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**MORINAGA & CO., LTD.**

**Q&A Session at Results Briefing for Fiscal Year Ended March 31, 2022**

**(held May 17, 2022)**

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Q. Could you please tell us about your progress with structural reforms in the confectionery and foodstuffs business aimed at achieving the targeted operating income margin of 10%?

A. The increase in depreciation and amortization and higher raw materials prices are the main reasons for the confectionery and foodstuffs business's struggles with profitability. There was a need to attain a certain level of sales for chocolate so that we could recover the substantial capital investment carried out in the past, and we managed to increase sales of chocolate year on year in fiscal 2021. Sales of biscuits, which make a relatively large contribution to profits, remained brisk due to the tailwind from strong stay-at-home demand. We need to continue to increase the sales weighting of biscuits and sugar confectionery, which are both relatively profitable.

We plan to increase sales prices as required in fiscal 2022 to address the issue of rising raw materials prices, the second reason confectionery and foodstuffs business's struggles with profitability. We are also working on a wide range of other measures such as reducing the number of sales items, streamlining production, and reducing costs.

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Q. What is your approach to cash allocation? I believe you have positive net cash as well as extraordinary gains from the sale of cross shareholdings. While you're using some of the cash for a JPY 10 billion share buyback, you're not changing your capital investment target set out in the 2021 Medium-Term Business Plan. What kind of cash allocation is involved in the JPY 10 billion share buyback amount based?

A. The Strategic Investment & Alliance Department, which we established last year to specialize in the pursuit of inorganic growth, is looking at ways we can allocate management resources to achieve inorganic growth. Although our cash position may appear excessive at this point, we intend to allocate substantial cash to investment for growth.

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Q. How do you plan to strike a good balance between cash allocation and shareholder returns in the context of raising the dividend on equity ratio (DOE) in the longer term?

A. Our basic policy is sustained, stable shareholder returns. We believe DOE is the most appropriate metric related to capital policy from the perspective of providing stable dividends. Our goal is to maintain the forecast DOE of 3.6% for fiscal 2021 and increase it in the longer term. We aim to maintain a good overall balance by continuing to pay careful consideration to the dividend payout ratio and free cash flow.

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Q. What initiatives are you implementing in pursuit of inorganic growth? Would it be right to assume that your intention to utilize net cash in an effective way means you're considering a fairly significant M&A deal?

A. We referred to inorganic growth for the first time in our 2021 Medium-Term Business Plan. We believe M&A deals worth several tens of billions of yen are a possibility. Potential deals are still under review, so we can't publically disclose any information at this stage. We are considering various options, such as accelerating growth of focus domains and moving into peripheral markets.

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Q. I understand that you have left your operating income target, as stated in the 2021 Medium-Term Business Plan, unchanged at JPY 21.5 billion. How do you plan to accelerate profit growth this fiscal year?

A. Yes that's right, we haven't changed the operating income target of JPY 21.5 billion. Although net sales are steadily expanding, our operating income forecast for fiscal 2022 is JPY 16.5 billion because profit will be severely impacted by factors such as rising raw materials prices. Investment in the U.S. and Direct Marketing businesses in fiscal 2021, the first year of the period covered by the 2021 Medium-Term Business Plan, will begin to bear fruit later on as we head toward attaining the targets we set out in the plan. We're also seeking to expand the "in-" business. When formulating the 2021 Medium-Term Business Plan we set what we considered to be realistically achievable targets. The increase in raw materials prices has accelerated dramatically in recent months, and that's a factor that has changed considerably since we set the targets. Changes to the business environment are likely to occur after the price increases we've scheduled for the first half of fiscal 2022. We will continue to flexibly implement a variety of measures as needed as we work toward achieving our 2021 Medium-Term Business Plan targets.

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Q. Does that mean you believe that the operating income target of JPY 21.5 billion is achievable if you can absorb the impact of higher raw materials prices by increasing sales prices, even though it's uncertain whether the price increases will be successful? And given the forex rate assumption of 128 yen to the US dollar for your fiscal 2022 forecast, would it be correct to say that you're factoring in realistic increases in raw materials prices?

A. We believe we can get close to our target for operating income. We factored in realistic raw materials cost increases when calculating targets, but revisions are possible due to the risk of further increases.

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Q. The frozen desserts business posted a loss for the fourth quarter of fiscal 2021. Was that due to increased depreciation and amortization and higher raw materials prices? And what is your outlook for the business in fiscal 2023 and beyond?

A. Raw material prices surged in the fourth quarter. There was also an increase in depreciation and amortization. Overall profitability was down on a consolidated basis, due in part to spending on advertising in the second half.

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Q. What is your stance on capital investment? In fiscal 2021, capital investment came to JPY 20.4 billion versus the planned JPY 24.4 billion. Your capital investment plan for fiscal 2022 is JPY 16.0 billion, showing a gradual decrease. I assume this is due to consideration given to free cash flow, but I recall that when you announced the 2021 Medium-Term Business Plan, you indicated that you intended to invest aggressively in infrastructure. Is your infrastructure program progressing as planned? Are you still planning substantial capital investment in fiscal 2023 and beyond?

A. Total investment under the 2021 Medium-Term Business Plan is unchanged at JPY 45.0 billion. However, we have reviewed some spending in light of the changing business environment. We have also carefully examined investment efficiency from a capital cost perspective. While we are revising some investments, we may invest more in growing the four focus domains and projects that are important from a management perspective. For example, this fiscal year we're investing in additional production lines in Taiwan for *HI-CHEW* products to export to the United States, but we will still need more. We may therefore bring forward our plans to invest in additional production facilities. We're making investment decisions that are appropriate for the growth of each business.

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Q. What are your concerns about supply issues in the U.S. business? You're exporting *HI-CHEW* from China and Taiwan to the United States, but are you concerned about shipping disruptions, lockdowns in China, and U.S. labor shortages?

A. U.S. labor shortages are a cause for concern, and shipping container shortages remain a risk, but we do not have concerns about supply capacity issues impacting progress toward achievement of the sales target of the U.S. business. We will need to implement a variety of new measures to facilitate further growth of the U.S. business in fiscal 2023 and beyond.

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Q. You stated that you'll need to boost supply capacity if *HI-CHEW* is to continue growing at the current pace. Can you update us on your thinking about business bases and the scale of investment involved?

A. We're still considering ways to globally connect and coordinate our production bases, including our production bases in Japan.

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Q. I believe sales of *in Jelly* were brisk due to increased demand for products to consume when feeling unwell. What steps are you planning to take from now on to attract and acquire more customers?

A. Our *in Jelly* strategies continue to be expanding target consumer groups and working to promote new settings in which to consume the products. In fiscal 2020, demand dried up to a certain extent due to the decline in the movement of people amid the pandemic. We began promoting *in Jelly* as a way to boost energy levels while working from home, and we also added new products with fruit-like mouthfeels to appeal to a wider range of consumers. These initiatives are beginning to produce results. In fiscal 2022 we're continuing to sell frozen *in Jelly* products, which I made mention of at the results briefing in November, and we're planning to expand into supermarket sales channels. *in Jelly* is one of our core product ranges, and we'll continue to promote new settings in which to consume *in Jelly* products and expand target consumer groups, harnessing their strengths such as delicious flavors and pleasant textures in order to dominate the spouted pouch jelly drink market.

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Q. Why have you decided not to raise the price of *in Jelly* products?

A. Raw materials cost increases are affecting a broad range of businesses. We will be flexibly taking a wide variety of steps as needed not only for *in Jelly* but for all of our products in response to changes in the business environment.

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Q. You're recording brisk topline earnings growth in the four focus domains. The products that you were hoping would sell well are selling well. Why is that?

A. In the 2021 Medium-Term Business Plan, we decided to concentrate management resources on the four focus domains. These businesses have grown as a result of setting concrete targets for each domain, devising marketing strategies, and having sales teams take the lead in rolling out sales channel policies consistent with the strategies for each domain. We have also been able to respond in agilely way in relation to production as well. It has truly been a Group-wide effort. While it is exceedingly difficult to maintain strong sales permanently, we will put into action the initiatives we discussed today for each business. Focus domains accounted for JPY 11.0 billion of the JPY 13.0 billion increase in consolidated net sales in fiscal 2021. The whole Group is taking action, spurred by the resolve of the management team. The Group will continue with its concerted efforts to achieve its 2030 targets as early as possible.

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Q. Does this mean your employees have developed a better understanding of the Morinaga Group's goal announced last year to change into a Wellness Company, and you're all moving in the same direction?

A. We have traditionally announced three-year medium-term business plans, but last year we also formulated and unveiled our very first long-term business plan: the 2030 Business Plan. It was also our first attempt at using a backcasting approach to develop a plan to realize a long-term vision, namely our 2030 Vision. We have spoken directly with over 1,000 employees about the 2030 Business Plan and feel that they are developing a deeper understanding of it. Our employees were initially surprised by our stated goal of changing into a Wellness Company, and we are seeing a variety of changes occurring, such as an initiative to define "health of mind" within the company. We will continue with our Group-wide efforts to achieve the aims of 2030 Business Plan.

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Q. The U.S. Business is achieving profit growth. What's next in the profit cycle? Are you moving into a phase of investment recovery or are you still in the investment phase?

A. I think we are still in the investment phase. Business activity was generally limited by the pandemic in fiscal 2021 and we made a profit because selling and advertising expenses were lower than expected. Operating income came to JPY 1.4 billion, driven by sales growth and boosted by the flourishing US non-chocolate candy market. We plan to invest part of the profits earned through *HI-CHEW* products in *Chargel*, our new jelly drink product in the United States, as a step toward achieving our 2030 target for net sales in the U.S. Business of JPY 30.0 billion. The achievement of *HI-CHEW* sales of JPY 10 billion in fiscal was a milestone on the way to reaching our longer term sales target of JPY 20 billion. It's within reach if we can maintain our current momentum.

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Q. What has been the market's reaction to *Chargel*? Do you have a sales target?

A. Sales of *in Jelly* are twice the sales of *HI-CHEW* in both Japan and Taiwan. Given the success of *in Jelly*, we see potential for *Chargel* sales to eventually double *HI-CHEW* sales in the US. We also think *Chargel* has huge potential considering the sheer size of the energy drink and energy bar market in the US. We haven't announced any sales targets, but our plan is to take our time in patiently nurturing the business.