

Analyst Briefing for FY2015 Outlook & Strategy

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Briefing materials:

https://www.ube-ind.co.jp/ube/en/ir/ir_library/presentation/pdf/keiei_change_challenge_2015_en_17111521.pdf

Questions:

General

Q1.

What are your ambitions as incoming President? Which parts of the present management strategy will you keep and what will change?

A1.

The chemicals business has the most room for growth out of the business segments we are involved in. Competition in the chemicals industry is accordingly intense, but we will keep aiming to secure growth centering on chemicals. We previously took the stance that our non-chemicals businesses would support this growth, but moving forward, we will need to secure growth in each business segment. Of course, our non-chemicals businesses will be expected to generate stable revenues, so we will emphasize stable growth.

Q2.

UBE's operating profits have been down for the last three years. Is it just because of the downturn in external conditions for your core products? Or is it because of inconsistencies internally, such as things not going according to the mid-term management plan?

A2.

There are two reasons for it.

(1) External conditions for our non-chemicals businesses have been very favorable, which we are capitalizing on. The business environment for the chemicals business has not been good, and it won't return to what it was because the structure of the caprolactam market has permanently changed due to new and expanded production capacity in China. Therefore, we are shifting our focus from caprolactam sales to nylon sales. Of course, we need to lower costs for caprolactam, and we need a stable supply of raw material caprolactam for nylon sales.

(2) We are pursuing R&D and product development, but did not concentrate our efforts enough. As a result, we did not have products ready in the pipeline. We will catch up.

Q2-2.

UBE has integrated the chemicals businesses in order to act more quickly and will pursue various efforts including R&D. Do you think you can revive the chemicals business through these initiatives?

A2-2.

Yes, I think we can revive the business.

Q3.

UBE has made structural changes such as ceasing caprolactam production at the Sakai Factory. Right now, are there any businesses that need restructuring?

A3.

Not right now. There may be businesses where we will need to implement a balanced contraction depending on the business development, but that is only to be expected and something that we will fully execute as needed. At the same time, we will secure growth where there are opportunities.

Q4.

UBE has various plans for future international business development in the pharmaceuticals and cement and construction materials segments. However, looking at UBE's international business development until now in the specialty chemicals segment, I was disappointed that UBE chose to establish joint ventures instead of going on its own by using promising technologies. How will UBE decide to pursue international business development with or without a partner?

A4.

One factor is whether we can handle the scale of investment as a company. Another factor is whether we need to act quickly.

With the electrolyte joint venture, our thinking was that we needed keep up with surging demand in order to be competitive amid global developments. Therefore, we teamed up with a partner that could act quickly and had a broad sales area. Unfortunately, the market for lithium-ion batteries did not grow the way we projected and the direction changed. As you say, we possess electrolyte technologies and will make a renewed push for global business development by forming an electrolyte subsidiary.

As for the joint venture with Samsung, they are a major customer with significant demand, and we need to develop the business in line with Samsung's business strategy. Once Samsung's flexible display business is fully launched, it will deliver various benefits for our polyimide business.

The approach for international business development will depend on the conditions at the time and on the business. There is no fixed blueprint, such as not partnering when we have a technology advantage.

Q4-2.

Does that mean that the cement and construction materials, machinery, and chemicals businesses will develop their own strategies for international business development?

A4-2.

Since we have an internal company structure, the internal companies will basically develop their own business strategy. Of course, we will look at the strategy from the perspective of what is best for the entire UBE Group, in pursuing international business development.

Organizational Changes

Q5.

I suppose it is related to reviving the chemicals business, but what is UBE trying to achieve with the organizational changes?

A5.

(1) First of all, we separated pharmaceuticals from the two chemicals businesses, since the business model is different.

(2) The chemicals business was previously separated into two parts, but had common R&D and production organizations. In my opinion, separating the chemicals businesses was advantageous during a period of business expansion. However, today we need to act quickly in terms of deciding which business resources to concentrate on, so it makes sense to integrate the chemicals businesses.

(3) Our R&D resources were rather dispersed until now. From now on, the Chemicals Company and Corporate Research & Development will develop the technology strategy together. This will energize our deployment of R&D resources.

Q6.

Tell us more about the organizational changes. Is the integration of the chemicals businesses aimed at concentrating your business resources in specific areas of chemicals? Or is it aimed at focusing on intellectual assets, since the chemicals business is such a broad field? Also, UBE has not changed the organizations of its non-chemicals businesses. Does this mean that changes are not needed? Will changes be needed in the future?

A6.

(1) By integrating the chemicals businesses, we will methodically address the many issues that we need to address, by prioritizing and setting deadlines.

(2) The cement and construction materials business is the largest of our non-chemicals businesses. In this segment, it is more important that we enhance business collaboration with Ube Material Industries, Ltd., as opposed to changing the internal organization.

Q6-2

What about the Energy & Environment Division and Machinery & Metal Products Company?

A6-2

The Energy & Environment Division is a small business segment, while the Machinery & Metal Products Company operates as a subsidiary. These segments need to operate as separate internal companies.

Nylon and Lactam Chain

Q7.

What is your final target in terms of the percentage of UBE's internal consumption of caprolactam? UBE has 20 to 30 kilotonnes of compounding capacity, which is comparably less than the capacity of its competitors. To what extent will you increase the compounding capacity?

A7.

Taking into account the market conditions for caprolactam, we will continue to supply a certain amount of caprolactam to specific customers. To begin with, we will raise the rate of internal consumption to 80%. We need to increase our compounding facilities, and enhance our marketing and technical development to facilitate the adoption of our products by customers. This takes time. We will start by outsourcing production and ultimately pursue internal production, M&A activity, and alliances.

Q8.

Your competitors have also shifted their strategy to nylon. Will the market end up the same as caprolactam? What is your strategy for expanding sales?

A8.

(1) In the extrusion market, which is our strength, we need to better support markets in Eastern Europe, South America, and North America. We will capture market share by increasing our production volume and actively pursuing these markets.

(2) In the injection market, we will increase our compounding business for automotive applications. With the compounding business, we need to establish compounding facilities in each region we service, so we will first increase our compounding facilities. This takes time, but it is necessary in order to increase our business in the injection market.

In any case, we will differentiate ourselves from the competition by enhancing the performance of our products.

Synthetic Rubber

Q9.

The supply and demand situation for synthetic rubber has also declined, with new production capacity being added in China over the last few years. Although rubber is different from caprolactam, isn't there a risk that spreads will keep shrinking as numerous Chinese competitors enter the market?

A9.

Spreads could certainly shrink as the supply and demand situation eases for Chinese-made general purpose synthetic rubber. Our understanding is that Chinese manufacturers do not have high operating rates. In UBE's case, specialty products account for a large proportion of our synthetic rubber products. We are also building relationships with customers by manufacturing products to meet their specific requirements. As a result, our business has not been impacted by the supply and demand situation for general purpose synthetic rubber, nor will it be impacted in the future. We will continue using the same approach to develop the synthetic rubber business.

Polyimides

A10.

In the electronic materials market, profits from a product with a 70% global share should normally be around 20 to 30%. So why has UBE failed to generate profits from polyimide chip-on-films (COF)? If the issue has to do with how prices are set, should we conclude that the entire specialty chemicals business including battery materials is structured so that UBE cannot generate much in the way of profits?

A10.

(1) Firstly, the COF market has not grown as much as we had projected back when we were considering capital investment for COF. Although we do capture 70% of the market, our operating rates are still insufficient to be profitable. Although there is a big market for films for dual-layer copper clad laminates (CCLs), it is difficult to capture market share. To capture market share, we will market newly developed grades to increase volumes and profits.

(2) In terms of pricing, although we have secured a large market share, the presence of our competition makes it difficult for us to raise prices. Prices for polyimides have not decreased to the same extent as they have for battery materials. The reason why we are not generating profits from polyimides is not because of selling prices. Rather, we need to increase actual production volumes compared with our production capacity, which we are tackling this fiscal year.

Battery Materials

Q11.

In the battery materials business, what were the actual operating rates for each of your facilities in fiscal 2014, and what are the projections for fiscal 2015? When will it become necessary to expand the facilities? At what point in the current fiscal year do you expect volumes to increase?

A11.

I cannot talk about specific operating rates, but we have considerable production capacity available. The amount of capital investment in electrolytes is not very large (the depreciation is not significant), and volumes for our plant in China are not projected to grow by that much relative to the production capacity. We need to secure considerably more orders. We also have production capacity available for separators. Looking ahead, we will expand production for separators, or scrap and build older facilities to migrate to higher-efficiency facilities, and we will increase volumes. We will shift our focus to the automotive market, both for electrolytes and separators.

Q11-2.

By 2018, what percentage of your net sales will be to the automotive market? What about to the coating separators market?

A11-2.

We expect that the majority of net sales will be to the automotive market. We will increase our net sales of both coating products manufactured by Ube Maxell, Co., Ltd. and products manufactured by UBE.

Machinery

Q12.

In the machinery business, UBE said two or three years ago that it would strengthen the servicing business. Where is UBE currently, in terms of expanding the servicing network outside of Japan?

A12.

We currently have 22 servicing locations, covering almost all of our customers. We may need to add another one or two more service locations. If anything, we need to increase our servicing staff and develop the parts supply framework, to expand the servicing and capabilities of our servicing locations.

R&D

Q13.

UBE pursues a lot of interesting R&D that is unique and niche leading, but we have the impression that it does not contribute very much to short-term revenues. The R&D section in the presentation describes innovations in nylon and synthetic rubber. If UBE can realize these innovations, then it would have a big impact on increasing revenues. Are there any breakthroughs coming in the next two to three years?

A13.

It depends on what you consider to be innovative. At the very least, we will continue realizing improvements compared with the competition, over the next two or three years. We will try to generate major results over the long term, that will in turn lead to breakthroughs. We have continued making refinements and realizing improvements in the longstanding nylon and synthetic rubber businesses. Securing a major breakthrough in the next two or three years is a lot to ask.

Q14.

The commercial release of Tyranno fiber for ceramic matrix composites (CMCs) is said to be five or six years away. Can you give us an idea of the timeframe? There are only two companies in the world that can make it, and the other company is quite far ahead and says that they will shift to mass production. They must be receiving a lot of inquiries. At the same time, certification is likely to be time-consuming, since it is for aviation applications. How long do you think it will take to gain certification?

A14.

By our projections, the commercial release is about five or six years away. This is in line with our joint development schedule with engine manufacturers. We are not behind schedule.

Capital Investment and Financing

Q15.

Capital investment was projected at ¥140 billion under the current mid-term management plan, and it currently stands at ¥117 billion. What is it projected to be for the next mid-term management plan? UBE seems to have a lot of plans to strengthen production, such as local manufacturing of die casting machines and expanding fine chemicals production.

A15.

We are still reviewing capital investment and financing for the next mid-term management plan. For the chemicals business, our capital investment projection for the next two years is about the same as before.

Dividends

Q16.

UBE's target is to pay dividends of 30% or greater. Does this mean at least 30% every year, or 30% averaged over several years?

A16.

It means 30% or greater averaged over several years. There will be years when we will prioritize investment to secure future growth, depending on the conditions at the time.