamaguchi from Performance Products. Yes, global automobile production is now projected to be slightly lower than previously forecasted. Our projection is for production to decline in H1 and then recover in H2.

However, demand from Japanese OEMs and the Asian market is very strong, to the extent that production cannot keep up with it. Therefore, while there might be some impact of the reduction in automobile production due to semiconductor shortages, we do not foresee a decline in sales volume of our mainstay automobile-related products such as engineering plastics and Lamous artificial suede. In the meantime, US automakers seem to be struggling in procuring semiconductors, which is slightly affecting our business in North America.

So, true, operating income is expected to decline from Q1 to Q2, but this is due to such factors as worsening terms of trade and an increase in fixed costs. We do not expect market factors to adversely affect our sales volume from Q4 to Q1 and Q2. In fact, there's an upside potential, should the business in North America recover.

Mr. Umebayashi: I see. In other words, there was no advance shipments in Q1, am I correct?

Yamaguchi: Yes, that is correct. Now there is a possibility that order inquiries are outpacing the strong performance of the automotive market, and we are paying close attention to whether or not the distribution inventory is building up. For the time being, though, we do not anticipate a reactionary decrease in volume.

Mr. Umebayashi: I see, thank you. My next question is somewhat similar in nature, about separators, specifically demand for consumer electronics applications. Following a very strong Q4, you were not expecting sales volume to grow that much in Q1, including the fact that production would not catch up. But it actually turned out that demand continued to be strong, especially in comparison to the demand and production levels of final products. So, I'm wondering whether or not we should worry about the possibility of this being advanced shipments, to be followed by a reactionary decline going forward.

Ishikawa: Ishikawa for separators. For consumer electronics applications, demand for smartphones in China was very strong in Q4 and Q1, but we anticipate that demand will decline slightly going forward due to a glut in distribution inventories. But as far as automotive applications are concerned, demand is expected to be very strong, including in Europe as mentioned earlier.

Mr. Umebayashi: I see. That's all from me. Thank you.

Mr. Okazaki: Okazaki from Nomura Securities. First on Homes. You said that the application of the Accounting Standard for Revenue Recognition pushed up operating income in Q1 by ¥1.8 billion. Do I understand correctly that it will not be repeated in Q2 onward? Also, page 22 shows that the operating income from overseas businesses, etc. increased year-on-year. I take it that this was due to the acquisition of McDonald Jones. Will you describe the organic growth of McDonald Jones itself and the trend in the Australian housing market?

Sakai: This is Sakai of Homes. The positive impact of applying the Accounting Standard for Revenue Recognition in Q1 was greater than anticipated. And we expect that this factor will slightly push up operating income in Q2 as well, but the amount will not be as large as in Q1.

The Australian business is currently doing very well, and progressing well along the plan assumed in the May forecast.

Mr. Okazaki: I see. Was the application of this accounting standard already incorporated in the previous forecast? Also, are there any concerns about the COVID-19 impact on the Australian business?

Sakai: The application of this accounting standard was factored in in the May forecast. Regarding the COVID-19 impact on the Australian business, we are a bit concerned about some suspension of construction work at the moment, but we do not expect much long-term impact.

Mr. Okazaki: I see. Thank you. My next question is on Critical Care. Could you kindly comment on the year-on-year growth rate of defibrillators for professional use and LifeVest in Q1? Qualitative response would suffice. Could you also share your outlook for Q2?

Hamamoto: Hamamoto from IR. I'm afraid I'll have to refrain from giving the exact growth rate. In FY 2020, the full-year sales in Critical Care increased by about ¥49 billion year-on-year, majority of which was contributed by ventilators. More than half of the ¥49 billion increase was recorded in H1 of the fiscal year, but in Q1, the ventilator contribution was not so large. So, in Q1 of this fiscal year, the growth of defibrillators and LifeVest more than made up for a year-on year decrease in sales of ventilators.

As for Q2, we expect defibrillators and LifeVest to continue to grow, but not enough to make up for the year-on-year drop in ventilator sales given that in the previous fiscal year, ventilator shipment peaked in Q2. And thus Critical Care expects lower sales and lower profit year-on-year for Q2.

Mr. Okazaki: I see. I believe the pre-COVID-19 growth rate was around 10%. Can we expect a return to that level?

Hamamoto: Yes. Defibrillators and LifeVest were affected by COVID-19, but demand is firmly returning at the moment, and so we expect the growth rate to return to the pre-COVID-19 level.

Mr. Okazaki: I see. That's all. Thank you.

Mr. Omura: Omura of UBS Securities. My first question is on Homes. I think the business environment surrounding order-built multi-dwelling homes has changed over the last few years, things turning in favor of this particular business. What is your take on the environment surrounding orders for multi-dwelling homes? Also, in light of this steady growth, what kind of growth rate do you expect for the coming few years?

Sakai: Sakai from Homes. The environment for orders for multi-dwelling homes is generally favorable. And we are taking actions to grow the multi-dwelling homes. In particular, we are working to increase large-scale properties such as value-added rental housing, and the average unit price is rising accordingly.

The number of housing starts is expected to decrease going forward in line with Japan's demographic change, and we recognize that multi-dwelling homes are in a similar environment, but we believe that there still is room to increase our market share for both unit homes and multi-dwelling homes. And we are taking actions accordingly.

Mr. Omura: I see. Are you seeing any changes in the order environment or demand trends due to COVID-19 impact?

Sakai: There has been no major change in demand trends, but the means of attracting customer traffic has changed significantly. In the past, we mainly resorted to attracting customer traffic physically to model homes, but now it is done virtually, attracting customer traffic online through websites and the like. But the basic trends seem to remain the same.

Mr. Omura: I see, thank you.

Mr. Okazaki: Okazaki from Nomura Securities again. Can you give us the market prices and price spreads of AN as always, the Q1 actuals and assumptions for Q2, as well as your future outlook on supply and demand.

Takahashi: Takahashi from Basic Materials. Market prices and spreads in Q1 were AN $2,709 per ton and propylene $1,069, for a spread of $1,640, which was slightly higher than previously forecasted.

As for Q2, we originally assumed that supply and demand balance would gradually relax. Prices are assumed to be on average, AN $2,100 and propylene $1,000, for a spread of $1,100.

Spreads in Q1 were at a high level due to the impact of cold waves in the US, but have gradually declined since. Still, they remain slightly higher than expected due to maintenance turnaround campaigns and production disruptions.

Toward H2, demand is expected to basically remain strong, but with additional supply from the completion of maintenance turnaround as well as a possibility of new capacities coming online in China, we expect supply and demand balance to steady rather than relax. Our plants are expected to basically be on full operation excluding the impact of maintenance turnaround.

Mr. Okazaki: Can you elaborate on what you mean by new capacities in China?

Takahashi: It's not certain at all, but there's a possibility that some new capacities scheduled for next fiscal year might start operating earlier in light of the current market situation. So, we will be watching the development closely. But as mentioned earlier, demand is strong, so we believe the supply-demand balance to remain stable.

Mr. Okazaki: I see, thank you.

Mr. Watabe: Watabe from Morgan Stanley MUFG Securities again. Regarding the Basic Materials business, it was explained that the increase in profits due to inventory valuation gain in Q1 exceeded the decrease of ¥3–4 billion due to maintenance turnaround. How much was the impact of inventory valuation gain? Can you also comment on the year-on-year change?

Takahashi: Takahashi from Basic Materials. While the difference in inventory valuation gain increased profits, it is difficult to give an exact amount, partly given that there's a delay in transferring the difference to sales prices. Last fiscal year, market prices fell sharply in Q1, so you might want to look at the impact of inventories this year as the reversal of what happened last year.

Mr. Watabe: So, in that respect, if we assume that impact of inventory valuation gain pushed up profit by about ¥10 billion year-on-year, it seems that there wasn't much increase coming from other factors, despite a gain in relation to AN. Would that be a fair statement?

Takahashi: Yes, in that there was an impact of maintenance turnaround as well as the effect of a decrease in sales volume.

Mr. Watabe: I see. Do I understand correctly that there was no impact of inventory valuation gain on Performance Products?

Yamaguchi: Yamaguchi from Performance Products. I wouldn't go as far as to say no impact, but nothing major that you should be concerned about.

Mr. Watabe: I see thank you.

Hamamoto: Thank you. This concludes the conference call. Thank you for your participation.