

NIPPO LTD. (9913 JP)**FY22 OP HIT A RECORD. FLATTISH FY23 GUIDANCE DUE TO SURGE IN ENERGY AND RAW MATERIALS COSTS****FY22 RESULTS**

Nippo Ltd. [hereafter Nippo] reported FY22 results with operating profit [OP] of ¥1,912mil (+42.5% YoY) on sales of ¥38,886mil (+9.6% YoY), which surpassed the firm's forecast (OP of ¥1,790mil on sales of ¥37,500mil), thanks to 1) change in sales mix due to growth in the Mobility segment, primarily due to better-than-expected auto production, and 2) translation gains from weaker yen.

FY22 sales increased by ¥3,395mil (+9.6% YoY), of which sales growth in the Mobility Segment contributed ¥2,245mil, thanks to strong demand for power train parts and component, as well as gradual recovery in auto production. As a result, sales breakdown of Mobility Segment improved from 36.9% in FY21 to 39.4% in FY22.

FY22 OP increased by ¥570mil YoY (+42.5% YoY), despite the negative impact from as rise in labour / personnel costs (-¥229mil YoY) and other fixed costs such as distribution / energy (-¥188mil YoY). Those negative factors were well offset by improvement in operating cost (+¥987mil YoY) which increase translation gain of FOREX of ¥154mil.

Nippo also reported extraordinary expenses due to (1) the write off of impairment costs (¥55mil) and (2) losses associated with the withdrawal from non-profitable businesses (¥35mil).

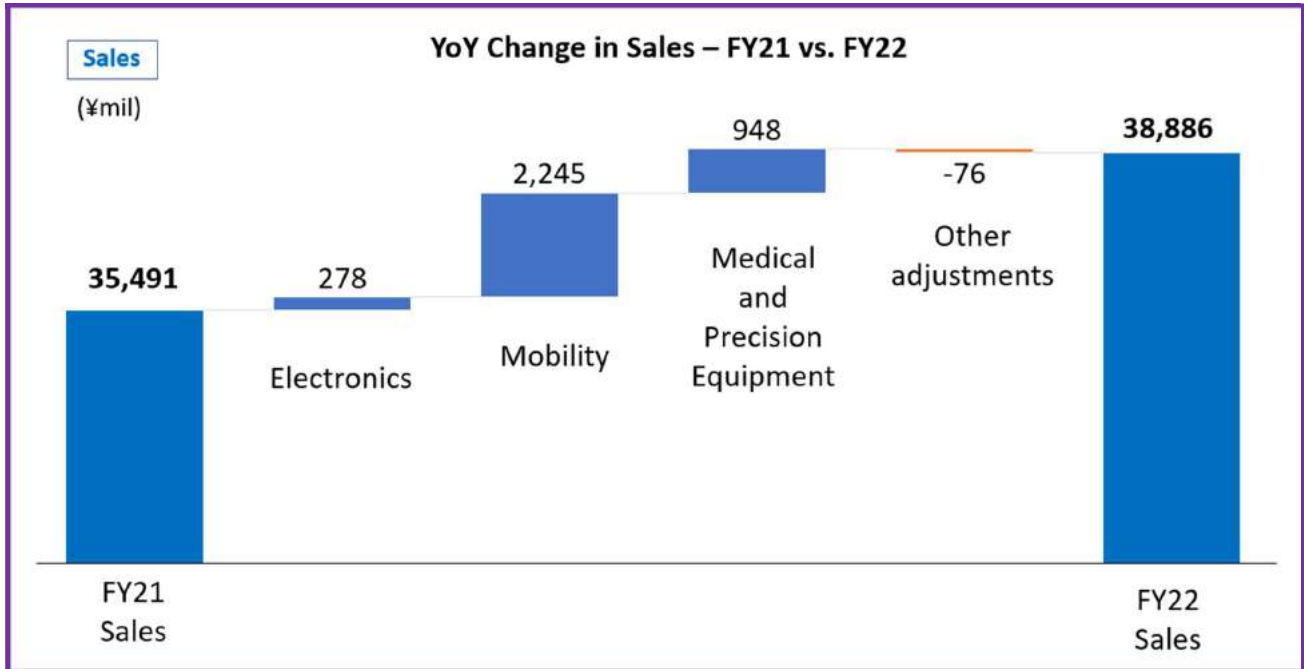
In FY22, Nippo paid an annual dividend of ¥33.00/share, which is a 23.4% of pay-out ratio.

| Nippo Ltd. (9913 JP): Earnings Summary (Cumulative) | | | | | | |
|---|--------|--------|--------|--------|---------|--------|
| (¥mil) | FY21 | | FY22 | | | |
| | 1H | FY | 1H | FY | YoY (%) | FYCE |
| Sales | 17,403 | 35,491 | 18,606 | 38,886 | 9.6 | 37,500 |
| COGS | 14,495 | 29,592 | 15,296 | 32,076 | 8.4 | N/A |
| Gross Profit | 2,907 | 5,898 | 3,310 | 6,809 | 15.4 | N/A |
| GPM (%) | 16.7 | 16.6 | 17.8 | 17.5 | +0.9ppt | N/A |
| SG&A | 2,265 | 4,556 | 2,381 | 4,897 | 7.5 | N/A |
| SG&A / Sales (%) | 13.0 | 12.8 | 12.8 | 12.6 | -0.2ppt | N/A |
| OP | 641 | 1,342 | 929 | 1,912 | 42.5 | 1,790 |
| OPM (%) | 3.7 | 3.8 | 5.0 | 4.9 | +1.1ppt | 4.8 |
| RP | 651 | 1,423 | 905 | 1,871 | 31.5 | 1,710 |
| NP* | 467 | 1,031 | 590 | 1,269 | 23.1 | 1,170 |

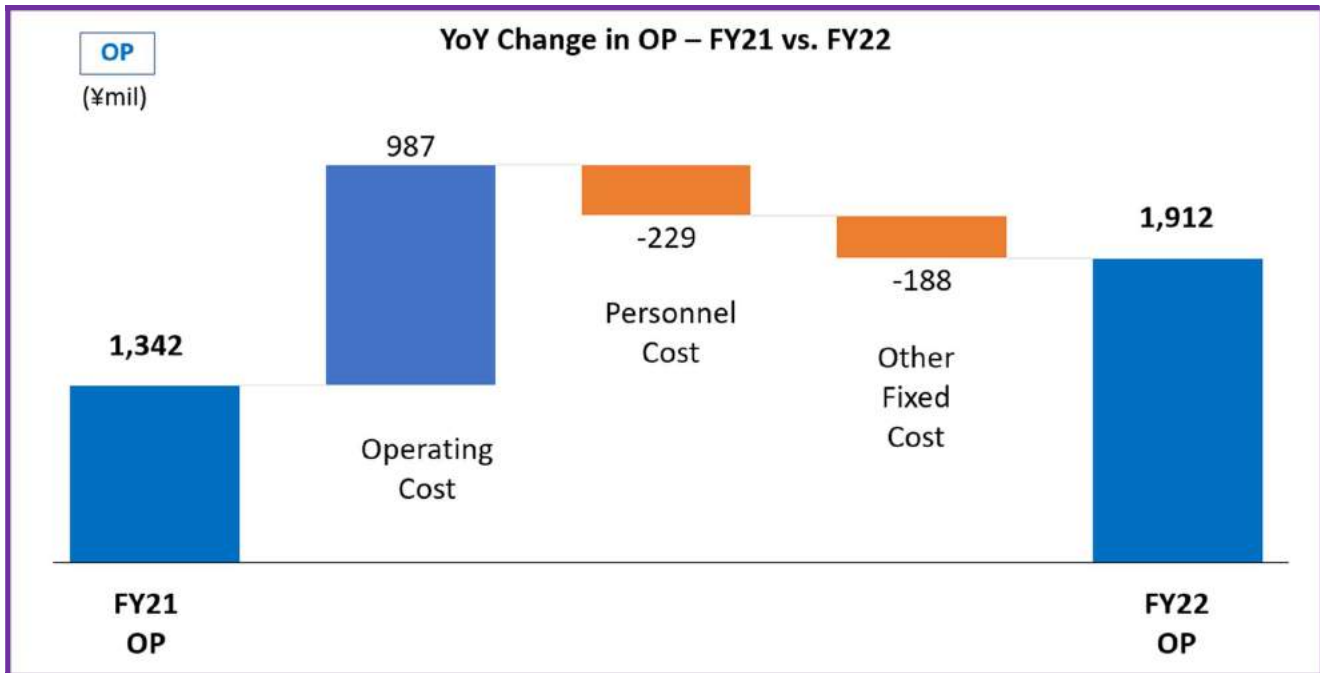
Source: Nippon-IBR based on Nippo's FY21 and FY22 earnings materials
* Net profit attributed to the parent's shareholders

EXECUTIVE SUMMARY

- Nippo Ltd. [hereafter Nippo] reported FY22 results with operating profit [OP] of ¥1,912mil (+42.5% YoY) on sales of ¥38,886mil (+9.6% YoY), which surpassed the firm's forecast (OP of ¥1,790mil on sales of ¥37,500mil), thanks to 1) change in sales mix due to growth in the Mobility segment, primarily due to better-than-expected auto production, and 2) translation gains from the weaker yen.
- For FY23, Nippo is guiding for flat sales growth but expects OP to decline -4.3% YoY, based on the following assumptions:
 - Semiconductor supply disruptions will likely continue in some sectors and regions.
 - The cost of energy and resources will remain high.
 - There will be some negative impact from economic security measures.
 - Nippo plans to make upfront investment for growth from FY26 onwards.
- After the successful achievements during the previous medium-term plan, Nippo has launched a new 3-year medium-term plan that it deems to be an investment period.
- The continuation of the existing take-over counter measures will be proposed at the coming AGM on 23 June.
- For FY23, Nippo plans to pay an annual dividend of ¥40.00/share (pay-out ratio 29%), vs ¥33.00/share (23.4%) in FY22. In the final year of the new medium-term plan (FY25), the firm aims to pay out 35%.



Source Nippo Ltd. FY22 earnings presentation material



Source Nippo Ltd. FY22 earnings presentation material

FY23 OUTLOOK

| Nippon Ltd. (9913 JP): Earnings Results & Forecast | | | | | | | |
|--|--------|--------|--------|--------|---------|--------|---------|
| (¥mil) | FY21 | | FY22 | | | FY23 | |
| | 1H | FY | 1H | FY | YoY (%) | FY CE | YoY (%) |
| Sales | 17,403 | 35,491 | 18,606 | 38,886 | 9.6 | 38,900 | 0.0 |
| COGS | 14,495 | 29,592 | 15,296 | 32,076 | 8.4 | N/A | N/A |
| Gross Profit | 2,907 | 5,898 | 3,310 | 6,809 | 15.4 | N/A | N/A |
| GPM (%) | 16.7 | 16.6 | 17.8 | 17.5 | +0.9ppt | N/A | N/A |
| SG&A | 2,265 | 4,556 | 2,381 | 4,897 | 7.5 | N/A | N/A |
| SG&A / Sales (%) | 13.0 | 12.8 | 12.8 | 12.6 | -0.2ppt | N/A | N/A |
| OP | 641 | 1,342 | 929 | 1,912 | 42.5 | 1,830 | -4.3 |
| OPM (%) | 3.7 | 3.8 | 5.0 | 4.9 | +1.1ppt | 4.7 | -0.2ppt |
| RP | 651 | 1,423 | 905 | 1,871 | 31.5 | 1,810 | -3.3 |
| NP* | 467 | 1,031 | 590 | 1,269 | 23.1 | 1,270 | 0.1 |

Source: Nippon-IBR based on Nippon's FY21 and FY22 earnings materials
* Net profit attributed to the parent's shareholders

Nippon is guiding for FY23 OP of ¥1,830mil (-4.3% YoY) on sales of ¥38,900mil (+0.0% YoY). The firm's forecast is based on the following assumptions:

- There will still be semiconductor supply disruption in some sectors and some regions.
- Costs of energy and resources will continue to remain high.
- There will be some negative impacts from economic security measures.

FY22 was the last year of the three-year medium-term plan which focused on, 1) developing differentiating technology and enhancing cost competitiveness area, and 2) building a new business model.

In FY23, Nippon assumes that both of its existing core businesses, namely, Electronics and Mobility, will see flat sales growth as components shortages will likely remain an issue, OP will see dip -4.3% YoY due to upfront investments for growth. These investments are expected to bear fruit from FY26 onwards, when Nippon will launch its next medium-term plan.

Nippon plans to pay an annual dividend of ¥40.00/share, which generates a pay-out ratio of 29%, an improvement from FY22's shareholder returns of ¥33.00/share (23.4%).

SEGMENT PERFORMANCE AND OUTLOOK

Electronics Segment

The Electronics Segment FY22 OP declined -5.9% YoY to ¥1,245mil on sales of ¥16,854mil (+1.7% YoY). In Q4 alone, segment OP was ¥276mil (-22.7% YoY / -8.0% QoQ) on sales of ¥4,125mil (-1.6% YoY / -3.6% QoQ). Approx 80% of segment earnings are derived from Nippon acting as a specialist trading company, handling electronics components and parts for household equipment. The decline in demand for smartphone-related parts weighed on business levels of semiconductor-related materials. On the other hand, the firm enjoyed solid demand for circuit board materials for base stations and servers. Management is aiming to increase sales from manufacturing activities such as slitting process of photosensitive dry films in Vietnam, and wafer polishing jigs in Okinawa, both of which contributed to the segment earnings in FY22.

Nippon is guiding for FY23 segment OP of ¥1,245mil (+0.0% YoY) on sales of ¥16,900mil (+0.3% YoY). The firm assumes demand for smartphone parts will continue to see a downtrend, while orders for circuit board materials and semiconductor wafer polishing jigs will likely remain firm in FY23. Although there is the lack of clarity in inventory adjustment levels for smartphone materials and impact of semiconductor supply shortage, Nippon expects FY23 segment earnings should be able to match that of FY22.

Mobility Segment

Mobility Segment reported FY22 OP of ¥1,535mil (+47.3% YoY) on sales of ¥15,337mil (+17.1% YoY). Here, Nippo manufactures and sells moulded plastic parts and modules used mainly in auto-use electronic control components to OEMs and Tier 1 makers. Although auto and auto parts makers in Japan reduced their production on the back of semiconductor shortages, production trends at some makers have started to show signs of recovery. In the firm's core factories in Thailand and Indonesia, demand for powertrain parts remained solid.

At the same time, Nippo also made efforts to improve the segment's profitability by introducing automation and improving cost competitiveness. The firm also changed depreciation cost method from declining balance to straight method so as to better track cost management. In Q4 alone, segment OP was ¥361mil (+23.6% YoY / -0.3% QoQ) on sales of ¥3,530mil (+7.6% YoY / -21.7% QoQ), generating an OPM of 10.2%, up from FY21's Q4 OPM of 8.9%.

Nippo is eyeing FY23 OP of ¥1,470mil (-4.2% YoY) on sales of ¥15,400mil (+0.4% YoY). Management assumes flattish growth in sales as the global auto production recovers, but remains cautious due to semiconductor supply shortages still remains in some areas, and there could be further disruptions caused by economic security measures. On the other hand, FY23 segment OP is estimated to fall by -4.2% YoY on the back of upfront investments for growth, such as further advancement in automation and product development based on Nippo's core technology competence, winding technology. Furthermore, the firm assumes that segment profit will be squeezed by higher energy and resource costs.

Medical and Precision Devices Segment

Some 80% of segment sales is generated from precision equipment parts – the main product is ink jet and laser printer units – and the remaining approx. 20% is from components used in medical equipment. The printer units business has high seasonality in 2H, and was impacted by supply shortage of semiconductor and electronic components, therefore, the 1H earnings were in the red. However, the Q3 and Q4 performance offset the 1H loss. FY22 segment OP was ¥126mil (vs an operating loss of -¥17mil in FY21) on sales of ¥6,889mil (+16.0% YoY). Orders for medical equipment parts to the Thai factory remained solid. And while printer parts were negatively affected by the shortage of semiconductor and electronic components, production started to recover in Q3.

Nippo is guiding for FY23 segment OP of ¥100mil (-20.6% YoY) on sales of ¥6,900mil (+0.2% YoY). Segment sales are estimated to remain flat YoY thanks to solid orders for medical equipment parts offsetting the weakness in the printer parts business. While demand for printer-related parts is recovering, the firm remains cautious because of uncertainty on printer makers' changes in production location and production volume. The firm aims to build a production base in Japan for medical equipment parts, which will incur upfront investment and will cap the OP growth in FY23. Nippo aims to start mass production in FY25.

| Nippo Sangyo (9913 JP): Sales and OP by Segment | | | | | | | | | | |
|---|---------|--------|--------|--------|--------|--------|--------|---------|--------|---------|
| (¥mil) | | FY17 | FY18 | FY19 | FY20 | FY21 | FY22 | | | |
| | | FY | FY | FY | FY | FY | FY | YoY (%) | FYCE | YoY (%) |
| Electronics | Sales | 15,458 | 14,269 | 17,611 | 18,263 | 16,576 | 16,854 | 1.7 | 16,800 | 1.4 |
| | OP | 258 | 222 | 994 | 1,046 | 1,324 | 1,245 | -5.9 | 1,200 | -9.4 |
| | OPM (%) | 1.7 | 1.6 | 5.6 | 5.7 | 8.0 | 7.4 | -0.6ppt | 7.1 | -0.9pp |
| Mobility | Sales | 15,278 | 17,172 | 18,303 | 15,963 | 13,092 | 15,337 | 17.1 | 14,400 | 10.0 |
| | OP | -18 | -34 | 931 | 485 | 1,042 | 1,535 | 47.3 | 1,490 | 43.0 |
| | OPM (%) | n/a | n/a | 5.1 | 3.0 | 8.0 | 10.0 | +2.0ppt | 10.3 | +2.3pp |
| Medical and Precision Equipment | Sales | 7,457 | 7,747 | 6,896 | 5,877 | 5,941 | 6,889 | 16.0 | 6,100 | 2.7 |
| | OP | 82 | 302 | 156 | -43 | -17 | 126 | n/a | 100 | n/a |
| | OPM (%) | 1.1 | 3.9 | 2.3 | n/a | n/a | 1.8 | n/a | 1.6 | n/a |

Source: Nippon-IBR based on Nippo Sangyo's earnings presentation materials

| Nippo Sangyo (9913): Sales and OP by Segment (Quarterly) | | | | | | | | | | | |
|--|---------|-------|-------|-------|-------|-------|-------|-------|-------|---------|---------|
| (¥mil) | | FY21 | | | | FY22 | | | | | |
| | | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | YoY (%) | QoQ (%) |
| Electronics | Sales | 4,031 | 3,983 | 4,372 | 4,190 | 4,319 | 4,132 | 4,278 | 4,125 | -1.6 | -3.6 |
| | OP | 331 | 320 | 316 | 357 | 306 | 363 | 300 | 276 | -22.7 | -8.0 |
| | OPM (%) | 8.2 | 8.0 | 7.2 | 8.5 | 7.1 | 8.8 | 7.0 | 6.7 | -1.8ppt | -0.3ppt |
| Mobility | Sales | 3,391 | 3,352 | 3,067 | 3,282 | 3,620 | 3,680 | 4,507 | 3,530 | 7.6 | -21.7 |
| | OP | 307 | 306 | 137 | 292 | 378 | 434 | 362 | 361 | 23.6 | -0.3 |
| | OPM (%) | 9.1 | 9.1 | 4.5 | 8.9 | 10.4 | 11.8 | 8.0 | 10.2 | +1.3ppt | +2.2ppt |
| Medical and Precision Equipment | Sales | 1,405 | 1,294 | 1,528 | 1,714 | 1,439 | 1,497 | 1,996 | 1,957 | 14.2 | -2.0 |
| | OP | -12 | -81 | 47 | 29 | -14 | -63 | 101 | 102 | 251.7 | 1.0 |
| | OPM (%) | N/A | N/A | 3.1 | 1.7 | N/A | N/A | 5.1 | 5.2 | +3.5ppt | +0.1ppt |

Source: Nippon-IBR based on Nippo Sangyo's earnings presentation materials

MEDIUM-TERM MANAGEMENT PLAN (FY23~FY25)

FY23 is the first year of the new three-year medium-term management plan which will complete in FY25. Nippo considers the next three years as a period during which the firm will focus on proactively promoting new products and materials that were developed through the new business model established during the previous medium-term plan. In the new business model, the firm aims to offer added-value based on Nippo's own ideas, rather than just responding to enquiries from clients.

Review of FY20~FY22 Medium-Term Plan

Following the successful completion of the previous plan, which surpassed the final year target of OP of ¥1,500mil+ (CAGR of +5.6%) by achieving FY22 OP of ¥1,912mil (CAGR of +14.5%).

Nippo also overshot three key KPIs under the previous plan, in addition to the earnings targets. Those are:

1. RoE of more than 9.0%. Nippo achieved 11.1% in FY22.
2. D/E ratio of less than 0.6x, which was also achieved throughout the three years. As of FY22, D/E ratio was 0.4x.
3. Cash dividend of ¥20+ was already realised in FY21. FY22 annual dividend improved from ¥10.00/share in FY20, ¥28.00/share in FY21, and to ¥33.00/share with FY22.

Summary of the new Medium-Term Plan (FY23~FY25)

In the new medium-term plan, Nippo has three fundamental principles:

- Achieve the following two numerical KPIs:
 - 1) Generate consolidated OP of ¥5,730mil vs. FY20~FY22 total OP of ¥3,880mi. In the final year (FY25), Nippo aims to achieve consolidated OP of ¥2,000mil (3-yr CAGR +1.5%).
 - 2) ROE of 10.0%+ on average over three years vs previous plan's average of 7.3%.
- Introduce Business Portfolio Management

In order to achieve sustainable earnings growth and enhance enterprise value over the medium-to long term, business resources will be allocated to businesses with high growth potential and profitability.

- Achieve PBR 1x by improving efficiency of the balance sheet and enhancing profitability.

Capital Allocation

Nippo had approx. ¥10,000mil in cash and cash equivalents on its balance sheet as of the end of FY22. The required working capital is estimated at approx. 1-month of sales (i.e. approx. ¥3,200mil). During the medium-term plan, Nippo plans to allocate capital to the following areas:

- Investment on the existing businesses, which will be within depreciation cost each year.
- Investment on new businesses enhancement of business functions such as investment for growth, patents, creating expertise, alliances and M&A, which Nippo plans to allocate approx. ¥3,000mil out of approx. ¥4,000mil free cash flow over the three years.
- Shareholder return of ¥1,060mil and aiming to achieve 35% pay-out ratio.

POISON PILL

At a Board of Directors meeting held on 19 May 2023, the decision to propose the continuation of countermeasures against large-scale purchases of the company's shares (ie takeover defense measures) should continue, subject to shareholder approval at the 72nd Ordinary General Meeting scheduled to be held on 23 June 2023. The measure was voted for at the last year's AGM, and is effective until the end of the coming AGM scheduled. Nippo introduced the poison pill and exercised countermeasures on the back of ToB attempts by its largest shareholder, Freesia Macros Corporation [FMC] (6343 JP). However, the firm suspended the countermeasures when FMC withdrew its bid.

Nippo states that the firm's Board does not categorically refuse takeovers. The Plan was introduced for the Board to carefully consider proposals placed on the company in its duty to enhance enterprise value and protect shareholders' interest. Due to the nature of the business, which works closely with its clients' product development projects, and, in some case, manufactures under technological license agreements, the firm believes measures are needed to evaluate potential acquirers.

The Plan sets out prerequisites for the potential acquirers to submit which include 1) the Statement of Intention to the Company and 2) Provision of Necessary Information. Upon submission of the information, Nippo's Board will acknowledge receipt of the bid and disclose the proposal by the acquirer to the company. Subsequently, the Board will set the Board Assessment Period, and then an Independent Advisory Committee will be established regardless of whether any countermeasures will be triggered or not.

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