LIXIL Corporation

Financial Results Briefing for the Fiscal Year Ended March 2023 for Investors and Analysts

April 28, 2023

Event Summary

[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 2023 for Investors and Analysts	
[Fiscal Period]	FY2023 Annual	
[Date]	April 28, 2023	
[Number of Pages]	25	
[Time]	17:00 – 17:58 (Total: 58 minutes, Presentation: 24 minutes, Q&A: 34 minutes)	
[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 and Leader, Finance and Treasury Corporate Accounting and Treasury/Tax
[Analyst Names]*	Sachiko Okada	Goldman Sachs
	Daisuke Fukushima	Nomura Securities
	Hiroki Kawashima	SMBC Nikko Securities
	Masahiro Mochizuki	CLSA Securities
	Masashi Miki	Citigroup Global Markets

Ryo Yagi	Mitsubishi UFJ Morgan Stanley Securities
Yuki Kuwana	Mizuho Securities

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

Presentation

Moderator: It is now time to commence the financial results briefing session for the fiscal year ended March 31, 2023 of LIXIL Corporation.

First, let me introduce today's explainer. This is Kinya Seto, Director, Representative Executive Officer, President, and CEO.

Seto: Thank you very much.

Moderator: This is Sachio Matsumoto, Director, Representative Executive Officer, Executive Vice President, and CFO.

This is Kayo Hirano, Senior Vice President, Leader, Investor Relations Office and Leader, Finance and Treasury Corporate Accounting and Treasury/Tax.

I am Kawai, Investor Relations Office, and I will be the moderator for today's session.

Please refer to the explanatory materials for this meeting on the Company's website in the Investor Relations section.

I will then explain today's proceedings. First of all, Mr. Seto, President, would like to explain our financial results for the fiscal year ended March 31, 2023. A question-and-answer session will follow. Please limit each person to two questions first. 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, 2023. President Seto, please begin.

KEY HIGHLIGHTS

Summary of results for the fiscal year ended March 2023

Revenue and profits increased year-on-year for Q4 (3 months) FYE2023

- Cost increases caused by higher raw material prices and JPY depreciation were mitigated. Revenue and profits increased due to price optimization while increase of components costs and labor costs are realizing later.
- The pace of profitability improvement has slowed, due to higher fixed costs per unit sales as volumes declined on sluggish demand
- Impact of supply chain disruptions in Europe and inventory adjustment in the U.S. have been resolved from Q4

Revenue increased while profits declined for Q4 (12 months) FYE2023

- Revenue increased due to price optimization implemented in April 2022
- Japan: Profit declined due to the difference in timing of cost increases, including component costs, and price optimization
- International: Profit declined due to cost increases caused by higher raw material prices, supply chain disruptions in Europe caused by the Ukraine crisis, as well as an increase in the COGS from logistics delays and inventory adjustments in the U.S.

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Seto: Hello, everyone. I would like to begin by discussing our financial results for the fiscal year ended March 31, 2023 and our outlook for the fiscal year ending March 31, 2024.

First of all, in the fiscal year ended March 31, 2023, which ended this past March, the picture has changed considerably between the three quarters ended last December and the last Q4. In the first nine months of the fiscal year, we optimized prices since the beginning of the year. We also had some foreign exchange problems, which led to an increase in revenue, but the cost of raw materials, components, and the weak yen caused costs to rise significantly, and we optimized our prices in response. The time lag between the price optimization inevitably caused a very large decrease in profits.

In addition to this, I believe that the first nine months of the year were marked by an even larger decline in profits due to logistics delays in the international markets, mainly caused by Russia's invasion of Ukraine and COVID-19 in the United States.

The logistics disruption has almost been resolved, and on the other hand, the high cost of raw materials has been eliminated. In January, we thought that this would be a very good sign, but unfortunately, demand has rapidly worsened, especially in Japan.

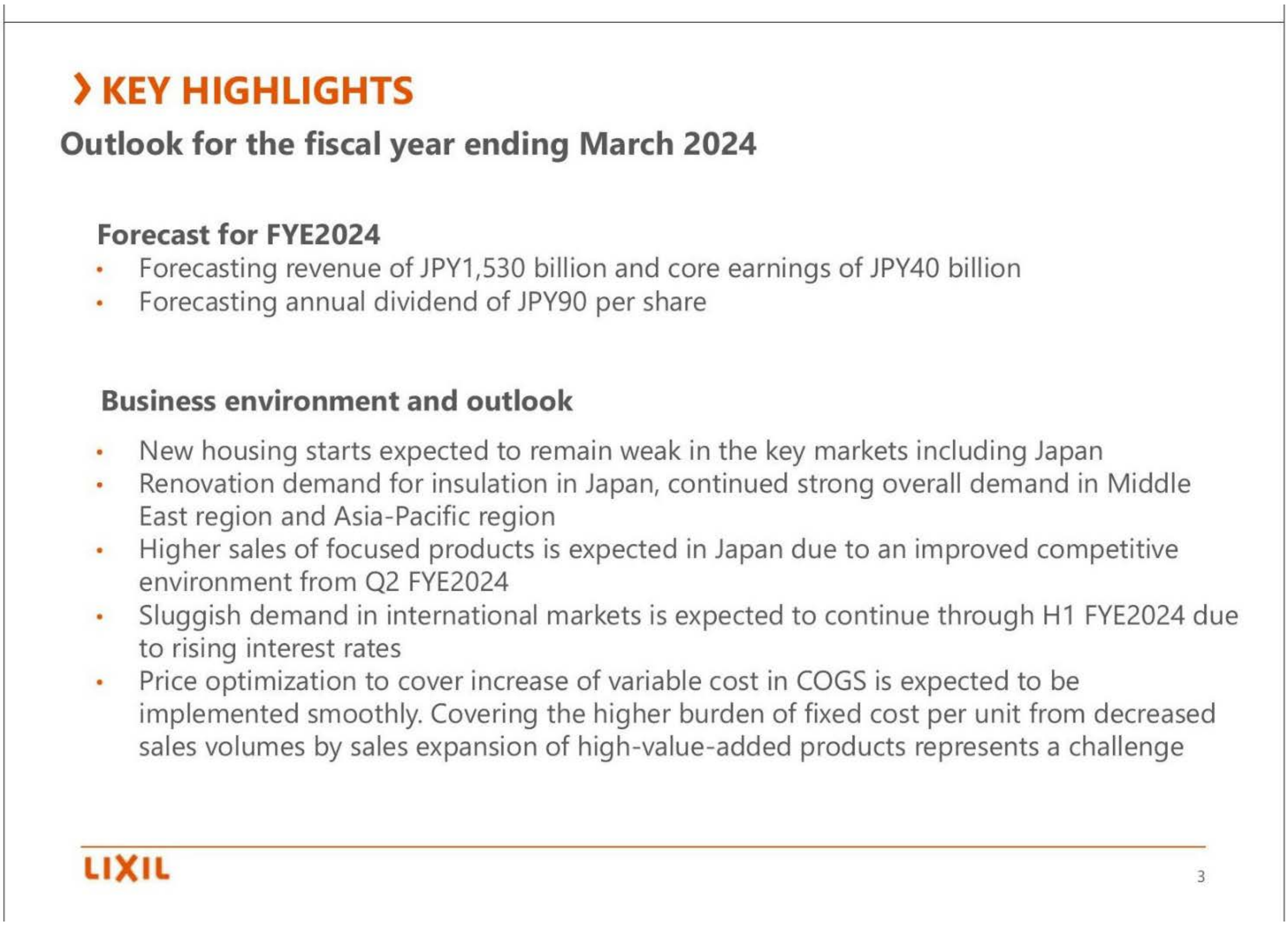
It says that revenue and profit increased with regard to the last quarter. I expected for a larger increase in both revenue and profits, especially in the last quarter. However, while the problem of cost increases, especially in raw materials, as I mentioned earlier, was resolved, the decrease in production volume itself caused fixed costs to rise. As such, profitability did not recover as much as expected, resulting in smaller increase in profits.

Since we are in the equipment industry, we inevitably have a high breakeven point, so a drop in production as a number of units would be very significant. Even if the sales itself increased due to price optimizations and the weak yen, if the quantity of each piece produced itself decreases, the impact of higher production costs per unit will inevitably have a negative impact on profitability.

On the other hand, the number of new housing starts, which was forecasted at an annual rate of less than 900,000 in January, dropped to 850,000 in February, and the decrease in the number of detached houses in particular was very severe. The demand for detached houses fell by 11% or more for the entire year, and the large decrease in new construction of detached houses, which is our main market, was a major factor in the slump in demand in Japan.

In the international markets, the demand for housing generally begins to decline about six months after interest rates rise, but last year, prices rose intermittently and interest rates rose, and the outlook for this year is for interest rates to rise to about 5% in total from January 2022. It is expected that the demand will probably recover at least from this May/June. Although the slump is not as severe as in Japan, I think it can be said that demand has been decreasing due to the impact of the interest rate hikes.

That said, in many ways regarding Q4, I think the biggest summary of the last three months is that the drop in demand, in any case, has reduced the scope of the increase in revenue and profit.



On the other hand, for the fiscal year ending March 31, 2024, we currently forecast sales revenue of JPY1,530 billion and core earnings of JPY40 billion. The annual dividend remains unchanged at JPY90 per share.

As for demand, we see it as weak, especially in the first six months. We think it's tough. We see this as particularly challenging with respect to Japan.

Another thing is that we have always responded to various cost increases by optimizing prices. LIXIL has been ahead of other companies in optimizing prices frequently, and of course, other companies are following suit, but between the speed at which they are following suit and the speed at which we alone are optimizing prices, orders tend to concentrate in the hands of other companies and our share of the market, especially in H1 of FYE2024, is expected to suffer.

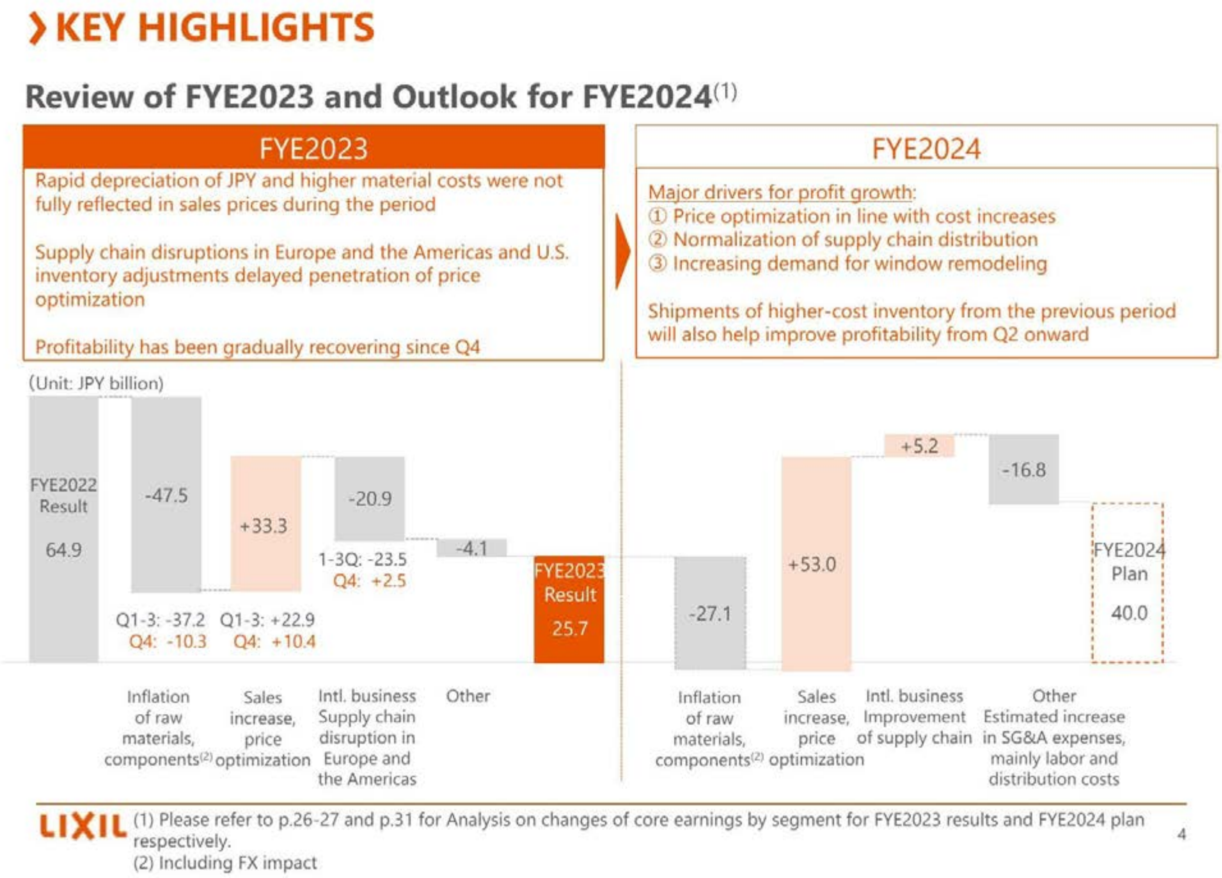
In many cases, the competitors, and we also have some of them, have deals where the old price is guaranteed for a while after the price increase, or the price increase is kept low for a few months after the price increase. During that period, some orders will shift to competitors, so for H1 in Japan, in addition to sluggish demand, we expect to face a bit of a struggle in terms of market share.

Finally, when we look at our business in the big picture, we are selling highly value-added and differentiated products, and we need to make structural reforms to some extent with respect to equipment for commodity products. In this sense, profits will be overwhelmingly bottom-heavy, and although we are currently forecasting JPY40 billion, we believe that more than 80% of the profits will be generated in H2.

We are in difficult times with sluggish demand, but I believe that it is during in tough times that we need to take such drastic measures.

On the other hand, I believe that the demand for thermal insulation and renovation will continue to grow in Japan, as exemplified by the recent subsidies for windows, and that demand for environmental products will also become a very important demand in the future.

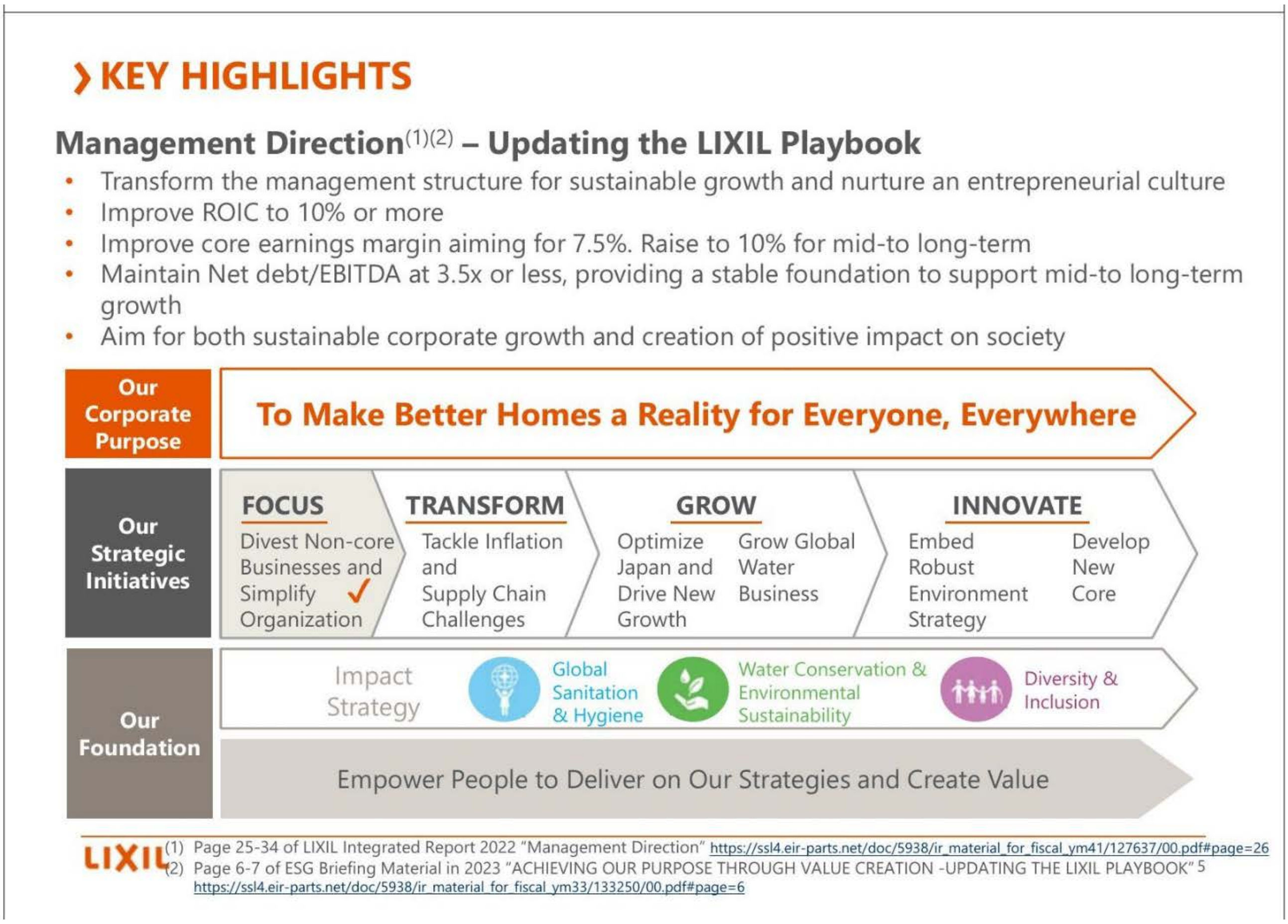
We have to continue the price optimization in such tough business environment, but the price optimization we did last year will be in full effect for this fiscal year, so I think that is a positive factor. We also intend to become a more resilient company by quickly eliminating the fixed cost burden for this reduced production volume, although the situation will continue to be difficult for some time.



This is a review from the last fiscal year to this fiscal year. It is a big change from the fiscal year ended March 31, 2022. As I mentioned earlier, one of the major factors was the time lag in passing on higher raw material, components, and logistics costs to customers. In addition, the supply chain disruption in the Americas and Europe had a further impact, resulting in a very disappointing result of core earnings of JPY25.7 billion.

We believe that the higher raw material costs will continue, but on the other hand, as I mentioned earlier, we believe that the price optimization will be effective for one year. In that sense, the positive effects in profit and the improvement of the supply chain will be effective, and we expect to achieve core earnings of JPY40 billion for now.

On the other hand, if we look at things from a longer perspective, as I mentioned earlier, we are in the equipment industry, so we have to work tirelessly to increase our profit margin. If enough profit is taken, the Company can respond to changes in demand to some extent. In this sense, improvement in sales gross profit is achievable by price optimization and enhancement of value of our products and services rather than improvement gross profit from production.



Then, the cost of the production facilities will be lowered. As I have explained many times in this Playbook, our strategy is to simplify our organization and focus on our core businesses without ceasing.

We are also considering a cycle in which we not only optimize our Japan business as a growth strategy, but also bring products that match the environment, which itself can promote the growth potential of our international business, which in turn leads to new innovations.

On the other hand, as a new requirement, we also have to deal with this inflation and supply chain issues that we have talked about many times. The following table is a brief overview of what we intend to do in the long term.

First of all, we have to deal with this inflation and supply chain challenge, but of course, we have to do many things. The easiest thing to do is to optimize prices, but the fluctuating parts are also quite important.

We consider brass as one of our two major raw materials, and aluminum as the other.

In this context, copper, the main component of brass, is a strategic commodity in the world, and its price volatility is much higher than that of other materials. It is the most volatile commodity, with large price ups and downs occurring, like semiconductors. We are thinking of converting this to plastic or zinc over the long term, which will not only lower the cost but also stabilize the cost.

On the other hand, aluminum itself is a relatively stable material, but we can add value by using aluminum scrap instead of bauxite as a raw material, in consideration of the environment, so that our customers can continue to buy our aluminum related products. In that sense, I think we can make the material more stable.

In terms of procurement, we try to keep the places where we make and sell products as close to each other as possible. For example, the US used to buy a great deal of goods from Asia, but we are now trying to make it possible to produce 80% or more of the goods in Mexico. Then, if it is in China, we will do what we can to make it complete within China. We will continue to change our procurement structure as much as possible.

Also, while we do not manufacture core components, we have factories in India and Saudi Arabia, for example, for knockdowns, where we can add value, and I think this will make it easier for us to apply supply chain issues.

Secondly, with regard to the Japan business, we are finally able to change prices in a flexible manner, and we are also digitizing our catalogs. I believe that platform-based production has made it possible to release more and more new products with a smaller investment. In addition, we have been able to make all of our products environmentally friendly, so I think we are adding value in this sense as well.

In terms of constant cost reduction through digitalization, we have finally reached the point where we can monetize the use of RPA and the introduction of no-code, and we are planning to increase productivity by introducing AI next.

Also, as for international markets, we will shift our focus to high value-added products. We will work to increase sales, especially in the shower and color fields, and at the same time, we will focus on breaking away from the commodity business, which has been exposed to great volatility. Basically, our strategy is to invest intensively in profitable areas and sell our products there.

This time, not only that, but I will also make a distinction regarding investment, saying that this business is a global business, and this business is a regional business.

We have the widest business scope in the water-related business, operating in 140 countries around the world, and that is our strength, but it is also our weakness in terms of efficiency, so we have to develop more of those global products to make this all our strength. I believe that in order to make all of this a strength, we need to develop more of those global products. I am going to push for this.

As for innovation, we have shift our challenges to the environment to the fullest. We, when it comes to environmental strategies, we have to reduce our carbon footprint, our CO_2 emissions, then preserve clean water and use it to improve the environment and circularity, recycling. With respect to all three of these areas, we are putting the investment to these areas considerably.

As for CO_2 reduction, perhaps our biggest contribution in Japan has been a major focus on window remodeling. The window remodeling is said to have the potential to reduce 14 million tons of CO_2 emissions, if all windows that do not meet environmental standards of FY2016 in Japan now, were made triple paned.

This is a figure that could be the largest contribution of all industrial sectors, and of course, the reduction of 6.6 million tons of CO_2 emissions, with priority given to detached houses, is a major business opportunity that must be addressed by the industry as a whole, not just by our company. I believe that it is important for us to provide appropriate products for this business opportunity.

On the other hand, to reduce CO_2 emissions, we are increasing the ratio of recycled aluminum gradually. This is currently at 70%, but we are aiming for 100% by 2031. In fact, for example, we are now receiving a great deal of demand for products that use 100% recycled aluminum. Our company, and Hydro in Norway, are the only companies in the world that can provide building materials using 100% recycled aluminum.

The current trend in the world is to look at reduction of CO_2 emissions not only in terms of operational carbon, which is used in everyday life, but also in terms of embodied carbon, which is used in production, and carbon in recycling, which is used in the lifetime of the product. I think this will attract a great deal of attention, such as our *PremiAL*, which is made from 100% aluminum scrap.

In terms of CO_2 reduction, aluminum accounts for a large portion in buildings. 30% or 40% of the world's CO_2 comes from construction, so I think there is a big contribution to be made there.

In terms of water conservation, it is not simply a matter of reducing the amount of water taken from factories, for example, or reducing the amount of water used for our own production, but also of creating an environment where blackwater is less likely to occur in order to supply clean water, for example. We have been trying to make sure that blackwater does not drip down and that everyone in the world has access to a toilet. In addition to this, we are currently working on a project to improve the wastewater itself that comes out of here.

We are also developing products, such as the *Everstream Shower*, which is basically a system for reusing heated water, and *KINUAMI U*, which reduces the amount of water and heat needed to heat the water by producing bubbles from the start. Showers are another major area.

Finally, when it comes to resource recycling, there is *Revia*, which can use all waste plastics, and *PremiAL*, the recycled aluminum product I mentioned earlier. I believe that this innovation itself will be one of the reasons for us to be able to earn high profit margins in the long run.

› PERFORMANCE HIGHLIGHTS

Revenue increased but profits decreased year-on-year

- **Revenue: JPY1,496.0 billion, up 5% year-on-year**
  - Q4 (3 months) YoY: +1% in Japan and +14% in international markets (+3.4% excluding foreign exchange impact)
  - Q4 (12 months) YoY: +1% in Japan and +12% in international markets (-0.1% excluding foreign exchange impact)
- **Core earnings: JPY25.7 billion, down by JPY39.1 billion year-on-year**
  - Q4 (3 months) YoY: -JPY0.6 billion in Japan, +JPY2.5 billion in international markets and –JPY0.3 billion for consolidation adjustment/other factors
  - Q4 (12 months) YoY: -JPY20.7 billion in Japan, -JPY20.9 billion in international markets and +JPY2.5 billion for consolidation adjustment/other factors
- **Profit for the year[1]: JPY16.0 billion, down JPY32.6 billion year-on-year**
  - Decreased primarily due to decrease in core earnings

LIXIL (1) Profit for the year = Profit for the year attributable to owners of the parent

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As for the highlights of the financial results, as I mentioned earlier, revenue of JPY1,496 billion is said to have increased by 5%, but this is basically due to foreign exchange rates and price increases and there was not such a large increase in the volume of products. Rather, it means that the number of products is decreasing. We believe that this is, to some extent, unavoidable given the current demand situation.

Regarding core earnings, as I mentioned earlier, we were not able to fully demonstrate our capabilities during the first nine months due to delays in responding to rising costs and during the last three months due to a decline in demand.

› FYE2023 CONSOLIDATED BUSINESS RESULTS

JPY billion	Q4 (12 months) FYE2022	Q4 (12 months) FYE2023	Q4 (12 months) Increase/decrease (YoY)	Q4 (12 months) %	Q4 (3 months) FYE2023	Q4 (3 months) Increase/decrease (YoY)	Q4 (3 months) %
Revenue	1,428.6	**1,496.0**	+67.4	+4.7%	**372.2**	+18.0	+5.1%
Gross profit	486.9	**468.6**	-18.2	-3.7%	**116.2**	+2.7	+2.4%
(%)	34.1%	**31.3%**	-2.8pp	-	**31.2%**	-0.8pp	-
SG&A	422.0	**442.9**	+20.9	+4.9%	**111.4**	+1.1	+1.0%
Core earnings (CE)(1)	64.9	**25.7**	-39.1	-60.3%	**4.7**	+1.6	+52.0%
(%)	4.5%	**1.7%**	-2.8pp	-	**1.3%**	+0.4pp	-
Profit for the year including Discontinued Operations(2)	48.6	**16.0**	-32.6	-67.1%	**5.0**	-2.1	-30.0%
EPS (JPY)	167.21	**55.54**	-111.67	-66.8%	**17.32**	-7.11	-29.1%
EBITDA(3)	145.6	**107.6**	-38.0	-26.1%	**25.1**	+1.7	+7.1%
(%)	10.2%	**7.2%**	-3.0pp	-	**6.7%**	+0.1pp	-

- **CE margin:** Declined by 2.8pp YoY (Improved by 0.4pp YoY for Q4 (3 months))
- **Gross profit margin:** Declined by 2.8pp YoY (Declined by 0.8pp YoY for Q4 (3 months))
- **SG&A expenses:** Increased by JPY20.9 billion YoY (Japan JPY0.2 billion increase, International JPY6.7 billion increase, forex effect JPY14.0 billion increase) mainly due to expanded sales activities and higher logistics costs. SG&A ratio remained at the same level as the previous year.

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

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In Q4, the ratio of building business to consolidated net sales increases, which normally results in a slight decline in profits. Essentially, these three months of the fiscal year ended March 31, 2023 can show a significant effect of the lower cost of goods. Therefore, I was hoping for better results. However, I was a little disappointed with the results.

› FYE2023 BUSINESS RESULTS BY SEGMENT

Revenue increased in all businesses, core earnings fell year-on-year from JPY depreciation and continued high component costs. LHT turned profitable in Q4 (3 months) due to price optimization.

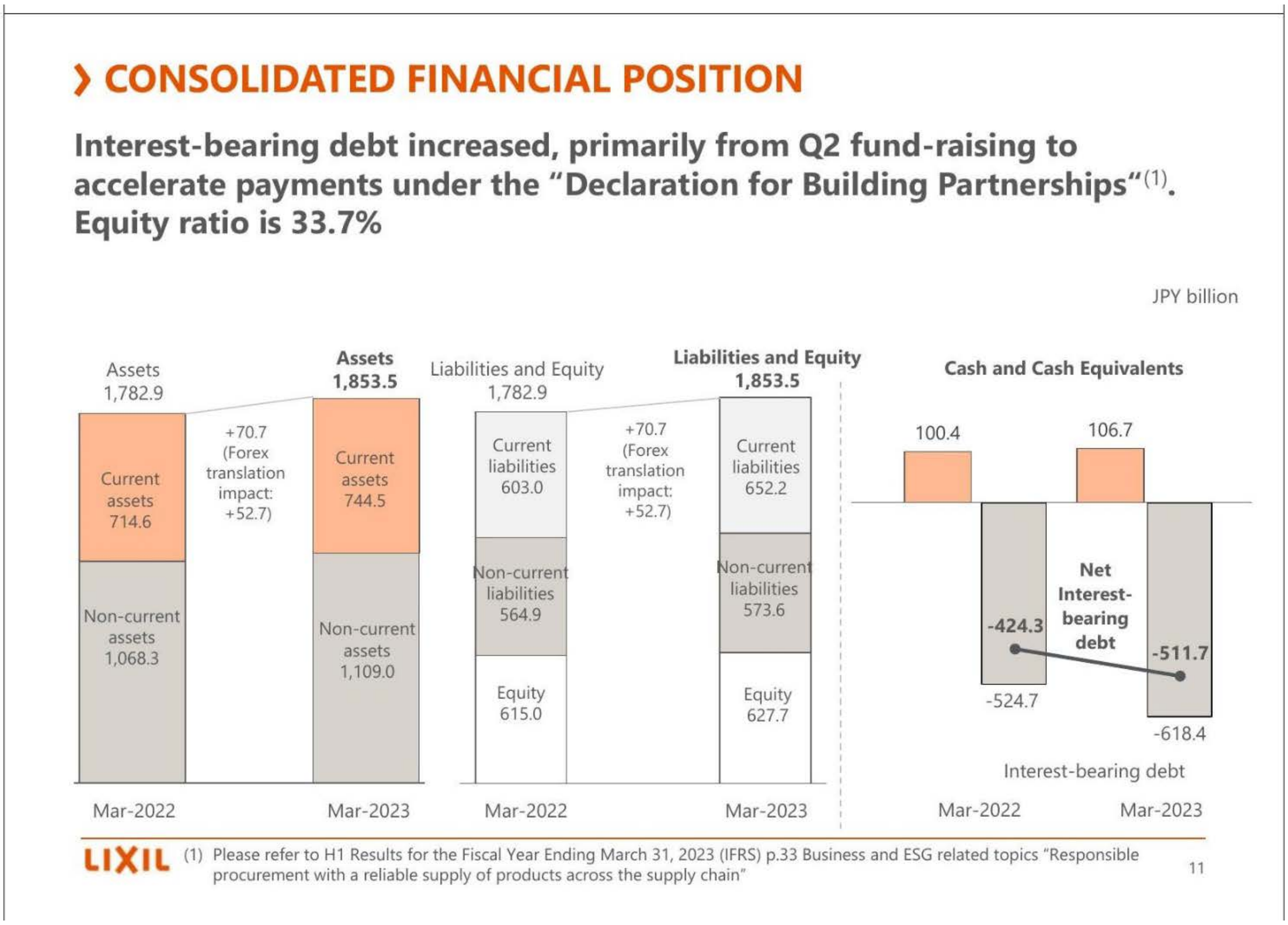
New reporting segments	JPY billion	Q4 (12 months) FYE2022 [1]	Q4 (12 months) FYE2023	Q4 (12 months) Increase/decrease (YoY)	due to segment change [2]	excluding segment change	Q4 (3 months) FYE2023	Q4 (3 months) Increase/decrease (YoY)	due to segment change [2]	excluding segment change
LWT	Revenue	862.2	**915.3**	+53.1			**232.1**	+17.1		
	CE	76.6	**47.3**	-29.4			**11.2**	-0.9		
LHT	Revenue	584.2	**598.2**	+14.0	+4.3	+9.7	**143.9**	+1.1	-0.5	+1.6
	CE	31.7	**19.4**	-12.3	+1.2	-13.5	**3.9**	+2.8	+0.1	+2.6
Consolidation, adj. & other	Revenue	-17.8	**-17.5**	+0.3	-1.2	+1.4	**-3.8**	-0.2	-0.4	+0.2
	CE	-43.4	**-40.9**	+2.5	+0.1	+2.5	**-10.4**	-0.3	0.0	-0.3
LIXIL	Revenue	1,428.6	**1,496.0**	+67.4			**372.2**	+18.0		
	CE	64.9	**25.7**	-39.1			**4.7**	+1.6		

Forex impact[3] Q4 12 months: Revenue +JPY56.8 billion, CE +JPY4.9 billion
Q4 3 months: Revenue +JPY12.3 billion, CE +JPY0.5 billion

LIXIL (1) Please refer to "Notice Regarding Change in Reporting Segments" disclosed on July 29, 2022 for full-year and quarterly results for FYE2022 in the new reporting segments (2) Includes consolidation adjustments added by the change of reporting segments (3) Forex translation effect gain(loss) from international subsidiaries 9

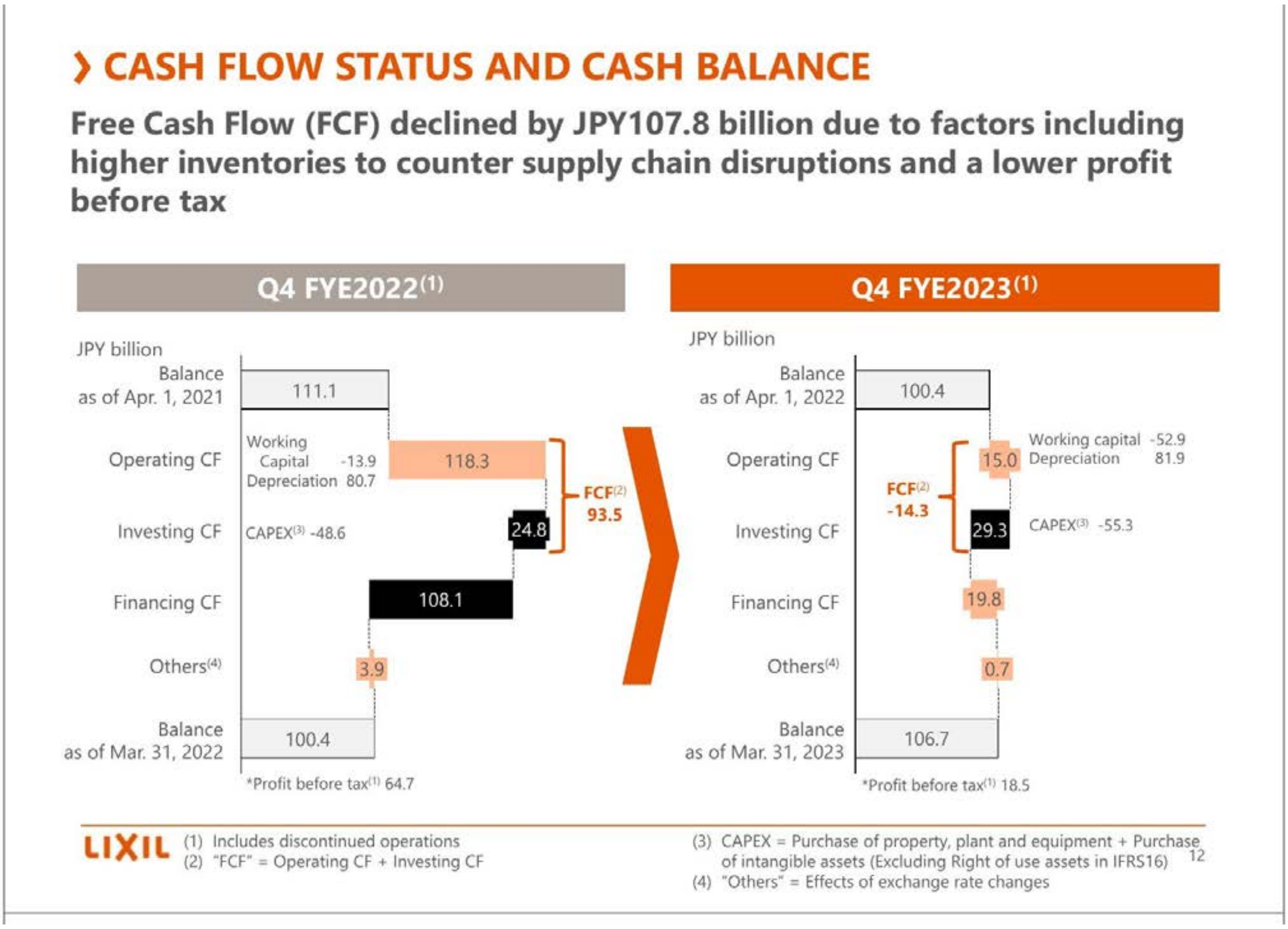
In terms of segments, LHT is finally recovering from the negative impact of the weaker JPY in H1 of the fiscal year and is showing positive YoY growth in Q4. The major source of profit here is the exterior business. With regard to the exterior business, our competitors are finally going to raise their prices this April, and if this penetrates, we will be able to regain market share. We see an opportunity to increase profits here significantly.

On the other hand, in the area of water-related products, the situation continues to be very difficult due to price increases by suppliers in the low-margin kitchen and bathroom business in Japan, although for international business, the focus is on faucets.



Unfortunately, although our policy has always been to focus on assets in a more efficient manner, it was necessary to increase our inventory due to various factors, including foreign exchange rates and COVID-19 pandemic this time.

Then, as it says here, accelerate payments under the declaration for building partnerships. This is a request from the government, so unfortunately, due in part to this, we have taken a step back in terms of interest-bearing debt and equity ratio in the current fiscal year. I would like to repay this by the earnings from the next fiscal year onward.



The same applies to cash flow, which has shown signs of improvement, albeit slight, since this quarter, and I would like to further stabilize the Company by making steady improvements here.

Since there are more details and contents to follow in the pages that follow, and since we would like to have enough time for questions, I will end my explanation here.

Question & Answer

Moderator [Q]: Okay, we will now have time for questions and answers.

Now, let me introduce your first question. We have received two from Ms. Okada, Goldman Sachs Securities.

First, I believe that you have been implementing business structure reforms, but it has been difficult to see the effects of these reforms due to recent increases in component prices and logistics costs. How effective has this been in the current margin?

Seto [A]: I believe that Q1 of FYE2022 was the last period before these component price increases and logistics stoppages, and the core earnings margin rose to 6.7% at that time. Since this is Q1, historically the quarter with the lowest profit and the lowest revenue, we would have been able to generate a margin of 7% or more if nothing had happened.

However, I think we have solved the problems that Ms. Okada mentioned here, such as the rise in component prices and logistics costs. In reality, the fixed costs have risen due to insufficient demand for our current capacity. This Q4, and then the first six months of the current term, especially the first three months of the current term, are probably difficult to see with regard to that. We need to promote further structural reforms here, including some things that we have not been able to do very well during the COVID-19 pandemic.

Moderator [Q]: Now, let me introduce you the second question. The core earnings margin of LWT international business was 4.5% in FYE2023, while GROHE landed at 11%. What is the cause of this difference? Also, what is your view of GROHE's core earnings margin for the fiscal year ending March 2024?

Seto [A]: LWT's international business is largely GROHE's faucet business and American Standard. American Standard sells both so-called sanitaryware and faucets. Faucets are a very profitable business, and that is why we have decided to focus our portfolio on faucets, and we intend to increase the number of faucets in the future.

On the other hand, American Standard's business in sanitaryware, especially for retail, has very low profit margins. This is because there is some competition with retail private brands.

As for these products, and as I indicated earlier in the Playbook, as for products that are highly commoditized and have low profit margins, to some extent, we are going to withdraw from them while trying to increase and improve the business where customers properly recognize the value and give us the price and margin. Answering to your question on what this difference is, is the difference in product mix. GROHE business mainly sells faucets, and as a whole business, sanitaryware with low profit margins other than faucets are included.

In fact, this is also true for the Japan business, and it is often said that LIXIL's Japan business is not as successful as TOTO's. This is also influenced by the composition of the product lineup. In Japan, on the contrary, the profit margin for sanitaryware and toilet seats is high, while the profit margin for kitchens and bathrooms is usually low. The profit margin for the Company which has large sales of kitchens and bathrooms is low overall, but conversely, the Company has a high profit margin in Japan for sanitaryware and faucet fixtures.

In a sense, improving this product mix is one of our major strategies. The profit margin of GROHE for the fiscal year ending March 31, 2024 has two basic components. One is the change in materials, such as the change from brass to zinc that I mentioned earlier, which will increase the profit margin.

Then there is also this mix in the faucets. The flushing fittings, which are called flushing, the shower, and faucet, we have such faucet fixtures, but now, the demand for the faucet is slightly decreasing and the demand for the flushing is increasing. The profit margin for flushing is lower than the other two. On the other hand, the profit margin of showers is higher, so it is hard to say since it depends on whether sales of these showers will increase. We are basically looking at similar lines as for the final landing spot.

Moderator [Q]: Next, we received two questions from Mr. Fukushima from Nomura Securities.

The first. To what extent are sales and profits from window renovations factored into your plan for the fiscal year ending March 31, 2024?

Seto [A]: Regarding window renovations as a whole, sales are normally between JPY20 billion and JPY30 billion per year now, in a typical year. In the case of this year, we are looking at quite a large amount of money because of the subsidies coming in.

The size of the subsidy is JPY100 billion, but the subsidy rate ranges from 33% to about 50%, so we figure 40%, and the overall subsidy range for window renovations can be calculated as approximately JPY250 billion.

The ratio differs depending on what the product is, for example, interior or exterior windows, but if we assume half the price of construction and half the price of the specified product, our share as an industry is JPY125 billion. Of this, we have about 40% market share, so JPY50 billion. We believe this is about the size of our window renovation sales for this fiscal year.

As for profits, relatively high profit margins are available for the regarding window products. We will probably know a lot more about this exact number in about two months. As I have mentioned many times before, the profit margin varies greatly depending on the combination of windows, from high to low compared to standard sashes. I think what will happen in this area is something we will talk about again going forward.

On the other hand, there was talk that we may not be able to use up the JPY100 billion, but we are already receiving orders that are seven or eight times larger compared to the past, and we are having difficulty responding to them. I think there is a good chance that we will run out of the current subsidy, at least by the fall.

Moderator [Q]: Second question from Mr. Fukushima, Nomura Securities. Following the fiscal year ended March 2023, the fiscal year ending March 2024 will have the so-called "bogus dividend" and DPS exceeding EPS. What do you consider an appropriate dividend payout ratio? What is your medium- to long-term target dividend for final profit? Why did you not consider reducing the dividend this time?

Seto [A]: First of all, for us, we see a minimum dividend payout ratio of 30%. However, I would like to consider not only the dividend payout ratio but also DOE and many other things.

The main thing about dividends is that most individual investors expect that if it is this amount, it will be stable for a long time. I think it is a balance between the conviction that we will restore profits and the cash flow situation we have at the moment, rather than the final profit, which is more about cash flow and EBITDA as a whole.

In terms of EBITDA, even though the current fiscal year has not been very good, we have higher EBITDA than our peers, so in that sense, we should not think of lowering the dividend payout ratio just because we had a bad year or two.

As for the medium- to long-term target for final profit, we are considering this based on core earnings, and since we think the core earnings margin of approximately 10%, we think it would be reasonable to subtract from this figure.

Moderator [Q]: Next, we have a question from Mr. Kuwana, Mizuho Securities.

Regarding the growth strategy for international operations, particularly in North America, we recognize that the past three or four years have been a very difficult business environment against the backdrop of special factors, such as the COVID-19 pandemic, but the speed of profit growth in North America seems somewhat sluggish.

Please let us know what you think about your future growth strategy. Especially in North America, in light of the acquisition of Basco last December, please share with us your thoughts on organic growth and growth through M&A.

Seto [A]: I think the most important point is that we need to grow profitably, and in terms of North America, sanitaryware accounts for a large percentage of our sales. As I mentioned earlier, our sanitaryware business is focused on retail customers, and we sell products that compete with their retail customers and in some cases, their store brands.

When these products are destocked to a certain extent, depending on the store brand's sales, for example, if the overall demand for a product is low, the retailer will naturally prioritize its own brand, and orders for our brand will drop dramatically. This is what happened last summer and fall, and I think it is important to shift to a more profitable business, because those things, in total, make for a very low-margin business.

In that, we have two major pillars, one of which we call showering. I think it will be important to have a strategy to sell that product for the entire shower room, not just the shower.

Part of this was the acquisition of Basco. Basco mainly makes shower doors among showers. As a matter of fact, what is the first thing to buy or choose among shower room overall with regard to showers varies from country to country or region to region. In North America, this is considered to be centered on shower doors. Given that in some countries, the shower itself, and in some cases, the shower of the concealed shower (showers with valves and pipework hidden inside the wall) itself, is the choice, it was very important to bring Basco as the growth of showering in Americas.

On the other hand, as for shower products, we obviously have products that are not available in the international markets, such as *KINUAMI U*, which was developed in Japan, and *Body Hug Shower*. If people choose shower rooms, then we will have more products to sell, and showering is one of our pillars.

The other is to invest in Mexico, where we have been very weak in the high-margin faucet business, especially in the color strategy, to supply faucets with different colors with a very speedy supply chain. We are trying to expand here by selling colored faucets in the Americas' market. Therefore, at the rate of profit growth in North America, what we are trying to do is to change the content of our business.

Moderator [Q]: Next, we have a question from Mr. Kawashima from SMBC Nikko Securities.

First, please explain American Standard's goodwill impairment risk.

Seto [A]: This time, the risk of goodwill impairment has remained reasonably high due to the fact that interest rates have risen in the US and around the world. However, since last October, we have seen a significant decrease in inventory and signs of improvement in profit margins, so we do not think there is any risk here.

Moderator [Q]: Then the second one. How do you assess the impact of the price increase on demand and market share?

Seto [A]: I think this is a very difficult question. This is, of course, true that if only our company raises prices, we will lose out against the competition, which will affect our market share.

In the case of our business, considering that it is an equipment industry, especially for kitchens and bathrooms, raising prices will affect not only our market share, since there are several competitors other than TOTO, but also production gross margins will surely decrease.

However, on the other hand, given that demand for both kitchens and bathrooms will decline over the long term in line with the number of new housing starts, we may end up in a death spiral if we make no effort to increase profit margins by not raising prices and only protect production gross margins.

From that point of view, in a sense, even if there is a temporary impact on market share, other companies are ultimately following. The market share or the impact on gross profit during such a time lag will be negative for us in the short term, but in the long term, we are doing what we have to do. I think this is generally true for products in Japan.

However, this is a short-term discussion, and when considering what will happen in the long term, it is more important to create products for which demand and market share will not decline even if prices are raised. Therefore, we believe it is important to create products that are environmentally friendly and that provide benefits to our customers.

Moderator [Q]: Next, we have a question from Mr. Mochizuki, CLSA Securities.

He has a question for Mr. Matsumoto, CFO. Considering the fact that no earnings revisions were made in Q1 and Q3 and that the earnings revisions were very large, it seems that information on business operations did not reach management in a timely manner. Frankly, it looks like you are having problems with execution. Where do you see the challenges for execution as a business management issue? It would be helpful if you could speak to us in terms of shipping, cost control, and procurement. What are the challenges you face and how do you need to address them?

Matsumoto [A]: Thank you for pointing that out. As you say, we should reflect on the fact that we were unable to revise our performance in a timely and appropriate manner. On the other hand, we do not believe that this is the case if information from the field is not reaching management. We try to collect on-site information on a monthly or weekly basis, and we also conduct various reviews in a timely and appropriate manner.

However, we believe that continued improvement of accuracy in forecasting performance is necessary. It is difficult to reflect cost increases and exchange rate fluctuations in the balance sheet and the P&L in a timely and appropriate manner, as is usual in the manufacturing and equipment industries. However, we believe there is still room for improvement in terms of how we can improve the accuracy of this.

In other words, when you buy raw materials, they arrive at the port, you produce them, they get on the balance sheet, and when they are sold, the cost is recorded as a P&L. The manufacturing industry has a long cycle. If the longer length is a given, we would like to make further improvements in this point to increase accuracy.

Seto [A]: If I may add something, one of the differences between us and other companies is that we, very unfortunately, have a lower profit margin than other companies to begin with. Low-margin sanitaryware sales in the international businesses are a large portion. In Japan, sales of low-margin products, such as bathrooms, kitchens, and sashes account for a higher percentage of total sales than other companies.

If there are many products with low profit margins, the natural conclusion is that sales are large and profits are small, but then this is the equipment industry, so a small change in production volume will change profits in a blink of an eye. In short, the Company's first problem is that the breakeven point is too high and therefore the range of volatility is large when compared to other companies.

Secondly, as I mentioned earlier, we are doing business globally, in 140 countries, and I believe that the global supply chain is vulnerable to problems. I think that because we are doing business globally, the supply chain is long and problems can occur.

Regarding the first point, obviously we think that we can prevent volatility in the long run by changing to a more profitable product for us. As for the second point, we are going regional this time, which will also prevent some volatility there.

And lastly, we have been talking on the core earnings basis, but in terms of the volatility of the final profit, we are still a very large company and there are still many areas that need to be narrowed down. When narrowing it down, there are various ways to do this, such as selling the company or integrating companies. In this case, the timeline is very difficult to read and predict. The fact that it is difficult to predict is also an excuse, but there is also a structure that the outlook more likely to shift below the core earnings.

We are doing our best as a company, but the structure of the Company makes it very difficult to read profits, and I repeat, one of the reasons is that profits are low and the breakeven point is high, so one factor can make a big difference. If a company with a profit margin of 15% changes by 5%, the change is 10%, but if a company with a profit margin of 5% changes by 5%, it becomes zero. The first difference is that if 15% were 10%, it would be a 33% difference, but if 5% were zero, it would be a 100% difference.

The second difference is that the longer the supply chain is, the more likely it is to be hit by an impact from spread of COVID-19 or supply chain issues like this one.

And finally, if the company was formed through the merger of various companies and rationalization is underway there, the timeline may not be well read. Third, we obviously see this as a problem for our management team.

Moderator [Q]: Next, we have two questions from Mr. Takegawa from Sumitomo Mitsui Trust Asset Management.

The first is since the return of President Seto, the external environment has changed rapidly, and I think it has been difficult to announce the new medium-term management plan. I think it's about time you issued a new medium-term plan that includes the outlook, strategy, and cash flow allocation for the future.

Seto [A]: It's true that the situation didn't come as easily as I had hoped it would when I settled down, so I will fully consider the advice you are giving me.

Moderator [Q]: This is the second question. What changes in consumer behavior have you observed since the price increase? What are the trends for such as declining demand for nonessential remodeling, both in Japan and international markets?

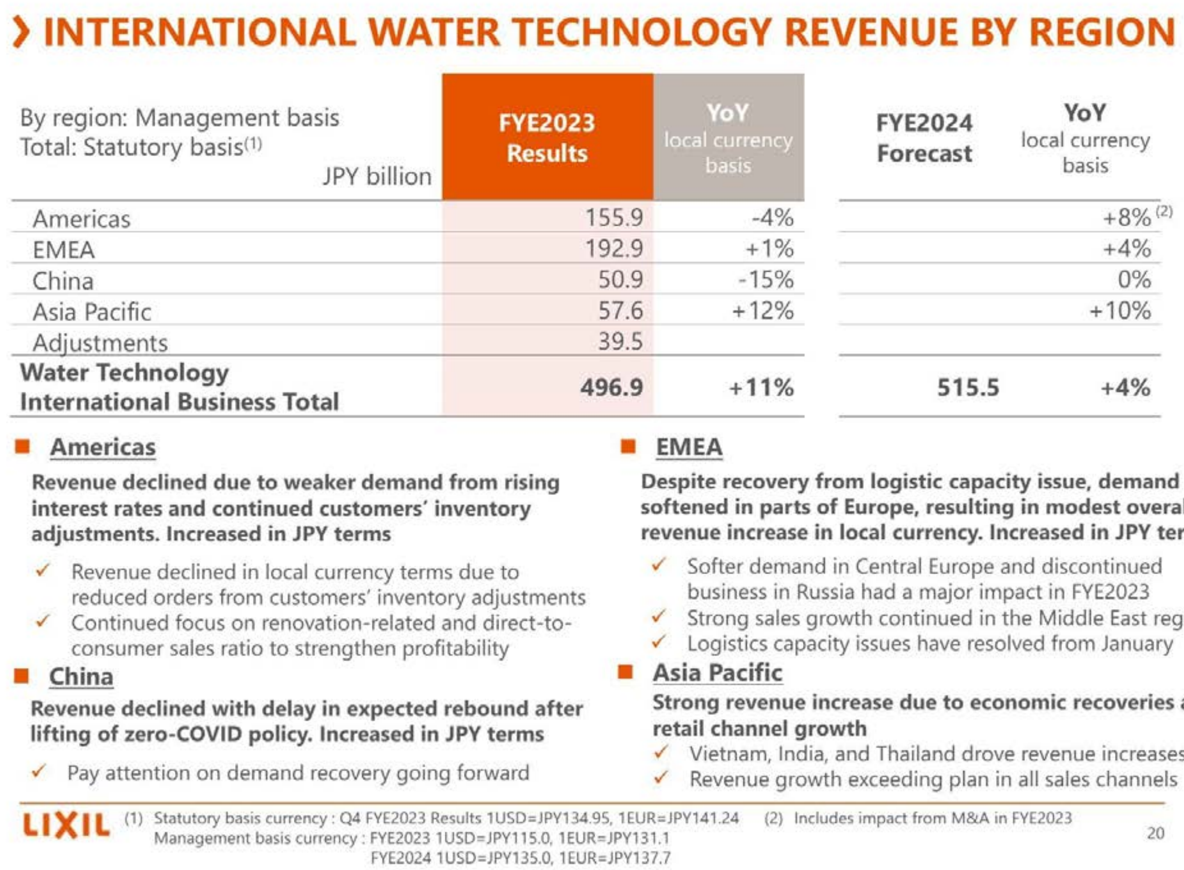
Seto [A]: Clearly, the biggest phenomenon that is happening in Japan is that the demand for low-cost housing, local construction companies, is decreasing, and the demand for new houses is decreasing. This has happened as a result of price increases for various products, which has made it difficult to sell low-priced houses at a low price per area price.

As a result of this, there has been a concentration of market share in the major companies, an increase in the percentage of high-efficiency houses, and an increase in the number of apartments and housing complexes. In addition, there is an increasing demand for heat insulation improvement work for remodeling instead of new construction.

In Japan, the positive part for us is that new construction is changing to remodeling. The negative impact is that the demand for small- and medium-sized local installers, our strongest customers, has been decreasing.

On the other hand, international countries have so far not seen much of a major drop in demand as a result of the price increases. The background of this is that it is mainly remodeling for international markets. Mainly, in the case of remodeling, it is when a faucet or something breaks or goes bad, so there is not much loss of demand for this unless the prices of other companies are lower. Basically, what has happened over the past two years or so is that commodity prices have risen very significantly, and all companies have raised product prices, so there have been no major problems there.

Our biggest disappointment in international competition was, as I mentioned at the beginning, that we stumbled in the supply chain, and I think it was our mistake in not responding adequately when demand was strong in H1 of last year.



Moderator [Q]: Next, we have a question from Mr. Miki, Citigroup Global Markets.

Financial results page, page 20. You are forecasting an 8% increase in sales in Americas this fiscal year in local currency terms. Excluding M&A effects, how much growth do you expect? I believe our competitors in the US are looking at a top line forecast of around 10% decline in 2023, but do you have any growth drivers unique to LIXIL?

Seto [A]: I would say about 5% of the 8% increase in revenue is due to M&A, so we are looking at about 3% excluding impact from M&A. Conversely, LIXIL was impacted by , distribution issues, the supply chain was clogged up and products cannot be delivered, and then destocking by our customers in FYE2023. As a result, revenue continued to land at lower level than it should have been for about six months, so we expect that the revenue will increase for this fiscal year.

However, in terms of LIXIL's own growth drivers, the purchase of Basco, as I mentioned earlier, has created the first entry point for showers, which should lead to sales of shower products, and the establishment of a factory in Mexico to color faucets has allowed us to compete with other companies in areas where we had been losing out because our supply chain was a little too long.

Moderator [Q]: Next, we have two questions from Alma Capital Mr. Grew.

The first is please explain the details of the change in the forecast for the consolidated adjustment of core earnings, from JPY40 billion in the past few years to JPY46 billion.

Matsumoto [A]: Thank you for your question. We have included this in the consolidated adjustments section, considering that there are more risks than we are looking at in each business, for example, risks such as subcontracting laws. Also, as Mr. Seto mentioned earlier, in terms of structural reform, as it relates to the question that follows, we are making an allowance for expenses incurred here.

Seto [A]: The current relationship with the Act against Delay in Payment of Subcontract Proceeds, Etc. to Subcontractors is that in Japan, now we are receiving request from the Japanese government, which is taking the lead, to improve the business situation for small companies.

On the other hand, we are not sure if we are able to transfer all of that, but we were still told to actively accept the requests for price increases from smaller suppliers first. For example, we have been told to actively accept subcontracts that have increased their labor or raw material costs, so in that sense, we are willing to cooperate with them for where we need to.

Moderator [Q]: Second question. What is the breakdown of the difference between the forecast for core earnings and operating profit, JPY12 billion?

Matsumoto [A]: We have received a similar question from another person after this. I would like to answer these two questions at the same time. The question is the reason for the increase in difference between core earnings and operating profit between last year and this year.

First of all, last year, we sold some of our assets in the international business, which resulted in a onetime gain. Also, as related to my previous answer, the items that are recognized as other income expenses rather than expenses in the restructuring are included between core earnings and operating profit.

I have answered similar questions all together.

Moderator [Q]: Next, we have two questions from Mr. Yagi of Mitsubishi UFJ Morgan Stanley Securities.

The first. What is your views on American Standard's profit for the fiscal year ending March 31, 2024?

Seto [A]: It is difficult to answer this question since we do not disclose this information, but in the fiscal year ended March 31, 2023, ASB incurred very high warehouse costs due to the logistics issues mentioned earlier, for example, and we were also unable to generate sufficient sales due to restocking. In the current fiscal year, the first thing to do is to come back to that number. We are also thinking of increasing the number of showerings around Basco and other efforts regarding the faucet business.

Moderator [Q]: Second. Please tell me what will affect the negative LWT and LHT in the material price for FYE2024 in the factor for change in core earnings.

Seto [A]: The basic idea is that the price increases during the last year will be in effect for one year this time. The biggest factor is that what did not come into effect for a full year during the last fiscal year works for a full year in this term.

Also, as Mr. Matsumoto mentioned earlier, price hikes from subcontractors, as well as those related to parts and other items, are to some extent wider and higher than in previous years.

Moderator [Q]: Silq Capital, Mr. Soda asked a question, but as Mr. Matsumoto explained earlier, it was the difference between core earnings and operating profit, so I will skip this one.

Matsumoto [A]: One more point, sorry. There was one that I did not fully answer earlier. The difference from operating income to net income, one of the major factors here, is the tax. The tax rate for the fiscal year that ended was low, as you can see.

Please refer to the note on page 17 of the disclosed financial statements (page 19 of the Flash Report in English).

The reason for the taxes and the expenses low in the period in which ended, was the tax effect portion of losses recognized in the past, which, in the past, could not be recognized. In other words, the tax return on the loss could not be recognized at that time, but now that it can be recognized, it was recorded as a tax return in the fiscal year ended March 31, 2023, which means that the tax rate was transitory and low.

Moderator [M]: We have answered all the questions we have received so far.

Since the above questions have been answered, 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, 2023. We look forward to your continued support of LIXIL. Thank you very much.

[END]

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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