

Minutes of telephone conference on Q1 financial results of FY2020

<Date and time> 4:00 p.m. – 5:00 p.m., Tuesday, May 12, 2020 (JST)

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- Q. It is very helpful that you have disclosed the forecast of the impact of the new coronavirus on sales volume from April to June. I trust the disclosed figures. Given the worst-case scenario in the subsequent third and fourth quarters, what numbers do you envision? I would like to see some suggestions about beer and soft drinks in Japan, and beer in Australia. Furthermore, what are the likely worst-case scenario about sales volumes for fiscal 2021?
- A. We have only given our estimate of the sales volume at this time, and it is all we can now. Given the government's May 14 and 21 expert meetings on Japan's declaration of a state of emergency, as well as the move to ease self-restraint in Australia, we think that the bottom will be reached in April or the three months from April to June. At the moment, it is very difficult to assume what will happen after July, so we would like you to make an estimate based on the range of sales volume forecasts for the period from April to June.
- Q. I would also like to see an indication of Normalized OP estimates for the same period. Should we assume that beer sales volume will be around -10% from July to September in both Japan and Australia based on April results or forecasts for the period from April to June? Assuming a decline in marginal profit of about 10 billion yen, do you want to make up about half of that amount?
- A. The sales volume may be around this level, but, as for Normalized OP, because there are too many factors that could have an impact, such as unit sales prices, we would like to refrain from giving figures of the impact on it to avoid some misleading information. I would like you to refer to the information disclosed, such as the marginal profit impact from January to March. The company is also considering cost reductions in response to the lowering of the top line, but will consider all possible cost-cutting measures, especially for beer as the mix will deteriorate. I can't give specific numbers at this time.

Q. Will domestic beer sales volume start recovering around Q4?

A. If the worst-case scenario continues, the situation in April will continue, but it's hard to say how much it will improve in the future.

Q. With regard to the sales volume estimate of retailer for soft drinks (see P13 of the presentation), the results for April were down and are expected to continue to be down from April to June. Why are you assuming a decline in all channels, not just convenience stores?

A. In addition to the impact of the refraining from going out, Kirin Beverage is not able to conduct in-store sales promotion activities as usual. Also, Kirin Beverage's sales volume was strong last year, and so a rebound from it is included.

Q. How did the market for beer and soft drinks in April?

A. The market is still unknown. As noted in the presentation materials, Kirin Brewery's sales volume in April was -14% for all beer products, -49% for beer, +0% for happo-shu, and +6% for new genre; for the four months from January to April, it was -5.7% for all beer products, -23% for beer, -4% for happo-shu, and +6% for new genre. Soft drinks performance by channel for the four-month period from January to April was -0.6% in retailer, -11% in convenience stores, -14% in vending machines, and -6.5% for soft drinks overall.

Q. With regard to the creation of synergies with FANCL, I believe your target for fiscal 2020 was 500 million yen to 1 billion yen, mainly from channel synergies. (*Channel synergies of 500 million yen to 1 billion yen are expected in 2024). Will there be a delay due to the new coronavirus? Is this situation advantageous for the health category?

A. There are no changes to the plan at this time. Due in part to the growing health consciousness, the number of accesses through mutual customer referrals between the FANCL and Kyowa Hakko Bio channels is also increasing steadily. Preparations for new products to be launched in Q3 and beyond, including the development of supplements, are proceeding as planned. The growing health awareness is a tailwind. In fiscal 2020, the company plans to achieve single-digit hundred of million yen in single-year Normalized OP from synergies.

Q. What is the impact of consolidating New Belgium Brewing out of Lion BSW's revenue +A\$78m and sales volume +17.8% year on year? It also states that "Other" in the change in Normalized OP is -A\$101 million and there was the impact of coronavirus including the decision to take back full kegs from our pubs and bar customers in the explanation section. I would like to know more about it.

A. New Belgium Brewing's consolidation impact was about half of Lion BSW's sales volume increase of 17.8%.

About two thirds out of the -A\$101 million "Other" were deterioration of price and mix. A shift from premium to established brands was seen since the beginning of the year due to the bushfire and floods, and the impact of the new coronavirus, which led to a higher percentage of sales of products such as XXXX Gold. It also includes the impact of the company's pricing strategy over the last year to maintain sales volume. The remaining one third includes -A\$8 million cost increase for taking back full kegs from customers. In addition, costs associated with the start of the consolidation of New Belgium Brewing have been included as an expense.

Q. How will Lion BSW's deteriorating price and mix affect April-June performance?

A. At present, this situation may continue for some time, as we are seeing a shift to, for example, 30-packs standard branded products. There has been a shift to home use due to the closure of restaurants, with stock demand coming in through March and its impact in April. In addition, the increase in home use has led to lower prices, but we expect to see a change in purchasing behavior due to deregulation.

Q. Is the margin higher for on-premise channel even at Lion BSW?

A. That is correct.

Q. Kyowa Hakko Bio's first quarter results show a 3.9 billion yen decline in revenue, but to what extent are quality issues affecting the company's results? With respect to the recovery of customers, would you like to explain how many businesses have been affected and to what extent they are recovering?

A. Most of the 3.9 billion yen decrease in revenue was due to a decline in the BtoB business, which was directly attributable to a decline in manufacturing at the Hofu Plant. We are proceeding with the relaunch from suspension of production,

while obtaining approval from the Ministry of Health, Labor and Welfare and Yamaguchi Prefecture. Due to its relationship with the authorities, it is not possible to give details of the approval to resume production. In Q1, it was slightly below plan, but the company is gradually resuming production while selling inventories. The launch will be accelerated in the future. Although the company's performance appears to be down at the moment, we believe that the full-year plan is still achievable.

Q. There is no mention of Kyowa Hakko Bio in the new coronavirus impact slide on P13 of the presentation material. Will it have no impact on the revitalization plan?

A. As for Kyowa Hakko Bio, the new coronavirus effect is not so much. There have been much demand about pharmaceutical ingredients, and we believe that an early recovery in manufacturing is necessary.

Q. With regard to the impact of the new coronavirus in the presentation on P13, please explain the rate of increase or decrease in March by channel, although Kirin Beverage's March sales volume was flat year on year. I would also like to know the March growth rates and on-premise ratios for Lion, Myanmar Brewery and Cork Northeast.

A. We have never disclosed details by channel on a one-month basis. Please understand the objective of the disclosure in details by channel on the presentation is to make the estimate of new coronavirus impact from April to June as clear as possible.

Q. The difference of change in products mix and in composition ratio of containers of Kirin Beverage in Q1 was up 300 million yen year on year. How would it have been if the effect of large PET price hikes had been excluded?

A. The following is a rough breakdown of the difference of change in products mix and in composition ratio of containers. The negative impact was due to an increase in logistics costs and a decline in sales volume at vending machines and convenience stores from late February to March, which resulted in a negative channel mix. Positive factors included last year's large PET price hike, an increase in small PET (ONEDAY BLACK), and a shift from bottle-shaped cans to small PET, which resulted in an overall improvement in the container mix. Including the impact of a decrease in sales of SOT cans, the net total of all these factors increased by 300 million yen.

Q. In Kirin Beverage's full-year plan, the difference of change in products mix and in composition ratio of containers is expected to increase by 1.3 billion yen, but given the impact of the new coronavirus, do you think it is inevitable that the mix will deteriorate in the second quarter and beyond?

A. The impact is inevitable because overall sales volume will be lower.

Q. Kyowa Hakko Bio posted a Q1 loss of 1.4 billion yen, compared to a full-year loss plan of 2.0 billion yen. It seems to me that the decline in profits is large, but how is it progressing? Is it correct to understand that the budget is designed so that the loss will be larger in the first half of the year?

A. In Q1, the speed of the relaunch was slightly lower than planned. This resulted in a profit level that was lower than planned, as you pointed out. The company plans to move closer to its full-year plan in the second half of the year, as the fixed cost per unit of production decreases as production volume increases in the third and fourth quarters.

Q. Why was Kyowa Hakko Bio's decline in Normalized OP larger than expected when compared to revenue decrease? Also, it is said that manufacturing will be approved in due course, but what will be allowed to resume, and to what extent can sales be controlled? Also, what will happen in the second quarter and beyond?

A. Production will be restarted after confirming the manufacturing procedures of the product and receiving approval from the authorities. We are currently keeping our customers waiting, including drug manufacturers, and so we prioritize such items. Based on that priority, production volume will increase as we gain approval from the authorities. In addition, we will strive to improve profits by controlling SG&A expenses, including in the B to C business.

Q. What percentage of Kyowa Hakko Bio's products have been approved by the authorities as part of the annual plan?

A. The number of items is confidential. I would like to refrain from giving details.

Q. I believe that you were planning to make a large investment in ERP introduction for the corporate and Lion corporate in your initial plan for the year, but is this investment also suspended? How much of a cost buffer do we have as a company?

A. The head office and operating companies have been trying to cease all investment and cut costs as much as possible. However, ERP-related costs have already been incurred, and stopping the plan would result in higher costs due to the prolonged implementation of the plan, so we are basically proceeding as planned.

Q. I think it will also change how much cost can be controlled by suspending investments depending on the situation on the top line. How much decline from top line decrease can be absorbed on the cost side?

A. This is directly related to how far we can see the impact of the new coronavirus, but it is difficult to do so at this time. We will deepen the discussion about what the top line will look like and how far we can cut costs accordingly. It's hard to give a concrete answer at this point.

Q. Will Lion BSW's "Other" of -A\$101 million increase from Q2 onwards? Or is the "Other" in the first quarter large because it includes the cost of taking back the kegs? Also, do you include the impact of cost reductions in the first quarter results?

A. It depends on the convergence of new coronaviruses and cost-cutting, but it is impossible to say that it will shrink in the second quarter. To the extent possible, cost savings have been made and the impact is partly included in -A\$101 million. In addition, costs associated with the start of the consolidation of New Belgium Brewing have been included as an expense.

Q. What is the current state of the sale process for the Lion Dairy and Drinks?

A. The ACCC (Australian Competition and Consumer Commission) approved it in February, and it is currently awaiting approval from the Foreign Investment Review Board (FIRB). The timing is up to the authorities, but we expect it to be closed in the second quarter.

Q. After the new coronavirus has been contained, I believe the Japanese beer market will see a change in ratio between on-premise and home use, more home drinking, and an acceleration in down-trading. It is true that Kirin Brewery is in a relatively advantageous position compared to the competition, but I still think all players're going to have a hard time with channel deterioration. Given that the market will change after the convergence of the new coronavirus, how is the

company discussing additional measures and revising its strategy in order to achieve a 25% Normalized OP margin on sales revenue excluding liquor tax by 2027?

- A. There are something to change and somethings to keep. What hasn't changed is the company's strategy of investing in and strengthening key brands rather than relying on new products and focused marketing, which it has been pursuing so far. Because of this, Q1 results were steady. On the other hand, what needs to be tweaked is a strategy that takes into account the change in consumption behavior of customers and the state of society after the new coronavirus. The changes that have existed in the past, such as EC, SNS, home delivery, and health consciousness, may accelerate, while things that have temporarily left us may return, such as television viewing and home cooking. We do not yet know if on-premise channel, department stores, and so forth will recover. We are considering how to strengthen our future investments, including in EC and subscriptions, too.

Q. Does this mean that the main focus is on marketing strategy? You have been aggressively reducing marketing expenses for on-premise channel, will you continue to do so?

- A. The company has already made efforts to improve the efficiency of sales promotion expenses for on-premise market and will continue to do so, but in addition, the company will continue to reduce allover costs. We will work to change fixed sales promotion costs to variable costs and to reduce other fixed costs as well.

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