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Meiji Holdings Co., Ltd.
Food Segment – Strategy of China Business
The Online Briefing Q&A

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Presenters:

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*This material has been edited to make it easier to understand some of the questions and answers.

Q-1-1-1

I would like to know is more details on the situation in the drinking milk and yogurt business, where the drinking milk business has been struggling, and the prospects for improvement in the future.

I am interested in two things. First, what is the composition of commercial and home use, and for example, in the case of chilled milk, there has been a considerable impact from competitors. What will be the recovery strategy in that area in the future?

Another thing I'm interested in is business use. I understand that you are looking to expand the number of new users. I would like to confirm whether or not the growth that has been achieved up to now will continue again after the coronavirus.

A-1-1-1

Ueda: As for the decrease in milk for consumer use in FY2021, last year, products were sold without any sales promotion. Other companies, especially a strong local manufacturer, naturally responded with a great deal, as they were expected to catch up with the previous year's sales. We were not able to make the decision to sell at a reduced price at that point in time. I think that is the main reason of decreased sales.

However, we could not leave it as it was, so we appealed our strength other than price. After that, in line with this, we were expanding sales to places where we were still able to get more, where there was still room for sales expansion. The net increase in sales from these new customers is now on top of the negative figure for last year, and we are now in a situation where we are seeing positive growth.

In addition, since there was a drinking milk supply plan in 2020, we could hardly implement any marketing measures at that time, so we decided to implement new marketing measures on drinking milk. Until then, the truth is that we had actually done very little.

So, we have been trying to expand the region, expand the area, add new customers, and combine various measures to make our products more attractive again. I think we are seeing the results of these efforts in the drinking milk business.

In addition, I think it is very significant that we have been able to acquire new customers in the

commercial market, and naturally, other companies are targeting the chains we have acquired and are now coming to acquire them.

However, it is not only a question of price, but also whether the product is suitable for the cafe chain, which is very important. After all, customers use drinking milk that goes well with their own coffee, and in fact we are selling it at a higher price than other companies.

That's how much they understand the value of our products. This means that the Meiji brand is well recognized by consumers in stores, and I think the value of the product is very high there. This advantage, I feel, will continue for the time being, and it can still be taken in commercial market.

In addition, I believe that marketing Meiji products and Meiji drinking milk in stores, with marketing measures and marketing costs, will increase the value of the products and create a synergistic effect.

Matsui: I would like to add some additional information about gable-top milk containers. The production lines for the gable-top milk containers in Meiji Dairies (Suzhou) had a single line of 3,000 packs when it was first established, then it was augmented to 6,000 packs, and then to 12,000 packs.

Until the middle of fiscal year 2021, the number was 12,000. Up to this point, we have always had to keep doing business with them, asking them to hold back on sales because we didn't have the production capacity. Therefore, we have been unable to renew our products or aggressively promote them since the start of the project.

In the meantime, other companies have been doing all kinds of tricks. At those times, we were unable to respond in a timely manner. As a result, we have been in a bit of a difficult situation in 2021, partly due to the impact of the coronavirus.

However, Meiji Dairies (Suzhou) also increased its production by 18,000 packs in the middle of FY2021, and production lines for the gable-top milk containers in Meiji Dairies Tianjin will be further increased in FY2023, so we are already taking measures such as product renewal and the addition of new products in FY2022 to see how we can make a comeback. So, I see no problem at all from 2022.

Q-1-1-2

What is the sales composition ratio between home and commercial use, if you only consider chilled milk, and if possible, if there is a disparity in profit margin, please give us a comment on that as well.

A-1-1-2

Ueda: The situation with drinking milk for home and commercial use is that there is somewhat more drinking milk for commercial use now. I think it is 5.5 to 4.5. That's how the commercial use exceeds. The profit margin is almost even, or maybe it's more in the commercial use.

Q-1-2

I am very interested in the synergy between *SAVAS Milk*, and *SAVAS bars*, but I was wondering if there is a specific launch date for *SAVAS Milk*, or if it will be next year or so, waiting for the new plant. Can you tell us a little bit about the timeline of the future strategy of the *SAVAS* brand?

A-1-2

Matsui: The full-scale production of *SAVAS Milk* and *SAVAS bars* in China coincided with the launch of Meiji Food (Guangzhou).

However, we are planning to start by making *SAVAS Milk* on a trial basis in other countries, and then introduce it to China first, in order to explore the market.

As for *SAVAS bars*, we are planning to sell them in the Chinese market by importing them, in the same way as we have already started selling them in Japan, in order to develop the market in advance.

We will wait for full-scale production and sales in China until Meiji Food (Guangzhou) starts operations, but before that, these products will be marketed in the form of imports upfront.

Q-2-1-1

I would like to ask a little more about the intensification of competition. After all, in terms of the

intensification of competition this time, do you think that it was possible to keep the sales by increasing production capacity and making market investments? Did you not have structural risks in the first place, such as failure to differentiate? I would like to reconfirm if there really wasn't any risk there.

A-2-1-1

Matsui: First of all, in terms of the intensifying competition for drinking milk, we were not really able to do anything about it because of the upper limit of our production capacity. The product lineup of drinking milk products has not changed at all since the Company's inception.

In this situation, other companies have entered the chilled products market. They have also launched all chilled products, from low-priced to high-priced products.

At such times, we couldn't take timely measures to counteract it and increase the value of the brand, which is our big regret.

Therefore, since we have a good prospect of building up production capacity, we will gradually renew such products, add to the product lineup as we increase production capacity.

Q-2-1-2

I understand. You are not aware that you are structurally at risk or that you are not differentiated in any way, and you are confident that you can recover as long as you increase your product lineup, increase your production capacity, and enhance your marketing. Do I understand correctly?

A-2-1-2

Matsui: Yes, our Meiji brand drinking milk, which is sold under the *CHUNYI* brand, is well differentiated. In fact, in Japan, there is little differentiation between different types of drinking milk, except for our *Oishii Gyunyu*, and it is my impression that the only way to sell drinking milk is to sell it cheap. However, in China, people are aware that good things are expensive.

People buy Meiji drinking milk even if they pay a higher price because it is a reliable and safe Japanese brand of Meiji.

Therefore, I believe that we can still compete in the drinking milk market if we implement proper marketing measures.

Q-2-2-1

In all categories, you have been saying that as long as you make progress in developing North and South China and increase the number of products, you will see growth. From a management perspective, where do you see the greatest growth potential after all? Is there any risk to the contrary? I would appreciate it if you could explain a little more in terms of the potential and risk of this growth.

A-2-2-1

Matsui: In South China, there are already ice cream and confectionery factories, and the Meiji brand is already well established there. The only thing we didn't have before was drinking milk and yogurt.

Therefore, we do not consider it too risky to expand our drinking milk and yogurt business in South China in the future. If there is a risk, it is procurement of raw milk. Raw milk production is mainly in the north of China, so it is very difficult to procure raw milk in the south, but on the contrary, in the south market, drinking milk is expensive, so it sells at a high price. In that sense, I am not worried about the drinking milk and yogurt business in South China.

East China also handles drinking milk and yogurt, as well as confectionery, and is newly making ice cream, and already has about 20% of its sales from ice cream.

We are not worried here either, as the population is large and people there are willing to pay for delicious food.

The biggest risk and challenge for us is North China. As for North China, the Meiji brand has not yet fully penetrated the market.

So, we decided to build a drinking milk and yogurt factory here and first promote the Meiji brand with it. So, promoting drinking milk and yogurt which are daily foods is the best way to penetrate Meiji brand because those are very highly exposed product.

The strategy is to promote the brand and link it to chocolate, ice cream, and nutritional products. In this sense, North China has the biggest obstacle. I think we need to focus our efforts on this area.

Q-2-2-2

In terms of categories, you feel that the category with the greatest potential is basically the drinking milk and yogurt category, is that correct?

A-2-2-2

Matsui: Regarding drinking milk and yogurt, it is a local business. Since this is a local business, building a factory there can create a large amount of sales. So, there is a challenge there in that sense. We have to set up a new business in a new place, and a new business had to be set up quickly.

As for ice cream and confectioneries, those can be shipped from distant factories, so we have already tapped into that market. Regarding ice cream and confectioneries, the production capacity is full, and a new factory is being built, so they are very low risk.

For drinking milk and yogurt, the factory will be built to create a market there and to create demand there. Ice cream and confectioneries are already at full capacity, so we are building a factory, and that's the big difference.

Q-2-3-1

You have indicated that the sales of probiotic functional yogurt in FY2023, and FY2026, will increase sixfold and threefold, respectively. Please tell us how much you expect in terms of sales specifically.

Also, you have mentioned the keywords, such as pioneer, leader, and so on, but in terms of market potential here and your company's market position, which position do you expect it to be in the market?

It doesn't matter if it's top-down or bottom-down, so please tell us about the market potential, achievement accuracy, and your thoughts.

A-2-3-1

Ueda: I can't quite give you specific numbers, but they are as shown in the slide.

We will try to make it work, but then we will naturally take more than this curve, and we will do various tricks to make it work.

One is to let people know that lactobacillus are good for them, and we hope to be able to mix such activities and marketing well.

However, China has various regulations, and we would like to increase sales at once by successfully conveying information that does not fall under such regulations and is beneficial to the health of Chinese people, or perhaps by using such information as a trigger.

Therefore, I think that if this area can be developed, it is possible that this type of probiotic functional yogurt will expand rapidly, as it has happened in Japan.

If that happens, I believe we will naturally become a leader and will be able to become pronoun with that product. Yet this 2021, and then next year 2022, are still the first or second year of its launch. Therefore, there are many things to do at this stage.

After the first year, we have learned that some things are not very effective, and some things could be more effective if we do more. About that, we are planning now with the Company's consent to spend more than last year on marketing investments.

Matsui: I would like to add something. As I am sure you all remember, *LG21* and *R-1* did not sell at all in Japan at first. But once the value of this product was recognized, it sold much better.

So, I believe that if the recognition of this value, the recognition of the value of *R-1* and *LG21* products, can be promoted in China, then suddenly the volume of goods will increase. Therefore, it is very difficult for us to communicate the value of each product to our customers because unlike Japan, the power of television is not very strong. Therefore, it is not very effective to use TV to disseminate the products as in Japan.

So, in that context, the problem is how to convey this value to our Chinese customers. This is what we are currently doing through trial and error.

We are taking various measures, such as seeking the help of experts from Japan to strengthen

relationships with professors and joint research and are making preparations for such activities. Therefore, we do not know where we will hit the mark, but I am sure that we will succeed by continuing to work on this project.

Q-2-3-2

I understand. It took about 20 years to go to 100 billion in Japan, and you want to do it at a faster pace in China, so it is like you have this image of 2026. Is my understanding correct?

A-2-3-2

Matsui: Yes, that is what I would like you to believe.

Q-3-1

I think you have presented a very ambitious sales target. In response to that, where do you think the bottlenecks are likely to be in the future? I am sure that there are various areas, such as administration, production, and sales, where you think you need to tighten the reins or take some risks in order to achieve this plan. Could you please tell us main points?

A-3-1

Ueda: Regarding the first bottleneck in achieving the sales target, I feel that there is a bottleneck in production.

Last year, for example, there was a planned power outages at an ice cream factory in Guangzhou, which meant that production could not be carried out as planned.

Also, I think it is difficult to get people to work in the factories, and in that sense, there is a possibility that it will hinder production a little. We are trying to prevent that from happening, but I do feel that it is a risk.

Also, as a bottleneck in the actual sales process, I wonder if it is possible to speed up the sales process to meet the deadline for opening a new market after all. I think that this also raises the issue of recruiting people, and the issue of whether or not people can be employed.

I don't have much anxiety about the system inside. However, depending on the coronavirus situation, the entire plant might be shut down for four or five days.

Furthermore, the fact is that we will not know if it will be over in four or five days until it actually starts. Especially this time, the first lockdown in Shanghai due to the coronavirus is something that no one has ever experienced before.

So, while we can see such crisis, I think there is a possibility that other crisis may occur that we do not know about.

We will do our best to ensure that this does not happen, and we, including the sales front and the Head Office staff, are committed to doing our best.

Matsui: Here is my perspective on the coronavirus. In China, fortunately, the government takes thorough measures, so the spread of infection has been contained in a short period of time.

So, the period of impact is not as long, and the impact has not been as great as in other countries. Also, it is true that the east side of Shanghai is in lockdown right now, but our factory in Meiji Dairies Suzhou is in trouble because of the large volume of goods. Because the west side is going into lockdown tomorrow, and the residents on the west side are working very hard right now to stock up on stuff.

So, sales have been very strong. Perhaps it will stop again from tomorrow, but we are now struggling to find a way to capture such demand.

In fact, there are many difficulties, such as logistics being halted. In such a situation, we have been able to seize opportunities by continuing to supply goods.

Q-3-2-1

When you look at your business in China in the next 5 to 10 years, is there any possibility of M&A? Regarding infant formula, exports from Japan to China are not allowed, but in the future, do you see the infant formula business as an opportunity for your company? Could you tell me a little about the possibility of M&A and the development of the infant formula business?

A-3-2-1

Matsui: As the person in charge of the local operations here, I can say without a doubt that, since we have invested so much in the production sites, the business will not be viable unless we first turn the plant around. For 10 years, we will work very hard to keep this plant running at full capacity. This way, fixed costs can be earned, and profits can be made. As we are just trying to get there, we are not considering M&A to increase net sales, at least locally.

However, I believe that M&A, which will create the future of the new Meiji, is not out of the realm of possibility. China is a place where there are many new seeds of business.

Since we are doing business in China, I believe that we should not miss such opportunities if there are any good ones for the future of Meiji.

As for the infant formula, of course we are steadily making preparations for this. We had been in the infant formula business in China until 2018, so the brand image is still there.

Our hope is to revive demand for infant formula in China before the brand image is lost. We are in the process of thinking hard and moving forward with various ideas.

Q-3-2-2

I would like to know if you think that the resumption of infant formula sales is likely to happen in the next one or two years, or if you really don't know. Please tell us about the sensitivity of the situation.

A-3-2-2

Matsui: Regarding infant formula, we are in the process of thinking about various ways to start business in China as soon as possible, but China has very strict regulations regarding infant formula.

We are currently struggling there to figure out how to clear this regulation. So, I can only say that we are working on it as quickly as possible.

Q-3-2-3

I understand what you said earlier about not considering M&A to increase sales, but looking at your

company's market share, it seems difficult to achieve top market share on a stand-alone basis. I was frankly surprised.

In Japan, I think that unless you are a top one or two food manufacturer, you cannot build up sustainable profits, but in China, is it a little different? Is it possible because you can build a market with only value-added products, or do you have to take the position of a top manufacturer in China in the future? Please explain your thoughts on this.

A-3-2-3

Matsui: If we want to get market share, we probably have to get into the volume zone in the lower price range. However, I think that the low-priced volume zone probably does not match the safe, secure, and reliable Japanese brand and the Meiji brand, as I mentioned earlier.

Therefore, we believe that the very low-price volume zone is a place where we cannot take advantage of our strengths. Therefore, it is my opinion that at this stage, we should not be in the business of aiming for market share yet.

Even with drinking milk and yogurt, it is still the mid- to high-end price range, and we are handling chilled products. If we want to target market share, we must definitely target long-life (LL) milk, which has a large volume zone, but LL, in my opinion, is already red ocean.

It is in our company's best interest to participate in such places. We do not think it is a good idea, at least not now.

Q-4-1

I would like to ask you about the yogurt category.

In terms of sales composition, I would like to know how much is the sales of yogurt among the sales of milk and yogurt sales, the growth strategies of yogurt and functional yogurt, differentiation factors, and so on.

Perhaps profitability of yogurt has been an issue until now, so I would like to know what the situation is now.

A-4-1

Ueda: Regarding the composition ratio of the drinking milk and yogurt category, six is drinking milk and four is yogurt.

The latest situation of yogurt sales is at the same level as the previous year, in all markets.

As for yogurt, our yogurt products have been introduced to major customers since last September, and are now exceeding the previous year's level.

As for yogurt, *Meiji Bulgaria Yogurt* is the main in the yogurt. As for that *Meiji Bulgaria Yogurt*, until now, we have not invested enough in marketing.

We are now in the process of planning to introduce a new yogurt drink product, as the product range was somewhat limited. We have also changed the size of *Meiji Bulgaria Yogurt*, and it is doing well now. I think this is also an effect of the renewal.

We are also planning a new flavor for *Meiji Bulgaria Yogurt Drink*. We are sure that we are able to get sales from it because it was a product that we had already sold in the past. This is one of the reasons why yogurt is growing in this area.

Therefore, yogurt sales were poor until around October, but we hope you understand that they are now on the road to recovery.

The other part of our growth strategy is the new plant. They will set up a machine at the new plant, and the machine is not what we have in Japan, but we cannot tell you the details. They are planning products that use new technology. In that sense, I think this will lead to the revitalization of the sales floor or the market.

We believe that the launch of new products, together with other products, will have a synergistic effect on sales.

Matsui: Let me say a few words about *Meiji Bulgaria Yogurt*. The other day I had a chance to talk with doctors from the Shanghai CDC, and we wanted to promote *R-1* and *LG21*, but what they highly praised was *Meiji Bulgaria Yogurt Plain*.

For *Meiji Bulgaria Yogurt Plain*, we don't use sugar. Yogurt that is not sweetened with sugar has never been popular with Chinese people.

However, the CDC doctors say that there has been a change in the way people value things like zero fat, zero calories, zero sugar, and so on.

So, they said that such plain yogurt, yogurt without sugar that is tasty enough to be eaten is very good.

Therefore, we have not been able to show our presence in the market because our yogurt has not been very sweet, but I expect that will change in the future.

Q-4-2-1

I would like to ask what kind of trends you expect to see in the profitability of the China business as a whole in the future, given the current high cost of raw materials and the fact that you have said that you will spend quite a bit of money for growth.

I think you are aiming for sales of about JPY80 billion in FY2026, depending on the exchange rate, but how much margin do you expect to generate if you reach that level?

A-4-2-1

Matsui: Regarding the profit and loss of the Chinese business, we are strengthening our sales structure and reorganizing our sales structure for the year 2022.

In order to rapidly increase net sales from now on, we have increased the number of Japanese expatriates in order to accomplish this in a short period of time. We are also increasing our Chinese staff. So, first, fixed costs are increasing.

Then for 2023 to 2024, the three plants will start up at the same time. This would lead to a situation where the fixed costs of that plant would also be very high.

Our profitability will unfortunately be difficult due to this fixed cost burden. The measure of whether our business in China is doing well is whether or not sales are growing steadily.

If sales continue to grow as planned, we expect to have more than a double-digit profit margin by 2030, although it will still be tough in 2026.

Therefore, we plan to have our sales monitored to see if they are growing properly, and if they do as planned in 2030, we will be able to achieve a sales and operating profit margin higher than that

of businesses in Japan.

Q-4-2-2

For FY2026, you are aiming for a surplus, but in the mid-high single digits, or something like that?

A-4-2-2

Matsui: Right, we cannot expect a high profit margin yet for 2026 because it is not long from the start-up of the plant in 2023 or 2024.

Q-5-1

I think that your company's business in China still has issues in selling, sales, and marketing capabilities.

So, how do you plan to enhance these points in the future, marketing, sales, and your own efforts? After all, do you think you should be working with more outside help to improve your sales force, or are you working with strong distributors? Please tell me the details of this point.

A-5-1

Ueda: The place where we sell our products by ourselves is part of the major distribution, but we are making a decision to expand the market in collaboration with a strong distributor in each region and area although.

We believe that this would be optimal for now. However, I wondered if the shape would be different for each business. Especially for confectioneries, When the scale of the project reaches a certain level, I think selling our products by ourselves is a possible option. For now, we believe that if we work with strong distributors and powerful agents, it will be more efficient to use them to develop the business and get sales.

We are already facing the issue of strengthening marketing, so we will try to solve this issue one by one by transferring good human resources from Meiji in Japan and successful examples from there. We will also continue to implement marketing measures that are appropriate for China.

Q-5-2-1

Regarding chilled milk, are there any new entrants here, or will there be more in the future? Also, I wonder if major companies in China will take advantage of economies of scale to increase cost competitiveness, and low-priced sales and price competition will intensify, leading to a physical competition. I would like to know about this point.

A-5-2-1

Matsui: Regarding chilled milk, there are certainly new entrants. However, in China, there is a clear distinction between high-priced products, medium-priced products, and inexpensive products, depending on the product.

Therefore, although there is price competition within the high price range if it is in the high price range, and price competition within the medium price range if it is in the medium price range, I do not think it will happen that all drinking milk will become cheap and unprofitable business like in Japan.

In that sense, each companies have properly divided their products into different price ranges. I believe that the industry as a whole has been able to compete without excessive competition that could lead to loss of profit or loss, and that each company has been careful to avoid such competition.

Q-5-2-2

Also, in the area of chilled milk in the high price range, are there many new entrants in this area? I think they are showing up in the higher price range here because it is still a growing market.

A-5-2-2

Matsui: So far, from what I'm hearing, I know that few companies are pushing their products into the higher price range, but I haven't heard much about new entrants in the higher price range.

Ueda: Yes, from what I'm hearing from the sales field, there are not many competitors yet in high

price range.

So, in that sense, we feel that it is of great value for us to offer our products there. Therefore, we would like to target that area.

Q-5-3-1

Up to the third quarter, it seems that the business in China has largely decreased. Is this due to the decrease in chilled milk sales alone? Could you tell us how you plan to reduce the deficit here for the next fiscal year?

A-5-3-1

Matsui: I think there are three factors that caused sales decrease up to the third quarter of FY2021. The first was the sluggish demand for drinking milk and yogurt.

And the other thing is, we strengthened the structure of the new organization called Meiji China, and we also increased the number of Japanese in various ways to help build the new structure. There are also investments in new information systems. The office is new and bigger. We have fixed costs in that way.

The last is the increase in marketing expenses. As for functional yogurt and SAVAS, they are products that will make our future, and we are spending an excessive amount of money on marketing them compared to the size of our immediate business. We are investing in with the idea that it will be a pillar of our company at any cost in the future.

Therefore, while sales are steadily increasing, fixed costs must be absorbed, but if we can improve something, for drinking milk and yogurt, we are currently working to improve the situation by 2022 at all costs. Other than that, if we reduce fixed costs, the future foundation will collapse, so we do not intend to reduce that. We will also continue to invest in marketing expenses for functional yogurt and SAVAS.

In that sense, as long as net sales increase steadily as planned, I believe the future will be fine for us. I think now is the time to do it without getting too caught up in the profit and loss in front of us.

Q-5-3-2

Therefore, you are asking us to keep an eye on sales for the next fiscal year, and if sales increase, that's good, but the situation in terms of profitability will still be a bit difficult for a while next fiscal year, right?

A-5-3-2

Matsui: Yes, to be honest, that is the case.

Q-6-1

The first one overlaps with the previous question, but could you tell us about the competition in the chilled milk market with local Chinese manufacturers? For example, in the disposable diaper market, Japanese products had an advantage in the beginning, but as the quality level of local manufacturers improved over the years, the advantage diminished.

I would like to know if there is a risk that local manufacturers will eventually catch up with your superiority in the chilled milk market.

A-6-1

Ueda: Local manufacturers are still coming out with new products, of course. However, I do not have the impression that our drinking milk is now threatened by that local manufacturer, on the contrary.

We have not been able to do anything so far, and I think that is the problem, so depending on the measures we take from now on, we can maintain the gap with local manufacturers.

Especially when it comes to price competition, we will not participate in that. We will fight in a completely different world. We believe that this is a high price point, a medium-to-high price point, and that is where we can compete.

Q-7-1

Please tell us about functional yogurt here. It is said that there are many people infected with H.

pylori in China. What is the potential of *LG21* and *R-1*, and if there are any bottlenecks in terms of marketing?

We have also received a question about how the value of lactobacilli will be disseminated and penetrated.

A-7-1

Ueda: I have heard that China has a very large number of people infected with *H. pylori*. However, the understanding of why *H. pylori* is bad has not advanced.

First of all, we need to promote understanding of why *H. pylori* is not good. That is where *LG21* has a chance to win, of course. Therefore, we are now working with researchers to research and publish papers on the effects of *LG21* bacteria, and to make them available to the public, so that people in China will know about them and buy our products. We are working behind the scenes to somehow create such a process.

The same applies to *R-1*. *R-1* sold very well in Japan, initially because something about *R-1* bacteria was effective against influenza. I have heard that Chinese people are also concerned about immunity.

We need to first have people understand why the immunity is good for the Chinese people. We want them to understand that they should do it, and that they should boost their immune system, and that by taking the *R-1* bacteria, they can boost it, and they will also understand that. We are currently working on a plan for such a connection with the product. In Japan, similarly, when such things were connected, it led to explosive sales, and many members who have that successful experience are now coming from Japan to China. These people are now considering various measures, making use of their experiences.

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