

# Business Report 2013

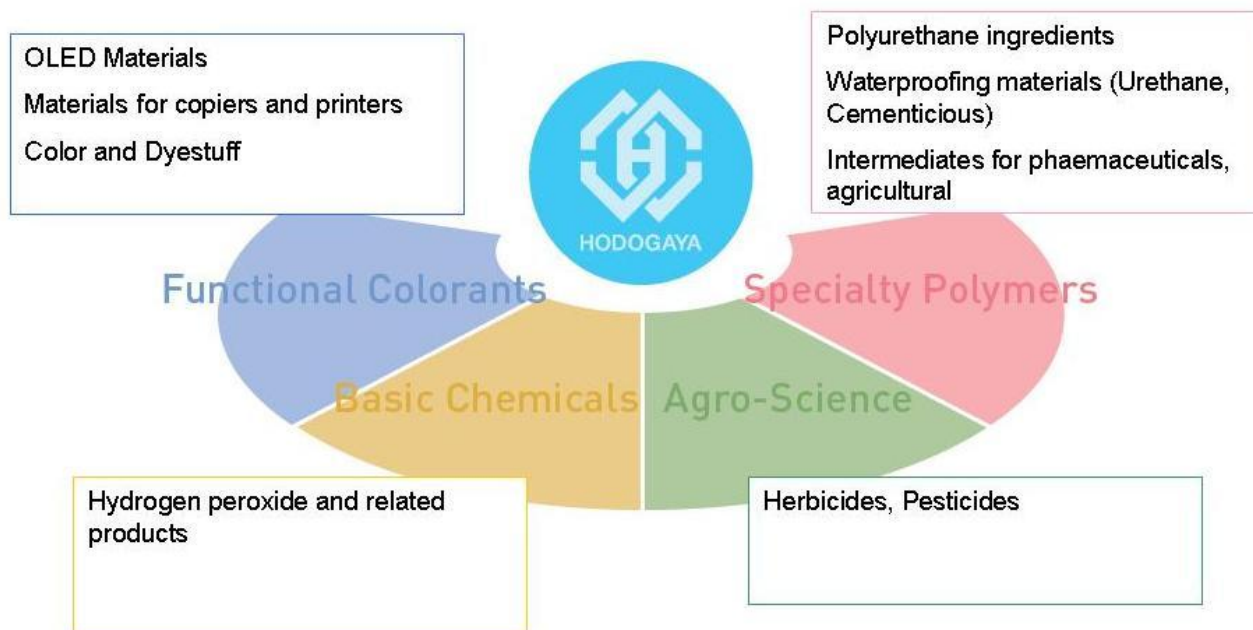
April 1, 2013 - March 31, 2014

## Hodogaya Chemical Group: Management Philosophy

Through constant innovation of chemical technology, we will provide high-quality products and services throughout the world and contribute to the creation of an environmentally conscious society.

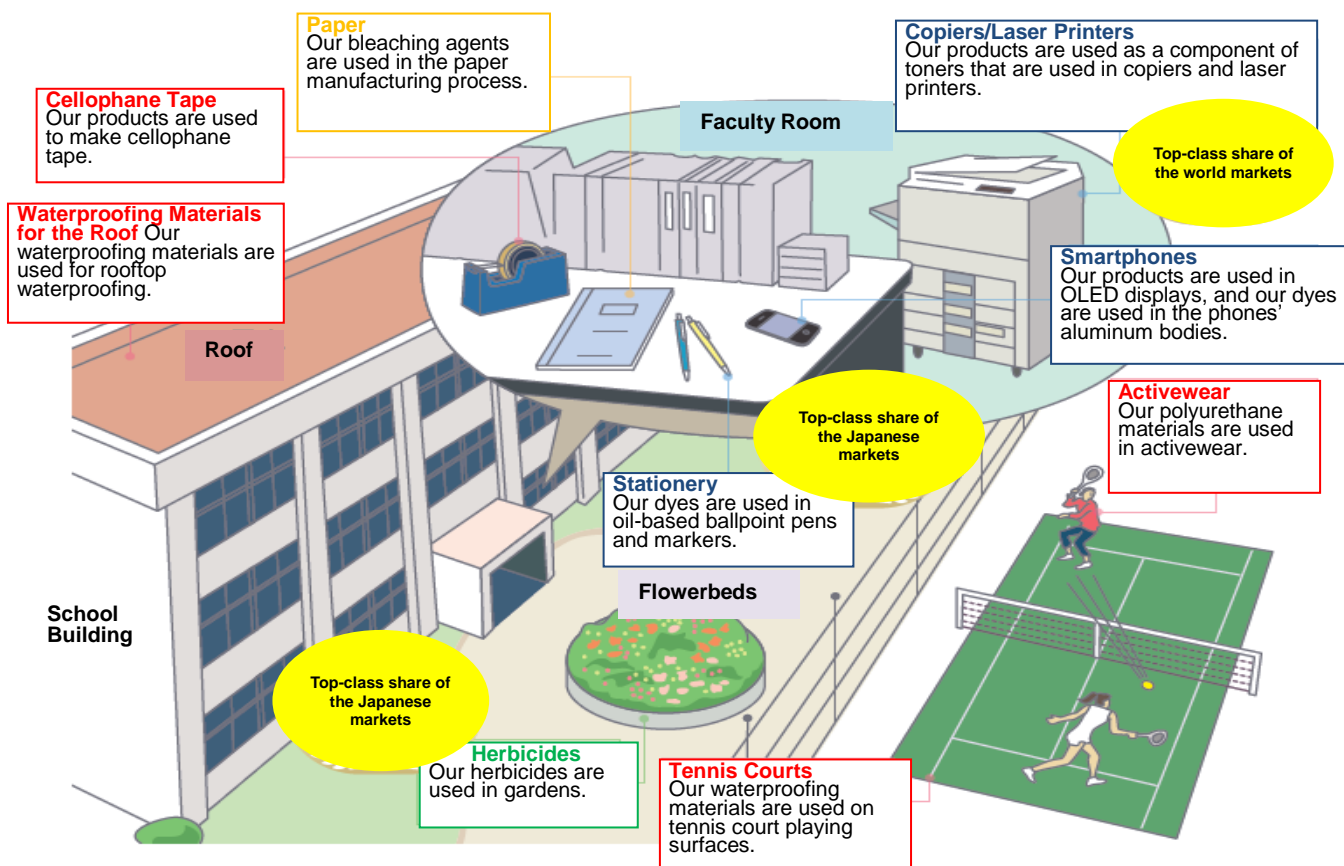
## Business Overview

One of the things that make the Hodogaya Chemical group unique is that in each sector, whether it is Functional Colorants, Specialty Polymers, Basic Chemicals, Agro-Science, or Logistics, etc., there is a highly specialized group company. With Research & Development, Manufacturing, and Sales working together in a Trilateral Business Plan, we are able to meet the various needs of our customers quickly, and with products and service of the highest quality.



## Series: Hodogaya Chemical is in Your World Part 1: In the School

Chemistry is used to create many of the materials that form the foundations of our society and our modern lifestyle. Chemistry is at the heart of everything from fashion to food, furniture to housing, pharmaceuticals to the latest IT equipment. From the time it was founded over 97 years ago, the Hodogaya Chemical group has used its high-level skills in chemical technology to meet the needs of each era and bring dreams of the future to life. Let's look at a few examples.



## Message from our President

**With steady determination and a bold action plan, we have built a strong foundation for future growth.**

As our Group approaches its 100th anniversary in 2016, we have worked towards completing a strong foundation for future growth with our mid-term management plan, “HONKI 2013”, which we launched in 2011. Though the business environment remained harsh in this final year of the plan, we were able to maintain a steady vision of the company we want to be at our 100th anniversary, and devote ourselves to various initiatives, such as strengthening core businesses and new business development.

I would like to take this opportunity to let you know about our results for FY 2013 (April 1, 2013 – March 31, 2014), and our prospects for the future.

Toshikazu Kitano  
President and CEO  
July 2014

### **FY 2013: Consolidated Results (Millions of Yen)**

	FY 2013 Results	Changes Gains/Losses
Net Sales	35,687	+1.4%
Operating Income	34	△96.2%
Ordinary Income (△=losses)	△310	-
Net Income (△=losses)	△1,271	-

### **Highlights of FY 2013(ending in March, 2014)**

In the final year of our mid-term management plan, we worked on various initiatives.

Looking back at the financial climate of 2013, future prospects remained uncertain in Japan as the gradual recovery that was spurred by the government’s fiscal and monetary policies, increased personal consumption due to last-minute demand in advance of the sales tax increase, and improved employment figures were countered by rising raw material and fuel prices as a result of the weakening Japanese yen.

It was under these conditions that our Group approached the final year of our mid-term management plan “HONKI 2013” (**H**odogaya as **O**nly one, **N**umber one with our **K**ey technology and **I**magination). As part of “HONKI 2013”, we merged with Nippon Peroxide Co., Ltd. to bolster one of ‘Core Businesses’ Hydrogen Peroxide and related products. With this merger, we were

able to reduce costs at our Koriyama plant. In the area of 'Growth Businesses', we ramped up production at SFC CO., LTD. (Republic of Korea) in preparation for new developments in the OLED business.

Consolidated sales for the year grew to 35,687 million yen, an increase of 496 million yen over the previous year.

The OLED and Hydrogen Peroxide businesses were adversely affected by increasingly severe cost competition, but revenues increased due to growing demand in the Polymer Materials, Construction Materials, and Specialty Chemicals businesses, as well as strong performance by home garden herbicides in the Agro-Science business.

In terms of profit and loss, our efforts to cut costs did make an impact, but operating income was down by 864 million yen from last year, at 34 million yen, due to the weakening yen's impact on raw material and fuel costs and increased research costs. Ordinary losses came to 310 million yen (last year's ordinary income was 611 million yen), and our net losses came to 1,271 million yen (last year's net losses were 90 million yen) because of an extraordinary loss we posted in connection with carbon nanotube development work.

Upon consideration of performance trends, future business development, and unquantifiable risks, etc., we set the year-end dividend at 2 yen per share. With the mid-term dividend of 2 yen per share, the annual dividend comes to 4 yen per share.

### March, 2014 Financial Statement: Points of Interest

- POINT 1: Increased revenue from the Functional Polymers and Agro-Science businesses as a result of increased demand.
- POINT 2: Reduced revenue in the Functional Colorants and Basic Chemicals segments, due to increased competition.
- POINT 3: Reduced operating income as a result of increased raw material prices and research costs. Net profits for the period were reduced by an extraordinary loss related to carbon nanotubes.

## **An overview of our mid-term management plan**

Although some numerical targets were not reached, we successfully ‘planted seeds’ for the future.

As our Group approaches its 100th anniversary in 2016, our vision of what we want to be is “a corporation that steadily supplies ‘Only One/Number One’ materials in the global and niche markets,” and to this end, we have taken up the challenges of our mid-term management plan, “HONKI 2013”(Hodogaya as **O**nly one, **N**umber one with our **K**ey Technology and **I**magination) since 2011. The “HONKI 2013” plan provides for the creation of a strong foundation for future growth by 2013, as well as the fortification of each category of business (Core, Growth, Cultivation and New Product Creation); in FY 2013, the final year of the plan, a number of initiatives were implemented in pursuit of these goals.

In order to focus on ‘strengthening core businesses’ , ‘business expansion and new business creation’ and ‘strengthening our corporate structure’ under “HONKI 2013” , our Group implemented a broad array of management initiatives. However, we faced business conditions that were harsher than we had expected, and as a result, our Group’s performance over the past three years suffered.

Under these extremely harsh conditions, it took more time than expected to reap the results of our various initiatives, and so, we unfortunately were unable to reach our numerical (sales) targets. On the other hand, we did successfully implement all of the measures we had planned for the three-year period.

### ● **“Core Businesses”**

With regard to existing businesses such as Imaging Materials and Hydrogen Peroxide, etc., we devoted our energies to reducing costs. The Yokohama office of Hodogaya Logistics Co., Ltd. (in our Yokohama plant) added three hazardous materials warehouses, making it even better able to handle hazardous materials logistics. In addition, to strengthen the Hydrogen Peroxide and related products businesses, we merged with Nippon Peroxide Co., Ltd. on July 1, 2013.

### ● **“Growth Businesses”**

To step up efforts to expand the OLED business, we fortified our Research and Development capabilities, strengthened our collaboration with SFC Co., Ltd. (Republic of Korea) and increased SFC’s manufacturing capacity. In the Imaging Materials business, we added manufacturing facilities for new high-performance, environmentally friendly CCA (charge control agents for toner). We also worked closely with customers in the ink jet printer dyes and color treatment dyes (for hair color) sectors to develop new products and bring them to market.

- **“Cultivation Businesses”**

Drawing on the knowledge we have acquired from existing products, we embarked on projects such as the development of CCA for chemical toners, toner-related materials, and new polyols.

- **“New Product Creation”**

We kicked off a ‘New Product Exploration Project’ at our Tsukuba Research Center. The project team is exchanging information with Japanese governmental organizations and universities and investigating research topics focused on the environment and energy.

- **“Strengthening Our Corporate and Global Structure”**

In May, 2012, we consolidated our Group headquarter functions in Yaesu, Tokyo to solidify our Group-wide management structure. We have also approached the issue of strengthening the corporate structure from various angles, establishing, for example, local offices in Korea and Shanghai to boost sales capacity, and entering into a collaborative relationship with Jai Research Foundation in India.

Looking forward to our 100th anniversary in 2016, we will concentrate on fully integrating the effects of the initiatives we have implemented. As we look toward increasing sales, profits, and speed, we will also be working internally to absorb the burdens imposed by the measures we implemented as we push toward our vision of what we want to be: “a corporation that steadily supplies ‘Only One/Number One’ materials in the global and niche markets.”

## Forecast for FY 2014

**This is the Group’s ‘year of rebuilding’, in which we strive for profitability with firm resolve.**

The environment in which our Group businesses have had to operate for the last few years has been extremely harsh, and despite our best efforts, 2013 marked the second year in a row in which we ended the fiscal year in the red.

We consider 2014 to be our ‘year of rebuilding’. With a steady focus on expanding sales efforts and cutting costs, refining the research and development selection and focus process to bring new products to market more quickly, preparing our workforce for global business, and technology succession, we will make a strong push for profitability, never forgetting meanwhile that safety comes first.

The forecasted consolidated results for FY 2014 are as follows: 36,500 million yen in sales (an increase of 2.3%), 600 million yen in operating income, 150 million yen in ordinary income, and 100 million yen in net income. The annual dividend is expected to be 4 yen per share.

I thank our shareholders for their continuing support.

## Overview By Business Segment

### **Functional Colorants**

Although demand for printer materials continues to be sluggish, the Imaging Materials business held steady, thanks in part to the weakened yen.

The Dyes and Colors business was boosted by new color treatment dyes that came to market and progress made in aluminum dye inventory adjustment, finishing on a par with last year's results despite continued weak demand for small digital home appliance products.

The OLED business saw decreased revenues as a result of increasingly severe competition and a temporary increase following a subsidiary company's change of accounting period in the previous fiscal year.

Sales in this segment came to 8,993 million yen, with operating losses of 1,204 million yen.

Imaging Materials	CCA (Charge Control Agents), a critical component of toner. Materials for the OPC (Organic Photo Conductors) drums that are central to copiers and laser printers. Dyes for ink jet printers
Color and Dyestuff	Dyes for coloring aluminum, high-end stationery products and various inks. Hair Coloring Agents Colorants for processed foods and cosmetics, etc.
OLED Materials	Hole Transport Materials and other principal components of organic EL displays and lights.

### **Specialty Polymers**

Revenues increased in the Polymer Materials business, thanks to strong performance by PTG (an ingredient of polyurethane), and greatly increased demand for adhesive products overseas.

Strong performance was also seen in the Construction Materials business, with sales of urethane waterproofing materials and waterproofing construction benefiting from the jump in demand that preceded the sales tax increase.

Sales in the Specialty Chemicals business grew as a result of steady demand in the polymer-related, pharmaceutical and contract manufacturing areas.

Sales in this segment came to 12,661 million yen, with operating income of 356 million yen.

Functional Polymers	Materials for clothing, automobiles, industrial components, leisure products, etc. Adhesive Release Agents
Construction Materials	Urethane waterproofing materials (for building and parking structure roofs, etc.) Cementitious waterproofing materials (for sewage facilities, water treatment plants, underground pits, etc.)
Specialty Chemicals	Intermediates for pharmaceuticals, agricultural chemicals, polymers, electronics materials, etc.

### Basic Chemicals

The main sector of the hydrogen peroxide business, paper pulp, saw some recovery thanks to the weakened yen, and industrial chemicals performance was strong, but overall results were flat due to decreased demand for veterinary medicines.

Revenues for hydrogen peroxide derivatives fell as a result of increased competition.

Sales in this segment came to 6,929 million yen, with operating income of 56 million yen.

Basic Chemicals (Hydrogen peroxide)	Bleaching agent for paper pulp, fibers and clothing, etc. Pollution treatment and other forms of environmental cleanup. Parasiticides for Farmed Fish
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### Agro-Science

In the Agro-Science business, both home garden herbicides and lawn herbicides performed well, and revenues increased.

Sales in this segment came to 5,259 million yen, with operating income of 386 million yen.

Agro-science	Herbicides, pesticides and growth control agents for crop fields, golf courses, green areas, etc.
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## **Glossary: Parasiticides for Farmed Fish**

Sakana Guard is a veterinary medicine that is approved for fisheries under the Japanese Pharmaceutical Law. The medicine, the main ingredient of which is hydrogen peroxide, is approved as an external treatment for skin and gill parasites on tetraodontiforms (puffer fish, etc.) and perciformes (yellowtail, sea bream, etc.). Fisheries are able to effectively remove these parasites simply by immersing the fish in a bath of seawater containing the medicine.

Because it breaks down into oxygen and water, this helps fish farmers raise healthy fish without polluting the ocean.

## **Topics**

### **Hodogaya Contract Laboratory Co., Ltd. joins forces with JRF (India)**

In April, 2014, our Group company Hodogaya Contract Laboratory Co., Ltd. (“HCL”) formed a collaborative relationship with Jai Research Foundation (“JRF”) to expand its contract testing business. Hodogaya Chemical and the JRF group formed a joint venture company, and changed its name to Hodogaya JRF Contract Laboratory Co., Ltd. (“HJC”).

JRF’s area of specialty, complementary to the former HCL’s activities, is safety testing using animals. The new venture will focus on surveying and selection of target customers, and participation in trade shows, etc. in the areas of agrochemicals, pharmaceuticals, and chemicals, as HJC and JRF gradually proceed with personnel and technology exchanges.

### **Hodogaya Chemical establishes HODOGAYA (Shanghai) TRADING CO., LTD. in China**

In April, 2014 we established HODOGAYA (Shanghai) TRADING CO., LTD., an overseas affiliate in Shanghai, China.

In the 17 years since we established our Shanghai office in 1997, we have worked on establishing relationships with Chinese customers and gathering information. With the establishment of the new company, we move from ‘liaison office’ to ‘sales hub’ in China, strengthening our function and reach, and enabling us to pursue faster and more focused business development in this market.

## **Feature Article: Knowing our history**

### **100 years of Hodogaya Chemical Part2: 1945~1970**

- 1949 Listed on the Tokyo, Osaka and Nagoya stock exchanges
- 1950 Began manufacturing agricultural chemicals
- 1954 Became the first manufacturer of MDI (an ingredient of polyurethane) in Japan
- 1959 Began manufacturing Cathilon and Spilon dyes
- 1960 Founded Nippon Polyurethane Industry Co., Ltd.
- 1963 Founded Nippon Peroxide Co., Ltd.  
Established a central research center  
Began manufacturing PTG (an ingredient of polyurethane)
- 1966 Began manufacturing hydrogen peroxide
- 1967 Became the first manufacturer of urethane waterproofing materials in Japan  
Opened a New York office (this became the affiliate company HODOGAYA CHEMICAL (U.S.A.), INC. in 1986)
- 1968 Founded Aizen Co., Ltd.

#### **Moving past the turbulence of the post-war period**

##### **Developing new products and diversifying the business**

In the turbulence that followed the end of World War II, our company once again set its sights on private-sector demand. Catching our breath with the production of artificial sweeteners and pharmaceuticals, and riding the wave of the economic effects of the Korean War, etc., we were able to get back on track with dyes and industrial chemicals. Around 1950, we started production of agricultural chemicals and sodium chlorite.

We also began developing new products, and in 1954 we became the first in Japan to manufacture MDI (which would grow to a global scale as the primary product of Nippon Polyurethane Industry Co., Ltd., founded later). We also began large-scale manufacturing of p-Dichlorobenzene at our Koriyama plant, using Chlorine produced by electrolysis.

In the latter half of the 1950s, we contributed greatly to the eradication of tuberculosis by supplying therapeutic chemical products, and we began production of the Spilon dyes that are still a key product today. Around this time, we moved our main electrolysis operations to our Koriyama plant, and began production of caustic soda using a mercury process. In 1963, recognizing the need to put even more effort into new product development, we established our central research center in Oji, in Tokyo's Kita Ward. In that year we also founded Nippon Peroxide Co., Ltd., and in 1966 we began manufacturing hydrogen peroxide.

In 1967 we opened an office in New York, and we also brought urethane waterproofing materials, the mainstay of our construction materials business, to market. We became active in chlorinated aromatic chemicals in the Industrial Chemicals area, and in the Dyes and Colorants area, we established Aizen Co. Ltd. to manufacture and sell food dyes. The 1950s and 1960s were a period of active diversification for our Group.

# CONSOLIDATED FINANCIAL STATEMENT

## CONSOLIDATED BALANCE SHEETS

*Hodogaya Chemical Co., Ltd and its Consolidated Subsidiaries for March 31, 2013 and 2014.*

	MILLIONS OF YEN	
	2013 Mar. 31	2014 Mar. 31
<b>ASSETS</b>		
<b>Current Assets</b>	23,057	20,815
<b>Fixed Assets</b>	28,707	30,110
Tangible Fixed Assets	23,009	23,279
Intangible Fixed Assets	1,888	1,528
Investment	3,810	5,303
<b>Total Assets</b>	51,765	50,926
<b>LIABILITIES</b>		
Current liabilities	14,480	12,423
Fixed liability	8,048	9,351
<b>Total Liabilities</b>	22,528	21,774
<b>Shareholders' equity</b>	24,453	22,861
Common stock	11,196	11,196
Capital surplus	9,590	9,589
Retained earnings	5,358	3,770
Less: Treasury share at cost, 5,035,247 shares in Mar. 31, 2013	(1,691)	
Less: Treasury share at cost, 5,054,476 shares in Mar. 31, 2014		(1,695)
Valuation and Translation Adjustments	3,002	4,093
Share warrant	72	51
Minority interests	1,707	2,144
<b>Total Shareholders' equity</b>	29,236	29,151
<b>Total Liabilities and Shareholders' equity</b>	51,765	50,926

## CONSOLIDATED STATEMENTS OF INCOME

*Hodogaya Chemical Co., Ltd. and its Consolidated Subsidiaries for April 1 - March 31, 2013 and 2014.*

	MILLIONS OF YEN	
	FY 2013	FY 2014
	Apr.1-Mar.31	Apr.1-Mar.31
<b>Net Sales</b>	35,191	35,687
<b>Cost of sales</b>	24,084	25,094
<b>Selling, general and administrative expenses</b>	10,208	10,559
<b>Operating income</b>	898	34
Other income	446	338
Other expenses	733	683
<b>Ordinary income</b>	611	(310)
Extraordinary income	436	321
Extraordinary expenses	108	679
<b>Income before income taxes</b>	939	(668)
<b>Current</b>	512	277
<b>Deferred</b>	426	(945)
<b>Minority interests</b>	517	325
<b>Net income</b>	(90)	(1271)

## STOCK (AS of March 31, 2014)

### AUTHORIZED NUMBER OF SHARES

200,000,000

### NUMBER OF COMMON SHARES ISSUED

84,137,261

### NUMBER OF SHAREHOLDERS

9,630

### MAIN SHAREHOLDERS (TOP 10 COMPANIES)

Shareholder	Number of Shares Held (in thousands)	Percentage of Shares Held (%)
Tosoh Corporation	16,828	20.0
Hodogaya Chemical Co., Ltd.	5,054	6.0
Mizuho Bank, Ltd.	2,987	3.6
The Norinchukin Bank	2,274	2.7
Meiji Yasuda Life Insurance Company	1,645	2.0
The Master Trust Bank of Japan, Ltd.	1,571	1.9
The Toho Bank, Ltd.	1,483	1.8
Mitsui Sumitomo Insurance Co., Ltd	1,414	1.7
The Yamaguchi Bank Ltd.	1,300	1.5
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	1,201	1.4