

Briefing Materials for FY2024/2Q (August 1, 2024)

Question and Answer Session

Satoshi Yamaguchi, Representative Director & President

Takeshi Saeki, Managing Executive Officer, CFO and CRO

Q1

Your 2024 outlook for the vegetable beverage market size assumes that it will bottom out. I feel that the functionality of vegetable beverages is ambiguous and it appears to me that the market has been influenced by other markets. What is your outlook for the market size and whether it should be recognized as a sustainable reversal, i.e., a change in consumer perception of the vegetable beverage market? Can you share your thoughts? (UBS Securities Japan Co., Ltd.: Ihara)

A1 (Yamaguchi)

We predict that the vegetable beverage market will reverse course this year for the first time in years. There are two reasons for this prediction.

First, tomato juice is driving the overall vegetable beverage market. In the past, these beverages were mainly for the elderly and for those who were concerned about blood pressure and cholesterol, but now the number of young women who are interested in beauty has increased significantly, and, as a result, sales are doing well. This trend started last year and we expect it to continue in the future. In addition, the purchase rate of tomato juice is still only about 10% overall, providing room for expansion. Going forward, we believe that the strong performance of tomato juice is likely to drive the market for vegetable beverages.

Second, sales of the Yasai Seikatsu series, which had been sluggish, have been recovering, mainly at convenience stores, due to our measures to stimulate demand.

These are the two main reasons why we expect the overall reversal of the vegetable beverage market to continue going forward.

Additional Question

Should we understand that Kagome has been increasing its market share and that the market has been sluggish, but we are now entering a phase where the market is also expanding? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

Yes, that is correct.

Q2

What is your outlook for the International Business in the next fiscal year and beyond?

This year, the International Business was experiencing a tailwind thanks to the high price of tomato paste, but the price of tomato paste is expected to decline in the future.

Can you share your thoughts on how much this price is expected to decline and how you estimate the impact it will have on the International Business. Also, in a situation that is affected by the price of tomato paste, is there an ideal core operating income and core operating income margin for the International Business. What would this actual amount look like? (UBS Securities Japan Co., Ltd.: Ihara)

A2 (Yamaguchi)

The market for tomato paste is expected to start to decline after the 2024 production run. This is due to the fact that market conditions have risen sharply over the past few years, and primary processing manufacturers in various countries have started to increase production. Prices will be affected by how much primary processed tomato products can be produced this summer, but this summer's production has just begun, and information on the progress of production in each country has not yet been determined. Therefore, it is still difficult to predict how much the market for tomato paste will decline. After another month or two, the situation will become clearer.

For Kagome's International Business from FY2025 onward, we are facing two challenges: how to rein in volatility in primary processing, including synergies with Ingomar, and how to secure growth in secondary processing. While looking at the balance between the two, shifting from a structure with a high ratio of primary processing to a structure with a high ratio of secondary processing over the medium term should lead to the stable growth and profits of the International Business.

At this time, it is difficult to answer the question of the ideal profit margin, but we recognize that the first major issue to be addressed is what to do with the category of primary processed products, which are susceptible to market conditions, after 2025.

Q3

Is there anything you can quantitatively show about the world's tomato production. Can you share any kind of sensitive information, if any? (UBS Securities Japan Co., Ltd.: Ihara)

A3 (Yamaguchi)

As for the production of processing tomatoes, the industry newspaper [TomatoNews](#) has published an outlook for this year, which says in 2024 plans call for increased production compared to the previous year. China is trying to significantly increase production this year from last year. Conversely, California is moving to reduce production rather than increase it. I think that the level of production in China will be an especially important point.

California is the world's largest producer of processing tomatoes, with a production volume of more than 10 million tons. China is also planning to produce more than 10 million tons this summer. Last year, China's production volume was 8 million tons. Whether or not it reaches 10 million tons will have a significant impact on the market conditions of tomato paste from 2024 onwards. In any case, China has announced 10 million tons as a target, so I think we need to pay close attention to how close it comes to reaching this target.

Additional Question

How many tens of thousands of tons of tomatoes are produced in the world now? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

Last year, the global production volume of processing tomatoes was around 44 million tons. It has been reported that this year's production volume will be around 47 million tons.

Additional Question

If you think about it, does the outlook suggest production will increase by about 7 to 8%? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

Yes, this number is based on the processing tomato crop.

Additional Question

Does this include the portion that will be used to produce tomato paste? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

Yes, and in addition, the actual production volume will also be affected by the crop situation. It is still early August, and processing will continue until the middle of October, so I think there will still be fluctuations depending on the weather during this time.

Q4

In terms of synergies with Ingomar, I think that creating synergies with Ingomar is one of the key points, as the International Business will face headwinds from the next fiscal year onward. What kind of time horizons are you using, how much synergy will you create, and how will it contribute to Kagome's performance? (UBS Securities Japan Co., Ltd.: Ihara)

A4 (Yamaguchi)

Ingomar has also started tomato primary processing for this year's crop from July 20th. As a short-term synergy with Ingomar, how much production loss can be reduced is an especially important point. Ahead of the start of the processing season, Ingomar and Kagome discussed the issues. Through this summer's production, I believe that we have started a phase in which we will examine the extent to which each issue and theme can really be realized.

Therefore, at the end of this year's season, we will be able to see the extent and possibility of reducing production losses or improving quality. I believe that this will also clarify the specific scale of synergies.

In addition, for long-term synergies, managers from the Global Agri Research & Business Center are visiting Ingomar's contract farmers to hear in detail about the challenges faced by tomato cultivation and processing tomato farming in California. We are also currently setting a theme for solving the problems of agriculture itself in California. Short-term and long-term factors will combine to gradually create a clearer synergy with Ingomar in the future. As I mentioned earlier, the challenge for the International Business after 2025 is how to stabilize primary processing through synergies with Ingomar during the coming downturn in the tomato paste market.

Additional Question

Is my understanding correct in that you are expected to be able to disclose an update, including specific synergy amounts to some extent, by the end of this fiscal year, when

the outlook for production losses is clear? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

Yes, we will strive to disclose that information.

Additional Question

At the previous financial results briefing, there was a bar graph that showed synergies were at about this level. Can we understand that there is a possibility that synergies of billions of yen will be created? (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

We are currently in the process of verifying this possibility in line with actual production. Therefore, we will be able to answer as soon as this data is finalized.

Q5

Ingomar's margin in the first quarter was 8.2% in yen terms. This declined slightly to 7.4% in the second quarter. I believe that various structural reforms are underway, and the impact of the decline in the tomato paste market in FY2024 may also occur in the future. I'd like to know your thoughts on this margin level, and in terms of the short term, do you think the margin is declining amid the various cost pressures that are occurring, and, outside of market fluctuations, does Kagome have any proactive measures it will implement to provide room for improving the core operating income margin compared to this margin in terms of operations? What is your thinking on the margin only for Ingomar? What kind of improvement measures are you considering? (Tokai Tokyo Intelligence Laboratory Co., Ltd.: Araki)

A5 (Saeki)

First, I would like to talk about our margins for the first half, the first quarter, and the second quarter. In acquiring Ingomar, we are valuing their assets and liabilities at market value. This fiscal year, inventories were valued at the time of acquisition, and it was incorporated into our consolidated financial results.

Therefore, the buyers and sales amounts of inventories are generally predetermined, and the margin is low for the current fiscal year. In monetary terms, it is about 9 billion yen on an annual basis, and due to the effects of market value accounting, we value inventories at a higher amount.

The figures for the first quarter were 8.2% and 7.4% for the second quarter, respectively. Based on the actual situation of Ingomar, we have acquired a margin of about double this.

This trend will likely remain unchanged in the third quarter. In the fourth quarter, there will be a decline in the cost of sales of paste for the current fiscal year, so there is some uncertainty, due to market conditions and other factors, as to whether the profit margin from the first quarter to the third quarter of this fiscal year will be maintained.

As a side note, the impact of marking inventories to market will only occur in 2024. Therefore, in 2025 and later, the part of the increase in cost of sales will basically disappear due to this market-based valuation. This is why it is difficult to say what percentage the margin will be at this stage. Although, the impact of this year's decline in profits by about 9 billion yen will not be a factor next year.

Additional Question

I understand that the book value has been rounded up to the market value. I don't know the actual situation—having adopted IFRS and making it a consolidated subsidiary—the book value is the market value and the market value itself will continue in the next fiscal year. I think that the spread between the two will not change. (Tokai Tokyo Intelligence Laboratory Co., Ltd.: Araki)

(Saeki)

That is true for property, plant and equipment, for example. The figure of roughly 9 billion yen that I have just mentioned is the figure for inventories. Nearly all of the inventories at the time of acquisition were acquired in January 2024. Most of the inventories the company had in January 2024 will be sold out this year. Therefore, I said that the impact will disappear after 2025.

(Yamaguchi)

I will explain the proactive measures to increase and improve margins. Ingomar is located in California and produces almost a year's worth of production during the summer. In two and a half months, more than 1.3 million tons of tomatoes are delivered to its factory uniformly. The company's business is to see how much product it can produce that matches the quality while maintaining a high operating rate of the line. I believe there are many areas for improvement in that business. For example, the yield of tomatoes in the field, the method of

planting tomatoes to deliver them in a uniform manner, various measures to maintain a high operating rate of the line, and the improvement of the level of quality control are all factors that are directly linked to profits. This is why improving these together with Ingomar will be the basis of the synergy I mentioned earlier.

We will now begin to work on individual areas and I have the impression that there are many opportunities to create synergies as we are heading into the summer production.

Q6

When you made Ingomar a consolidated subsidiary, the financing was 36 billion yen, which is probably the largest ever for Kagome. You used a bridge loan in response, and on June 14, you announced a secondary offering, raising about 21 billion yen, which somewhat decreased the financial risk compared to the one-year bridge loan with a financial risk of 36 billion yen. Does cash and deposits sufficiently cover the remainder? What are your thoughts on the financing? (Tokai Tokyo Intelligence Laboratory Co., Ltd.: Araki)

A6 (Saeki)

We completed the all sales of treasury shares. In the end, the amount of cash that came in was about 23 billion yen. As for what to do with the remaining 13 billion yen, calculated by subtracting this 23 billion yen from the 36 billion yen, we are basically thinking of covering it with cash on hand.

To provide more context, it was not until the beginning of July that the funds from the sale of treasury shares were deposited. Therefore, the financial statements you have do not contain this in terms of numbers. We are thinking of using the money received in July to pay off the loan. Although we have not yet decided on the specific timing of this repayment, we intend to complete this repayment by the end of this year. Our financial soundness should return to an equity ratio of 50% at the end of this fiscal year, according to our current estimates.

Q7

Recently, the Japanese yen has suddenly appreciated past 150 yen to the dollar. While this may be different for primary and secondary processing, can you provide a simple explanation of how Kagome will be affected by the economic environment and exchange rates? (Nippon Life Insurance Company: Momose)

A7 (Yamaguchi)

Currently, our operations are almost evenly divided between the International and Domestic Businesses. Compared to Kagome of the past, which was previously a domestic-centered business, we are now in a situation where our operations are balanced against exchange rate volatility.

(Saeki)

As Mr. Yamaguchi just mentioned, there are two main effects of foreign exchange rates. The first is the procurement of raw materials for the domestic business. In our case, 95% of raw materials are sourced from overseas. Therefore, the impact of foreign exchange rates is that raw materials costs rise when the yen depreciates. The second point is the international business. The international business is conducted on a local currency basis and will be converted into Japanese yen at the time of consolidated financial results. If the yen depreciates when converting, profits will naturally increase on a yen basis, so there is an advantage in the second effect.

Our business environment is growing with the International Business. Compared to the Domestic Processing Business, sales are almost the same, while profits are higher in the International Business. Therefore, in the current business environment, a weaker yen would be slightly more positive in terms of profits. In terms of sales and core operating income, we estimate that the depreciation of the yen by 1 yen will increase sales by about 400 million yen and profit by about 30 million yen.

However, the exchange rate is very complicated, and in terms of Japanese yen conversion, for example, it accumulates at the average rate of each quarter, so it does not mean that the short-term appreciation of the yen or depreciation of the yen will be directly reflected in the business results. To complicate matters further, when importing domestic raw materials from overseas, we have a long-term forward exchange contract in place. Specifically, we contract an amount half of the past performance for the subsequent four years.

At the end of the previous year, when the business plan for the next year is decided, the raw materials procurement plan is also decided. At that time, we use a short-term forward exchange contract for one year for 30% of the remaining half. Therefore, we are directly exposed to the impact of foreign exchange rates in the form of almost 20% of our annual procurement. In this way, we are taking various measures to moderate the exchange rate as much as possible. While I mentioned earlier that the impact of the depreciation of the yen by

1 yen would benefit us by about 30 million yen in terms of profits, it is complicated and not easy to adjust these measures.

Q8

Japan is also getting extremely hot. I found it difficult just to walk outside to come here. I have heard the news that the United States is also getting very hot. If this continues, how will Kagome's tomato business be affected? What measures are you taking against global warming? (Nippon Life Insurance Company: Momose)

A8 (Yamaguchi)

Climate change is progressing rapidly and the swing is getting bigger. Processing tomatoes are grown in open ground, so they are directly affected by climate change, and the impact is very large. I think this is the area that we need to take the most action on in the medium term.

Our research organization related to agriculture, which had been dispersed across multiple offices, have been consolidated in last fall into a single organization, the Global Agri Research & Business Center. By combining them into a single location, we can invest in research more efficiently and focus on the research and development of various agricultural technologies, such as tomatoes that grow well even in hot weather or with little water, or soil diagnosis that further increases yields. I believe that achieving this represents our response to climate change, and if we do not respond, it will be difficult to procure raw materials for tomato processing in a stable manner in the medium to long term. For the next 10 or 20 years, I think the key will be how well Kagome can engage in agricultural research.

Q9

This question is about Kagome's share price. Your performance in the second quarter was also very strong, but on the other hand, today your share price has fallen further. I would like to know what kind of management issues are causing this downward move. As President, do you have anything to add? Having covered Kagome for about seven years, I don't think your share price and fundamentals are really linked. I feel that Kagome needs to become a company that is easier for institutional investors to see, including in terms of the investor composition. Given this, I would like to know your thoughts on management that is conscious of your company's medium- to long-term share price. (UBS Securities Japan Co., Ltd.: Ihara)

A9 (Yamaguchi)

I'm sure you can understand that it's hard to comment on the share price here, and I haven't seen the details of the share price today. I'll check on the details later. Can I comment on our view of the composition of shareholders?

Additional Comment

For example, if we objectively analyze the share price movements in today's financial results, it may be true that Kagome is currently performing well, but the market may be wondering whether the profits of the International Business will really be maintained next year and onward. In terms of the shareholder composition, there is a trend that share prices will continue to move in a way that makes it difficult for institutional investors to make purchases. I would like to ask you, as the President, what are the company's management issues from the perspective of both sides. (UBS Securities Japan Co., Ltd.: Ihara)

(Yamaguchi)

I think one is how to look at the shareholder composition. We are currently operating with the support of 190,000 individual shareholders in Japan, but while we will continue with our shareholder policy in the context of a changing business environment and the ratio of our business domestic and overseas, we are also discussing internally whether this is sufficient or whether it is necessary to encourage institutional investors to own more shares. As the ratio of the International Businesses increases, I believe that one of the issues is what kind of shareholder policy to adopt.

One other issue is how to maintain growth potential and secure profits in the International Business in 2026 and beyond, including the balance between primary and secondary processing.

A situation different from the current one will arise in the future, such as changes in market conditions. We must prepare for the next measures as soon as possible. If share prices are reacting to such a situation today, I think it is necessary to present a clear plan.

Opinion

Having seen the price action, I feel that Kagome's share price is moving in an overly complicated way, and I wonder if there is anything that can be done about it. I always think that it is difficult for institutional investors to hold Kagome's shares long-term because of this price action. I hope that Kagome considers various approaches to this,

such as shareholder returns. (UBS Securities Japan Co., Ltd.: Ihara)

Q10

My question is about Ingomar. The ratio of human resources to the weighting of the International Business has risen sharply, and I would like to hear about the human resources strategy that you currently have in place based on this. Specifically, I would like to know what kind of person is currently at the helm in order to create synergies with Ingomar, and what kind of analysis is being done while tracking the results as KPIs. (UBS Securities Japan Co., Ltd.: Ihara)

A10 (Yamaguchi)

As the ratio of the International Business increases, what kind of human resources strategy to adopt in the medium term is a major issue, and we are considering and implementing projects for the medium-term human resources strategy within the company. If we simply continue on with Kagome's human resources strategy so far, we recognize that there are some areas that are lacking in terms of the speed of development of this business and the support that we have now, and we are trying to fill those gaps.

As for Ingomar's human resources, we will be sending expatriate personnel from management, quality control, and finance to the United States. Ingomar is positioned under the umbrella of global food company, and the necessary staff are being sent from Japan to share information closely at first.

Greg, the CEO of Ingomar so far, has agreed to stay on for the time being and work with Kagome. As a result, we have been able to avoid a situation where there is a sudden change in management resulting in a vacuum, and the handover is being carried out well.