

[Q&A Session Minutes]
Presentation on 3Q FY2022 Financial Results

Date & Time:	Wednesday, November 9, 2022 16:00-17:00 (JST)
Presenters:	Shinjiro Akieda, Senior Executive Officer, General Manager of Corporate Planning Dept. Takashi Hayashi, Executive Officer, General Manager of Accounting Dept.

Q. Could you please explain the trends in store prices and volumes of beer and soft drinks after the price revision in October?

A. (Akieda) We were able to raise the retail price of both beer and soft drinks as expected. Sales volume is affected by temporary demand, so we will have to wait and see, but at the moment it is within our initial forecast.

Q. Soft drinks prices seem to vary from store to store in convenience stores and supermarkets. Please tell us how much you expected for the prices to increase and any updates on the current situation.

A. (Akieda) It is difficult for us to give you our prediction for a recommended retail price, but based on past experience with price increases, we assumed that the retail price at convenience stores would increase by around 10 yen. Supermarkets have a lot of variation due to promotions by each company and other factors. As we proceed with the negotiations with our customers, we will increase the selling price during a discount promotion, since we have increased the manufacturer price. Price increases in stores are steadily progressing.

Q. I know there will be some instability around cost increases for the next fiscal year. Could you give us a rough idea of the degree of increase, breakdown, etc.?

A. (Akieda) At this point, we expect costs to increase by 45-50 billion yen compared to this year. Roughly speaking, we expect costs to increase by 20 billion yen for Kirin Brewery, 10 billion yen for Kirin Beverage, 10 billion yen for Lion, and 5 billion yen for Mercian, etc. Based on this, each operating company is working to set their profit targets for the next fiscal year.

Q. Similar to this current fiscal year, is it possible to respond with profit improvement measures in the next fiscal year?

A. (Akieda) This is exactly what each operating company is examining closely. Basically, we will implement price increases at each company. Kirin Brewery, in particular, will see the full effect of the price revision next year. In addition to this, we hope to achieve profits of the pre-COVID-19 level by accumulating the cost reduction measures at each company.

Q. Regarding this fiscal year, there seems to be some variation in the results for each segment. Based on the progress made up to September, what is your evaluation for each operating business at this time? I would also like for you to include in your evaluation around the temporary demand before the price revision in the domestic alcoholic and non-alcoholic beverage businesses.

A. (Akieda) Regarding Kirin Brewery, we are putting in our efforts to achieve the 73 billion yen target we announced at the 2Q financial results announcement. We have been able to implement the price increase, and we believe that this will lead to an improvement in profitability as retail prices rise. However, we believe there is a possibility for a rebound of the temporary demand to continue through November and beyond, so we will have to wait and see. In addition, we believe that the continued increase in marketing investment by our competitors may have an impact on our sales, but we are aiming to achieve the plan while taking into account the downside risks. It will be challenging for Kirin Beverage to cover all cost increases by the price increase this year, but we believe it can achieve its targets through cost controls. The Company as a whole is on track to achieve the revised Normalized operating profit target of 172 billion yen. We will absorb the cost increases to steadily achieve the target. In the Pharmaceuticals business, growth of the global strategic products is progressing in line with the plan, despite some variation by region and drug. With the drive from foreign exchange rates, we believe that we will be able to land on the plus side. As for Coke Northeast in the U.S., we are in a good business environment with volume growth, although we are raising prices in the face of heavy inflation. We believe that profits will increase exceeding the plan.

(Hayashi) In the Australian business for 3Q, the recovery of the on-premise channel as well as the implementation of price increases have contributed to improved profitability. Sales of the on-premise channel have returned to 90% of the pre-COVID-19 level. Profit improvement measures are being implemented in response to the cost increases. In addition, profit contribution from the U.S. craft business contributed to strong profits through 3Q.

Q. Despite the high hurdle to increase profit by 9 billion yen in H2, off-premise sales volume did not achieve its target, but profit was not bad. Is this because of the growth of the on-premise channel and U.S. craft which has a better mix of products?

A. (Hayashi) The off-premise channel was down 5% YoY for January to September. We believe it will be a challenge to make a quick recovery. Since strengthening the brand is a management issue, we will not reduce marketing expenses through cost controls this fiscal year, but will make solid investments. Although we will make efforts to raise the top line toward the peak season, we view the H2 targets to be challenging. (*Note: Previous year's 3Q was significantly affected by the COVID-19 lockdown, so the increase in profit for the July-September period appears larger.)

Q. You mentioned that the cost increase for the next fiscal year will be 45 to 50 billion yen. What is the reason for the increase from a few months ago and where is the cost pressure? What will be the profit drivers to offset the costs to achieve the profit level that you plan to raise further in the next fiscal year?

A. (Akieda) The level of cost increases rise each time we update our plan. Most of the cost increases are raw material prices, due to the prices of commodities themselves and the impact of foreign exchange rates. In particular, the prices of imported raw materials, etc., have been rising. Kirin Brewery has annual contracts, so we are currently in the process of negotiating next year's prices. The cost of raw materials, etc. contracted in yen is higher than the previous forecast due to the effects of both the raw material market conditions and foreign exchange rates. In Japan, the cost of electricity, gas, and other crude oil-derived fuels has also risen considerably. Although we can make a hopeful observation that prices will not rise any further, we still cannot be reassured. The price revision in Japan this year is expected to offset the cost increases for the next fiscal year. In order to achieve next fiscal year's profit level, in addition to Kirin Brewery, Kyowa Kirin, which is growing as a global specialty pharmaceutical company, and Coke Northeast, which is performing well in the U.S., will contribute as the growth drivers of profits for the next year.

Q. What are the profit drivers for Kirin Brewery?

A. (Akieda) The biggest profit driver is the incremental profit from the annual contribution of the price increase. In addition, the mix will be improved by growing premium products while investing in brands.

Q. You have been holding back on marketing investments for the past few years, what will you do next year?

A. (Akieda) We will invest the amount necessary to increase brand equity while keeping an eye on the competitors. We have no intention of reducing our investment to a level that would damage the brand.

Q. What is Lion's results for July-September in the on-premise channel, off-premise channel, and the market? How much has the marketing transformation that is currently being implemented contributed to the results? Please also tell us about the profit drivers for the next fiscal year.

A. (Hayashi) The on-premise channel was approximately double the previous year's level due to the impact of a lower volume last year, partly due to the COVID-19 lockdown, and the off-premise channel decreased by 10% YoY. We recognize that the market is not significantly different from that of Lion. In response to the cost increases in the next fiscal year, we will increase profitability by raising prices and reducing costs. Lion will increase its investments in marketing. Sam Fischer, the new CEO, is currently working on the plan for the next fiscal year, so please wait for next year's announcement for more details.

Q. Are there any successful examples of Lion's marketing transformation?

A. (Hayashi) XXXX (Four-X), the brand with the priority marketing focus, had negative impacts in H1 such as Omicron and the floods, but it is performing at the same level as the previous year and is in-line with the plan, which we believe is a positive sign. Lion also plans to focus on Hahn, its third largest brand by sales volume, from now on into the 4Q.

Q. I would like to know more about Kirin Brewery for the next fiscal year. The initial assumption of the profits effects for the price revision was 30 billion, and since it was 8 billion this fiscal year, it would be about 20 billion for the next fiscal year. Even if the price revision takes full effect, with a cost increase of almost 20 billion, it seems that profit will not increase?

A. (Akieda) Your understanding is correct, but the assumption of incremental profit from the price revision that we had previously explained was not a definite value. At this point, we believe that there will be a slight increase in profit, and that the increase in profits from the price increase will be more than enough to cover the cost hikes. However, since this will be offset by a decline in demand, we will consider controlling costs if demand goes below our expectations. We have not yet seen the full impact on demand. Although it is within our expectations at this point, prices are rising for various products, and if income do not rise, people may become more conscious to spend money.

Q. Regarding down-trading after the price increase at Kirin Brewery, is there an emerging trend towards saving money? Could you give us more details?

A. (Akieda) At the moment, there has not been any major shift to cheaper products, but it depends on the income environment going forward.

Q. You mentioned the profits effects of the price increase was 30 billion yen after factoring in the elasticity of 0.4, but was the elasticity higher than expected or was the profits effect higher than previously assumed?

A. (Akieda) The range of price increase varies by product and container. We believe that the price will be higher than initially expected because of the effects of the changes in the product mix. The downside risk is difficult to read. It would be simple if only beer were to increase price, but since many other products have also seen price increases, we would like to wait for an analysis of how this will affect consumer behavior.

Q. Kirin Brewery initially announced that costs will increase by 10 billion yen, but that has now turned into 20 billion yen. In other words, there will be an additional cost increase of 10 billion yen, but are you going to make drastic cuts in marketing investment? What are your thoughts on additional price increases?

A. (Akieda) The situation has changed since the initial assumption, and we are considering how to use variable marketing expenses accordingly. We do not think it is necessary to make drastic changes in marketing expenses. We will need to consider price increases if the situation with raw materials and demand fluctuates in the future. Next fall, the liquor tax will be revised, and it will be difficult to revise prices at the same time as the liquor tax revision, so even if we do raise prices, we would like to consider the timing.

(Matsuo) As of 2Q, we had mentioned that Kirin Brewery's cost increase forecast for the next fiscal year would be 10 billion yen for cans. I would like for you to understand that the total estimate of 10 or more billion yen is raised to 20 billion, which does not mean that we are increasing the cost by 10 billion yen.

Q. Lion and Coke Northeast have performed very well in 3Q. What are the latest U.S. consumption trends and potential risks going forward?

A. (Hayashi) At the moment, demand is catching up despite price increases in the overseas market. We need to keep a close eye on consumption trends with the possibility that the market will soon reach a plateau. In particular, according to the October results, the Australian off-premise channel is performing soft, and we believe that this should be taken into consideration. On the other hand, soft drinks are an essential product, so we do not think we need to worry that much.

Q. In the July-September period, sales and unit prices of Coke Northeast grew on a local currency basis, but did the volume grow?

A. (Hayashi) Volume is also growing by single-digit percentages.

Q. Looking at the retail prices of Kirin Brewery, the pricing policies do not seem to be aligned. For example, for zero sugar beer and RTDs, there is a price gap with the competitors that have not raised their prices. Do you see any difference in momentum?

A. (Akieda) As you are aware, there is some price variation in zero sugar beer and RTDs, but at this point, this price difference does not have a significant impact on the competitive environment, and there is no impact on momentum.

Q. You mentioned that you have been able to implement price revisions in Japan that can absorb the cost increases in the next fiscal year, but what about Kirin Beverage? If the cost of raw materials increases by 7 billion this fiscal year and 10 billion for the next fiscal year, won't you be unable to absorb the higher cost of raw materials because you said that the profits effect of the price revision would be 10 billion? Will there be any change in the price revision effect? Will there be an upside effect?

A. (Akieda) Kirin Beverage's profit level from 2021 to 2023 has changed from 20 billion yen to about 18 billion yen, so please understand that we have not been able to absorb the costs. I mentioned earlier that we will be able to cover next year's cost increase with this year's price revisions. One change in the market environment is that vending machine prices are also being revised. Therefore, we believe that we will be able to absorb the cost increase in the next fiscal year because we are getting more of the effect of the price revision than initially expected.

Q. I understand that the Health Science domain and Kyowa Hakko Bio are in a challenging situation. Will you be able to turn the business around for the next fiscal year? It seems that Citicoline is not selling as well as expected in the U.S. Please explain whether the situation is a drawback or whether it can be resolved.

A. (Akieda) It is true that sales of Citicoline in the U.S. have slowed. There had been quality issues and supply challenges. Sales were not going well during the period when there were these issues. We are on track to resume sales, but we are slightly behind the schedule. We would like to resolve the situation by strengthening sales promotion to make up for the delay.

Q. Is it correct to understand that Kirin Beverage will require further price revisions to return to its original profit level? Can Kyowa Hakko Bio achieve a V-shaped recovery?

A. (Akieda) Your understand is correct regarding Kirin Beverage in terms of returning to a pre-COVID-19 profit level. However, there are a large number of players in the beverage industry, and it will not be easy to revise prices. It will be difficult to implement a price revision by a single company, but we will consider the possibility without ruling it out. Regarding Kyowa Hakko Bio, although it will depend on the level of the V-shaped recovery, we are working steadily to recover from the quality issue and build a structure that can generate profits. Although the timing has been delayed, we would like to make it a highly profitable business as the core of our BtoB business in the health science domain. We intend to take on the challenge of recovering profits in the next fiscal year as well.

Q. Compared to the original plan for H2, it appears that raw material costs for domestic alcoholic beverages were lower than expected in the 3Q. Also, in the Others in Others, the plan was that there will be LC-Plasma related costs incurred in H2, but was this cost not incurred in 3Q? Please explain the details. Finally, please share the progress of system expenses in corporate expenses.

A. (Akieda) Regarding the cost of raw materials for domestic alcoholic beverages, Kirin Brewery has mainly annual contracts, so the price impact in a single year is small and costs did not increase as much as expected. As for the Others in Others, we recently rolled out new commercials for LC-Plasma, but the timing of this brand investments has been shifted to October and beyond, and Myanmar Brewery's profit has been added as well, so it appears that no costs were incurred in 3Q. Fortunately, our system have been operating more stable than expected, so system expenses have not been incurred as much as planned.

Q. Kirin Beverage's mix was expected to improve in H2, but unit price fell in 3Q. Please explain the situation.

A. (Akieda) Kirin Beverage is focusing on small PET bottles, but we also consider large PET bottles such as 2L to be important SKUs for *Nama-cha* and *Gogo-no-Kocha*. We have been investing in marketing if we can ensure that it will be profitable, and attempted a sales promotion during the July-September period, which is the peak season for Kirin Beverage. As a result, the mix appears to have weakened slightly in 3Q alone compared to the past periods.

Q. Has the focus on small PET changed?

A. (Akieda) Not all quarters will have this mix. We will implement promotions for large PET bottles when demand can be seen and profits can be expected.

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