

Nippon Shikizai, Inc.

Summary of Financial Results for the Fiscal Year Ended February 28, 2022 [Japanese Standard] (Consolidated)

Nippon Shikizai, Inc. has announced its consolidated financial results for the fiscal year ended February 28, 2022. Please refer to the contents of the report disclosed below.

Consolidated Financial Results

- **Net sales:** 8,702 million yen (4.8% decrease from the previous period)
- **Operating income/loss:** -267 million yen (—)
- **Ordinary income/loss:** -171 million yen (—)
- **Net income/loss attributable to owners of parent company:** -122 million yen (Net loss attributable to owners of parent company of 848 million yen in the previous period)

Summary of Consolidated Operating Results

During the fiscal year ended February 28, 2022 (March 1, 2021 to February 28, 2022), the direction of the Japanese economy remained shrouded in uncertainty. As COVID-19 lingered interminably (fourth, fifth and sixth waves), the national government issued a declaration of a state of emergency and a state of semi-emergency for Japan's major cities. Vaccination expanded, yet the pandemic continued to exert significant impacts on the Japanese and global economies. Most recently, the continuing spread of the omicron variant prompted efforts to put an end to the pandemic, such as a third vaccine shot. However, the risk remains that further variants will emerge and spread, leading to further declarations of states of emergency and other restrictions on activity. Overseas, a number of factors complicate prospects. In terms of the COVID-19 pandemic, uneven progress was made in each region and country according to rates of vaccination. While some countries moved toward dealing with COVID-19 on an endemic basis, scrapping the use of masks, trends with the omicron and other variants and other considerations fomented lingering uncertainty. Separately, the Russian invasion of Ukraine introduced a new source of concern. Worldwide logistical bottlenecks, rising cost of living and other issues raise concerns of further impacts on economic activity.

The cosmetics industry, which is the domain of operations of Nippon Shikizai Inc., continued to suffer significant impact from the pandemic, led by makeup products. In Japan, personal consumption slumped as mask-wearing became routine and consumers refrained from dining out and other unnecessary outings. Inbound demand failed to recover as the national government continued to tighten entry restrictions. This trend compounded the decline in demand for cosmetics, particularly for makeup. Overseas as well, the continuing spread of the global pandemic depressed demand for cosmetics. Countries and regions that had made progress in vaccination programs were able to relax various anti-pandemic measures, thereby enjoying a resumption of economic activity and a recovery in consumption. However, the emergence of new variants such as the omicron variant put the brakes on recovery in demand for cosmetics in some countries and regions. Overall a mood of uncertainty persisted.

Guided by the Medium-Term Business Strategy Vision, which covers the period FY2017 to FY2021, Nippon Shikizai Group strove to increase productive capacity and accelerate its globalization. Under the greater-than-expected impact of the COVID-19 pandemic and its prolonged impact, however, the Group was obliged to operate in an unforgiving environment. Orders from domestic and overseas cosmetics manufacturers struggled, while factory availability declined due to employees falling ill with COVID-19. To increase productive capacity, the Group had implemented the phase-3 expansion project at Tsukuba Factory and conducted capital investment in overseas subsidiaries, but inability to use the increased capacity persisted. Unavoidably, the Group shut down Suita Factory in

August 2021.

Going forward, the Group expects that new infections will be restrained through continued vaccination and treatments will be developed and introduced for COVID-19 sufferers. However, the timing of the end of the COVID-19 pandemic, and therefore the speed of the anticipated recovery in the domestic cosmetics market, remain unclear. The Group is primarily focused on rebuilding its operating base, to move from an operating loss to a profitable basis and return business results to pre-pandemic levels as soon as possible. The Group has newly drafted a Medium-Term Business Strategy Vision (FY2022–FY2026), aiming to reach its target state for the centenary of Nippon Shikizai in 2030. Over the near term, the Nippon Shikizai Group will seek to respond to customer needs by developing prescription and production technologies that reflect cosmetic trends under the pandemic. Looking to the medium-to-long term, the Nippon Shikizai Group will develop a “clean beauty” approach to cosmetics and respond to the needs of the SDGs and the like. In this way the Group will redouble its efforts to extend its strengths under the new environment and achieve an early recovery in business results.

With the results above as background, the operating results for the consolidated fiscal year under review were as follows.

The Group’s net sales fell 4.8% compared to the previous fiscal year, declining to 8,702 million yen. Key factors in this result included the following: 1) The wearing of masks became ingrained and people refrained from unnecessary outings as measures against COVID-19 infection, reducing consumer demand for makeup cosmetics; 2) Inbound demand from visiting foreign tourists evaporated; and 3) The global spread of the COVID-19 pandemic reduced overseas orders for products, resulting in a generalized slump in orders; moreover, 4) Factory operation geared down amid the outbreak of a delta cluster at Zama Factory and infection of some employees with the omicron variant, which obliged some employees to wait at home; 5) Material arrivals and shipments were delayed due to logistical congestion, impacting production and logistics; and 6) Impact of COVID-19 on the Group’s consolidated subsidiary in France reduced revenues from that source.

Despite strenuous efforts to cut costs amid declining net sales, the Group recorded losses in the period under review. The completion of the phase-3 expansion project at Tsukuba Factory engendered increases in various costs, resulting in an operating loss of 267 million yen (compared with a loss of 831 million yen in the previous fiscal year). Thanks to appropriation of 166 million yen in subsidy income, ordinary loss eased to 171 million yen, compared with ordinary loss of 588 million in the previous fiscal year. Net loss attributable to owners of parent company was 122 million yen (improved from net loss attributable to owners of parent company of 848 million yen in the previous fiscal year), as the Group appropriated extraordinary income of 83 million yen from sales of fixed assets arising from the closure of Suita Factory.

Segment Business Information by Region

(Japan)

As described above, demand for cosmetics products in Japan and worldwide struggled amid the COVID-19 pandemic. Orders from domestic and overseas cosmetics manufacturers tumbled, and production and logistics were also impacted. Net sales declined 4.1% from the previous fiscal year to 6,563 million yen. In earnings, despite strenuous efforts to cut costs amid declining net sales, various costs increased in connection with the phase-3 expansion project at Tsukuba Factory. The Group recorded an operating loss of 285 million yen (against an operating loss of 964 million yen in the previous fiscal year).

(France)

Europe, where the Company's French subsidiary, Thépenier Pharma & Cosmetics S.A.S. ("Thépenier"), is located, suffered an economic downturn during its fiscal year (January to December 2021) due to the COVID-19 pandemic. This state of affairs affected both Thépenier's medical and cosmetics operations. Net sales dropped 7.2% from the previous fiscal year to 2,201 million yen. In earnings, factors such as the decrease in net sales and an increase in expenses from capital investments caused operating income to contract 85.7% from the previous fiscal year, to 17 million yen.

Outlook

In the business environment of the coming fiscal year, ongoing trends in the COVID-19 pandemic and the measures taken to counteract it are forecast to continue to impact deeply the economies of each country and the demand for cosmetics in each. The new modes of living ushered in by the COVID-19 pandemic (in Japan, these include the normalization of mask-wearing and an increase in working from home) are influencing consumers' needs for cosmetics, changing that demand not only quantitatively but qualitatively as well. To respond to these changes in the market, cosmetics ODM manufacturers will need to offer new prescriptions that serve emerging consumer needs and develop prescriptions that add new value. At the same time, these manufacturers must move forward with preparing strategies anticipating the move to the endemic (post-COVID-19) phase. The Nippon Shikizai Group believes that these approaches will be vital for cosmetics ODM manufacturers to effect recovery of business results and drive renewed growth.

Against this background, the Group's new Medium-Term Business Strategy Vision (FY2022–FY2026) calls for the reconstruction of the Nippon Shikizai Group's business foundations, orienting them toward post-COVID-19 recovery and future growth. Key strategies for achieving this Vision include strengthening and expansion of products with a strong competitive edge; vigorous pursuit of the "clean beauty" market; and transformation into a highly profitable constitution. The Group will aggressively pursue efforts on all of these fronts.

The COVID-19 pandemic casts a long shadow over the Group's forecast of consolidated business results for the upcoming fiscal year (fiscal year ending February 28, 2023). While orders received will remain dramatically lower than their levels before the pandemic began, signs of recovery are beginning to flicker into life. Moreover, though prospects remain uncertain, the Group recognizes that the advance and continuation of vaccination and the introduction of effective treatments are gradually lessening the risk of another major downturn. Under these conditions, the Group forecasts an increase in full-year net sales of 20.3% over the previous fiscal year to 10,465 million yen. In earnings, as various cost-cutting measures and the like continue, the Group forecasts operating income of 191 million yen, ordinary income of 105 million yen and net income attributable to owners of parent company of 136 million yen.

Given uncertainty over the severity and chronological extent of the effects of the COVID-19 pandemic and the impact of the Russian invasion of Ukraine, the Group's forecast of consolidated business results for the upcoming fiscal year (fiscal year ending February 28, 2023) is subject to change.

(%: change in full year from the previous year or in 2nd quarter (cumulative) from the same period previous year)

	2nd quarter (cumulative) (increase/decrease)	Full year (increase/decrease)
Net sales	5,318 million yen (Up 22.1%)	10,465 million yen (Up 20.3%)
Operating income	129 million yen (—)	191 million yen (—)
Ordinary income	88 million yen (—)	105 million yen (—)
Net income attributable to owners of parent company	60 million yen (—)	136 million yen (—)
Net income per share	29.08 yen	65.24 yen

Basic Policy on Distribution of Earnings and Dividends in the Period Under Review and Next Period

The Nippon Shikizai Group regards the improvement of capital efficiency and the return of earnings to shareholders as two of its most important management issues. The Group's basic policy on dividends is to maintain continuous and stable dividend payout. As such, dividends are distributed in response to growth in business results.

With respect to the distribution of dividends at the end of the consolidated fiscal year, as originally forecast, no year-end dividend is distributed for the period under review, due to the appropriation of a net loss attributable to owners of parent company. In the upcoming fiscal year (fiscal year ending February 28, 2023) as well, the Group expects not to distribute a year-end dividend. This is because, despite the positive figure cited for net income attributable to owners of parent company in the forecast of consolidated business results for the upcoming fiscal year above, trends in the impact from COVID-19 remain unclear.

[Appendix]
Consolidated Financial Statements
(1) Consolidated Balance Sheet

(Thousands of yen)

	At February 28, 2021	At February 28, 2022
ASSETS		
Current Assets		
Cash and deposits	1,078,582	1,323,082
Notes and accounts receivable - trade	1,504,068	1,638,184
Electronically recorded monetary claims - operating	125,004	194,216
Merchandise and finished goods	755,809	691,181
Work in process	164,377	194,678
Raw materials and supplies	943,818	819,854
Other	147,716	149,917
Total Current Assets	4,719,378	5,011,114
Non-current Assets		
Property, Plant and Equipment		
Buildings and structures	10,173,062	10,025,487
Accumulated depreciation	(4,915,046)	(4,975,756)
Buildings and structures, net	5,258,016	5,049,730
Machinery, equipment and vehicles	4,649,757	4,686,827
Accumulated depreciation	(3,022,116)	(3,222,484)
Machinery, equipment and vehicles, net	1,627,640	1,464,342
Tools, furniture and fixtures	1,048,155	1,059,234
Accumulated depreciation	(734,582)	(793,694)
Tools, furniture and fixtures, net	313,573	265,540
Land	2,155,986	2,139,815
Construction in progress	126,652	108,088
Total Property, Plant and Equipment	9,481,869	9,027,517
Intangible Assets	372,306	331,277
Investments and Other Assets		
Investment securities	491,338	416,453
Other	493,823	568,211
Allowance for doubtful accounts	(7,966)	(773)
Total Investments and Other Assets	977,195	983,891
Total Non-current Assets	10,831,371	10,342,686
Total Assets	15,550,749	15,353,800

(Thousands of yen)

	At February 28, 2021	At February 28, 2022
LIABILITIES		
Current Liabilities		
Notes and accounts payable - trade	371,459	525,136
Electronically recorded obligations - operating	447,214	555,230
Short-term loans payable	1,855,408	2,169,279
Lease obligations	94,714	85,233
Provision for bonuses	41,166	34,964
Other	738,017	741,813
Total Current Liabilities	3,547,981	4,111,658
Non-current Liabilities		
Long-term loans payable	8,099,696	7,564,323
Lease obligations	481,344	398,022
Provision for directors' retirement benefits	146,430	146,430
Net defined benefit liability	70,121	91,629
Other	114,472	91,331
Total Non-current Liabilities	8,912,064	8,291,736
Total Liabilities	12,460,046	12,403,395
NET ASSETS		
Shareholders' Equity		
Capital stock	714,104	714,104
Capital surplus	943,209	943,209
Retained earnings	1,220,652	1,098,620
Treasury shares	(3,857)	(3,857)
Total Shareholders' Equity	2,874,109	2,752,077
Accumulated Other Comprehensive Income		
Valuation difference on available-for-sale securities	254,893	202,507
Foreign currency translation adjustment	(38,299)	(4,180)
Total Accumulated Other Comprehensive Income	216,593	198,327
Total Net Assets	3,090,703	2,950,405
Total Liabilities and Net Assets	15,550,749	15,353,800

(2) Consolidated Statement of Income

(Thousands of yen)

	Fiscal year ended February 28, 2021	Fiscal year ended February 28, 2022
Net Sales	9,143,569	8,702,029
Cost of Sales	8,741,022	7,897,785
Gross Profit	402,547	804,243
Selling, General and Administrative Expenses	1,234,290	1,072,153
Operating Income (Loss)	(831,743)	(267,909)
Non-operating Income:		
Interest income	2,106	2,478
Dividend income	6,889	6,807
Subsidy income	285,045	166,485
Insurance income	8,509	-
Miscellaneous income	23,073	29,051
Other	15,354	7,689
Total Non-operating Income	340,979	212,512
Non-operating Expenses:		
Interest expenses	98,010	109,830
Other	183	5,846
Total Non-operating Expenses	98,193	115,677
Ordinary Income (Loss)	(588,958)	(171,074)
Extraordinary Income:		
Gain on sales of non-current assets	-	83,964
Total Extraordinary Income	-	83,964
Extraordinary Losses:		
Loss on retirement of non-current assets	215	4,860
Impairment loss	94,102	-
Loss on closing of factory	34,402	-
Loss on withdrawal of corporate pension funds	-	19,729
Total Extraordinary Losses	128,720	24,590
Income (Loss) before Income Taxes	(717,678)	(111,700)
Income taxes - current	42,172	10,331
Income taxes - deferred	88,819	-
Total Income Taxes	130,991	10,331
Net Income (Loss)	(848,670)	(122,031)
Net Income (Loss) Attributable to Owners of Parent Company	(848,670)	(122,031)

Consolidated Statement of Comprehensive Income

(Thousands of yen)

	Fiscal year ended February 28, 2021	Fiscal year ended February 28, 2022
Net income (loss)	(848,670)	(122,031)
Other Comprehensive Income		
Valuation difference on available-for-sale securities	32,288	(52,385)
Foreign currency translation adjustment	33,825	34,119
Total Other Comprehensive Income	66,114	(18,266)
Comprehensive Income	(782,555)	(140,297)
(Breakdown)		
Comprehensive income attributable to owners of parent company	(782,555)	(140,297)
Comprehensive income attributable to non-controlling interests	-	-

(3) Consolidated Statement of Changes in Equity

Fiscal year ended February 28, 2021

(Thousands of yen)

	Shareholders' equity				
	Capital stock	Capital surplus	Retained earnings	Treasury shares	Total shareholders' equity
Balance at beginning of current period	714,104	943,209	2,121,719	(3,857)	3,775,176
Changes of items during period					
Dividends of surplus			(52,396)		(52,396)
Net income (loss) attributable to owners of parent company			(848,670)		(848,670)
Net changes of items other than shareholders' equity					
Total changes of items during period	-	-	(901,066)	-	(901,066)
Balance at end of current period	714,104	943,209	1,220,652	(3,857)	2,874,109

	Accumulated other comprehensive income			Total net assets
	Valuation difference on available-for-sale securities	Foreign currency translation adjustment	Total accumulated other comprehensive income	
Balance at beginning of current period	222,604	(72,125)	150,479	3,925,655
Changes of items during period				
Dividends of surplus				(52,396)
Net income (loss) attributable to owners of parent company				(848,670)
Net changes of items other than shareholders' equity	32,288	33,825	66,114	66,114
Total changes of items during period	32,288	33,825	66,114	(834,952)
Balance at end of current period	254,893	(38,299)	216,593	3,090,703

Fiscal year ended February 28, 2022

(Thousands of yen)

	Shareholders' equity				
	Capital stock	Capital surplus	Retained earnings	Treasury shares	Total shareholders' equity
Balance at beginning of current period	714,104	943,209	1,220,652	(3,857)	2,874,109
Changes of items during period					
Net income (loss) attributable to owners of parent company			(122,031)		(122,031)
Net changes of items other than shareholders' equity					
Total changes of items during period	-	-	(122,031)	-	(122,031)
Balance at end of current period	714,104	943,209	1,098,620	(3,857)	2,752,077

	Accumulated other comprehensive income			Total net assets
	Valuation difference on available-for-sale securities	Foreign currency translation adjustment	Total accumulated other comprehensive income	
Balance at beginning of current period	254,893	(38,299)	216,593	3,090,703
Changes of items during period				
Net income (loss) attributable to owners of parent company				(122,031)
Net changes of items other than shareholders' equity	(52,385)	34,119	(18,266)	(18,266)
Total changes of items during period	(52,385)	34,119	(18,266)	(140,297)
Balance at end of current period	202,507	(4,180)	198,327	2,950,405

(4) Consolidated Statement of Cash Flows

(Thousands of yen)

	Fiscal year ended February 28, 2021	Fiscal year ended February 28, 2022
Cash Flows from Operating Activities:		
Income (loss) before income taxes	(717,678)	(111,700)
Depreciation	812,745	785,250
Impairment loss	94,102	-
Increase (decrease) in provision for bonuses	(37,441)	(6,202)
Increase (decrease) in net defined benefit liability	3,422	19,445
Increase (decrease) in allowance for doubtful accounts	(72,917)	(7,367)
Interest and dividend income	(8,996)	(9,285)
Interest expenses	98,010	109,830
Loss (gain) on sales of non-current assets	-	(83,964)
Loss on retirement of non-current assets	215	4,860
Decrease (increase) in notes and accounts receivable - trade	794,962	(191,556)
Decrease (increase) in inventories	246,154	167,710
Increase (decrease) in notes and accounts payable - trade	(783,546)	258,175
Increase (decrease) in accounts payable - other	(329,460)	22,201
Increase (decrease) in accrued consumption taxes	320,393	(52,466)
Other	80,961	(25,725)
Subtotal	500,929	879,203
Interest and dividend income received	7,898	12,881
Interest expenses paid	(97,880)	(110,221)
Income taxes (paid) refund	(5,427)	(525)
Net Cash Provided by Operating Activities	405,520	781,337

(Thousands of yen)

	Fiscal year ended February 28, 2021	Fiscal year ended February 28, 2022
Cash Flows from Investing Activities:		
Payments into time deposits	(80,000)	(180,000)
Proceeds from withdrawal of time deposits	80,000	200,122
Purchase of property, plant and equipment	(1,902,917)	(239,885)
Proceeds from sales of property, plant and equipment	-	103,340
Purchase of intangible assets	(66,840)	(8,185)
Purchase of investment securities	(2,535)	(598)
Purchase of shares of unconsolidated subsidiaries	-	(11,772)
Net decrease (increase) in short-term loans receivable	(1,662)	-
Payments of long-term loans receivable	(113,440)	(78,487)
Collection of long-term loans receivable	10,271	27,596
Net Cash Used in Investing Activities	(2,077,124)	(187,871)
Cash Flows from Financing Activities:		
Net increase (decrease) in short-term loans payable	75,640	129,870
Proceeds from long-term loans payable	3,460,232	1,461,238
Repayments of long-term loans payable	(1,508,397)	(1,834,188)
Repayments of lease obligations	(101,849)	(95,136)
Cash dividends paid	(52,637)	(11)
Other	-	(3)
Net Cash Provided by (Used in) Financing Activities	1,872,988	(338,231)
Effect of Exchange Rate Change on Cash and Cash Equivalents	3,627	8,095
Net Increase (Decrease) in Cash and Cash Equivalents	205,012	263,330
Cash and Cash Equivalents at Beginning of Period	754,545	959,557
Cash and Cash Equivalents at End of Period	959,557	1,222,888

(5) Segment Information

Performance by Business Segment

Year Ended February 28, 2022 (March 1, 2021 to February 28, 2022)

(Thousands of yen)

	Reporting Segment			Adjustment Amount (Notes 1, 2)	Consolidated Financial Statements Amount (Note 3)
	Japan	France	Total		
Sales					
Sales to outside customers	6,501,063	2,200,965	8,702,029	-	8,702,029
Internal sales and transfers between segments	62,677	375	63,052	(63,052)	-
Total	6,563,741	2,201,341	8,765,082	(63,052)	8,702,029
Segment income (loss)	(285,416)	17,612	(267,804)	(105)	(267,909)
Segment assets	13,422,317	2,785,863	16,208,181	(854,380)	15,353,800
Other items					
Depreciation	599,745	185,504	785,250	-	785,250
Increase of property, plant and equipment and intangible assets	83,044	182,763	265,807	-	265,807

Notes: 1. The adjustment amount of negative 105 thousand yen in segment income (loss) is an elimination of transactions between segments.

2. The adjustment amount of negative 854,380 thousand yen in segment assets is a reflection of consolidated adjustment between segments.

3. The segment income (loss) is adjusted with operating loss on the consolidated financial statements.

(Major Subsequent Events)

(Reduction of the Amount of Capital Stock)

At the April 12, 2022 meeting of the Board of Directors, the Company resolved to table a motion at the upcoming 65th Ordinary General Meeting of Shareholders, scheduled for May 25, 2022, to reduce the amount of capital stock.

1. Purpose of Reducing the Amount of Capital Stock

The COVID-19 pandemic has significantly perturbed the Group's business results and financial position. To ensure flexibility and maneuverability in capital policy and secure a sound financial base, the Group is reducing its capital stock and transferring the entire amount of reduction of capital stock to other capital surplus, in accordance with Article 447, Paragraph 1 of the Companies Act. This transfer does not change the total number of shares issued or the amount of net assets and so does not affect the number of shares held by shareholders or the amount of net assets per share.

2. Procedures for Reduction of the Amount of Capital Stock

1) Amount of reduction of capital stock

Capital stock is reduced by 614,104,050 yen, from 714,104,050 yen to 100,000,000 yen.

2) Method of reduction of the amount of capital stock

The entire amount of reduction of capital stock is transferred to other capital surplus.

3. Schedule for Reduction of Amount of Capital Stock

1) Date of resolution of Board of Directors	April 12, 2022
2) Date of resolution of the ordinary general meeting of shareholders	May 25, 2022 (scheduled)
3) Date of call for statement of objections by creditors	May 27, 2022 (scheduled)
4) Final date for statement of objections by creditors	June 30, 2022 (scheduled)
5) Effective date of reduction of amount of capital stock	July 1, 2022 (scheduled)

4. Future Prospects

This action is a transfer from one accounting item to another under Net Assets in the balance sheet. As such, the action does not change the amount of net assets and its effect on the business results of the Group is negligible. The implementation of this action is subject to the approval of the general meeting of shareholders.