Condensed Transcript of Q&A Session at MGC's FY2023 3Q Results Briefing

Date/time: February 9, 2024 (Friday) 18:00-19:00 am (webcast)

Presenter:
Motoyasu Kitagawa, Director, Managing Executive Officer, responsible for Corporate Planning and in charge of CSR & IR Division

(Note about this transcript)
This document has been translated from the Japanese original for reference purpose only. In the event of any discrepancy between this translated document and the Japanese original, the original shall prevail.
This transcript was edited for clarity and brevity at the Company's discretion. Additionally, forward-looking statements, including plans and targets, contained herein, like those in the briefing's presentation materials, are judgments based on information in the Company's possession as of the briefing's date and certain assumptions deemed reasonable by the Company. Forward-looking statements involve uncertainty. Actual outcomes may differ substantially from such forward-looking statements as a result of various factors.

Q1: With regard to the full-year forecast (P13), please explain your view with regard to 4Q for electronic chemicals, BT materials, and optical resin/polymer within Specialty Chemicals. If BT materials are forecast to see increased sales on a QoQ basis while electronic chemicals are to remain level, does that mean that the semiconductor market is expected to remain level but BT materials are to grow due to some special factor? Please explain the background to this. Also, is there any other reason for the decrease in sales of optical resign/polymer apart from seasonal factors such as Chinese New Year?

A1: Regarding electronic chemicals, although we have seen an upturn on the profit front compared to the previous forecast, mainly due to cost improvements and the sales mix, demand itself continues to slump. Adoption for use on new production lines of major customers has made steady progress, but currently orders are weak and we expect 4Q sales to be level with 3Q. Customers for electronic chemicals are themselves major semiconductor manufacturers, while there is some variation between customers, demand has been weak for customers across the board, including customers in North America as well as in South Korea and Taiwan, where demand had been relatively strong. In the front-end process washing field, demand recovery is likely to be postponed until FY2024. Meanwhile, BT materials show some variation in demand by application, and compared to the previous forecast, there is still weakness in demand for general-purpose materials used in home appliances and automotive and in low-warp materials for data center memory. Meanwhile, demand is strong for low-warp materials and others for smartphones, which make up the majority of sales. Furthermore, BT materials for certain FC-BGA substrates, which have seen increasing uptake over the past few years, have also started to show a clear recovery right now. Although there is some variation by application, overall demand is recovering on a QoQ basis, and we have remained firmly on course with our initial forecast for BT materials. Optical materials have been driven mainly by Chinese smartphones and middle-grade materials for developing countries in 2Q and 3Q. Furthermore, adoption of periscope cameras and other trends towards higher resolution are driving increased demand for high grade materials, which is also leading to improvements in the sales mix. Nevertheless, profits are expected to decrease from 3Q to 4Q due to an inevitable fallback following advance demand for Chinese New Year, which happens every year.

Q2: Regarding the profit-and-loss picture for BT in next fiscal year, can we assume it would be something like the second half of this year multiplied by two?

A2: They are our mainstay product, and as such we are aiming for the second half multiplied by two, plus a little more.

Q3: Regarding the former Aromatic Chemicals segment, why are net sales forecast to decrease with the deconsolidation of JSP while the operating profit forecast has not changed? Are we to understand that with 4Q being a period of low demand, JSP would also not generate much profit, so that its exclusion would make little overall difference at the operating profit level? Also, I had thought that the difference due to schedule maintenance in 4Q would be around \3.0 billion; can you reconfirm that it is only \2.0 billion?

A3: JSP’s previously disclosed forecast had full-year operating profit at \6.3 billion, but 3Q performance has been exceedingly good, so that the cumulative 3Q progress rate for operating profit was basically 100% at \6.4 billion. For that reason, there was no factor for numerical change versus the previous forecast. Moreover, JSP has revised its full-year forecast for operating profit upward to \7.5 billion, and if JSP were to remain a consolidated subsidiary of the Company, our operating profit forecast would also have been about \1.1 billion higher. The difference of \2.0 billion due to scheduled maintenance is correct.

Q4: I understand that the former Information and Advanced Materials segment 4Q operating profit came to near record-high levels, but could you give us an idea of the contribution to earnings of OPE and others as well as BT, and also annual net sales growth and next year’s expected sales?

A4: OPE’s presence in the former Information and Advanced Materials segment has been increasing. Sales volumes have grown beyond the initial forecast, and they have reached the point where it is large enough to be discussed as an item on its own in IR. They are used for high-end printed circuit boards that require low dielectric properties, and this is connected to use in generative AI servers and so forth. The value chain for generative AI is long, and while we are far from the end user as a supplier of resin, our products have been adopted by customers who are CCL manufacturers with strong positions in this field, and we recognize that they we have grown through collaboration with them. The growth of OPE has been extremely welcome from a perspective of diversification of our portfolio in the electronic materials business overall. However, there are a lot of uncertainties, such as the outlook for AI server-related demand going forward, and this has made it quite difficult to prepare figures for next year onward. We are currently examining them.

Q5: Could you give a rough idea based on 1Q of the scale by 4Q in terms of how many times larger it will have become? Also, can we understand that you have not seen many risks at this stage such as the emergence of a substitute product and so forth?

A5: Compared to the start of the year, it has grown by something like 1.4 to 1.5 times, and the growth has been faster than we initially expected. At this point I can only say that sales have reached the scale that we can present in our IR. We have heard that the Company’s materials are extremely highly rated, and we do not believe there is any risk of their being substituted. We will reliably provide a stable supply.

Q6: Among the four former segments, with regard to the Specialty Chemicals segment, could you explain about changes from 2Q to 3Q, and whether any special factors have been reflected in 3Q and 4Q? In addition, can you also tell us whether any profit has emerged from your Shanghai base for polycarbonate resin, and whether such profits are sustainable.

A6: First, operating profit changed from \7.2 billion in 2Q to \6.3 billion in 3Q, but the decrease reflected accounting factors such as deductions for application of the lower-of-cost-or-market method, despite positive factors such as a recovery in demand for optical materials and improvement in the profitability of polycarbonate resin. Net sales were almost the same in 2Q and 3Q, with the sales situation being flat. From 3Q to 4Q, sales and profits are expected to decrease. One factor for optical materials is Chinese New Year, and other factors include a decrease in sales of polycarbonate and an increase in one-time costs (such as impacts of the financial closing for the fiscal year-end and application of the lower-of-cost-or -market method). At our Shanghai base we are seeing a clear improvement in profit each quarter. One of the factors is widespread adoption among local Chinese EV manufacturers in applications for car headlights. Also, on the cost side, we are making improvements, particularly for raw materials, and for general purpose products also, we are becoming able to sell them without making a loss. We are narrowing down production volumes, and even if the volume is slightly less, we are investing into high-added-value products. We will continue to increase the ratio of high-value-added products and aim to survive as an entity with characteristic strengths.

Q7: On page 12 of the materials, you have “Others + 3.0” among the increase and decrease factors versus the previous forecast. Is “Electronic chemicals” here referring to a cost reduction? Will you be able to continue to increase volume while keeping costs down to a certain extent next fiscal year also?

A7: With ongoing weakness in demand for electronic chemicals, as a result of efforts by all bases, we see a cost improvement for electronic chemicals of approximately \1.0 billion in SG&A expenses and fixed costs.

Q8: Is methanol-related equity in earnings of affiliates for 3Q to 4Q based on market price trends? Are other factors such as foreign exchange rates included?

A8: The market price trend was 1Q USD 308, 2Q USD 285, 3Q USD 319, and in 4Q it is forecast at USD 340. So, the market prices for methanol in the first half went below USD 300, on top of which there was also a foreign exchange loss on a loan at Japan Saudi Arabia Methanol Company, Inc. due to the yen's depreciation that led to an overall loss on methanol-related equity in earnings of affiliates. However, in the second half we expect to make enough profit to offset the loss of the first half. Also, production is moving steadily at all bases.

Q9: The MXDA base in the Netherlands was planning to incur start-up expenses and so forth during this fiscal year, but it seems they are now expected to be booked next fiscal year. Will its actual operations start next fiscal year? I would also like to hear about the end customers in wind power generation.

A9: First of all, the construction has been delayed from our initial plans, partly due to the situation in Europe, and we hope to start operations next fiscal year. Demand from wind power generation is not yet that big, so it will not have such a large impact on plant capacity utilization. Most of the applications for MXDA is as a curing agent for epoxy resin, for example flooring applications as a coating material and so forth. It is also used for nylon in Europe and North America. Currently, demand for Europe is still weak, but we will set up the new plant and begin production. In terms of the balance with our two plants in Japan, the Japanese plants will shift their production to meet growing demand for the MXDA derivative 1,3-BAC and steadily growing demand for nylon.

Q10: 3Q profits give an extremely positive impression, with an increase of \0.7 billion from 2Q. Do you have the impression that 3Q performance exceeded your plans?

A10: Our impression for 3Q is that we produced good numerical results.

Q11: Regarding the factors for a decrease in profits in Basic Chemicals going from 3Q to 4Q, could you tell us of any factors other than the deconsolidation of JSP and the repair expenses for Mizushima Plant?

A11: With regard to aromatic chemicals, one factor was a deterioration in spread due to the slump in market prices for PIA.

Q12: In Specialty Chemicals, you have mentioned a decrease in profits in electronics chemicals, PC, and optical materials. Could you give an idea of the breakdown between them?

A12: The decreases in profits from 3Q to 4Q were something like just over \1.0 billion for inorganic chemicals, mainly super-pure hydrogen peroxide, and just over \2.0 billion for engineering plastics and optical materials.

Q13: What is the approximate impact of decreasing profits for POM for the year? Are you expecting any improvement in revenue next year?

A13: In terms of absolute amounts, we are generating a profit this year also, but compared to the previous fiscal year, it is minus around \10.0 billion. Next fiscal year, we expect market prices and demand to recover, and we think the results will not be as bad as this fiscal year. However, we think it would be difficult to return to the levels seen up to FY2021 and FY2022.

Q14: With regard to OPE, do you have sufficient supply capacity to meet demand? Is there any risk that you would reach full capacity early and be unable to provide supply going forward? Also, could you tell us what you can about your thoughts on increasing capacity next fiscal year and the fiscal year after that?

A14: There are currently no issues with production capacity. Consideration from a future BCP perspective is a separate matter, but for now, from this year to around next year, we believe that our present production capacity will be ample to respond to demand.