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Meiji Holdings Co., Ltd.
Financial Results for the Q3 of FYE March 2023 (FY2022)
The Telephone Conference Q&A

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Presenters:

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*This material has been edited to make it easier to understand some of the questions and answers.

Q-1-1-1

The first is that I wanted to ask you about the outlook for high raw material and energy prices in the next fiscal year, and your approach to price revisions. You said that JPY29.5 billion is scheduled to come out this fiscal year. I think you have already discussed about how much is likely to be paid out in the next fiscal year on a recurring basis or about the various price revisions, but I would like to know how you intend to offset these revisions.

My second question is that I am still very concerned about the quantity risk to this price revision. I would like to ask you to look back on this price revision for confectioneries, yogurt and drinking milk, and tell me first what went well, and what didn't.

Also, my great concern is the lack of measures for existing brands with revised prices as a result of the concentration of salespeople and promotion on sales of functional yogurt. So, I am very afraid that when we make the second or third price revision from here, these effects will appear again. Please tell me how you will implement measures for various products with limited resources.

A-1-1-1

Furuta: At this time, we are in the process of estimating specific figures, and we would like to present the cost increase for FY2023 and the effects of the price revision at the time of the announcement of financial results in May.

We have a very broad product portfolio, so some of the effect of the price increase may be immediate, while some may have a time lag. Even if prices are raised, prices are maintained for relatively high value-added products or products that are selling well. However, for other products, prices may go back down again, so the effect of price hike is not immediate.

Let me show some examples. We raised the price of confectioneries in May 2022. Due to higher-than-expected cost increases caused by foreign exchange and other raw material price hikes, unfortunately, the May price hike was not enough to absorb the cost increase. Therefore, we are thinking of another price hike.

Another is that in such an environment of market conditions and competition, we have to raise our prices while watching other companies raise theirs. It means that we may not raise our price enough.

Then, the profit structure changes, so unavoidably profits shrink more than before.

In this situation, we were not able to recover everything this fiscal year, but I believe we will be able to recover and offset enough of this fiscal year's cost increase in the next fiscal year.

Q-1-1-2

Yes, thank you. I would like to know if the idea behind the price revision this time is to recover the profit lost in 2022, which is roughly a gap of JPY29.5 billion and JPY19.8 billion, or in other words, a JPY10 billion price revision, while also offsetting the cost of raw materials that will rise next year. Is that the way we should think of it?

A-1-1-2

Furuta: Looking at the various products for which we raised prices, we believe that we will be able to recover the amount, since retail prices have been well maintained from our efforts.

On the other hand, we have to consider the cost increase in the next fiscal year, such as raw milk, packaging materials, and imported raw materials. Imported raw materials may not be as significant as this fiscal year because the market price is a little calmer. The price of packaging materials, however, may increase.

We'll have to discuss again how to pass on such cost increases of the prices in the future. Although there is a time lag, we would like to absorb the effects of cost increase by the price increase and corporate efforts including cost reduction.

Q-1-1-3

Am I correct in understanding that you are on track to return the profit level to the previous level by FY2023? Or are you revising prices with the awareness that you will return to profit levels in the medium term after a solid recovery in volume?

A-1-1-3

Furuta: Cost increases will continue in the next fiscal year. We believe that if we can recover it, we

will be able to return to a solid growth trajectory from 2024.

In 2015, the entire food industry raised prices. It was tied firmly to profits, and the effects of the price increases were felt relatively early. Therefore, if the effects of these price hikes are firmly established and the cost increases can be absorbed to some extent, I believe that we will be able to continue to return to such a revenue and profit growth trend.

Q-1-2

I would also appreciate a few comments on the functional yogurt regarding whether both enhanced promotion and price revision have been successful..

A-1-2

Furuta: Functional yogurt has turned around since Q3 and are performing well. As for other products, *Bulgaria Yogurt* is a particular concern, but other than *Bulgaria Yogurt*, sales have cleared the previous year's level.

However, in terms of the profit, it is not as high as before because of the cost increase. In terms of the top line, except for *Bulgaria Yogurt*, the retail price is well protected, and I do not think there is much of a problem.

Q-2-1-1

On page six of the document, in the section on the net of raw material costs and price increases that you explained at the end, you said that it is a downward revision of JPY1.3 billion. However, you revised downward the profit by JPY6 billion overall, which means the difference here is JPY4.7 billion.

Regarding the volume, do you think the JPY4.7 billion was due to the up-front investment in marketing expenses, or was it purely due to the lower-than-expected volume? I would like to have a more detailed explanation of each product.

A-2-1-1

Furuta: The difference between the November 8 revision and the February 9 revision is JPY6 billion, and I would like to give you a breakdown of this difference. First of all, the impact of the drop in sales volume is JPY2.7 billion. In addition, we have spent about JPY1.1 billion more on sales promotion expenses than in November.

Then, the energy cost is about JPY900 million higher than we estimated in November. The effect of the price hike was about JPY500 million less than we had expected. We have subsidiaries in China and a company called Meiji Feed. The cost increase and sales declines, resulted in an approximately JPY800 million decrease in profits at these subsidiaries compared to November.

Q-2-1-2

I understand. Is the main reason for sales volume decline the *Bulgaria Yogurt*?

A-2-1-2

Furuta: Yes. About JPY3 billion of sales volume decline was coming from the yogurt and cheese business. You can understand that most of it is due to *Bulgaria Yogurt*.

Q-2-1-3

Is there some kind of strategy behind the increase in expansion expenses from the original plan? Or is it more of a rebate thing? What are the implications here?

A-2-1-3

Furuta: It is not a rebate issue, but rather the cost of in-store promotion. We have spent a certain amount of money on sales promotion to get the top line growth.

Q-2-2-1

When you announced your Q2 financial results three months ago, it was just after the price increase. I think you made a first impression that demand for yogurt and drinking milk was very strong

compared to expectations. What changes in the competitive environment have occurred since then, and what unexpected things are happening?

A-2-2-1

Furuta: Our price of plain yogurt has gone up, but the store prices of other competitive products and private brand products have not gone up much, and customers tend to buy those. This is why our *Bulgaria Yogurt* has been struggling.

In the case of *Bulgaria Yogurt*, we have a large 400-gram family type and also drinks, but demand for drinks continues to be quite weak, aside from price. Therefore, I think it can be said that the market is now quite low-price oriented.

On the other hand, demand for drinking milk is not very strong, but our *Oishii Gyunyu* has been relatively strong, especially in the 450-gram medium volume. Therefore, looking at the *Oishii Gyunyu* brand alone, I think we can say that there is a clear trend toward increased sales. In general, however, the environment for the drinking milk business is not that good.

Q-2-2-2

Since the profit of the drinking milk business has not been revised downward, does that mean that it is coming in line with the plan due to the improved mix effect of the sales of that *Oishii Gyunyu*, etc.?

A-2-2-2

Furuta: Yes, we recognize that *Oishii Gyunyu* in stores is performing relatively well.

There are two aspects of the drinking milk business in this fiscal year. One is about the Asahikawa Plant and the Eniwa Plant. Now, these two plants are in operation, so the costs are extra. The Asahikawa Plant will be closed in March this year, and with this, it will reduce overhead costs, or fixed costs.

And secondly, the home delivery business is still struggling a bit. It can be said that this is a drag on profit and loss.

Q-2-3-1

For *Bulgaria Yogurt*, what are your future measures?

A-2-3-1

Furuta: This December is the 50th anniversary of the launch of *Bulgaria Yogurt*. We would like to consider a 50th anniversary campaign, as well as new products and measures to stimulate demand.

Q-2-3-2

So, you are not really thinking about lowering the price or anything like that.

A-2-3-2

Furuta: We are not considering lowering the price.

Q-3-1-1

Regarding the pharmaceutical business, you mentioned earlier that you are reviewing your operating bases, spinning them off, and optimally allocating personnel. Could you tell us about the objectives and what you are aiming for with these initiatives, such as spin-offs and optimal allocation of personnel?

A-3-1-1

Furuta: As you know, the market for pharmaceuticals has shrunk dramatically because of the COVID-19 pandemic. In particular, the number of outpatient visits has decreased and the number of surgeries has decreased significantly. Sales of our antibiotics and other drugs for infectious diseases have also dropped significantly.

On the other hand, NHI price revisions are now being made every year, and at the time this medium-term business plan was formulated, we saw the environment for the pharmaceutical business as being very difficult. The level of profit was also considered to be quite low. Under such circumstances, we have done structural reforms.

To build a profitable structure, we have decided to do what we can within the Company, and we have transferred our agricultural chemicals business, dissolved our joint venture with Korea, spun off our Odawara plant, lightened the personnel, and consolidated our research laboratories.

In the meantime, the effects of COVID-19 were weakening, and the restraints on outpatient visits were disappearing, so that sales of our infectious disease drugs and vaccines were recovering. In addition, in terms of NHI drug price revisions, we have many fundamental pharmaceuticals, and since the price of these drugs will not go down any further, there are some drugs whose prices will rather go up. In these circumstances, the impact of the NHI price revision has diminished considerably.

Compare to the initial situation where we expected the situation to be severe due to the impact of COVID-19, the external environment has improved, and the internal structural reforms have been successful.

Q-3-2-1

In Q3, there may be a reactionary decline from last year's good performance, but there was quite a large decrease in profit in nutrition business. Sales for nutrition business seem to be relatively firm, but I was wondering what the current situation is like. Is the trend of declining profits bottoming out?

A-3-2-1

Furuta: This is just the high cost of raw materials. Especially in Q3, if you look at the previous year, nutrition has decreased by JPY1.9 billion, but most of that is cost of materials. The increase in the cost of dairy ingredients, such as whey for protein, had a significant impact on the decrease in profit.

Q-3-2-2

It seems that there is no particular impact on the competitive environment, and sales don't seem to be getting that bad, so is it correct to understand that there is no particular problem with improving profitability by raising prices?

A-3-2-2

Furuta: If you look at the nutrition business, there is infant formula, protein, and enteral formula, but protein SAVAS has the greatest impact on profit and loss. We have raised the price, but it does not mean that we have recovered sufficiently. Therefore, we are raising the price one more time. In terms of the business environment or the competition, the sales at storefronts are still falling. On the other hand, we have been increasing the sales ratio of e-commerce, so in this sense, we have cleared the previous year's top line, but unfortunately, we have not reached that level because we are aiming a little higher.

Q-4-1-1

If you subtract the profit after the downward revision and the cumulative total to date, you should see an increase of about JPY600 million for Q4.

In this context, the domestic subsidiaries and other business have experienced a decrease in profits, but the yogurt and cheese business has increased profits by about JPY1 billion. I wonder why this area will see a turnaround in profits. Can you first give us some background on the increase in profits in Q4, or in food as a whole, please?

Then there was Q3 functional yogurt sales increase of about 3%, I think. I would appreciate it if you could tell me if this is *R-1* and *LG21* or new product sales.

A-4-1-1

Furuta: In the Q4 forecast, we are looking at quite a bit of profit increase in yogurt. The most important factor in this is the increase in revenues. Unfortunately, *Bulgaria Yogurt* was struggling a bit, but *R-1* has been performing very well since December, and *LG21* has already seen an increase in sales since last June.

Although we have raised the price of *R-1*, we are enjoying the benefits of both the increase in volume and the price increase. We hope to continue this trend for a long time, and if we can make it through March, I believe we will be able to realize a sufficient increase in profits of yogurt and cheese business.

The growth rate in Q3 of *R-1* was almost flat. As I mentioned earlier, the trend of increasing revenues started from about mid-November to December, and unfortunately, revenues were still declining in October. In addition, we are also engaged in home delivery services, but home delivery services are slightly down from the previous year, which is dragging us down.

If we look at the market alone, we can see that it has cleared the previous year's level. As for *LG21*, looking only at Q3, there was a 3.4% increase. Although home delivery is a little weak, *LG21*'s commercial sales are up about 9%, which indicates that *LG21* is doing very well.

Q-4-1-2

How is the pacing for *Shibou Taisaku Yogurt*?

A-4-1-2

Tanaka: Since its sales occupied more than 3% of the total functional yogurt sales, we believe that we are making progress according to our plan.

Q-4-1-3

Functional yogurt's sales are about JPY25 billion, so a little over 3% would be something around JPY700 million to JPY800 million?

A-4-1-3

Tanaka: That's correct.

Q-4-1-4

Also, when has *R-1* been increasing by double digits?

A-4-1-4

Furuta: It is as of December. Also, this is about commercial products. Home delivery has been a little slow, including drinking milk. Recently, overall home delivery sales are down a bit. We cannot

make enough new contacts due to a lack of staff, and home deliveries have dropped as a result of this.

In addition, regarding *R-1* and *LG21*, consumers are moving toward the new product called 5-star Custom.

Some customers have drifted over here and stopped buying *R-1* and *LG21*, for example, and I think it can be said that things are moving a little slower on the functional yogurt side.

Q-4-1-5

By the way, when you say that *R-1* was positive on the commercial market, how much was this positive in terms of percentage?

A-4-1-5

Tanaka: *R-1* commercial sales were up by two digits from December.

Q-4-2-1

Regarding the profit of pharmaceutical segment in Q3, I think that Japan and overseas profits have increased, while profits for vaccines have been almost zero. Could you please explain a little more about the situation here, and the increase or decrease in profits?

A-4-2-1

Furuta: In Japan, sales of antibiotics have been strong, and the increase in sales of these products is directly reflected in profits. Overseas, Medreich, which is engaged in CMO (Contract Manufacturing Organization) and CDMO (Contract Development and Manufacturing Organization) business in India, and a subsidiary in Spain are doing very well, and their sales and profits have been very strong.

Regarding vaccines, we estimated a large number of returns. We have deducted the amount of those returns, which has resulted in a considerable drop in profits. In the past, the return rate for influenza vaccines was generally less than 10%, but this time we expect the return rate to be more

than 20%.

The market as a whole is in the process of increasing production this season. We also have released about 11 million doses, compared to 10 million doses in the past. However, the vaccination rate is low for the large supply. It is said to be about 70%, and the remainder is almost returned at this time of year.

In these circumstances, we expect that we will receive returns of more than 20%, which will have a significant negative impact on our business as well.

Q-4-2-2

Does this mean that in Q3, the allowance for returns is already coming in?

A-4-2-2

Furuta: Yes. Allowance for returns was recorded in Q3.

Q-5-1-1

The first point is about costs and price increases. I think the price hike, starting this April, will make up for both the portion missed this year and the cost increase in the new fiscal year. Can we take the view that we can get about JPY10 billion of profit increase factor for the new fiscal year in this area?

A-5-1-1

Furuta: No. The price hike in next April will be mainly due to the increase in raw milk prices. As I mentioned earlier, for confectioneries, we will once again create profits by raising prices to cover the amount that was lost since May of last year.

However, in the next fiscal year, if the price of packaging materials or some raw materials goes up again, we will have to make a proper estimate and revise the price accordingly.

Q-5-1-2

I understand your assumption that if there would be no additional cost increases, JPY10 billion that was missed this year would be included in the next fiscal year as a factor in the profit increase. Am I correct?

A-5-1-2

Furuta: We included the JPY10 billion that was missed this year in the price hike in April.

Q-5-1-3

What is the cost increase for the next fiscal year factored in now? Are you saying that you have already included all the parts that you can estimate at this time?

A-5-1-3

Tanaka: We have already included estimated amounts such as price increase for raw milk for processed products from April 1 and basic energy cost hikes. But we don't know about going up from our present estimates further, so we don't include that.

Furuta: The price hike in March and April is based on the amount of cost increases that we had anticipated prior to the over-the-counter price increase. We do not disclose what they are and how much they cost at this time.

Q-5-1-4

Among the additional cost increases, is the risk of higher raw milk price for drinking milk a factor that should be considered? What about as a risk?

A-5-1-4

Furuta: We do not expect that at this time, but I think there is a risk.

Q-5-2-1

You mentioned the drop in volume, which was the reason for the downward revision. Do you see this as a market factor, or do you see this as a drop in market share or an image from losing the competition? To put it more simply, you are spending a lot of money on marketing, and while you may be getting some results in the functional yogurt area, I think that in total you are not getting a proper return, and that the marketing is not sticking. Could you comment on the marketing strategy?

A-5-2-1

Furuta: I mentioned earlier that JPY2.7 billion of the JPY6 billion reduction was a decrease in volume. This is mostly a yogurt and cheese business, of which *Bulgaria Yogurt* is being the issue. Therefore, how to lift up *Bulgaria Yogurt* is an extremely urgent issue. I believe that we will need to take measures to lift it up by launching a 50th anniversary campaign, with future marketing at a cost.

For other products, it is safe to assume that the volume decline will not have an impact. Therefore, we recognize that the biggest challenge at the moment is what to do about this *Bulgaria Yogurt*.

Q-5-2-2

Is this a market factor or are we talking about market share?

A-5-2-2

Furuta: The overall market is also weak. We assume that the needs might be fleeing to other various products. Other companies' yogurt products are not doing so well, they cannot raise prices too much.

Q-6-1-1

For *R-1* and also *LG21*, can you describe the top line trend for volume including commercial and home delivery for November and December?

A-6-1-1

Tanaka: Sales of functional yogurt as a whole, both commercial and home delivery, have gone from a mid-single-digit decline through October to a mid-single-digit gain in November and a double-digit increase in December. We do not disclose monthly sales trends for *R-1* and *LG21*.

Q-6-1-2

So, you are seeing an increase in sales of almost 10% in December.

A-6-1-2

Furuta: Yes. In November, we started TV commercials and promotions. We have seen a return of what we call dormant customers, such as those who used to buy *R-1* and *LG21*.

Although there have always been loyal customers, but users who used to drink or eat *R-1* and *LG21* but left recently have returned, leading to an increase in sales in November and December.

Q-6-2

In the food segment, you said at the November meeting that if the exchange rate was JPY130, there would be no need for an additional price increase. Since it has been decided that the raw milk price of processed products will increase in December, it would make sense to raise the prices of yogurt, natural cheese, etc.

Could you please explain in more detail about the background of the additional increase in the price of ice cream or confectioneries that do not contain much nonfat dry milk, and what circumstances have changed since three months ago that led to this price increase?

A-6-2

Furuta: The cost increase was more than expected. We estimated that we could absorb some of the cost increase by raising prices in Q2, but in reality, it was much larger than that.

In addition, energy costs are also quite high, so we have decided to raise the price further and revise the price.

Q-6-3

The NHI drug price revisions for the next fiscal year will have a negative impact on profits, which is usually around JPY5 billion. I was wondering if this amount will still be there next fiscal year or if the impact will become smaller.

A-6-3

Furuta: Nothing has been decided on the NHI drug price revisions yet. The number of fundamental pharmaceuticals has become relatively large, so if we assume that the same range of NHI drug price revisions is applied as before, the impact of it will not be as great as it was this year or last year.

Q-7-1-1

First of all, I would like to ask you about *R-1*. Can you tell us if the very strong momentum can be maintained in the future, or do we need to consider the risk of weaker sales momentum?

A-7-1-1

Furuta: We would like to maintain this strong momentum and continue the trend of increased sales. We are getting users back again, and we are trying to keep this going.

Of course, it is difficult to maintain a steady increase in revenues over time, but we would like to bring revenues to a certain level and maintain that level. I will not say how high that level will be, but we would like to consider marketing measures that will enable us to maintain an upward trend in sales in Q3 and Q4, and in the next fiscal year.

Q-7-1-2

Regarding *R-1*, you spent quite a bit of marketing costs in Q3, but is it correct for me to understand that you will continue to invest aggressively in the brand in the future?

A-7-1-2

Furuta: Functional yogurt contributes significantly to profits, so we would like to maintain a certain level of marketing investment for *R-1*, *LG21*, and *PA-3*, as well as for the new product *Shibou Taisaku Yogurt*. We would like to market them in such a way that we can maintain an upward trend in sales.

Q-7-2

In addition to this solid marketing investment in each brand, did your company itself take any measures to increase sales outside of marketing, such as focusing more on functional yogurt, or strengthening the increase in sales? If there is something like that, I'd like to know since it may be a factor of sustainability.

A-7-2

Tanaka: We have also been very intensifying our efforts on promotional activities at the storefronts. We have been disseminating various academic evidence during the winter season during this period. By carefully communicating the evidence to our business partners on site, we ask them to expand their sales areas for our products. I feel that people now believe in the certainty of *R-1* once again.

Q-7-3-1

Also, marketing expenses for nutrition business came out quite a bit in Q3, didn't they? What was this used for?

A-7-3-1

Tanaka: The cost for nutrition is being used to expand EC-related sales, and we believe it is having an effect.

Q-7-3-2

I was wondering if you could tell me what the total sales of SAVAS were in Q3.

A-7-3-2

Furuta: Sales of powder type was up by 6.7% in Q3. In cumulative total, it was up by 1.0%. Sales of SAVAS milk was up by 10% in Q3, and up by 9.5% in cumulative total.

Q-7-3-3

So, you didn't quite reach your plan.

A-7-3-3

Furuta: We have not reached the plan. We see that soy protein is struggling a lot. Female users have left the market, and the storefronts themselves are also relatively weak.

However, as Tanaka mentioned earlier, sales on e-commerce are on track to increase revenues considerably. Originally, sales from e-commerce accounted for approximately 60% to 70% of the powder type. I believe that firmly developing and increasing this route will lead to increased revenues in the future.

Q-7-3-4

I see. So, you have invested quite a bit there.

A-7-3-4

Furuta: Yes, We would like to continue investing here.

Q-7-4-1

For the next fiscal year, do you feel that you will, or should use this marketing investment, such as sales expansion expenses, in a very aggressive manner?

A-7-4-1

Furuta: Of course, we have to keep an eye on profits, but by raising prices, there is a tendency for the sales volume to drop a little. I think we need to spend a certain amount of money on marketing to grow again, and also to ensure that everyone will continue to purchase regularly.

Therefore, rather than trying to make a profit by cutting the marketing expenses, we will create a solid top line. I believe that this will lead to an increase in revenue next year and the year after, or perhaps to a growth strategy.

Q-7-4-2

I understand. It is very difficult to read whether or not the sales expansion costs, etc. here can be recovered, right?

A-7-4-2

Furuta: That is correct.

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