SHIKOKU CHEMICALS CORPORATION Q&A Session on Results Briefing for the Fiscal Year ending March 2022
(May 10, 2022)

Q1: This concerns the transition to a holding company structure. What would you like to realize specifically once the company has a holding company structure?

A: The company holds Corporate Strategy Meeting twice a month. However, when we have detailed discussions of the chemicals and housing materials businesses, it is difficult for all executives to grasp everything about the two business areas and make quick decisions. Furthermore, the balance between the chemicals and housing materials businesses, which has a sales ratio of 1:1 until now, has eroded and has roughly doubled recently to about 2:1. It has become difficult to manage those businesses as one company, given their business forms and significantly different profitability. Based on the above, we decided to transfer a certain degree of authority to each business and transition to a holding company structure so that they can make speedy management decisions in line with their business characteristics.

Q2: Please tell us the outlook for capital investment and depreciation expenses. In addition, I would like to ask about the future business contributions of the production facilities for fine chemicals and chlorinated isocyanurates, which were explained as active investments.

A: We made successive capital investments in a multiple fine chemicals plant (TAP-4；Tokushima Advanced Chemicals Plant-4) , and a facility for chlorinated isocyanurates. The company's depreciation is calculated using the constant rate method over an eight-year durable life (depreciation rate of 25%). The production facility for chlorinated isocyanurates, which was built with an investment of 5 billion yen, is scheduled to start operations in July this year. The depreciation expenses for the six months to the end of December 2022 are forecast at about 600 million yen. Moreover, the depreciation expenses for TAP-4, which was built with an investment of 2.5 billion yen and started operations in July 2021, are forecast at about 300 million yen.

With regard to TAP-4's contribution to the business, resist membranes, antireflective coating, underlayer membranes, and other special organic compounds are used in semiconductors, whose miniaturization is advancing. These are known collectively as semiconductor process materials, and TAP-4 is being used as a production facility that can implement everything from trial production to mass production of the chemicals used in them. This will enable us to enter the semiconductor process materials market. We have set a sales target of 2 to 3 billion yen for this semiconductor process materials sector in our long-term vision and are aiming to develop it as a pillar of the fine chemicals

business.

The production facility for chlorinated isocyanurates is one of the facilities for the realization of a “deliver cleanliness to people across the globe by protecting the environment and ensuring sanitation,” which is the goal of our organic chemicals business. We will supply products to the world per customer needs. From now on, we will aim to achieve a sales target of 20 billion yen in the organic chemicals business while looking at the further expansion of facilities, the establishment of overseas bases, and M&A.

Q3: How significant are the impacts due to the soaring price of crude oil and disruption in logistics on the fiscal year 2021 results and fiscal year 2022 outlook?

A: With regard to the increase in costs, raw material costs in the fiscal year 2021 increased by a total of 3 billion yen compared to the previous term, 800 million yen for chemical products, 700 million yen for housing materials, and 1.5 billion yen for logistics costs.
Concerning the impact of raw material prices, naphtha, methane gas, the oil used for insoluble sulfur, etc., can be raised as the price increases derived from crude oil, which mainly affects the chemicals business. The cost of raw materials in the chemical business in the fiscal year 2021 increased by about 800 million yen compared to the previous term.
In the housing materials business, the soaring price of aluminum ingots is having an impact. The LME price at its highest point last year was 3,300 dollars a ton, but there were times when it came close to 5,000 dollars a ton temporarily because of the impact of Russia’s invasion of Ukraine. At present, the cost is trending between 3,000 and 3,500 dollars a ton, so it has reached a high level compared to last year. Costs increased by about 700 million yen compared to the previous term.

Logistics costs increased by about 1.5 billion yen compared to the previous term in the fiscal year 2021, particularly because of the soaring price of transportation to North America and the occurrence of warehouse costs in preparation for logistics disruption. In particular, transportation costs for exports to North America have been affected. Shipments to North America are often of chlorinated isocyanurates, but when you compare marine shipping costs (for 20-foot containers) with pre-Covid-19 costs, there were cases where bids of ten times the price were offered because it is so difficult to secure shipping space owing to the impact of global economic recovery. In this situation, the company strived to secure profitability by price pass-through.
Although the US economy is on a recovery trend, the chlorinated isocyanurates market has been increasing prices significantly. The business forecast for the fiscal year ending December 2022 may give the impression that profit has not increased compared to the growth in sales, but this was to avoid misleading people by assuming uncertain matters while we are in such unstable

circumstances.
As for housing materials, while raw material costs are soaring, the forecast for the term ending December 2022 is for increased profits compared to the previous year. This is based on the fact that we set out price increases of 10% with the revision of the catalog from April 1 this year, but if the soaring price of aluminum goes even further up, it will affect profits.

Q4: Exchange rates, inflation, and other aspects of the business environment have changed, but has the company established a standard for changing the assumptions of the long-term plan? For example, are you considering accelerating capital investment if the yen weakens?

A: If the yen weakens by one yen against the assumed exchange rate, sales will increase by 130 million yen and profits will increase by 65 million yen. In this year's budget, the exchange rates are 120 yen to the dollar and 130 yen to the euro, but these are settings that anticipate safety. As for whether the timing of investment can be accelerated if the yen weakens, we are currently making capital investments at considerable speed. During the Challenge 1000 period, we are planning to invest approximately 50 billion yen (including M&A, not just equipment), and we are already considering our next investment. I cannot talk about M&A specifically, but we are considering whether we can pursue M&A in Japan and the US at all times.

Q5: Which raw materials require attention, and what is the future outlook?

A: Sulfur can be raised. Carbon disulfide was the company's founding business, and, at that time, sulfur, a raw material, was collected in the mountains. However, we now use sulfur (molten sulfur) generated as an impurity when refining oil. Charcoal was formerly used as the carbon source, but we currently use methane gas left over when refining oil. The price of molten sulfur is currently close to 500 dollars a ton in the Asian market. Apart from being used in the production of carbon disulfide and insoluble sulfur, sulfur is used in the production of sulfuric acid. When reacted further with potassium, sulfuric acid forms potassium sulfate, which is used in agricultural fertilizers.
In Asia, demand for agricultural applications is increasing because of food production associated with population increases, but because use in agricultural applications in Japan is not extensive, the impact of soaring prices is not so great. Even with price increase negotiations, it is expected to cost around 100 to 150 dollars a ton. If the price of sulfur continues to soar above this, it is thought that cheap mountain sulfur may also be mined. Replacing methane gas with natural gas would also be cheaper. We do not think that the soaring of raw materials prices will continue forever. If it continues, the chemical business will change structurally.

Q6: I have heard before that imidazole is a hardening agent for epoxy resin and that the hardened product has excellent heat and moisture resistance. I think that demand for the use in cars will increase because of the spread of EVs, but what kind of situation are you in? In addition, there are resin hardening agents other than imidazole, but I think that imidazole allows the manufacture of resins with higher heat resistance. Please tell us about the relationship between heat-resistance and imidazole.

A: Epoxy resin is used as a general-purpose resin, and there are various hardening agents. Imidazole is one of them, and by attaching multiple special functional groups to the basic skeleton, it is possible to harden the resin with multiple binds to it. This is related to heat and moisture resistance. Performance changes by using catalysts, and the company has know-how in that kind of molecular design.
High temperature has become one of the keywords related to the power semiconductors that are attracting attention with the shift to EVs. While conventional performance of insulation, high-frequency, and low dielectric properties are required, the trade-off is balanced by increasing heat resistance, which conflicts with the aforementioned properties. Imidazole is a resin hardener, but because the company carries out both molecular design and mass production, we are also differentiated from other companies by that point. Our imidazole is well regarded by automotive resin manufacturers.

While the higher functionality of semiconductors is advancing under Moore's law, semiconductors with the line width of the integrated circuit of transistors miniaturized to five or three nanometers are being mass-produced. It is said that the width will be two nanometers in 2025, but semiconductor process materials such as resist membranes, underlayer membranes, and intermediate membranes will be required to realize that. The development of the new materials that will be used in such next-generation semiconductors has been progressing under the surface, and the company is using its excellent synthetic capabilities to undertake development while meeting with users. These are products with high added value, and the amount of sales as sample work is currently increasing, but it is not yet the stage of mass production or repeat demand, I will refrain from answering with specific figures for sales and the like.

Q7: Please tell us the details of the organic chemicals business and fine chemicals business with regard to the analysis of the changes in segment profit in the financial results briefing materials (p9). Also, please tell us about the impact of GliCAP on revenue.

A: Our organic chemicals business consists mainly of chlorinated isocyanurates. North America is the largest market, accounting for about 80% of exports. In North America, people have pools at home, and the sales unit price increased because of tight supply and demand caused by people

isolated at home because of Covid-19, production stoppages at local competitors caused by natural disasters, etc. The company, whose production is based in Japan, continued supply and implemented a significant price pass-through because the prices of raw materials and logistics soared, leading to an increase in profits.
Sales in the fine chemical business increased by about 20% compared to the previous year for functional materials and by about 10% for electronic chemical materials. For functional materials, we carry out small-lot production of many products, and the brand composition changes every year. However, in the term ending March 2022, the average sales unit price increased because of an increase in high value-added products. At present, Glicoat-SMD, an anti-corrosion agent for printed circuit boards, is the main electronic chemical material, but if sales of GliCAP increase from now on, further increases in profits can be expected.

Q8: The company will transition to a holding company structure, but what kinds of synergistic effects can be expected?

A: We decided on the transition to a holding company structure based on differences in profitability because of differences in the details of business and business environments. Until now, the chemicals and housing materials businesses have had the synergistic effect of compensating for each other's profits, but that tendency has weakened over the past few years. The profits of the housing materials business declined for two years running, and segment profit for the term ending March 2022 was about 2.5 billion yen, and the segment profit margin was 14.3%. Compared to our three competitors in the housing materials business, the company is overwhelmingly the profit pursuing type. However, we need to increase profits to make returns to customers, employees, shareholders, and community, our stakeholders, not just aim to increase sales. In the past, the company has been good at increasing profits, but we are aware that we have not been so good at increasing sales. To overcome this situation, we will split the company into three companies: a chemical business company, a housing materials company, and a shared service company that will play the role of head office management division. We think that it is difficult for employees engaged in business to consider sales strategies based on new ideas and to make a major shift, the shared service company and holding company will have to draw up big policies.

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