

[Key Q&A] Conference Call on Financial Results for the Second Quarter of 2018

[General]

Q. How would you summarize H1? What are your strategies for recovery?

A. While the overall profit in January to March was within our expectation, April to June was worse than expected, specifically due to the following reasons:

- In Japan, the major source of profit, *Tokucha* and 185g canned coffee, decreased more than expected, resulting rapid change in product mix.
- In Japan, while we did not expect big growth for overall sales volume this year, the demand for aseptic products such as *Craft Boss* and *Green DAKARA Yasashii Mugicha* grew higher than expected, making us needing to build up stocks beforehand and utilize co-packers to prepare for the summer. All of these resulted in supply chain cost increase.
- Also, some core brands in some regions face growth stagnation.

Regarding H2, in addition to expectation of supply chain cost improvement, we will reinforce activities to *Tokucha* and 185g caned coffee to put a brake to adverse product mix in Japan.

Also, in Europe, we will continue strengthening *MayTea* and core brands to aim for sales recovery.

[Japan]

Q. Can you explain about your medium-term approach on ensuring continuous profit growth?

A. In order to generate profit, topline holds a critical role, and the existence of popular products is even more appreciated. With that said, our sales grew above market, and we also have popular products such as *Craft Boss*, so there is no issue. However, currently the lack of supply capacity for aseptic products is our weakness, suppressing our profit in a short-term. Regarding this, we have decided to add new production lines, which will start operation in Ujigawa Factory in H2, 2019, and Haruna Factory in Spring, 2020. With the operation start, both our in-house production rate and capacity to demand will increase, which make profit growth from sales growth possible.

Secondly, we will strengthen healthy categories which is the core of our high added-value portfolio by utilizing our knowledge and experience. In the aging Japanese society, not only the quantity of longevity, quality also grows more important, making “health” an important value. In this situation, currently most FOSHU and Foods with Functional Claim often uphold “losing-weight” efficacy, from next year, we would like to launch products with efficacy that is not surrounding the “losing-weight” theme to expand.

Finally, evolving vending machine business. While vending machine market faces difficult situation in H1, our company is able to keep our sales flat due to the acquisition of Japan Beverage. On the other hand, with change of cost structure in vending machine business due to societal factors, it is more and more critical to consider ways to increase operation efficiency. For

example, implementation of wireless machines allow us to get timely information of sales of the machine, which can improve operation efficiency, and we had been expanding implementation of these wireless machines for Japan Beverage. These require investments, but we will proactively proceed.

We would like to achieve profit growth through taking these approaches together.

Q. Why is Tokucha declining? What will you do about this?

- A. While heavy users continuously drink the product because they feel its efficacy, light users who occasionally drink *Tokucha* just to match their meals are shifting. These light users did not lose interest in health consciousness, but rather shifting to other products and/or services. To deal with this, this autumn we are launching new campaigns for *Tokucha* to not only let heavy users to continue the drinking habit, but also re-introduce the benefits of *Tokucha* to light users. We aim for recover the trend by taking these 2 approaches together.

Q. How is coffee category doing? How much is the cannibalization between 185g can and PET?

- A. In convenience stores, it is true that shift to PET happened due to shrink of 185g can shelf and expansion of PET shelf. *Craft Boss* also absorbs consumers from convenience store counter coffee and tea category, in which case, its function is rather on pioneering new market. As a result, overall sales of coffee category increased. Also, from January to June, it is estimated that 185g canned coffee declined by approximately 10% in the market, but we remain steady, and *Craft Boss* is expected to grow twice as much as last year.

Q. Other companies have announced collaboration on vending machine operation, what is your thought on this?

- A. The 2 key points for profit growth in vending machine business are increasing sales per machine and optimizing operation costs. The collaboration that can achieve point 1 includes mutual product supply, which is not under consideration at the moment. On the other hand, collaboration to enhance efficiency in operation costs is beneficial to our company, and we will actively consider this possibility.

[Europe]

Q. Please explain further details in each country other than the weather.

A. (France)

Core brands such as *Orangina* and *Schweppes* continued to perform well, and share went up. Furthermore, *MayTea* is also growing, so there is no big concern regarding the topline. On the other hand, there are some issues in supply chain. We have been working on them by taking some short-term strategies such as improving supply-demand forecast, logistics, and warehouse locations. While societal factors such as truck shortage also caused temporary cost increase, we

estimate the problem to be solved in medium-term

(UK)

After sugar-tax implementation in April, the remaining of pre-tax products on the shelf, and active promotions by competitors caused uncertainty in the market. As we enter June, we see some signs of recovery for *Lucozade Energy's* sales. When looking at competitors, while sales of taxed products greatly decreased, sales of products exempt from tax grew. We believe that this is the sign of consumer acceptance to low-sugar strategy, which we took in advance than other competitors.

(Spain)

In addition to overall market deceleration, competition is also getting more aggressive, which may result in longer time for recovery. While we will enhance our strong brand Schweppes as well as expanding *MayTea* in Spain, new product penetration takes longer than France and UK.