Question and Answer Session

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Q1

This question pertains to feedback from the first year of the Let's Eat Vegetables Campaign. Can you share KPI or other indicators, if any? Also, how will you develop and further promote the Let's Eat Vegetables Campaign in its second year?

A1 (Yamaguchi)

As for feedback of the Let's Eat Vegetables Campaign in its first year, initiatives under the Vegetable Promotion Project involving 19 participating companies got off to a slow start due to COVID-19. Nevertheless, we have been able to try out various forms of collaboration individually with several companies, such as Hoshino Resorts. For example, we have seen positive results from a very large number of bookings for vegetable-themed travel, which has resulted in the strong satisfaction of participating companies. Additionally, working with partners in the distribution and retail industries, we have marketed various vegetable-inspired menu options and the importance of eating vegetables to consumers in-store. Although vegetable beverages did not grow to the point of lifting the entire market, these activities have certainly helped to boost our market share in vegetable beverages. In this sense, we feel that the first year of this campaign has been a success to some extent.

In FY2021, we will be able to carry out activities throughout the entire year. The other day we hosted a regular meeting of the Let's Eat Vegetables Campaign at our head office with the 19 companies taking part in the Vegetable Promotion Project. This year we will hold these regular meetings quarterly to ensure that initiatives with these participating companies make steady progress.

Looking ahead, we will focus on invigorating activities through collaborative projects with the 19 participating companies to convey the value of vegetables in ways that we could not do on a standalone basis. This will help us to expand the campaign and make it a social movement.

Q2

I have a question about the international business in terms of Kagome Inc. of the

United States. I believe the company should aim for a profit margin of around 7% to 8%, but currently the company's profit margin is low. How do you view the current issues, how will you solve them, and what is the target profit margin for the company and timeline? During your explanation, you mentioned that HIT of Portugal will improve its profit margin to the 4% level. Can you share more details about profit margin with regard to the United States?

A2 (Watanabe)
We were unable to provide a specific target for KIUS' profit margin at this results briefing. There are several factors at play across a number of fields, so we recognize that some tweaking of the target profit margin is required.

Looking at the upstream side of product development, one factor is somewhat poor R&D efficiency. This means that despite the large number of new products under development, the actual adoption rate by customers is low. Or, there are a large number of unsuccessful products where the lot adopted by individual customers is small, the number of products is too large for order made, resulting in poor efficiency. In this sense, we need to narrow down each individual problem a little more.

Second is the problem of productivity. This relates to the issue about poor R&D efficiency and the rising number of SKUs I just talked about. This is also affected by the fact that over the years we have not really made in-depth reductions in production cost, which has resulted in a production system with slightly higher costs than competitors. We need to embark on a review of our production system to slim down production costs and make them cheaper so that we can pursue manufacturing with the same cost competitiveness as competitors.

Third is the review of our sales and marketing system, but this level of priority is somewhat lower than compared to the previous two items I talked about. KIUS has sales and marketing spread across the entire United States that it uses to share various forms of information, but, for example, there is still a little room for increasing efficiencies in terms of priority level of customers and development of potential customers. This is related to the review of our development system I talked about in point one. We will enhance communication between sales and development, and increase sales and marketing that produces successful products. By making improvements in these areas, we will increase KIUS' profit margin. This concludes our current outlook.

Q3

You forecast a recovery and increase in profits of 200 million yen this fiscal year for Kagome Inc. When do you think the previously noted three issues of development, production and sales will be resolved to boost profits a little more?

A3 (Watanabe)

Despite the impacts of COVID-19, we are moving ahead steadily with addressing the issues in development, production and sales. We believe results will begin to appear in 2022, contributing to profits in 2023. This is the timeline we envision. Over the next year we will make changes where they need to be made.

Q4

Can you provide an update on e-commerce? On page 7 of the results briefing materials, it says e-commerce sales were up 21%. When looking at the current share of the e-commerce channel and the first and second halves, is this growth rate beginning to slow down or is it sustainable? Also, what type of measures specifically will you implement in the future to grow e-commerce?

A4 (Yamaguchi)

As for our e-commerce, currently our own direct marketing is the main format, and in addition to this, over the past several years we have been seeking to grow our presence in retailer e-commerce. With COVID-19, sales of direct marketing and e-commerce are growing, so we believe this is a field to focus on in the future.

Strengthening our direct marketing, of course, involves product strategy. In 2021 we will focus particularly on strengthening collaboration with retailer e-commerce with the aim of acquiring new customers for Kagome. We view this as an important issue. The growth rate of direct marketing and e-commerce is expected to remain high next fiscal year on par with this fiscal year. We believe this growth will be sustained.

Q5

Large container products in e-commerce appear to be selling briskly. Will this result in a deterioration in the product mix?

A5 (Yamaguchi)

Office demand is falling substantially mainly for vegetable beverages, but this demand will shift to large containers through mass retailers or e-commerce and direct marketing. This trend is obvious. We see this trend continuing in FY2021. We expect the market share of products with large containers, for example, 720 ml PET bottle or 1l paper containers, will rise.

As for products with large containers, and PET bottles in particular, we introduced a line with new technologies for aseptic filling at the Nasu Plant several years ago, and we are producing bottles in-house. This establishes cost competitiveness and we are making arrangements to increase production capacity. For large containers, with the impacts of COVID-19, the share will likely rise over the next several years, while the share of personal- size containers will decline, conversely. This is the outlook we have in place.

Q6

Can you provide additional details about the top line in Japan? The forecast for this fiscal year calls for top-line growth of 3.2 billion yen. Specifically, in which channels and how will you grow the top line? In addition, when looking at initiatives such as the Let's Eat Vegetables Campaign over the long run, how will they be included in the top line? Similarly, which channels and which products will help boost the top line? What are your thoughts on the top line with a longer term perspective?

A6 (Yamaguchi)

First, let me share how we view the top line of our domestic processed food business. In FY2021, we will continue to capture sales by combining our Let's Eat Vegetables Campaign with vegetable beverages to address rising health-consciousness due to COVID-19. Of the 3.2 billion yen increase in revenue next fiscal year, vegetable beverages will account for 1.6 billion yen, so the top-line growth will mainly come from vegetable beverages.

In terms of expansion into the plant-based domain, which we have promoted over the past several years, last fiscal year sales of Yasai Seikatsu 100 Soy+, which is a blend of vegetables, fruit and soybeans, were robust, so by adding additional new products, we will look to support the top-line growth of vegetable beverages.

Regarding consumer foods, ketchup and tomato sauces, etc., in food and others, sales trended strongly last fiscal year due to rising demand for eating at home. This trend continues even in January 2021. In the food business, we will maintain the momentum in FY2021 by promoting more condiments than the previous fiscal year. The key is proposals of dishes. In particular, in January 2021 we appointed Remi Hirano, a cooking influencer, to disseminate information on menu proposals for the home. Through this, we hope to maintain the top-line growth of condiments including tomato ketchup and tomato sauce, etc.

As for products for institutional and industrial use, the impacts of Japan's state of emergency will make it difficult to return to the same level as before COVID-19. However, we will do what we can. For example, we will plan campaigns in support of restaurants.

Direct marketing and e-commerce are expected to maintain robust growth. Our measures in this area are as I discussed earlier. Looking at this from a somewhat longer perspective, the key will be what type of measures and how can we increase the share of direct marketing and e-commerce.

Supplements are the key to increasing sales in direct marketing and e-commerce. We launched commercials for supplements preemptively at the end of last year. By adding the top-line growth of supplements to the top-line growth of vegetable beverages, we aim to support the medium- to long-term growth of direct marketing.

Q7

This question pertains to top-line growth this fiscal year using sales promotion expenses. What are your thoughts regarding the trade-off with sales growth and profit generation when sales promotions don't result in top-line growth? Or, are you emphasizing the top line this fiscal year and next fiscal year? Are you thinking more about profits? Can you comment regarding the balance in this area?

A7 (Yamaguchi)

The greatest point of emphasis in FY2021 will be top-line growth. We expect sales promotion expenses, too, will increase by 1.6 billion yen. Sales promotion expenses that could not be spent in FY2020 due to COVID-19 amount to around 1.0 billion yen, including in-store taste testing and sampling. On top of this, we have included expenses that will help to grow the top line by 500 to 600 million yen.

Next, I would like to talk about the ability to capture profits. We have established a strong ability to generate profits thanks to company-wide earnings structure reforms over the past several years. We will emphasize top-line growth, but we expect expenses to fluctuate depending on COVID-19. We will manage the company with swift decision making, while closely monitoring the situation, including looking for profit growth.

Q8

You will introduce ROIC-based management in the future. What approach will you use to improve the denominator of invested capital? Can you comment regarding the denominator of ROIC?

A8 (Watanabe)

We believe that our approach to the denominator of ROIC will evolve each year. We have just started focusing on ROIC internally. Currently, the concept has yet to fully penetrate the company, as some don't know the difference between ROA and ROIC. First, in the initial fiscal year, we will begin by raising employee awareness toward slimming down the balance sheet we are using now.

The Investment Committee is now working to incentivize this. We will evolve our approach to ROIC-based management by focusing on how to increase revenue versus investments and how to connect this with increasing profits. Therefore, when answering based on this denominator, now we are looking at the entire balance sheet. Even if we reduce each item of the balance sheet, once we can no longer shrink it further efficiently, next we will prioritize investment each year while considering revenue and profits. In this manner, we are thinking of evolving our management approach internally a little at a time.

Q9

There are two stages to improving invested capital. The first stage is reducing the overall balance sheet. What options do you have to streamline the balance sheet?

A9 (Watanabe)

Streamlining the balance sheet can be performed from current assets or from non-current assets, mainly in the form of cross-shareholdings. These are the two options we have. We will focus on these two areas as the first stage of ROIC-based management.

Q10

On the non-current asset side, will you slim down the balance sheet in terms of shares owned, and inventory for the current asset side?

A10 (Watanabe)

Inventory is the single largest item. Inventory from raw materials to products and then accounts receivable. Managing these stricter may prove difficult in Japan, but overseas there is still room for improvement.

Q11

Do you have a new mechanism or will you look to reforms of current systems for improving working capital? Or, will you raise the awareness of employees toward that end? Can you provide a final comment on this?

A11 (Watanabe)

In terms of working capital, there is the possibility to insert a new mechanism in the sense of cash management, but this year we have begun an approach to raise the awareness at the individual employee level.

Q12

This question is about your earnings forecast for domestic processed food during this fiscal year. During the previous results briefing for the second quarter, the quantitative targets for the second Mid-term Management Plan were revised downward and the forecast for this fiscal year appeared close to these revisions. For FY2020, the results for the second half have outstripped the interim explanation by a large amount. The strength of second half results for FY2020 appear to be due in their entirety to special factors. Is this understanding correct? Or, does this forecast incorporate some form of risks? Can you provide details about your approach to the earnings forecast for this fiscal year?

A12 (Yamaguchi)

We believe the factor behind upward trend in results for the second half is the major impacts of COVID-19. Specifically, there was strong sales of basic condiments due to stay-at-home demand and strong sales of vegetable beverages due to rising health consciousness of consumers. Products for institutional and industrial use saw a substantial decline in sales, but sales of products addressing demand to eat at home outstripped this decline. FY2021 is difficult to predict because of the changing situation with COVID-19 infections. Specifically, the sales situation of our products will be determined based on the balance achieved between eating at home, home meal replacements and food service.

Given this, the forecast for this fiscal year is based on the situation of the second half of last year, and adding in COVID-19, it provides an assumption of the sales level of each of these segments. In this sense, the FY2021 forecast utilizes the lessons learned during FY2020.

Q13

In that case, many aspects of results for the second half of FY2020 have been attributed to special factors, but these factors will no longer be in play this fiscal year. The forecast is based on this assumption, correct?

A13 (Yamaguchi)

We don’t believe that the factors from last year will be gone completely. For example, products for institutional and industrial use should recover if the impacts of COVID-19 ease, and consumer foods had special factors. This year we are making efforts, including promotions, with an eye toward how much of last year’s sales we can maintain. Therefore, we don’t believe that these special factors will be removed completely. We prepared the forecast for each category based on what happened last year.

Q14

In that case, there are many aspects of uncertainty this fiscal year. Is it correct to assume that you have incorporated these as risk factors into the forecast?

A14 (Yamaguchi)

It is extremely difficult to forecast what will happen. For this reason, we have incorporated these elements of uncertainty as risk factors. Japan issued another state of emergency in January 2021. As a result, sales of products for institutional and industrial use have fallen somewhat below the assumption, and conversely, consumer foods or beverages are above this assumption. We don’t really know how long this will continue, but we believe it is important to swiftly address these changes in situation over the course of the next year.

Q15

Similarly, with regard to domestic processed food, I have a more detailed question about changes in business revenue and the negative 300 million yen impact of fluctuations in cost of goods in this fiscal year’s forecast. I believe you have included the cost increases for raw materials and cost decreases for cost of goods in this fiscal year’s plan. Can you provide a quantitative feel for these, if any?

A15 (Yamaguchi)

As you asked, we have incorporated the uptrend in raw materials costs. In regard to how far we can reduce cost of goods in response to higher raw materials costs, there is also the mechanism at work that we have engrained within our efforts to strengthen our ability to generate profits, such as in-house projects to lower cost of goods. As for next fiscal year, we are establishing a clear picture of the challenges we will face in lowering cost of goods. This includes reviewing the blend of product contents and improving plant productivity. At present, each division is working to address these challenges. We have calculated the increasing part and decreasing part, so you can think of this fiscal year's plan as the current situation of cost of goods.

Q16

In that case, how much will your raw materials costs increase this fiscal year? If it is difficult to answer quantitatively, can you share how the forecast was created based on which products will rise and by how much?

A16 (Yamaguchi)

Our mainstay raw materials are primary processed agricultural goods, such as tomato paste and condensed carrot juice, etc. The cost of these materials are rising due to very strong business inquiries for domestic raw materials and given the situation of agriculture in Japan and the impacts of climate change, etc. Overseas, too, tomato paste has been seeing market prices decline as of late, but due to rising demand to eat at home worldwide, the market price is starting to rise. We see this as the rising price of these primary processed agricultural goods.

Q17

Based on your explanation, I understand that the cost increase in raw materials will be absorbed by decreased cost of goods. Are rising raw materials costs getting to the point where you will consider price revisions. Can you provide details in terms of pricing?

A17 (Yamaguchi)

As of the current point in time, we do not plan to make a move in terms of pricing in FY2021. Raw materials costs have not risen to the point of considering price changes.

End