

**【Q&A Session Minutes】**  
**Presentation on FY2019 Financial Results**

Date: February 17, 2019 (Mon), 10:00-11:30

Presenters: Yoshinori Isozaki, President & CEO; Noriya Yokota, Director of the Board, Senior Executive Officer & CFO; General Manager of Corporate Planning Dept., and General Manager of Accounting Dept.

Q. The Normalized Operating Profit forecasts for FY2020 are at the same level as the results of FY2019. How much do you expect the upside and downside risks are? Given the guidance of 2019 MTBP, the Normalized EPS growth in FY2021 should be around 20%, but is it feasible?

**Isozaki:** FY2019 results and FY2020 plan are not satisfactory. We achieved the FY2019 plan, but I do not think it is necessary just to achieve it. I believed that we would be able to earn more profits, but as a result the extents to which Kyowa Hakko Bio and Lion did not achieve the forecasted profits were beyond the expectations. It is necessary to rebuild as soon as possible. At the beginning of FY2019, Kyowa Hakko Bio anticipated JPY8-9 bn in Normalized Operating Profits, and Lion did not anticipate any decline. The changes in the business environment have exceeded expectations although we managed to achieve the planned Normalized Profits. Similarly we should achieve FY2020 plan at least. We will endeavour to rebuild the businesses above, recover earnings, and exceed our plan. The growth driver will be Health Science, but the contribution to earnings will be from next year onwards and will grow gradually.

Q. Please explain about the current situation in Australia.

**Isozaki:** Lion BSW is in an extremely tough situation. In the past several years, Australian beer market has been suffering from the volume decline of around -2%, but Lion has made profits by raising prices. However, there are limits to price increases. Moreover, the presence of national brands has been declining worldwide. Thus, the market will be in a downtrend at the macro level. Against the backdrop, Lion aims to raise profitability by cultivating highly profitable products in such categories as contemporary, premium, craft. As I mentioned at the presentation on 2Q 2019, competition in the Australian beer market intensified significantly by the aggressive price competition of the rival in the 1H of 2019, which has been eased. Lion recognized that it needed to further strengthen their brands and more shift their focus on profitable products. We are not going to lead price competition.

Q. Please explain more about FY2020 guidance. Will the forecasts for profit declines at Kyowa Hakko Bio and cost increase in Lion corporate be one-time? Is it fair to think that profits from FY2020 onward are expected to increase? The long-term vision is outstanding, but Kirin needs to show the ability to grow until it reaches there so that we are persuaded the vision is feasible. What about profits from FY2021?

**Yokota:** As Mr. Isozaki explained earlier, the environment of the Australian beer market has been changing, and it has been more and more difficult to raise prices. Product prices have continued to rise due partly to the effects of Container Deposit Scheme, and consumption has stopped growing. The situation is closer to the Japanese beer market. Kirin Brewery has invested in brands and achieved profit growth over the past few years. We have frequent discussions with Lion leadership, and by leveraging Kirin Brewery's best practices, Lion's profits can turn around. We think it necessary for Lion to come back into growth stage during 2019 MTBP. The profit forecasts for Kyowa Hakko Bio in FY2020 resulted in a negative surprise. Kirin Holdings owned 95% shares in Kyowa Hakko Bio and Kirin's people have entered it, and the problem has become clear. Although Kyowa Kirin has the strength in R&D, Kirin can be stronger in the area of manufacturing management. Currently, Kirin's human resources are allocated to resolving the issue. We are confident that we can solve the problem by manufacturing according to the procedure. We should recover profits quickly and make them even better than before. Kyowa Hakko Bio will be in the red in FY2020, but we also think it should recover within 2019 MTBP. Lion and Kyowa Hakko Bio both will be able to get into growing stage in the next medium-term business plan, which will bring together food, pharmaceuticals, and Health Science. We should achieve it in a couple of years.

Q. Do you mean that the profit decrease from the problem of Kyowa Hakko Bio can continue in the next fiscal year as well? Is it unlikely that the profits will return to the level of FY2018 by 2021?

**Yokota:** It would be difficult for Kyowa Hakko Bio to recover its profits to the level of FY2018, JPY8 bn, by FY2021, but we would like to return it to that level as soon as possible. While solving the problem, Kyowa Hakko Bio and Kirin Holdings will increase the sales of high-value-added materials. Kyowa Hakko Bio sells high functioning amino acids for pharmaceuticals raw material, and there are few suppliers globally in the sector. While raising prices for existing products like the competitors, we would like to recover earnings.

Q. Are synergies with FANCL in the presentation under the current ownership? If Kirin Holdings acquire majority shares in the future, would it be more likely to create more?

**Isozaki:** Synergies of JPY5.5 to 7bn are under the current ownership. Increasing equity is

quite another because Not only Kirin but also FANCL's Board decisions are required. FANCL and Kirin are focused on maximization of synergies at this stage.

Q. What are the proportions and growth rates of both the Australian beer market and Lion by category in 2019? Also, what are your forecasts for revenues excluding New Belgium Brewing, etc., which will be consolidated from FY2020? What will the strategy will be in 2020 taking FY2019 into consideration?

**General Manager in charge:** Lion forecasted a decrease in beer sales volume in Australia in 2019, but the results were below the plan. Although it achieved the sales volume target in the 2H, Lion was unable to recover the shortfall in the 1H. By category, classic category products represents 30-40% of the total market, while Lion has a higher ratio. We cannot talk about detailed figures here, but classic category tends to decrease and contemporary increase. As Lion has higher percentage of classic category than the market, its sales volume decreased more than the market. The main reason why revenues are expected to increase in 2020 is consolidation of New Belgium Brewing, which generated approximately 200m USD of sales in 2018. Sales volume in Australia alone are expected to be negative by about 1%. Lion will be more focused on brand strengthening to improve its mix and shift from classic to contemporary, craft, and premium. To do so, it will invest in brands and focus on 5 brands, including *James Square* and *FURPHY*.

Q. What is the risk of impairment of Kyowa Hakko Bio?

**Yokota:** It depends on the future cash flows, and we currently believe that the decline in earnings is temporary. There are few global suppliers of high functioning amino acids, and there will remain demands for them. It is necessary to restart the manufacturing process according to the procedure, verify the record of manufacturing and quality by a third party, and obtain approval from the authority, the Ministry of Health, Labour and Welfare, etc. I would like you to understand that the operating loss will be temporary.

Q. When do you expect the authority will allow the factory to resume production?

**Yokota:** Kyowa Hakko Bio has already resumed production of some products. Approvals will be made gradually while confirming each process.

Q. Will the problem of Kyowa Hakko Bio have a negative effect on the synergy generation with FANCL?

**General Manager in charge:** We do not think there will be such impact. This issue relates mainly to pharmaceutical ingredients. As shown in the presentation, Kyowa Hakko Bio's

strength to generate synergies with FANCL is the capability to create new ingredients with the power of microorganisms, produce large quantities of ingredients in low cost, and refine materials. FANCL understands it, too. The synergy between Kyowa Hakko Bio and FANCL is expected to be around JPY3bn due to cost synergies stemming partly from the construction of a new plant by FANCL.

Q. I understand Kirin's long-term vision and its path to growth, but do you think that the current business portfolio is perfect? Do you think there need to be improvement? From the market perspective, there is a view that the Kirin Group's business structure is still halfway. For example, Kirin Holdings still owns approximately 50% shares in Kyowa Kirin. What challenges do you think there are, or are you satisfied with the business portfolio now?

**Isozaki:** I think it almost impossible to get to the best portfolio no matter how hard you work. I'm not satisfied with what it is, and I don't think it will be satisfactory. We are always considering Kyowa Kirin, but we should focus on how much synergy we can generate with it instead. The first priority is synergy.

Q. How much synergy can you generate with Kyowa Kirin? What kind of synergy do you expect?

**Isozaki:** Basic research is the same, although the output can be pharmaceuticals or food and beverages. Pharmaceuticals require more precise clinical trials. In some cases, clinical trials are conducted in the Health Sciences, but they are less time-consuming and less expensive than pharmaceuticals. If it is judged that it is useful as a medicine in the course of research, you can go to the medicine. Even if it is judged that commercialization as a pharmaceuticals is not implemented, there is a possibility in the Health Science. Pharmaceutical data are very useful in doing so. Based on this data, we can shift to Health Science. Pharmaceuticals data is the key to synergy.

Q. Kirin Brewery's Normalized Operating Profits in 2019 did not increase if excluding the effect of corporate cost reclassification. It was able to win competition and gain momentum, but its profit did not grow as the mix deteriorated. It is important to increase profits by increasing sales and improving mix in 2020. I think the only answer to how to improve the mix is to strengthen *Kirin Ichiban*, with which Kirin Brewery was not able to grow profits so far.

**Isozaki:** I think that Kirin Brewery was able to achieve the planned profits with such a negative trend. Previously, Kirin Brewery launched new products every year, but in 2019, it did not launch new products or did not offer more discounts. We have a higher proportion of

new genre than the market, and the mix has deteriorated according to the trend. The liquor tax on traditional beer will be lowered this year. Among these, I think the question is how we can realize premiumization. We will keep a close eye on the competitors and take action if there is an opportunity. The liquor tax revision is adverse to new genre, and the outflow to RTDs is expected to continue. However, Kirin Brewery is steadily controlling sales promotion expenses. The current consumption deteriorates the mix, but Kirin is not spending as much sales promotion expenses as it used to. And I want to raise prices if there is a chance. Kirin Brewery is also further strengthening craft beer which leads to an improvement in the product mix.

**General Manager in charge:** Kirin Brewery is particularly focused on caned products of *Kirin Ichiban*. As some worldwide events are supposed to be held in Japan, Kirin Brewery will focus on cans in the mass retailers. In addition, it is working to strengthen its non-alcohol beer taste beverages, in which it had not previously invested, with the aim of improving its product mix.

Q. The liquor tax revision will accelerate the shift to RTDs from beer products, and the competitive environment will become quite fierce. Competition is also expected to intensify in new genre the liquor tax of which will increase due to brand shakeout. What do you expect the business environment will be like from this coming October?

**Isozaki:** Shifts to RTDs are expected to continue and will have an impact on new genre. Strengthening the brand remains crucial, and it makes no sense to compete on prices. Kirin Brewery is spending on brands, not to discount. In new genre, we will nurture *Honkirin* so that customers will choose it. I think brand strengthening of *Kirin Ichiban* has been going very well, and there will remain to be an opportunity. If there is an opportunity, I would like to think about price increase, but it also depends on the competitive situation.

Q. I understand Kirin Brewery would like to raise prices for beer if there were opportunities, but what about the price of new genre? Do you think every competitor will pass tax increase on?

**Isozaki:** Every company is struggling to raise profits, and it is also difficult to raise volume, so I think they will put importance to prices.

Q. To what extent has Kyowa Hakko Bio recovered so far? Although the issue appears to have been related to the management of Kyowa Kirin, how do you evaluate the JPY130 bn investment? It seems uncertain because the deal was between the parent and the subsidiary. Could it also lead to the issue of compensation?

**Yokota:** Some products have already been manufactured and shipped again, but we are currently in the process of developing a turnaround plan, and we are still unable to provide an overall timeline. We would like to recover as soon as possible. Disclosure will be made at the appropriate time. Kyowa Kirin was not aware of any deviation from the manufacturing procedures and discovered it after the share transfer. By allocating appropriate human resources, Kirin Holdings will rebuild Kyowa Hakko Bio. I decline to comment about the responsibility, but we will work to resolve this issue in a reasonable manner because Kyowa Kirin also has its own shareholders.

**Senior Manager of IR Section:** Production will not be resumed at once, but will gradually recover. We will communicate our progress on such occasions as today.

Q. I understand that the business environment for the domestic beer market remains severe. It is difficult to improve profitability without raising prices. What are the conditions for raising prices? Also, demand shift to RTDs is unavoidable, and so how can you improve the profitability of RTDs? How can you build a profitable structure that can earn through RTDs?

**Isozaki:** To improve profitability, it is needed either to raise sales prices or to cut sales promotion measures. Regarding selling prices, the first step was to revise the guidelines. However, if the next step is to raise prices, I cannot say more than I mentioned earlier. Changing trade conditions of RTDs has the biggest impact on its profitability. On the other hand, what we can do by ourselves is to lower logistics costs and raw material costs. Kirin Brewery continues to reduce logistics costs and review and improve raw materials. The other factors are difficult to be changed by ourselves alone. We want to change the environment whenever we have an opportunity, but we do not think it is possible to do it alone because we did it to fail in the past.

Q. Kirin Beverage has been doing well. Previously, however, you mentioned it was difficult to survive on a stand-alone basis. Do you think you can do it alone or still need some kind of partnership in the long run?

**Isozaki:** Japanese soft drink industry as a whole is very tough. Reorganization can happen. To this end, it is essential to strengthen its own business and brands. In the future, if reorganization is realized, the condition will be disadvantageous if the business is not solid.

Q. Myanmar Brewery expects Normalized Operating Profits to reach JPY15 bn. Please explain how you view the current situation including the market environment which can be tougher with Thai Beverage entering the market. What will its positioning in the Kirin Group be in the future?

**General Manager in charge:** Myanmar Brewery is performing very well. While the market is growing, the economy category is the fastest growing and the mix is deteriorating. However, Myanmar Brewery is expanding its sales volume to exceed the market. Manufacturing capacity has also been strengthened to meet the increased demand in the market. Going forward, while investing in production facility, Myanmar Brewery will work to strengthen its mainstream *Myanmar Beer* in order to further raise profitability.

Q. I would like to ask of Kirin's ownership of Kyowa Kirin and FANCL. If synergies are to be realized, it may be better to increase the company's ownership before achieving it, do you think? Kyowa Kirin was successful in growing through the global 3 products, and the pressure about listed subsidiary is getting bigger. What do you think at this point?

**Isozaki:** I am aware of the problem investors point out. We will continue to engage with the market and find the best answer. As for FANCL, we cannot decide our ownership by ourselves, and the first priority is to synergy creation. We aim to generate the synergy as I presented or more, and consider the ownership thereafter.