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Meiji Holdings Co., Ltd.
Revisions to Consolidated Financial Forecasts for FYE March 2024 (FY2023)
The Telephone Conference Q&A

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Presenters:

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Bunjiro Yao Member of the Board and Vice President, Meiji Co., Ltd.

*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 ask about page six of the slides. For JPY4 billion deficit in China business, what categories were negative and how much were they negative? In short, we would like to confirm how much of a deficit the drinking milk and yogurt business for the consumer market will be this year.

A-1-1-1

Furuta: We expect a deficit of approximately JPY4 billion from China business in FY2023, but please understand that the majority of this deficit is due to drinking milk and yogurt. Since there is a surplus in confectionery and ice cream, the deficit in milk and yogurt is currently more than JPY4 billion.

Q-1-1-2

I understand. If so, would you say that more than JPY4 billion means that there is a slight surplus in other categories, such as confectionery and other ice cream products?

A-1-1-2

Furuta: That's right. We disclose sales, but we do not disclose profits by business category, so I can only give you a rough idea. As I mentioned, the drinking milk and yogurt business lost more than JPY4 billion. I think it is fair to say that it will be recovered through confectionery and ice cream, and the total will be JPY4 billion.

Q-1-2-1

On page nine, you say that the drinking milk and yogurt business will break even in three years, but will it be profitable in the first place? If this is the case, various cost reductions will be achieved, such as reductions in depreciation of fixed costs due to impairment losses. You are saying that after three years China business as total will break even. But to begin with, at what level do you see the drinking milk and yogurt business will be after three years?

I think there was talk about *Meiji Oishii Gyunyu* and I am aware of the question of whether it is worthwhile to do this without withdrawing from the business, but I wonder what the profit level will be in the next three years and what the future holds. Could you explain the reason why you are continuing the business?

A-1-2-1

Yao: As for your question about the timeline for returning to profitability, our priority is structural reform, and we have a plan to expand our business while continuing to make a certain amount of marketing investments.

At present, we plan to break even in the drinking milk and yogurt business, including commercial use, on an EBITDA basis in FY2026 and on an operating income basis in FY2027. We plan to break even on an operating income in FY2026 for China as a whole, including confectionery and ice cream businesses.

Q-1-2-2

If that is the case, you are saying that you will be in the black in terms of operating income in four years, but I think you have already been in this business for quite a while. And if you are aiming for zero in another four years, I think some would point out that there is no point in doing this. What do you think about that?

A-1-2-2

Yao: In the drinking milk and yogurt business for the consumer market, the superiority of chilled milk was recognized at one time, and we were able to turn a profit. However, this time, as I explained, we have been caught in a price war due to intensified competition.

Therefore, as a future measure, we believe that localization is, of course, necessary, but we are planning to break even by introducing products such as *Meiji Oishii Gyunyu* that are recognized for their unique value as Meiji in Japan.

Q-1-3-1

Regarding AustAsia, would you also agree that the company will be profitable by FY2026?

A-1-3-1

Furuta: As for AustAsia, the company is an entity accounted for using equity method for us. They are currently in deficit, but they have issued a five-year plan on how to turn this deficit around, so we expect them to follow this plan and turn a profit.

We believe in their revival plan and hope to see them turn a profit, even though they are expecting a deficit in FY2023, and FY2024.

Q-1-3-2

Is it correct that you are assuming that we will be in the black in FY2026?

A-1-3-2

Furuta: That's right. The company is expected to be in the black from FY2025 in their plan.

Q-2-1-1

I would like to ask whether this impairment loss is sufficient. Regarding AustAsia, the acquisition cost was JPY28 billion, and the impairment loss was JPY6.2 billion. I guess it depends on how long this deficit will continue, but I would like to confirm that this is enough impairment. Also, regarding the drinking milk and yogurt business, since the amount of impairment loss for fixed assets is not the whole amount, I would like to know what assumptions were made to record this impairment loss and whether there is any possibility of further impairment loss.

A-2-1-1

Yao: We have recorded the impairment loss based on our judgment that this amount is sufficient in our discussions with the accountant. Now, for our part, this amount is sufficient.

With this impairment loss, our value from AustAsia will reduce by JPY6.2 billion and we will reduce the value of our fixed assets in China by JPY14.3 billion. It contributes to reducing our fixed cost burden and strengthening the competitiveness of its drinking milk and yogurt business in the future.

Q-2-1-2

In the drinking milk and yogurt business, how much of the fixed assets are expected to be accounted for by the drinking milk and yogurt business?

A-2-1-2

Furuta: I'm sorry but the fixed assets are not disclosed.

Q-2-1-3

Is it correct to understand that if this plan is followed, there will be no further impairment losses and that the cash flow will be used to run your business?

A-2-1-3

Yao: That is correct. Our business plan is based on the assumption that further impairment is not necessary.

Q-2-2-1

I would like to ask you about JPY22.5 billion in the extraordinary income recorded this time. Your company originally set a target of reducing its cross-shareholdings by about 30% from the 2020 level on a book value basis. By last year, it had reduced its cross shareholdings by about 20%. What kind of progress has been made toward this 30% reduction target? Please tell us how you plan to reduce your cross-shareholdings and how this will lead to improved ROE and enhanced returns to shareholders.

A-2-2-1

Furuta: With regard to our cross-shareholdings, we have been working steadily to reduce them by

30% on a book value basis, as targeted in the 2023 Medium-Term Business Plan. However, since there was also this impairment, we additionally sold our cross-shareholdings in Q4.

I believe that the sale has reduced our cross-shareholdings considerably, and I believe that the percentage of total assets has probably dropped as well.

As we further reduce our cross-shareholdings in the future, we intend to use the funds to invest them firmly in our growth strategy.

Q-2-2-2

For the sale of cross-shareholdings, how much room do you think is there for further reduction in your company, and do you think you can reduce it further from here?

A-2-2-2

Furuta: I would like to explain our policy on the reduction of cross-shareholdings when we announce the 2026 Medium-Term Business Plan in May.

Q-3-1

One thing I would like to do is to make a confirmation of the discussion so far. I think you mentioned that the remaining assets of the China business are undisclosed, but should I assume that there is still some risk rather than no more risk since all the assets have been written off? Even if it is non-disclosed, I would like to know as much as possible about something like a sense of level.

A-3-1

Furuta: The assets in this case are naturally drinking milk and yogurt, or in short, the assets of the dairy business were impaired. Therefore, we have not impaired the confectionery and ice cream assets.

There are still drinking milk and yogurt assets. However, regarding the risk of impairment of its assets, if our revival plan is steadily implemented, we do not expect any impairment of fixed assets. As I mentioned earlier, we are seeing steady top-line growth in confectionery and ice cream, so we do not see any impairment risk.

Q-3-2-1

I would like to ask you about the outlook for the future. In your forecast of a JPY4 billion loss for the current fiscal year, I would like to confirm whether the loss in the China business is larger in H2, or whether there is a trend toward improvement. In the future profit and loss forecast, I think there is an item for growth other than the drinking milk and yogurt business. Is this something you are already working on? Please allow me to review this for future revenue projections.

A-3-2-1

Furuta: Regarding JPY4 billion deficit for the current fiscal year, the deficit has increased in Q2 and Q3 compared to Q1. As Yao mentioned earlier, this is partly due to the intensifying competition in the market, and partly due to the increased depreciation and fixed cost burden due to the start of operation of the Tianjin plant last spring, and the deficit is gradually increasing.
Yao will explain the future business prospects for confectionery, ice cream, and B2B.

Yao: The drinking milk and yogurt business includes both the consumer B2C business and the commercial B2B business. In addition, whether it is the new plant in Tianjin or in Guangzhou, the drinking milk and yogurt business will use the same fixed assets because the plants can be utilized for both consumer and commercial use.
So, it is true that drinking milk for the consumer market is now caught in an extremely competitive environment and is not profitable, but as I mentioned earlier, we will increase added value by introducing products of unique value.
If it is determined that this will also take some time, we can take into consideration the balance between the current B2C drinking milk and yogurt for the consumer market and the commercial milk and cream business, etc. Specifically, we believe that it is possible to expand the business by adjusting the balance between the commercial business and the drinking milk and yogurt business for the consumer market. We believe that by adjusting the balance, it is possible to expand the

business by utilizing fixed assets.

However, as Furuta mentioned earlier, we have decided to build one new ice cream factory and one new confectionery factory at a time, because the existing factories are not able to produce enough ice cream and confectionery. We believe that it is possible to operate this plant and grow the business.

Q-3-2-2

I would like to confirm on page nine. It is my understanding that the growth in marginal profit on sales is the increase in sales in the drinking milk and yogurt business, and the growth outside of the drinking milk and yogurt business refers to confectionery and ice cream. Is this understanding correct?

A-3-2-2

Yao: That is correct. We have created a revival plan with this intention.

Q-4-1-1

First, I would like to ask what your perception of your company's competitiveness is. The sales of drinking milk and yogurt for the consumer market are struggling in a very competitive environment. Also, the profitability of AustAsia's upstream farms is quite poor compared to the other upstream farms of dairy manufacturers in China.

Compared to competitors, which have to compete in both production and sales, I think your profitability is getting a little too tight. I wonder if you can really cope with this situation only by reducing fixed costs, reviewing the supply chain, etc., and I am concerned that your competitiveness may be declining structurally. What is your company's current position on this?

A-4-1-1

Yao: Certainly, if we only look at the current figure, I think you are right that the competitiveness of drinking milk and yogurt for the commercial market is declining.

The main reason is that chilled milk is now involved in price competition. For example, we are planning to launch other products, such as *Meiji Oishii Gyunyu* and *SAVAS Milk Protein* that have been well received in Japan, but we are aware that we would have been able to launch these products a little earlier if COVID-19 had not been involved.

The main reason for our current difficulties in profitability is that the launch of major new products was delayed due to the COVID-19 pandemic, which has prevented people from traveling between Japan and China for two to three years. We believe that we will be able to recover our competitiveness by introducing new products of unique value that have been well received in Japan.

In addition, AustAsia is also very capable of running a ranch. Three years ago, the company was very profitable, and now, the volume of raw milk sales is growing, and operations are not doing too badly.

However, there is a unique accounting treatment for ranching operations: the biological value is an evaluation index that measures the price paid for each cow, how much feedstuff each cow receives, and how much milk each cow produces. If feedstuff prices rise sharply and milk prices fall, the loss on the valuation of individual organisms will be very large, putting pressure on AustAsia's profit and loss.

Therefore, we recognize that AustAsia is an excellent dairy farm and company in terms of milk production and milk quality, and we believe that AustAsia can recover its performance by closely monitoring its revival plan.

Q-4-1-2

Major Chinese dairy manufacturers' free cash flows are positive right now, and there are comments that they want to make further investments in the future. But when I look at AustAsia's free cash flows, it is negative, isn't it?

I understand that there are a lot of non-cash costs that you just mentioned. But looking at the free cash flow statement, it is negative. Is it really correct to understand that the company is in a position to further enhance its competitive advantage by aggressively investing in the next revival plan?

A-4-1-2

Yao: Since we have dispatched a director to the company, we will be involved to a certain extent. But our current stance is to believe in AustAsia's revival plan and watch how it goes. We believe that it is not an unreasonable plan, and we believe that it is possible to recover their business performance.

Q-4-1-3

I understand that you are going to do a good job with the three-year revival plan this time. I think this revival plan will still take a certain amount of time when we look at the new fiscal year. Is there any nuance to this timeline that we can see when the deficit reduction plan will be put into action in FY2024?

A-4-1-3

Yao: Regarding this fiscal year, there is no doubt that the new plant in Guangzhou will start operation, and this will temporarily increase the fixed cost burden, apart from marginal profit.
However, it will still take time to introduce new products before we can adopt a strategy on the value-added side. So until then, we will mainly focus on the appropriate allocation of fixed costs for each business. Therefore, the first half of the three-year revival plan is centered on reform of the fixed cost side, while the second half is designed to maintain the fixed cost side and increase the marginal profit side.

Q-4-1-4

Am I correct in understanding that the deficit will already begin to shrink in FY2024?

A-4-1-4

Yao: The amortization cost of the new plant in Guangzhou will be included, so the deficit will probably increase slightly. However, we are confident that the fixed cost measures and marginal profit measures will take effect in FY2025 and that we will be able to break even on an EBITDA basis in FY2026.

Q-4-2

I think that the food segment, domestic food business, has been revised upward this time. I think the focus was on price hikes and costs, but are there any good stories or bright signs for FY2024 or the next one? Or is the image that they are still trying very hard to lower fixed costs, or rather, they are controlling expenses, so it's not quite a bright story yet? I would like a few comments on domestic food business, if any.

A-4-2

Furuta: As for the budget for FY2024 and the 2026 Medium-Term management plan, I will explain them again at the time of the announcement of the full financial results in May, but we believe that the price hikes have been well received and that recovery in volume has been achieved.

In fact, we are seeing top-line growth, and we believe we are making steady progress in reducing fixed costs. In that sense, we are hoping to show you a new product in FY2024, as new products will be launched, and their growth will be on the rise.

Q-5-1-1

I would like to know your thoughts on the sales and cost environment in the future. Are there any signs that this will change, and what might happen to change the current harsh competitive environment? I would appreciate it if you could organize and share your view on that.

A-5-1-1

Yao: As for the sales environment, we do not expect that the Chinese economy will suddenly recover and that we will be able to sell expensive products all at once. We have also put together a revival plan based on the assumption that the current economic situation in China will continue for some time.

On the other hand, China's population is about 10 times larger than Japan's, and there is no change in the fact that there are a great number of customers in each of the three regions of North, East, and South China.

We believe that the main reasons for the deterioration of our recent business performance were that we were caught up in price competition with other companies and that we were late in introducing products of unique value. It is enough in China to run one factory even if we gain a few percent of the market share by introducing unique value-added products. We believe that it is possible to recover our business performance by doing business with aggressive initiatives.

As for costs, feed prices in AustAsia have stabilized. Although AustAsia is still expected to lose money in FY2024, the deficit is expected to shrink significantly. The raw milk price is now at the bottom of the market. But once supply and demand return to normal, we believe that AustAsia's earnings will recover sufficiently.

Q-5-1-2

You are saying that AustAsia's costs are going down, but that the raw milk prices are going up because the supply and demand for dairy products is improving?

A-5-1-2

Yao: We have not seen such a rapid recovery, but from the perspective of AustAsia's profit and loss, feedstuff prices and other factors have settled down, so we are seeing a recovery trend in profit and loss compared to the previous situation in which profit and loss deteriorated significantly due to the steep rise in feedstuff prices.

Q-5-1-3

I understand. It is not so much that raw milk prices are going up, but rather that costs are likely to fall where they have been pushed up.

A-5-1-3

Yao: Yes. I think that is where it will start. This is a matter of supply and demand balance, so raw milk production cannot be controlled even if the raw milk demand is reduced. Therefore, since raw milk production was originally increasing on the basis that demand is expected to grow in the market as a whole, this has created a gap, and raw milk prices are falling under a very relaxed supply-demand situation.

In the future, dairy farmers will probably control the production of raw milk by turning cows over to meat production. Therefore, the supply-demand balance will naturally work in this manner, and as a result, we expect to recover from the current drastic easing trend.

Q-5-1-4

So is it correct that there are no signs yet of any bottoming out on the demand side?

A-5-1-4

Yao: I don't think the cutthroat price competition that exists today will continue for the next 10 years. The current cost competition is wearing away at everyone's strength, so I think it is only natural that drinking milk prices will return to an appropriate level once supply and demand stabilize. Therefore, we believe that the current environment will not last forever.

Q-5-2-1

The second is the fixed cost reduction section of the waterfall chart on page nine. You said that this plus JPY2 billion to JPY2.5 billion would be mainly for the first half of the three-year period. Please explain further details on this.

A-5-2-1

Yao: Regarding the reduction in fixed costs, the part about JPY2 billion to JPY2.5 billion, the plant itself is not operating well now because it is not generating the volume of goods that was initially expected. We have established a plan based on the idea that it should be possible to reduce fixed costs by a sufficient amount, mainly by maintaining the appropriate capacity of equipment, such as the appropriate allocation of personnel, line capacity, and products.

Q-5-2-2

So you don't think of it as reducing the number of lines to reduce fixed costs, but rather as increasing capacity by appropriately allocating the best-selling items?

A-5-2-2

Yao: The drinking milk and yogurt business includes both B2B and B2C businesses. We are actively shifting the sluggish B2C business to the B2B side, including personnel and facilities, and concentrating resources there to improve operations.

Q-6-1-1

My question is about the revised JPY3.5 billion increase for the food segment. It may be difficult to discuss in detail, but I would like to ask for a change of each business, and if possible, a quantitative image. If it is correct to say that overseas sales have been revised downward this time due to the impact of China, then other sales have been revised upward considerably? We would appreciate it if you could give us an image of each segment. I would like to ask in what areas the effect of the price hikes was strong and in what areas cost factors improved.

A-6-1-1

Furuta: The deficit in the China business increased considerably, but other overseas and domestic businesses performed well, so the overall operating income of the food segment increased. Unfortunately, I cannot give you any more specifics, but I would like to discuss those specifics with you when we announce our financial results in May.

Q-6-1-2

What factors do you attribute to the price hike effect that is mentioned in the release, or to the fact that costs are being held down more than expected? Can I just ask about that?

A-6-1-2

Furuta: The price hike effect basically means that the effect of the price increase has been properly realized as the volume has recovered.

In the area of expenses, general and administration expenses have been reduced, and overall expenses have decreased as a result.

Q-6-2

I would like to ask you about drinking milk and yogurt for the commercial market in China. I understand that you try to recover sales by introducing unique value-added products. But I think that the quality of your brands up to now, such as functional yogurt, has been one of your strengths, and you have been selling your products at high unit prices while promoting such value-added products. However, as a result, your company's high unit price products have been caught up in the price competition among competitors. I feel that the situation will not change with the introduction of *Meiji Oishii Gyunyu*, but I would like to ask you why you think the situation will improve with the introduction of a new brand.

A-6-2

Yao: I think you are asking whether we will be successful in introducing unique value products such as *Meiji Oishii Gyunyu*. To be honest, the current situation with chilled milk is that we were too inclined to secure the quantity to prioritize the operation of the plant, and we have had to make some unreasonable sales.

On the contrary, we believe that the impairment will allow us to reduce the fixed cost level to an appropriate level, and we will not have to make the unreasonable sales that we made in the past.

Therefore, as I mentioned earlier, thanks to the strong performance of B2B, we believe that we can improve the current situation by allocating sales to B2B and curbing unreasonable sales to B2B.

In addition, *Meiji Oishii Gyunyu* has been well-received by Chinese visitors to Japan, and we are aware that our brand recognition has been growing considerably.

Therefore, we believe that it is possible to increase sales and marginal profit from our unique value products by marketing them in China in such a way that people will remember and recall the drinking milk they had in Japan, and by marketing them in Japan and China in an integrated manner.

Q-7-1

On page 10, I would like to know a little more about the third point of future initiatives in China, management reform. You mentioned earlier the emphasis on sales volume, so perhaps this also applies. Could you tell us more about the problems with the current management structure and how you plan to improve and evolve it?

A-7-1

Yao: As for management reforms, we established Meiji (China) Investment Co., Ltd. and have been working to strengthen management capabilities under local leadership, but we regret that it was hard for us to handle everything on their own in such an extremely adverse market situation.

Therefore, in terms of management reforms, the main one is to hold management meetings between the head office in Japan and Meiji China on a monthly basis, to set policies emphasizing marginal profit from sales and to manage the monthly progress. I would like to participate in this management meeting.

Q-7-2

You said that the consumer market is struggling, and the commercial use is doing well, but can your company maintain its competitive advantage in the consumer use market? In other words, is there no need to consider the risk that a major player will attack with a lower price, and the momentum in the commercial market will falter? Can you give us some background on this?

A-7-2

Yao: You are right, and as for commercial use, the café chains are growing significantly now, so we are not involved in cost competition to that extent. The current situation is that market expansion is winning out.

However, we believe that the coffee chain will probably not continue to grow forever. We have a reputation for the extremely high quality of our drinking milk, and our ability to deliver a fixed quantity of drinking milk without running out at all gives us an unexpected competitive advantage in China for commercial use.

While taking advantage of these factors, we believe that demand for not only drinking milk but also fresh cream will continue to grow in the future. And we will further establish our superiority in commercial use by combining our high value-added cream business with our drinking milk business.

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