

February 4, 2022

NSK Ltd. Q&A Summary – Fiscal 2021 Q3 Financial Conference (Year Ending March 31, 2022)

Q1:

Demand for machine tools and semiconductor manufacturing equipment has been very strong. I would like to ask about the future supply situation.

A1:

During the previous peak period (2017-2018), we increased production capacity of our precision bearings and ball screws. Thanks to the effects of the expanded facilities, productivity improvements, and the availability of personnel, we believe that we will be able to supply enough to meet demand from the fourth quarter and beyond to the first quarter of the next fiscal year.

Q2:

What is the status of passing on rising raw material prices to sales prices? Will you be able to catch up? If there is a delay in passing on the cost, we would like to know if there is a need for additional measures.

A2:

There is a time lag of three months at the least, and usually about six months, depending on the timing of negotiations with automotive OEMs in particular, regarding the transfer of increased steel prices to sales prices. As of the end of the fiscal year, we expect to be able to pass on up to 80-90% of the steel price increases that we forecasted at the end of the second quarter. We will continue to negotiate for the unachieved portions and further increases in steel prices, and we believe that we can catch up. On the other hand, we will not be able to absorb the impact of the current increase in costs for transportation, electricity, sub-materials, etc., other than steel materials through our efforts alone, and we will need to pass these costs on to sales prices in new ways.

Q3:

Is it likely that you will be able to pass on the increased costs of transportation and other items other than steel materials to sales prices in the next fiscal year?

A3:

Yes. There is a formula for reflecting the selling price of steel materials, but inflation in other costs such as transportation, electricity, and sub-materials will be an issue from next fiscal year. So far, we have been able to absorb these costs through cost reductions, but we believe that further negotiations will be necessary.

Q4:

Although sales increased this quarter in the industrial machinery business, profitability is not in step. Is it correct to assume that profitability will return to double digits when the business environment settles down in the next fiscal year?

A4:

Profitability improvement has been slightly delayed due to the impact of rising transportation costs and steel prices, and we will make up for it through price increase negotiations in the fourth quarter. Also, productivity was an issue in the third quarter, and the increase in the number of employees did not lead to output. If demand is maintained and output increases, we believe we will be able to maintain a double-digit operating income ratio.

Q5:

What is the background of the impairment loss and structural reform in the steering business?

A5:

We are in the process of formulating a mid-term management plan that will start next fiscal year. In the process, we determined that it would be difficult to recover to the volume we had originally thought and that we would not be able to generate sufficient cash flow. As a result, we recorded an impairment loss. At this time, we decided to take significant measures to reform our business structure.

Q6:

Will the steering business remain a core business? Are you going to reevaluate the position of the steering business once again?

A6:

Yes. It will continue to be a core business and we will return it to profitability. There is no change in our strategy to ensure that this business will generate value in the future.

Q7:

How do you see the impact of the impairment loss, structural reform expenses, and depreciation and amortization in the steering business? What effect do you expect from in the next fiscal year and beyond?

A7:

The reduction in depreciation and amortization from the next fiscal year onward due to the impairment loss will be about 2 billion yen, and we hope to improve profits by more than 10 billion yen on an annualized basis through the transfer of production, cost reduction efforts at each site, and reallocation of human resources. Note that this profit improvement effect includes the reallocation of human resources within the company, so it does not mean that 10 billion yen will directly result in profit generation for the entire company.

Q8:

What do you think about the profit outlook for the steering business? Considering the balance between growth potential and profitability, will your position remain unchanged even if you take into account the balance between EVs, wind power, small-sized bearings and other fields with growth potential?

A8:

The steering business is an important business, and its value will not change due to our system unit development know-how and our commitment to safety and cutting-edge automotive technologies. As part of the business reform, we plan to allocate personnel involved in the development of some technologies related to the steering business to core technology development and growth areas (new EV product development and digital technology related). Since we have people with high IT expertise in the development unit of the steering business, we would like to use their help in the next mid-term business plan to advance our digital twin technology and digitalization of production.

Q9:

Is there any change in the profit margin of around 5% for steering systems?

A9:

No change. We will work on returning to profitability in the next one or two years, and with VW's business coming in, etc., we plan to see a turnaround in volume in 2023, and then continue to step up in 2024, 2025, and 2026.

Q10:

What will you focus on in the steering business, how large will it be, and what do you want to achieve strategically?

A10:

The strategy of the 6th Mid-term Management Plan was to expand the product line through the development of downstream assist products and to recover by winning new orders. Although we have completed the development of a rack type EPS (which is downstream assist), we have not yet received any orders. As for the path to recovery as a core business, we would like to go with a two-pronged approach: column type and pinion type. In addition, in order to compete in the steering market, we believe that we need to create a path to achieve a reasonable scale of sales.

Q11:

In terms of the product lineup, will you be focusing on the column type and pinion type?

A11:

Yes. We will concentrate on the column and pinion types, and draw a picture of the future that will allow us to secure a volume that will keep us in the black, and we will also look for opportunities to collaborate so that we can compete with a full lineup.

Q12:

In relation to the structural reform of the steering business and the reorganization of worksites, how many steering related worksites are there? Also, if there is a possibility that sales will return, won't it be counterproductive to change your production structure?

A12:

We have nine major steering plants. The number of plants is the same as that of the past peak, so we believe that we can cope with the future sales recovery.

Q13:

Is the level of operating income for the next fiscal year expected to return to the level of the initial plan for the current fiscal year?

A13:

Our basic policy is to return to the level of the initial plan, but due to various uncertainties in the business environment, etc., we cannot give you an answer now.

Q14:

I would like to know if there is a possibility of a share buyback and what your thoughts are on this. If there is an assumption that profits will return in the next fiscal year, taking into account the current stock price situation and the price-to-book ratio and the state of the balance sheet, we could send a positive message to the market.

A14:

We consider share buybacks on an ongoing basis. Even if we wanted to, we would not be able to do so unless we meet the following conditions: we are generating cash, the stock price is undervalued, and we are not planning a major investment.