

Financial Briefing for 2Q Results (for Investors)

13:00-14:00, November 8, 2021

<Q&A Summary>

Q.

Is the factor underpinning the growth in sales of prescription Kampo products impact from a growth in prescriptions related to COVID-19 or an increase in doctors prescribing new Kampo formulations reflecting e-promotions? What is your analysis for the sustainability of sales growth after COVID-19 winds down?

A.

According to our analysis, net sales rose ¥1.16 billion reflecting an increase in prescription opportunities related to Kampo medicines to treat COVID-19-related symptoms. This reflects benefits from new information provision activities through e-promotions. These are mutually related. It is difficult to distinctly separate the individual percentage of respective impact.

After COVID-19 winds down, there is, for instance, a possibility that skin irritations will decline in tandem with a decline in the ratio of mask wearers.

Given the pace of prescription opportunities is expanding, including an increase in doctors prescribing Kampo as one treatment choice for mental disorders or dizziness, we anticipate a certain level of continued sales growth.

A.

We are now able to deliver beneficial information via e-promotions to doctors working at hospitals, to whom we have previously been unable to deliver Kampo information. The opportunities to gather information from the Internet is increasing, mainly among young doctors. Tsumura's medical site also is expanding its online lectures and video content, and increasing viewership numbers and the number of cases of information recognition. Even after COVID-19 winds down, we aim to maintain ongoing growth for Kampo products.

Q.

In the China Business, it is my understanding that Tsumura aims to expand its market through M&A of companies dealing in OTC traditional Chinese medical products (for general consumers). Is priority placed on M&A of those companies with classical prescription Chinese medicines?

A.

In China, there is not clear distinction between OTCs and prescription pharmaceuticals like there is in Japan. The target for M&A are companies that possess OTCs or prescription pharmaceuticals for which the Tsumura Group cannot newly acquire manufacturing and sales approval. Although the drugs are already approved, it is the concept of the Tsumura Group to unearth classical prescription Chinese medical products that are not being sold to contribute to the health of the citizens of China. Among these prescriptions, there are both OTCs and prescription pharmaceuticals. At present, OTCs account for the majority. There is also the possibility that some of these prescription medical products can be converted into OTCs.

Q.

It is my understanding that Ping An Tsumura Pharmaceutical Co., Ltd., which was consolidated, will not post profit in FY 2021, due to unrealized gains. Is the ¥670 million decline in overseas external sales due to an increase in cost?

A.

In 1H, profit will not be generated due to intercompany eliminations as unrealized gains. However, we anticipate profit will gradually be generated from 2H. As you pointed out, ¥670 million is due to the increase in the Chinese external business.

Q.

Do you plan to see profit contribution in the full fiscal year of FY2022 owing to the elimination of the unrealized gains at Ping An Tsumura Pharmaceutical?

A.

In FY2022, it is without doubt that profit will be generated as the inventory cycle for a certain period will be completed. However, given the possibility of fluctuations due to sales and inventory trends, we cannot say definitely if we will assimilate all the profit during FY2022.

Q.

At the presentation scheduled for March 2022, will you touch upon the progress in M&A in the China Business or issues such as the timeline?

A.

Regarding the vision, we plan to divide our 10-year vision by milestones. In the China Business, we plan to show our ideas for the next step in realizing the timing for an M&A.

Q.

Should performance remain brisk in the domestic business and China Business, will there be concern about manufacturing capacity?

A.

There is no issue with the manufacturing capacity for the scale of sales and sales growth in external sales in China at present. In the prescription Kampo products business in Japan, we plan to carry out manufacturing at the Tianjin plant which is scheduled to start operations in FY 2022. In light of this, manufacturing capacity is not a concern.

Q.

Is there a risk of deterioration in the expense-to-sales ratio in 2-3 years from now should the yen continue to depreciate in value?

A.

We plan to enter into forward contracts for the next three years. Our goal is to stabilize our procurement expense.

Meanwhile, in the medium/long term, should the yen continue to depreciate in value, it is our opinion that it will be difficult to avoid impact on the cost of sales.

Q.

Is it possible to divide the positive impact from COVID-19-related prescriptions by general practitioner (GP) and hospital (HP) sales routes? Are more patients being treated for side/after effects at general practitioners as opposed to hospitals?

A.

Formulations related to COVID-19 have a major positive impact mainly at general practitioners. Patients search for medical facilities to get treated on an outpatient basis for COVID-19 side/after effects and the vast majority get treated at a general practitioner.

Q.

In your forecast revisions, you forecast a 1H net sales growth of ¥4.0 billion, and a 2H net sales growth of ¥1.0 billion. Meanwhile, you forecast a 1H operating profit growth of ¥2.9 billion and a full fiscal year operating profit growth of ¥1.6 billion. This appears to be a downward revision of ¥1.3 billion to 2H operating profit. Why is the reason for your cautious outlook for 2H earnings?

A.

We continue to plan for sales growth. In 1H, SG&A expenses were ¥1.0 billion lower than plans. However, of this, ¥400 million was R&D expense, sales system repair expense, and expense related to lectures, for which posting has been delayed to 2H. Also, from 2H FY 2020, we are seeing investment benefits. In 2H FY 2021, we plan to actively invest, mainly in e-promotions.

Q.

There was a dilution in share value of around 10% due to the implementation of a third-party allotment to raise capital for the Ping An Insurance Group in China. Did this garner a better evaluation for ROI?

A.

We plan active investments, including M&A moving forward. We aim to garner better evaluations for our ROI. At present, we do not believe investors will make this evaluation.

Q.

Are you still positioning the China Business as a growth business? Is there a possibility that the timing of monetization of the China Business will be pushed back?

A.

There are rising needs for quality for the raw material crude drugs and drug pieces in the crude drug platform. In the field of botanical/herbal drugs, where the quality of prescription pharmaceuticals is determined based on crude drug quality, we plan to leverage the strengths of the Tsumura Group, which has been tackling quality improvements from before. Furthermore, we aim for a large sales scale. We are negotiating M&A deals to enter the market for traditional Chinese medical products. Given that crude drugs will become more valuable further out, there is no change in our belief that the China Business is promising. At the March 2022 presentation,

we plan to convey our ideas on the China Business, which are outlined in the Long-term Business Vision 2031.

Q.

What have you ranked Sustainability Vision 2050 as a more dominant concept over the Long-term Business Vision 2031? Also, how do you interpret climate change risks?

A.

We have positioned the Sustainability Vision 2050 as the superordinate concept of the Long-term Business Vision 2031 as it is our belief that we should be sensitive to changes in the natural environment and crisis to achieve sustainable growth at the Tsumura Group, a handler of crude drugs that are the best of nature.

Climate change possesses the potential to greatly impact our business strategy and financial health. As measures to alleviate climate change risk, Tsumura is tackling the duplication of crude drug cultivation sites, nurturing of seeds that are resilient to climate change, and innovations to crude drug cultivation technologies. Also, given that large amounts of water are used during the Kampo formulation manufacturing process, thus far we have reused this water for purposes other than manufacturing processes. However, going forward, we plan to undertake recycling by reusing water during the extraction process, which uses the largest amount of water. In the past, there has not been a situation where we had difficulty procuring crude drugs. However, moving forward, we plan to confront issues with the natural environment through our business operations to realize our co-existence with nature.

[Important points]

The details in these materials were not transcribed as is from the Q&A session at our financial results briefing. Taking the purpose of these materials into account, this is an abridged version.