

**NIPPO LTD. (9913 JP)****PROLONGED ORDER WEAKNESS IN ASEAN AND SURGE IN ENERGY COST WILL CAP UPSIDE IN FY23 OP FORECAST****FY23 1H RESULTS**

Nippo Ltd. [hereafter Nippo] reported FY23 1H results with operating profit [OP] of ¥939mil (+1.2% YoY) on sales of ¥20,215mil (+8.6% YoY). Despite a decline in orders on the back of production adjustment by customers in ASEAN countries, the 1H result exceeded 50% of the firm's full-year guidance on the back of improved capacity utilisation rates thanks to:

1. A recovery in customers' production volumes reflecting the pick-up in auto production volume at Japanese OEMs in the Mobility segment, and
2. Foreign exchange translation gains from the weak yen.

FY23 1H sales increased by ¥1,609mil (+8.6% YoY), of which sales growth in the Mobility Segment contributed ¥825mil (+11.3% YoY), boosted by strong demand for power train parts and components, as well as the gradual recovery in domestic auto production.

The Electronics segment contributed ¥363mil (+4.3% YoY) to the YoY rise in consolidated sales as the firm saw solid growth in print circuit boards [PCBs] used in servers and base stations, dry films, and wafer polishing jigs.

In addition, the Medical and Precision Devices segment produced a +¥422mil YoY (+14.4% YoY) increase in 1H sales, thanks to recovery in orders in Vietnam and the Philippines.

Nippo Ltd. (9913 JP): Earnings Summary (Cumulative)						
(¥mil)	FY21		FY22		FY23	
	1H	FY	1H	FY	1H	YoY (%)
Sales	17,403	35,491	18,606	38,886	20,215	8.6
COGS	14,495	29,592	15,296	32,076	16,696	9.2
Gross Profit	2,907	5,898	3,310	6,809	3,518	6.3
GPM (%)	16.7	16.6	17.8	17.5	17.4	-0.4ppt
SG&A	2,265	4,556	2,381	4,897	2,578	8.3
SG&A / Sales (%)	13.0	12.8	12.8	12.6	12.8	+0.0ppt
OP	641	1,342	929	1,912	939	1.2
OPM (%)	3.7	3.8	5.0	4.9	4.6	-0.4ppt
RP	651	1,423	905	1,871	1,097	21.2
NP*	467	1,031	590	1,269	755	28.0

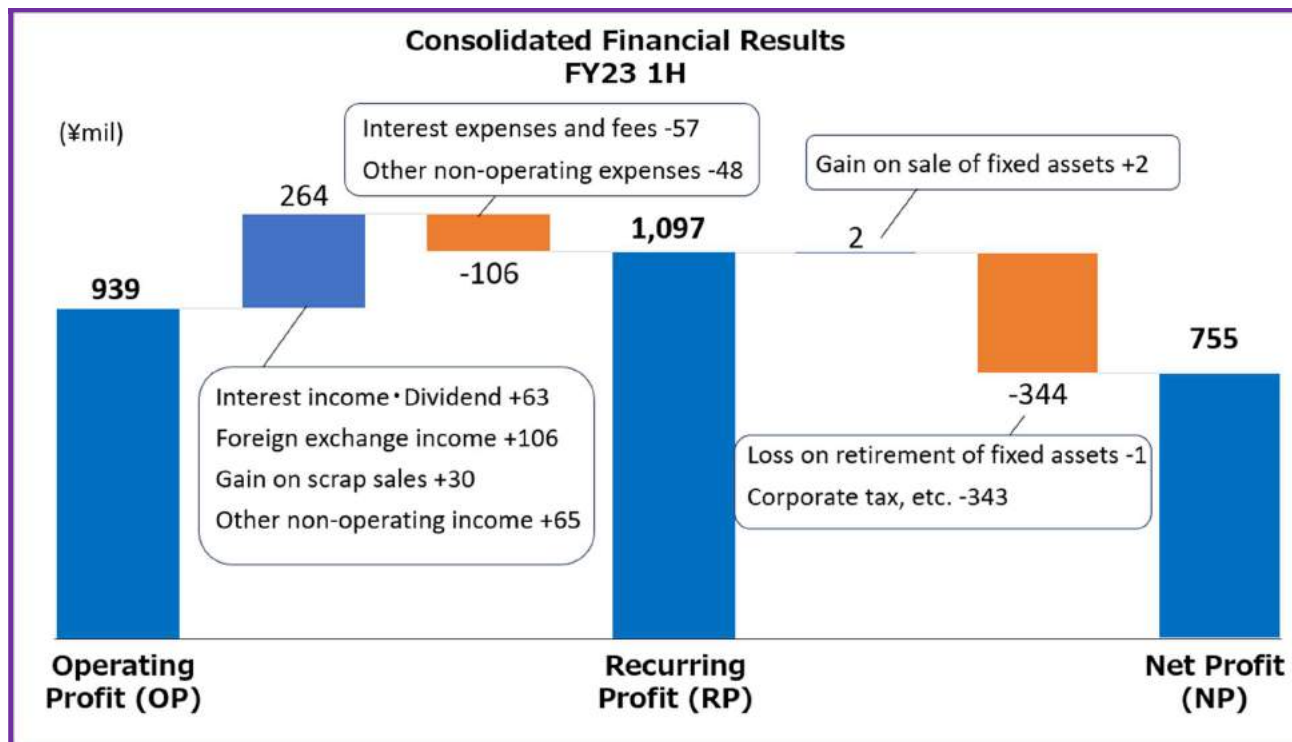
Source: Nippon-IBR based on Nippo's FY21, FY22 and FY23 1H earnings materials  
\* Net profit attributed to the parent's shareholders

FY23 1H OP increased by ¥10mil YoY (+1.2% YoY), despite the -¥349mil hit from higher labour / personnel costs and other fixed costs, such as depreciation cost, distribution, and energy (-¥348mil YoY). Those negative factors were well offset by improvements in capacity utilisation (+¥707mil YoY) which include FOREX translation gains of ¥36mil.

**EXECUTIVE SUMMARY**

- Nippo Ltd. [hereafter Nippo] reported FY23 1H OP of ¥939mil (+1.2% YoY) on sales of ¥20,215mil (+8.6% YoY). Despite weak orders due to production adjustments by customers in ASEAN countries, the 1H results exceeded 50% of Nippo's full-year guidance, thanks to an increase in orders from customers in Japan.
- While Nippo has kept its full-year FY23 forecast for OP of ¥1,830mil (-4.3% YoY) on sales of ¥38,900mil (+0.0% YoY), the RP target was raised from ¥1,810mil (-3.3% YoY) to ¥1,950mil (+4.2% YoY), and NP from ¥1,270mil (+0.1% YoY) to ¥1,340mil (+5.6% YoY) on FOREX translations. The firm has adjusted its FOREX assumption from ¥133/US\$ (average during 1H) to ¥140/US\$, and from ¥3.8/TB\$ to ¥4.0/TB\$ for 2H.
- With the success of Nippo's previous medium-term plan, it has launched a new 3-year (FY23~FY25) medium-term plan, with the following two numerical targets:
  - 1) FY23~FY25 total consolidated OP of ¥5,730mil vs FY20~FY22 OP of ¥3,880mil. In the final year (FY25), Nippo is aiming for consolidated OP of ¥2,000mil (3-yr CAGR +1.5%).
  - 2) ROE of 10.0%+ on average over three years vs the previous plan's average of 7.3%.
- Nippo also revised the annual DPS from ¥40.00 to ¥42.00, generating a payout ratio of 28.0%, up from FY22's DPS of ¥33.00 (23.4% payout). In the final year of the new plan (FY25), the firm is targeting a payout ratio of 35%.
- The continuation of countermeasures for large-scale purchases of shares was proposed at the AGM in June 2023, and approved.

Nippo also reported a net non-operating gain of +¥158mil and net extraordinary gain of ¥1mil, respectively.



Source: Nippon-IBR based on Nippo's FY23 1H earnings materials

## FY23 OUTLOOK

Nippo Ltd. (9913 JP): Earnings Summary (Cumulative)								
(¥mil)	FY22		FY23					
	1H	FY	1H	YoY (%)	FY CE (Old)	YoY (%)	FYCE (New)	YoY (%)
Sales	18,606	38,886	20,215	8.6	38,900	0.0	38,900	0.0
COGS	15,296	32,076	16,696	9.2	NA	NA	NA	NA
Gross Profit	3,310	6,809	3,518	6.3	NA	NA	NA	NA
GPM (%)	17.8	17.5	17.4	-0.4ppt	NA	NA	NA	NA
SG&A	2,381	4,897	2,578	8.3	NA	NA	NA	NA
SG&A / Sales (%)	12.8	12.6	12.8	+0.0ppt	NA	NA	NA	NA
OP	929	1,912	939	1.1	1,830	-4.3	1,830	-4.3
OPM (%)	5.0	4.9	4.6	-0.4ppt	4.7	-0.2ppt	4.7	-0.2ppt
RP	905	1,871	1,097	21.2	1,810	-3.3	1,950	4.2
NP*	590	1,269	755	28.0	1,270	0.1	1,340	5.6

Source: Nippon-IBR based on Nippo's FY22 and FY23 1H earnings materials  
\* Net profit attributed to the parent's shareholders

Nippo maintained its full-year FY23 forecast for OP of ¥1,830mil (-4.3% YoY) on sales of ¥38,900mil (+0.0% YoY) but revised up at the recurring profit [RP] level from ¥1,810mil (-3.3% YoY) to ¥1,950mil (+4.2 YoY), and net profit [NP] from ¥1,270mil (+0.1% YoY) to ¥1,340mil (+5.6% YoY) on revisions to its FOREX assumptions – from ¥133/US\$ (average during 1H) to ¥140/\$, and from ¥3.8/TBh to ¥4.0/TBh for 2H. The firm's forecast is based on the following assumptions:

- That there will still be semiconductor supply disruptions in some sectors and some regions.

- Energy and resource costs will continue to remain high.
- There will be some negative impact on supply chains from economic security measures.

Nippo is guiding for flat YoY growth in FY23 sales with an assumption that prolonged production adjustment of smartphone components will likely remain an issue. FY23 OP will see a dip (-4.3% YoY) due to upfront investments for growth. These investments are expected to bear fruit from FY26 onwards, when Nippo will launch its next medium-term plan.

The company also revised the annual dividend from ¥40.00/share to ¥42.00/share, which generates a pay-out ratio of 28.0%. This compares with FY22's shareholder returns of ¥33.00/share (23.4%).

## SEGMENT PERFORMANCE AND OUTLOOK

### Electronics Segment

The Electronics Segment FY23 1H OP declined -9.6% YoY to ¥605mil on sales of ¥8,814mil (+4.3% YoY). Approx 80% of segment earnings are derived from Nippo acting as a specialist trading company, handling electronics components and parts for household equipment.

The decline in demand for smartphone-related parts on the back of extended production adjustments by customers weighed on business levels of semiconductor-related materials.

On the other hand, the firm enjoyed solid demand for (1) circuit board materials for base stations and servers, (2) the slitting process of photosensitive dry films in Vietnam, and (3) wafer polishing jigs at its Okinawa facility. However, segment 1H OP fell -9.6% YoY primarily due to the initial cost associated with the dry film business at the Thai factory. In Q2 alone, segment OP was ¥323mil (-11.0% YoY / +14.5% QoQ) on sales of ¥4,505mil (+9.0% YoY / +4.5% QoQ).

Nippo has kept its full-year FY23 segment earnings guidance for OP of ¥1,245mil (+0.0% YoY) on sales of ¥16,900mil (+0.3% YoY). The company assumes continued weak demand for smartphone parts, while orders for circuit board materials, semiconductor wafer polishing jigs and the dry film business are expected to be firm in 2H. Although a lack of clarity remains regarding inventory adjustment levels for smartphone materials and the ongoing impact from semiconductor supply shortages, Nippo still expects FY23 segment earnings to be able to match that of FY22.

### Mobility Segment

FY23 1H segment OP fell -5.4% YoY to ¥768mil on sales of ¥8,125mil (+11.3% 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. During 1H, order for powertrain parts manufactured in one of Nippo's core factories in Thailand declined due to customers' weak sales trend in products bound for China. On the other hand, production of autos and auto parts in Japan recovered, leading to solid demand for powertrain parts manufactured in Nippo's Vietnam and Indonesian factories.

The decline in 1H OP was due to 1) the continued rise in energy costs, and 2) weak orders at the Thai factory lowered capacity utilisation. In Q2 alone, OP fell -19.4% YoY / -16.3% QoQ to ¥350mil on sales of ¥3,975mil (+8.0% YoY / -4.2% QoQ).

Nippo is eyeing full-year FY23 OP of ¥1,470mil (-4.2% YoY) on sales of ¥15,400mil (+0.4% YoY). Management assumes flattish growth in sales for 1) domestic auto production recovered during 1H but assumes the recovery in production volume will wane from Q3 onwards, and 2) orders for powertrain parts at the factory in Bangkok will also continue to decline from Q3 onwards. The YoY decline in OP is due to upfront investments for growth, such as for further advancements 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 costs of energy and resources.

### Medical and Precision Devices Segment

More than 80% of segment sales is generated from precision equipment parts – the main product is ink jet and laser printer units – and some 20% is from components used in medical equipment. The segment reported 1H OP of ¥79mil (compared to an operating loss of -¥77mil in FY22 1H) on sales of ¥3,358mil (+14.4% YoY).

Nippo provides OEM services for medical equipment parts in its factory in Nakhon Ratchasima [a.k.a. Khorat], Thailand. While the OEM service for medical equipment parts saw solid order trends, the printer parts business was affected by a decline in production by customers due to changes in customers' supply chains and the ongoing supply shortages in semiconductors and electronic parts. As a result, order at the factory in Khorat declined but that was offset but solid orders at Nippo's factories in Vietnam and the Philippines. In Q2 alone, the segment earned OP of ¥43mil (N/A YoY / +19.4% QoQ) on sales of ¥1,630mil (+8.9% YoY / -5.7% QoQ)

Management is guiding for full-year 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. However, although demand for printer-related parts is recovering, and has high seasonality in 2H, the firm remains cautious on the outlook given the uncertainty regarding printer makers' decisions to change production location and volumes. The firm aims to build a production base in Japan for medical equipment parts, which will incur upfront investment costs, thus capping the OP growth in FY23, and plans to start mass production in FY25.

Nippo Sangyo (9913 JP): Sales and OP by Segment (Quarterly)													
(¥mil)		FY21				FY22				FY23			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	YoY (%)	QoQ (%)
Electronics	Sales	4,031	3,983	4,372	4,190	4,139	4,132	4,278	4,125	4,309	4,505	9.0	4.5
	OP	331	320	316	357	306	363	300	276	282	323	-11.0	14.5
	OPM (%)	8.2	8.0	7.2	8.5	7.4	8.8	7.0	6.7	6.5	7.2	-1.6ppt	+0.7ppt
Mobility	Sales	3,391	3,352	3,067	3,282	3,620	3,680	4,507	3,530	4,150	3,975	8.0	-4.2
	OP	307	306	137	292	378	434	362	361	418	350	-19.4	-16.3
	OPM (%)	9.1	9.1	4.5	8.9	10.4	11.8	8.0	10.2	10.1	8.8	-3.0ppt	-1.3ppt
Medical and Precision Equipment	Sales	1,405	1,294	1,528	1,714	1,439	1,497	1,996	1,957	1,728	1,630	8.9	-5.7
	OP	-12	-81	47	29	-14	-63	101	102	36	43	NA	19.4
	OPM (%)	NA	NA	3.1	1.7	NA	NA	5.1	5.2	2.1	2.6	NA	+0.5ppt

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

Nippo Sangyo (9913 JP): Sales and OP by Segment											
(¥mil)		FY18	FY19	FY20	FY21	FY22		FY23			
		FY	FY	FY	FY	FY	YoY (%)	1H	YoY (%)	FY CE	YoY (%)
Electronics	Sales	14,269	17,611	18,263	16,576	16,854	1.7	8,814	4.3	16,900	0.3
	OP	222	994	1,046	1,324	1,245	-5.9	605	-9.6	1,245	0.0
	OPM (%)	1.6	5.6	5.7	8.0	7.4	-0.6ppt	6.9	-1.0pp	7.4	+0.0ppt
Mobility	Sales	17,172	18,303	15,963	13,092	15,337	17.1	8,125	11.3	15,400	0.4
	OP	-34	931	485	1,042	1,535	47.3	768	-5.4	1,470	-4.2
	OPM (%)	NA	5.1	3.0	8.0	10.0	+2.0ppt	9.5	-1.6pp	9.5	-0.5ppt
Medical and Precision Equipment	Sales	7,747	6,896	5,877	5,941	6,889	16.0	3,358	14.4	6,900	0.2
	OP	302	156	-43	-17	126	NA	79	NA	100	-20.6
	OPM (%)	3.9	2.3	NA	NA	1.8	NA	2.4	NA	1.4	-0.4ppt

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 end 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 its 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.

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

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

1. Achieve the following two numerical KPIs:
    - Generate consolidated total OP of ¥5,730mil over FY23~FY25 vs. FY20~FY22 total OP of ¥3,880mil. In the final year (FY25), Nippo aims to achieve consolidated OP of ¥2,000mil (3-yr CAGR +1.5%).
    - ROE of 10.0%+ on average over three years vs previous plan's average of 7.3%.
  2. Introduce Business Portfolio Management
- In order to achieve sustainable earnings growth and enhance enterprise value over the medium-to long term, resources will be allocated to businesses with high growth potential and profitability.
3. Achieve a PBR of 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.
- Shareholders 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 proposal to continue countermeasures against large-scale purchases of the company's shares (i.e., takeover defence measures) was put forward, subject to shareholder approval at the 72nd Ordinary General Meeting scheduled to be held on 23 June 2023. The renewal of the measure was voted for at the June 2023 AGM and is effective until the end of the next AGM in June 2024.

Nippo introduced a 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.

While the firm's Board does not categorically refuse takeovers, the Plan was introduced 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 cases, manufactures under technological license agreements, Nippo 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) the Provision of Necessary Information. Upon submission, 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.

## GENERAL DISCLAIMER AND COPYRIGHT

*This report has been commissioned by Nippo Ltd. (the Sponsor) and prepared and issued by Nippon Investment Bespoke Research UK Ltd (Nippon-IBR), in consideration of a fee payable by the Sponsor. Fees are paid on delivery of the report in cash without recourse. Nippon-IBR may seek additional fees for the provision of follow-up research reports and associated IR services for the client but does not get remunerated for any investment banking services. We never take payment in stock, options, or warrants for any of our services.*

**Accuracy of content:** *All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however Nippon-IBR does not guarantee the accuracy or completeness of this report and has not sought for this information to be independently verified. Opinions contained in this report represent those of the Nippon-IBR analyst at the time of publication. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance, or achievements of their subject matter to be materially different from current expectations.*

**Exclusion of Liability:** *To the fullest extent allowed by law, Nippon-IBR shall not be liable for any direct, indirect, or consequential losses, loss of profits, damages, costs, or expenses incurred or suffered by you arising out or in connection with the access to, use of or reliance on any information contained on this note.*

**No personalised advice:** *The information that we provide should not be construed in any manner whatsoever as, personalised advice. Also, the information provided by us should not be construed by any subscriber or prospective subscriber as Nippon-IBR's solicitation to effect, or attempt to effect, any transaction in a security. The securities described in the report may not be eligible for sale in all jurisdictions or to certain categories of investors.*

**Investment in securities mentioned:** *Nippon-IBR has a restrictive policy relating to personal dealing and conflicts of interest. It does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees, and contractors of Nippon-IBR may have a position in any or related securities mentioned in this report, subject to its policies on personal dealing and conflicts of interest.*

**Copyright:** *Copyright 2023 Nippon Investment Bespoke Research UK Ltd.*

For further enquiry, please contact:

Yumi Yamamoto-Tyrrell

Nippon Investment Bespoke Research UK Ltd

118 Pall Mall

London SW1Y 5EA

TEL: +44 (0)20 7993 2583

Email : [enquiries@nippon-ibr.com](mailto:enquiries@nippon-ibr.com)



Research Beyond Horizons  
Japanese Equity Specialist

- *Nippon Investment Bespoke Research UK Ltd (formerly known as NIB Research UK Ltd.) is registered in England and Wales (9100028) and is authorised and regulated by the Financial Conduct Authority <FRN: 928332>.*