November 2023

Financial Results Briefing Q&A Session for FY3/2024 2Q

[Time and Date]

11:00 a.m. to 12:30 p.m., Friday, November 10

[Presenter]

Koki Ando, Representative Director, President and CEO

Noritaka Ando, COO and Executive Vice President, and President & Representative Director of NISSIN FOOD PRODUCTS CO., LTD.

Yukio Yokoyama, Director, Chief Strategy Officer, and Managing Executive Officer

Takashi Yano, Executive Officer and Chief Financial Officer

Domestic Business

Q. With the weakening yen and rising freight rates, should we expect to see a wage increase in the Domestic Instant Noodles Business? With that in mind, should you consider raising the price of instant noodles in Japan in the next fiscal year?

A. We have had no discussions on the direction of price revisions at this time. This is because cost increases were relatively large this fiscal year, and we expect costs to be flat next fiscal year. One concern, however, is the exchange rate. The impact of exchange rates lags, but it could be a challenge at 150 yen or so to the dollar. And while we consider a future weakening of the yen to be a risk factor, we have no plans to revise prices at this time.

Overseas Business

Q. What will be your approach to profit growth for your Overseas Business FY 3/2025? Your growth has been considerable, but should we expect a continued target of high-single-digit to double-digit growth next year, as described in your mid-term plan? What are your thoughts on profit growth, particularly in the Americas?

A. We are finalizing our plans for the next fiscal year internally. We hope to grow within a mid-single-digit range, if possible. The situation differs from country to country in terms of exchange rates, raw materials, and other factors. We are looking at each situation closely. In any case, we believe profitable growth is possible. Premium products such as the CUP NOODLES brand are driving growth by selling well not only in the U.S., but also in Europe, Brazil, India, and other areas. In addition to the growth of base products, we are looking to increase our numbers by raising awareness and recognition of cup-type instant noodles, high-value-added bag-type instant noodles, and other premium products. We expect a slight amortization burden in the Americas associated with capital investment, as well as a small cost increase due to the transition to paper cups. We expect to shift costs by expanding our presence to penetrate the market further. The media has been positive in their coverage of our paper cup concept, resulting in a favorable impression. In any case, brand strength represents the foundation. At the same time, we are at a stage where we must be resilient against contingencies. By contingencies, I mean business continuity plans, supply chain management issues, Taiwan, and North Korea, among others. Contingencies mean that performance will never be flat, but we must put a corporate structure in place and have the resilience to cope.

Q. With rising earnings in the U.S. and increasing profitability in Asia and Europe (even when excluding equity in earnings of affiliates), it appears you have established a winning pattern. It appears that each entity is executing more effectively, or perhaps your ability to manage and exercise governance as a holding company is increasing. What is your opinion of your management and execution skills?

A. Under our structure, the holdings company and chief officers, serving as a staff department, support profit centers around the world. The chief officers own all functions from sales and production to finance and administration, supporting business units, or profit centers, in other words. We believe this structure is working well, and that we enhance our management capabilities when global activities linked skillfully to these functions run smoothly. It is also essential to have a supply of human resources, including various training programs to provide experience and development for managers who will eventually become presidents of larger operating companies. We also adopted a CEO system for our subsidiaries. Under this system, top management in the country is hired from among local management. We are not necessarily committed to transferring and installing presidents who come from the head office in Japan. We adopted this system slowly over more than a decade, but I think it is starting to have a positive effect.

Q. I understand that the U.S. is doing well, as explained. At the same time, I get the impression that July-September volume was somewhat of a challenge in the short term. I am sure that there was a reaction to the price increases last year in August. What is your opinion on the facts, and what do you expect for volumes in the second half of the year? Will the change to paper cups starting in January have a positive impact?

A. We attribute the slight slowdown in the U.S. in the first half of the year to the fact that we were more focused on instant noodle supply amid continuing demand. For example, we have increased our supply capacity by robotizing factories and improving inspections. In general, some might say that we should have promoted our products a little more. But we believe volume was slightly weak due to the fact that we responded to heavy demand without any promotion at all. On a sales basis, October results in the U.S. were a record high. We also posted the second-highest volume on record, second to April 2020 during the pandemic where we saw the highest month in terms of volume. This result wasn't due to any special factors. It was rather the effect of the promotions and displays we implemented. Premium and base product volumes were in the mid-10-percent range year on year. For example, grocery cannel, club cannel, and dollar cannel results were higher in response to our high-and-low promotions and effective in-store promotion at membership stores. According to the market data for October, the market itself was down slightly. But contrary to these figures, our volume alone was up 15%, which was very strong. I believe we will continue moving forward in this manner. In that sense, final sales may exceed last year on a volume basis. We expect a slight fall-off in profit for the second half of the year due to one-time payments of commissions and other fees associated with the purchase of real estate. And while costs may increase slightly with the transition to paper cups, we are planning for the medium and long term, understanding that we will maintain double-digit operating profit. We believe our base is very strong. If raw materials prices rise due to various factors, we will consider some type of price revisions. We expect that we will be able to raise profits.

Q. Looking at the actual U.S. stores gives one the impression that Korean manufacturers and other companies are stepping up the development of premium products. The new plant in South Carolina will include a production line for special premium products. Can we expect to see more development for NISSIN-style products or high-value-added products of the type that Japanese have come to enjoy? In how many years after the commencement of operations do you expect to cover the fixed cost burden of the new plant?

A. As you can see from looking at storefronts in the U.S., premium products are on the shelves in considerably more volume than in the past. Just off the top of my head, I can think of Chow Mein, Hot & Spicy, Fire Wok, Stir Fry, Stir Fry with Rice, Top Ramen Bowl, Cup Noodles Original, Raoh, Geki, and Fire Wok bagged noodles. In this same way, we see both mainstream innovations and innovations on the Asian section shelves, from cup-type instant noodles to premium bag-type instant noodles. For example, I think Geki is, to some extent, a reflection of the Korean manufacturers. I can't go into details yet, but we are studying other high-value-added products. We expect these high-value-added products, likely to be produced on lines at the South Carolina plant, to be part of our differentiation strategy. We must develop new premium products that are even more competitive. And we are confident that we will create a lineup even more powerful than our existing premium line. As for how long it will take to recover costs after launching operations, we know that the cost burden of depreciation will be high. However, the start-up of plant operations means an increase in production volume and sales, including premium products. Therefore, we expect to cover the fixed cost burden in about two to three years.

Q. We understand that the U.S. is down-trading more recently. Has the down-trade in the U.S. led to an increase in overall demand for your company? Or does that mean there is a headwind against your premium products?

A. We believe there is a down-trade situation in the US as well. For example, by channel, more consumers are shifting from grocery stores to dollar and membership stores. I think this is positive for us, since we occupy a large portion of the dollar and membership stores. On the other hand, there is another view regarding up-trade. Premium products in the instant noodles market are priced at around $1.50 to $2.00. For example, some consumers who used to purchase base products are now buying premium products. I think the major trend is showing that down-trade is providing a tailwind, and amid the down-trade, we are seeing the emergence of an up-trade to what we call premium products in our product lineup.

Q. The supply system in Brazil has improved considerably. We expect to see a further increase in volume in that country. Please update us on your view and outlook for Brazil. The numbers may not yet be apparent, but how much growth do you expect, roughly speaking?

A. Volume declined temporarily in Brazil in the first half of the current fiscal year. The decline was due to planned large-scale maintenance and resulting production issues. Volume has recovered more recently. We expect to achieve the plan for this fiscal year without any issues, and we will aim for a high-single-digit to double-digit increase in profit as planned, or even higher. With more than a 70% share in Brazil, we believe we are in a position to design the market over the medium to long term. The dish-type U.F.O. product, launched in August of the previous fiscal year, continues to do well. We fully expect to expand the instant ramen category by adding more container variations such as this. This market design is something that we must take the lead in doing. By increasing variations, we expect to grow sales and demand. I believe that Brazil will show growth for a while to come, as production volume is still insufficient, and there seems to be an urgent need to increase production capacity, including the construction of a new plant. We intend to accelerate the expansion of our ramen business into neighboring and other South American countries, including the investment of resources into exports. With such a recognized brand in Brazil, we want to accelerate category expansion and multi-category development of other food products using the NISSIN brand power. Candidates for products include not only ramen, but other food products such as confectioneries. Multi-category products will require time to set up production facilities, etc. Still, we recognize that Brazil is a market capable of even more growth if we include multi-category products.

Q. In the U.S., it appears that margins have been secured due in part to the recent lack of supply among competitors and in the market. I expect that you and your competitors will increase production in the future, and that supply will become available in the next fiscal year and the year following. This will represent a significant change in the environment. Will you be able to maintain current margins at that point? Also, it is conceivable that the current margins will serve to lower the barrier to entry, creating room for Chinese products, for example, to enter the market. What are your thoughts on these points?

A. In the first half of the year, we supplied products supported by relatively low marketing costs. However, I believe we will need to spend money on marketing in the future. I do not think it will be a situation of price competition and complete commoditization, as in the past. Looking at the market, we see a price gap developing between our products and those of our competitors, even for base products. The price differences stem from the changing relationship between brands and retailers, and I believe the prices are acceptable to consumers. At the same time, our basic direction is to expand premium products. We must expand the market firmly by launching new premium and high value-added products. Looking from the consumer standpoint, the position of cup-type instant noodles is changing from a traditional snack food to a meal. We see high growth potential, particularly as premium products are approaching the meal level. I have heard that more women in the U.S. are eating cup-type instant noodles for dinner. While not connected directly to margins, we think underlying support for these changing circumstances can lead to further growth.

Mid- to Long-Term Growth Strategy

Q. While your target was 80 billion yen in ten years, you reached that level in just three. Your CEO stated that the aim is for sales of 1 trillion yen, profit margin of 10%, and operating profit of 100 billion yen by 2030. That would mean profit growth in the mid-single digits over seven years. The shift to premium products is going well, the instant noodles market is undergoing solid expansion, and you generate profits in every region. Is this profit growth truly sufficient, or can the company aim higher? What are your thoughts?

A. Consider 1 trillion yen in net sales and core operating profit margin about 10% as the minimum line. In addition, we will definitely pursue mid-single-digit, 5% to 6% growth in terms of stable growth. You may have higher expectations, but our performance depends on global branding and how large we can grow our businesses. The U.S., Mexico, and Brazil are in good shape generally. The EU is also in good shape. We are getting back on track compared to the past. While conditions in China are somewhat difficult, we expect the market to be firm. The current state of Japan-China relations has had a considerable impact on perishable Japanese products in the food industry, but we are not overly concerned currently. In addition, our Non-Instant Noodles Business is growing steadily in Japan. We also recently announced the launch of a new plant in the U.S. to prepare supplies that support growth amid globalizations. Since the mid-single-digit figure includes the addition and increased depreciation of production and capital equipment, we expect cash flow to continue to be quite strong on an EBITDA basis.

Q. As business performance grows significantly, are there any issues not progressing as expected, or progressing at a slower pace than expected in relation the vision of your mid-term plan? What is your take on the issues at this point, which I suppose will be included in the new seven-year mid-term plan?

A. With certain exceptions, our major domestic subsidiaries are doing very well. Leading manufacturers, who have an easier time imposing price increase, are doing well. Those that have not been able to raise prices sufficiently are struggling somewhat. Among our domestic and overseas subsidiaries, Nissin Miyako Country Club, a golf course unrelated to our core business, experienced a slight downturn in earnings, but I believe the entity will become profitable in the future. Even among the companies that are struggling, the smaller entities that are underperforming do not have a significant impact. Another issue we recognize as a challenge is human resources. With business growth growing at a rapid pace, we are encountering challenges in securing human resources amid the global branding of our Overseas Business and the rapidly growing KANZEN MEAL business. We are hiring about twice as many mid-career professionals as new college graduates, helping new mid-career hires acclimate as quickly as possible through a job system and special attention. We must create a corporate structure, including in-house training, that allows mid-career hires to integrate easily and contribute their abilities quickly.

Q. While the revised mid- to long-term growth plan is one main message, I also noted that results deviated from the profit forecast on a single-year basis. Since performance was strong, it's not necessarily bad news. However, as you formulate the plan for the next fiscal year, do you have an expectation for a reasonable range of deviation? What is your approach to formulating performance forecasts?

A. We consider our mid- to long-term growth strategy in normal operations to reflect mid-single-digit growth. We plan to achieve this growth through innovation and marketing efforts. However, contingencies can arise and affect the business environment, just like turbulence affects an airplane. This turbulence may change assumptions and the business environment drastically. Therefore, we must always aim for medium- to long-term growth while maintaining the flexibility to change our base approach and revise our strategy when the ground shifts dramatically underfoot. For example, we did not assume that the pandemic would have a positive impact on our business. The result was a considerable positive contribution, and we believe that this is the reason why we responded so well to rising raw materials prices. In addition, the Russia-Ukraine conflict has increased raw materials prices. Looking at the short term, these factors decrease profits. Over span of a year or two, however, we will experience a positive outcome as we are able to implement price revisions and generate profits owing to our marketing and branding efforts, as well as the fact that we have built a structure that supports profit creation. These types of contingencies occur frequently. Extreme weather, environmental issues, etc., are stories that affect the profitability of all businesses. The abnormally warm weather for November had an impact to a certain degree. I don't think anyone could have envisioned the U.S. in its present state by looking at history. Volatility in the world is increasing, but our base assumption is mid-single-digit growth. In this context, we will always have to review and consider raising the bar internally.

<u>Other</u>

Q. With respect to operations at your subsidiaries as you look ahead to 2030, do you feel comfortable continuing under the current model, or do you feel some changes are necessary? Are there some issues that must be addressed? Specifically, there are several subsidiaries engaged in the same business and several in which you do not have a 100% stake, even when considering equity holdings. Do you think you should reorganize these entities? Also, what are the future potential and possibilities of M&A?

A. The basic question when considering independence, merger, or M&A in connection with a subsidiary is whether we can generate synergies. In parallel, we consider the importance of internal competition. Internal competition is an important factor not only for efficiency, but also for originality. We aren't looking for synergies alone, so in some cases, we are free to choose between independence, mergers, or M&A. The equity ratio also varies from case to case. We always consider carefully and address not only the efficiency of the business, but also the efficiency of capital. I also believe the potential of M&A takes many different forms. For instance, collaborations on premium foods market development or creating a wholly owned subsidiary. It depends on the size of the partner, our resources, governance, etc. We consider the optimal positioning in light of this balance. Based on that decision, we look at layers, for example, 100%, 50%, 30%, and so on. We recognize that there are advantages to being a majority owner and advantages to being a minority owner, and that we should look at each individual situation for the best balance. We always consider the possibility of M&A of all stripes in expanding our business or extending in multi-categorization.

Q. Your company appears to be highly productive, possesses the ability to raise prices, and is resistant to inflation and wage increases. If you can't raise wages, then it's assured that other food manufacturers can't either. What is your approach to sustainable inflation and sustainable wage increases?

A. The NISSIN FOODS Group is of the opinion that we must consider raising wages to some extent. Under Mr. Kishida's "new capitalism," the government is encouraging companies capable of raising wages to do so. Incentives such as tax credits for companies that raise wages are also being considered. At the same time, it is not sufficient for our company alone to raise wages. As overseas operations account for about half of our profits, I think we may encounter a structural problem, but certain domestic manufacturers may find it difficult to raise wages immediately due to their business structure. However, we must take the initiative, recognizing that raising wages is not an easy task.