

Minutes of telephone conference on 1Q financial results of FY2019

<Date and time> 2:00 p.m. – 3:00 p.m., Thursday, May 9, 2019

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Groups

Q. You mentioned consolidated Normalized OP was in line with the plan. Please tell us a breakdown of the progress made in each business. Kyowa Hakko Kirin's results seemed better than expected, is it right?

A. Both Revenue and Normalized OP were roughly on par with the previous year, and progress was on track to meet the full-year forecasts. Despite a decline in marginal profits, Kirin Brewery slightly exceeded its forecasts due to a delay in selling and other expenses. Kirin Beverage was slightly behind the plan. Changes of Kirin Tropicana's sales scheme have been factored into the plan at the beginning of the year. Lion in 1Q fell short of forecasts, mainly in the Beer, Spirits, and Wine (BSW) business. Myanmar Brewery slightly exceeded plans. Kyowa Hakko Kirin progressed steadily for the full-year forecasts.

Q. Strategic expenses have been spent little in 1Q. Will they be incurred from 2Q?

A. Strategic expenses have roughly been in line with the plan of 6.0 billion yen in full year. Since there are a number of projects including those that will be launched in the future, and the expenses will be used from 2Q onwards.

Kirin Brewery

Q. It is true that beer product sales volume of Kirin Brewery was steady, but marginal profit was -0.8 billion yen due to the impact of mix deterioration. Please tell us your views on that and outlook from 2Q. In addition, please explain in more detail the differences in composition of products, etc.

A. The decrease in traditional beer was about 17 thousand kl, and one of the reasons is because there was the temporary demand in March in the previous year before price revision of returnable container products in April. The rush of new product launch in new genre category by competitors has driven new genre market growth. It represents not only a huge opportunity for *Honkirin* but the negative impact on mix appeared by shifting from other categories to new genre. An Increase in sales volume of *Kirin Ichiban* in traditional beer category is the key to mix improvement, but the volume and marginal profits of beer products declined as a result of rush of new products by competitors in new genre in 1Q. The company plans recovery from 2Q by renewal of *Kirin Ichiban* in April. The differences of change in composition of products, etc include the positive impact from the price increase of returnable container products, and the negative impact from the increase in variable processing costs due to soaring fuel expenses, variable sales promotion expenses, and transportation costs.

Q. In marginal profits, new genre as a whole increased about 33 thousand kl. Please tell us how much PB product is included.

A. I'm afraid we can't explain about PB product because of confidentiality.

Q. You told that some of selling expenses had been delayed. Does it mean sales promotion expenses in 2Q will increase as a result of the renewal of *Kirin Ichiban* in spite of the decrease in selling expenses in 1Q? Do you mean the decrease in 1Q was because of gap in timing and on track for full-year plan?

A. Your understanding is right. Marketing expenses after the *Honkirin* renewal, and brand investments

related to *Kirin Ichiban* renewal in April to strengthen traditional beer category will be materialized in 2Q and onwards, so it will be used as planned.

Q. The more powerful brands *Honkirin* and *KIRIN The STRONG* become, the more difficult it will be to increase sales volume of *Kirin Ichiban* and improve traditional beer category. I understand *Kirin Ichiban* renewal will work to some extent, but I think marginal profit will not improve unless the mix deterioration stops. In addition to the brand renewal, do you have another initiatives for improvement?

A. I understand you mean that traditional beer will become more difficult category to improve as long as RTDs and new genre grow in this matured market, which appears true in terms of the industry as a whole. In our product portfolio, on the other hand, *Honkirin* and RTDs do not cannibalize *Kirin Ichiban*. Going forward, we will continue to focus on enhancing strong brands in each category. Due to the revision of the liquor tax, the composition of beer will increase, and it will be important to increase marginal profits along with this, and so we will keep focus on developing brands such as *Kirin Ichiban*. In addition, the increase in the composition of craft beer also contributes to the improvement of marginal profit, and so we will consistently implement the strategy.

Q. Has the expected effect been seen in the area of enhanced branded products through PB entrustment?

A. As we anticipated, collaborative efforts with retailers by leveraging PB outsourcing are going well. Kirin Brewery and retailers are making progress in such initiative as analyzing consumers' purchasing behavior. The share of our branded products in the retailers has been rising, which shows signs of achievement. We will keep the initiative on.

Q. We believe that the demand shift to new genre category has ill motivated capital market to invest in beer stocks. It is important that the demand for traditional beer will grow in the future, but at the moment it has not risen as the companies are strengthening their new genre categories. Do you think the beer category will grow with the liquor tax revision? In that case, will it be around the beginning of next year?

A. Competitors have launched new products in new genre since the beginning of this year, and *Honkirin* was launched in March last year. That's why the increase in sales volume of new genre in 1Q appears quite large, but we expect it will settle down shortly. We do not intend to launch a new brand this year, and we are considering a medium-to long-term strategy. It remains to be seen whether demand will shift to traditional beer category back or not, but we do not believe that new genre alone will continue to grow. We cannot make it clear when beer manufacturers will be more focused on traditional beer category, but we think there will appear such direction in the future.

Kirin Beverage

Q. Please tell us how the negotiations about price hike for large container products have progressed. Have the negotiations been completed and were generally in line with expectations? Also, do you expect that price increase will proceed in the industry as a whole?

A. Producer prices have been revised as planned on May 1. Negotiations with retailers are generally proceeding steadily, and it is expected that the retail price will gradually go up in the future. I believe that competitors' price increases have been also gradually reflected in retail prices. We will be paying close attention to the situation going forward. The forecast of sales volume is unchanged from the initial plan. I understand that the pricing this time is to improve profitability of large container products, and we cannot see whether it will spread to other containers such as small PET or not. We keep a close watch on trends in large container, the consumption tax hike in October, and competition, taking into account increases in raw material and logistics costs.

Q. Trade journal said not only producer prices but also sales promotion expenses would rise. Is it correct that the price revision will contribute to net revenue increase from 2Q after deduction of sales promotion expenses?

A. Your understanding is basically correct, and we need carefully to weigh the sales promotion expenses against soaring logistics costs.

Q. Despite struggle in coffee categories, the difference of change in product mix and in composition ratio of containers etc. was +0.2 billion yen. Why is it? As +0.2 billion yen looks small compared to the full-year forecast +2.3 billion yen, could you tell us how probable it is to realize the plan including the impact of the price revisions?

A. Positive 0.2 billion yen is mainly attributable to two factors. One is successful sales of small PET containers products particularly as the result of focusing on *Gogo-no-Kocha* and *Nama-cha*. However, the change to *Tropicana's* sales scheme had a bigger impact. As we changed the scheme from JV, the earnings of which were consolidated by equity method, to licensing scheme, only variable costs out of all costs were deducted to calculate marginal profits; it follows that marginal profit per case improved. In terms of containers alone, the mix deteriorated due to the struggling in sales of *FIRE*. We will keep focused on small PET products in the future. The effect of the price increase is to be included in the difference of change in product mix and in composition ratio of containers etc., but it is difficult to estimate the effect at this time. I think the impact will appear in the numbers after the middle of 2Q. Full-year Normalized OP forecast remains unchanged. *Gogo-no-Kocha* and *Nama-cha* are performing well, and we intend to improve profits through measures from 2Q onwards.

Q. How much impact will the change to *Tropicana's* sales scheme have on a full-year basis? Sales volume increase in 1Q was smaller than selling expense increase. Will there be some risks?

A. The full-year impact of change to the *Tropicana's* sales scheme cannot be answered due to confidentiality. Selling expenses in 1Q increased due to higher advertising expenses for *Gogo-no-Kocha* as we saw competitor new product in black tea category, which is the most important category of us. In addition, advertising expenses according to the launch of *FIRE ONEDAY BLACK* also had an impact. We will adjust selling expenses within the plan. Explaining how the change to the *Tropicana's* scheme is reflected in figures in the disclosure and the mechanism, profits from *Kirin Tropicana*, a joint venture, were formally consolidated by equity method. However, under the new scheme, profits were incorporated into each stage of profits, and unlike in the past, selling expenses were booked before Normalized OP, so selling expenses increased. On the other hand, sales volume has not changed since it was counted in the past as well, so the increase in selling expenses appeared to be significant. Although selling expenses increased, marginal profit difference of change in product mix and in composition ratio of containers etc. increased.

Q. Black tea category market grew by 7% in 1Q, what is your outlook for market growth going forward? What do you think of impact of competitors' entry on your profit?

A. Competitors have launched large new products, and each company has been enhancing these new products. In response, we launched *Gogo-no-Kocha The Meister's Milk Tea* at the end of March. The detailed figures about its performance to date remains to be announced, but it is currently contributing to the overall volume of the *Gogo-no-Kocha* brand. The market has been growing, but we will be paying close attention to what comes after, taking into account the other categories, as the seasons will change and products will be replaced.

<Lion>

Q. Sales volume of BSW was -14% year-on-year. Please tell us how much impact of each three factors: the increase in sales volume in last 4Q, the introduction of Container Deposit Scheme (CDS), and the delay in the Easter season. The situation for the mainstay brands such as a new product in contemporary category, craft beer, seems to be good, but I would like to confirm the momentum in organic basis. Is the increase in the unit sales price reflected in Revenue?

A. Last November, when CDS was introduced in Queensland, and December, when promotions were bolstered, and March, when Easter's demand was delayed in April this year, were the main factor behind the -14% (January-March). Comparing the six-month period from October last year to March this year, the sales volume is approximately -5% and Australia is approximately -3% as the breakdown. Easter's delay has been recovered in April. Unit sales prices are as noted. We also raised prices in February this year, and the average selling price has increased about 4% over the previous year.

Q. Excluding the impact of the delay in the timing of Easter, what was the progress made in BSW business toward the plan?

A. Even if we exclude the factor behind the delay, we has not fully recovered 1Q's behind yet. However, we believes we can recover as we still takes nine months in this fiscal year.

Q. According to the fact that sales volume of BSW in Australia was -3% in October-March, I feel like the competitive environment is getting worse than in the past? Also, was it worse in New Zealand than in the past?

A. We expect that the market will continue to be flat or slightly decline instead of growing significantly in the future. Lion will take initiatives to grow in value base, not in volume base by shifting from classic category to contemporary, premium, and craft categories. Rather than worsening market environment, the impact of the delay in the timing was significant, and we believe that a recovery is possible.

<Myanmar Brewery>

Q. Myanmar Brewery exceeded the plan in 1Q. Please explain the deterioration of the mix and the impact of the foreign exchange rate on profits. Could you tell me how the impact will be in 2Q and after, including competitive environment?

A. As the Myanmar market expands, the beer drinking population is also increasing with rising incomes, but the main entry comes from the economy category. Compared to the mainstream category *Myanmar Beer*, the volume of can containers of *Andaman Gold* in the economy category has increased significantly, and the mix appears to be worsening. However, the volume of both brands grew and the sales volume increase contributed to the increased profits. Considering that sales volume increased in economy category and 1Q was one of the peak seasons in Myanmar, the progress was expected to be in line with the full-year forecast and there are no revisions to the forecast.

Q. I understand Myanmar Brewery's sales volume assumption was a high single-digit growth. Does 13.1% increase in 1Q reflect special factors such as timing differences?

A. The 1Q's result was aided by a big campaign since January and relatively modest accept of price increases in the market. We hope more than high single-digit growth to continue, but I think it will settle somewhere in the future. Sales volume includes shipment of in-kind payment which was deferred from sales promotion, but because such shipment in 1Q last year was more than this year, sales volume increase excluding the impacts above was larger than +13.1%.