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Attention: All concerned parties

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Q&A for the Financial Results Briefing Session for the Fiscal Year Ending May 31, 2021 (Excerpts)

On July 16, 2021, we held an online financial results briefing for analysts and institutional investors for the fiscal year ending May 31, 2021. This document summarizes and makes public the main contents of the Q&A session during the briefing. Some of the contents have been edited for clarity.

Q1: I believe you have made color ratio modifications to illuminators for overseas customers. What specific modifications have you made? Do you plan to roll them out to major Japanese customers as well?

A1: The color ratio calibration function has been added to illuminators for overseas customers.

This function ensures stable testing quality at all times by calibrating color saturation for each image sensor. The benefit of installing this system is that it enables automatic calibration. And the benefit of realizing automatic calibration is that it eliminates separate calibration for each individual test that is conducted. You can think of it as a kind of automatic maintenance function.

In terms of whether or not the function will be sought by major Japanese customers, I personally believe it will. Calibration is necessary for each image sensor that is inspected, which I think is one of the reasons why people are required to come to work even in the face of the pandemic. So from this aspect as well, I believe that there is demand for an automatic color ratio calibration function.

Q2: With respect to the internet of things related works segment, the actual results of orders received just for the three months of the fourth quarter (slide 7 of the presentation material) show a substantial year-on-year increase. What are the factors of this increase?

Also, have orders already started arriving in relation to the new building in Nagasaki of a major Japanese customer?

A2: With respect to orders received, my impression is that the number of orders received specifically for pupil lens modules during the period up to the fourth quarter is, as a percentage of the total, higher than previous years.

Looking ahead, we expect steady performance of illuminators for Japanese customers compared with the previous fiscal year. Regarding illuminators for overseas customers, presently we do not expect the situation to worsen substantially, but since there are uncertainties in the trends of the second half, we have incorporated the risks into the earnings guidance provided at the beginning of the period.

In the new building in Nagasaki of a major Japanese customer, we believe that currently, the pre-process of image sensor production facilities is being launched and that, once this is completed, investment will be made progressively in the process relevant to us, the inspection process. At this stage, therefore, it is my understanding that orders related to the new Nagasaki building are not included.

Q3: With respect to your forecast of net sales in the internet of things related works segment for the current fiscal year (ending May 31, 2022), is my understanding correct that, compared with the previous fiscal year (ended May 31, 2021), you project an increase in net sales to major Japanese customers and a decrease in net sales to major overseas customers?

A3: With respect to illuminators for major Japanese customers, we believe we can definitely expect performance in the current fiscal year to exceed the lackluster results of the previous fiscal year.

The question is pupil lens modules and illuminators for overseas customers. Both of these achieved record net sales in the previous fiscal year. With pupil lens modules, orders continued to be strong in the fourth quarter and given the high levels of production volume and capacity utilization at our customers, our current view is that yet another record high is achievable. At the same time, the difficulty in assessing how much reuse of pupil lens modules there is on the part of customers is a risk in the current fiscal year. Normally, when a probe card is replaced, the pupil lens module to which it is docked is replaced at the same time. However, because pupil lens modules are costly, some customers want to continue using the same module for the same image sensor. How much of

such reuse there will be is difficult to assess. Although the risk has yet to emerge at the present stage, there are uncertainties.

Regarding overseas customers, trends in the second half are very much unclear at this point. Personally, I think that capital investment will remain firm in the next fiscal year. Nevertheless, I believe that the earnings guidance we have provided is most appropriate as a forecast presented at the beginning of the fiscal year.

Q4: While I think you have not indicated in your guidance your views on the level of orders that will be received in the internet of things related works segment, how much roughly do you anticipate? As the projected net sales for the segment is about 4.5 billion yen, do you expect orders to be at a similar level?

Also, if uncertainties over situation of major overseas customers in the second half are removed and orders turn out to be stronger than anticipated, or if orders start coming in for the new Nagasaki building of a major domestic customer, how much would you expect orders to grow?

A4: On customer orders, in view of the fact that the next fiscal year (ending May 31, 2023) will be the final year of our Medium-Term Business Plan, we expect the BB ratio to be definitely above 1.

In the second half, in particular, we anticipate orders to build up more strongly than the projection for net sales. Behind this projection is the launch of a major Japanese customer's new Nagasaki building. It is likely that the customer is planning to dramatically step up its production of image sensors, and in order to fulfill our responsibilities to the customer and its production plan, we have set one of our focuses this fiscal year on building up a structure for enhancing our manufacturing capabilities.

Negotiations for the next fiscal year have already started. As we are seeing flows that we have never seen in the past, we anticipate the delivery schedule to be much tighter next fiscal year.

If capital investment by major overseas customers continues at the level of the previous fiscal year or higher, and if orders for major Japanese customer's new Nagasaki building start coming in from the second half, which is a very optimistic scenario, we might be overwhelmed but also squealing with joy.

Q5: Net sales in the internet of things related works segment were a little less than 5 billion yen in the fiscal year ended May 31, 2019. The current production capacity is estimated to be around this level or slightly higher. How much are you planning to enhance your production capacity and how much do you expect the associated cost to be?

A5: For the medium to long term, it is the production capacity of pupil lens modules that I believe should be enhanced. Compared with illuminators, production of pupil lens modules requires greater know-how and is more challenging. It will take time to train people.

We anticipate that demand for pupil lens modules will increase in line with production increase at Japanese customers. We should focus this coming year on firmly building up our structure for enhancing our manufacturing capabilities. We are hoping to increase our production capacity by twice the current level.

Total capital investment required to build up the structure for enhancing manufacturing capabilities of pupil lens modules is projected to be roughly within 100 million yen. We are a company that started out from a small “four-and-a-half-mat” size room and are capable of building up a structure even without the resources such as people and goods. There is no need therefore to worry that capital investment would call for a large amount of cash.

With respect to illuminators, since these can be manufactured relatively flexibly, we have no particular plan for production enhancement.

Q6: With respect to pupil lens modules, it is mentioned in the quarterly report that new orders were received from a customer in China. Is this the same customer from whom orders were received for illuminators?

The quarterly report also mentioned that production of image sensors domestically in China would take time. What is the time frame that you envisage? Is there any possibility that its launch would be earlier than pupil lens modules for major overseas customers for which discussions are already ongoing?

A6: Orders for pupil lens modules have been placed by the same Chinese customer from whom we received orders for illuminators. The fact that pupil lens modules are used probably indicates that the customer is developing a considerably high-end image sensor.

However, the difficulty in testing image sensors lies in quantifying a person’s feelings and senses. For instance, what is the blue that people feel is beautiful? How can this feeling be presented as a parameter and developed into a test algorithm? These would take time to formulate. It does not suffice simply to be able to process digital signals or perform electrical treatment. In my opinion, it would take two to three years.

As existing manufacturers would probably be pushing ahead with various technological developments during this period, it is doubtful whether the Chinese manufacturer would be able to catch up. Still, I believe that we would be fully prepared to be of service when the Chinese market gets up and running, which is one of the scenarios in our projection.

With respect to pupil lens modules for major overseas customers, the business itself is making steady progress but what is different from Chinese customers is that with major overseas customers, we are pursuing a mass production phase. This will continue to be our challenge for this fiscal year. In particular, there is a tendency that use of pupil lens modules will expand as image sensors become more cutting edge, generating demand.
