Terumo Corporation
November 8, 2021

Q&A Session at the Financial Results Briefing for the First Half of Fiscal Year Ending March 31, 2022

Outlined below are the Q&As from the financial results briefing on November 4, 2021.

Questioner 1: As for the first question, we have received various comments on the financial results excluding Q2, and it is true that you are doing very well YoY, but in the comparison of Q2 with Q1, there are some things that seem to have peaked out a bit. In aiming for Q3 and Q4, how do you see the situation at hand, especially in terms of the Cardiac & Vascular business?
In other words, I would like to ask you to comment on the feeling of Q1 as the peak out, and Q2 and Q3, in which short term, will there be a slight decline or will there be a recovery, focusing on the Cardiac & Vascular business. This is the first one.

Terumo: Thank you very much.
This is Q2, and certainly compared to Q1, the spread of the Delta variant has affected North America and Europe in particular, where the majority of Cardiac & Vascular cases are located. However, if you look at Q2 as a Group, it is down from Q1. I think it's about a negative 5%. You can see this in TIS. I think the overall figure for Cardiac & Vascular is about 5% negative, but we are looking at it on a monthly basis.
The economy bottomed out in August, picked up in September, and is now recovering, albeit slowly, in October. Looking at the current October sales for Cardiac & Vascular as a whole, they have recovered to a level slightly higher than the average for Q1, so I think it is safe to say that the decline has passed. However, I can tell you that the top line has already returned to the current level, but the margins still declined significantly in Q1 and Q2. That's roughly a 4-percentage-point drop overall.
If you break it down into gross profit and expenses, if I talk about which is larger, the expenses listed under GP are increasing. This is because the restrictions on visiting hospitals have been loosened, and we are now able to do what we originally wanted to do. We also see it as a rather positive thing. Actually, this is more of an impact.
However, as I mentioned earlier, if you look at Q3 as a whole, even though we are currently recovering, in terms of the Cardiac & Vascular Company mix, the ratio of 58% in Q1 has dropped to 55% in Q2, so the company mix has deteriorated due to the decrease in the ratio of high-margin Cardiac & Vascular business. In addition, the ratio of North America, which is a relatively high-margin region, has dropped, and the ratio of Latin America and Asia has increased slightly. This

is what I said in QoQ.
In addition to a slight decline in the regional mix, there is also a shortage of staff, especially in North America, which has been widely talked about, as well as in hospitals. For us manufacturers, we are finding it difficult to hire workers for our factories, and this is also the reason for the increase in costs due to the decline in the utilization rate.
Although we are seeing a recovery in the top line within the pandemic, the increase in transportation costs, the disruption in the supply chain, and the shortage of personnel will still have an impact toward the end of the fiscal year. Some said, especially about the increase in transportation costs, that this freight increase will continue to trend all the way through next year.
As for the labor shortage, especially in the US, the additional unemployment insurance benefits were temporarily terminated in September. Therefore, from a macro perspective, I think that hiring activities will improve a little more than before. However, when we look at it locally, especially in Maryland where we manufacture TIS products, there is a lot of competition for people locally because Gore and Amazon have been built nearby, so it is a bit unpredictable. However, the top line is on a recovery trend. The labor shortage is also expected to improve from a macro perspective.
Also, regarding the expenses, once we look at this Q2 on a standalone basis, the full-year guidance, the target for overall operating income is below 17.5, but I think it will turn around from here as we are now able to conduct our businesses more actively. If we are able to do so, I see that we will be able to manage to catch up with the full-year guidance, margin-wise.

Questioner 1: I understand. Thank you. That's all from me.

Questioner 2: I would like to ask you about your financial results, but since Mr. Sato is here, I would like to ask you about your presentation. On page 5 of your presentation, I think this slide summarizes all of Terumo's greatest characteristics on a single page.
I think that the problem with Japanese medical device companies is that they are too dependent on manufacturing. Sysmex, for example, has acquired International Reagents, Inostics, Partec, and OGT, although I probably shouldn't name names. However, they have not contributed to growth. Olympus Gyrus is also declining, to be honest, and your company is the only one that is mentioned here, 3M, Vascutek, MicroVention, Clinical Supply, which is not mentioned here, which are Angio-Seal, Sequent, and Bolton. Many, but probably not all, of these acquisitions have contributed to your growth.
I would like to ask, what is the difference between your company, Sysmex, and Olympus? I think there was probably a pretty important hint in your earlier comment. I think the bottom line is that the US corporation is very independent, does not need to be remotely controlled, and has all the clinical trials, regulatory affairs, and intellectual property in place to be able to completely absorb an acquisition like this.

In short, I am thinking that if the local subsidiary in the US has not grown up, it cannot be done. I know it is difficult to comment, but where does this difference come from as to why your acquisitions seem to be going well and others not so well? This is the first point.

Terumo: Thank you. I don't feel comfortable talking about it in comparison to other companies. When it comes to acquisitions, we believe that the first choice is important. Acquisitions are a very risky area to begin with, so, to use a baseball analogy, we try not to touch the ball, not to hit it unnecessarily, and not to overreach.
In such a situation, I think it's really a matter of choosing the right opportunity, fulfilling it, and then next time, patiently supporting and developing the prototype. As I always say when we acquire a company, I look at it from the perspective of cultural affinity, compatibility, or managerial manageability.
Since then, we have somehow managed to make it this far by reaching out to each other even in difficult times from that perspective. As you said earlier, I think that when we get to this point, we have the ability to create new businesses autonomously or buy small companies.
This means that we have finally reached a stage where there is much less risk strategically compared to the old days when we did everything from Japan and made them into subsidiaries one by one. This is still a long way off, but that's how I feel.

Questioner 2: You say that this is a characteristic of your company, but could you tell us a little more about why the acquisition went so well? Do you just look at deals and make decisions based on that, or is that all you do?

Terumo: I'd say we're sticking to the basics. It's really not such a big deal, it's just a matter of sticking to the basics, and especially when you acquire a company and leave the subsidiary intact, and then grow it separately, you have to keep your eyes on it for the whole time.
Like American companies, if you integrate them into your own organization, they become yours in a few years, but if you keep them in a separate company like we do, they have a period of rebellion and a period of growth, just like human children. In that sense, I think it is important to take care of each stage properly.

Questioner 2: I understand. Second, the theme of the midterm plan is written on page 9, and I would really like to ask about radial techniques, but I will wait until the midterm plan. Instead, I want to ask about stent grafts.
Since it was just approved in August, I was wondering if I could ask you about how you felt about RelayPro in the US? RelayPro's strength was its Dual Sheath Technology, right? The thoracic aortic aneurysm stent graft has to be placed in a bent arch, so it is important to be precise in how it is placed, and with this technology, it can be placed quite accurately, as I recall. The external

diameter is also much thinner.
In February, Medtronic's Valiant Navion was also recalled, so Cook's Zenith Alpha is probably the main competition for stent grafts right now. It will take time for the various adaptations to come together, so I think full-scale sales will be next year, but how much share of this JPY50 billion market do you think you can capture? I would like to ask you for some hints. This is the last one.

Terumo: The Company President will talk about this in the mid-term plan next month, so I'll be a little reserved about it.
I don't think that we will be able to replace Gore in the medium to long term or the next medium term. However, I think it's fair to say that we would like to reach the level of Cook and Medtronic, as you mentioned. We are also in the process of examining internally how much we can quantitatively return next month.
As for the features, you are right, it is a matter of how well the stent graft can follow the arched part. The approval we got in August was still for the arterial aneurysm, and the applications for dissection are coming now. Once those two things are in place, things will start to unfold in earnest. In the medium to long term, we will have to wait until next month to see how much we can quantitatively recover. Thank you.

Questioner 2: Is it correct to say that Cook and Medtronic have a 10% or 20% share of the market?

Terumo: When it comes to thoracic stent graft market, I'd say that Gore is the largest group, about 30%. I also think that Medtronic and Cook are in the 20% range.

Questioner 2: I apologize for taking so long. Gore doesn't have a product with thin diameter, does it? 22Fr or less.

Terumo: I don't think it would probably be as thin as ours.

Questioner 2: I see. I understand. Thank you very much.

Terumo: Thank you very much.

Questioner 3: Hello. Thank you for your time. Regarding the CSL project, I believe the plan for this fiscal year was for JPY2.5 billion in SG&A expenses. I would like you to share the progress of this and any updates on the regulatory process in this area, even though I think the FDA application is about to be submitted.

Also, since there is quite a shortage of semiconductors, is there a possibility that these new machines, especially for CSL, will be subject to some negative factors in terms of production?

Terumo: Thank you very much. First of all, there's this upfront cost. We have not changed the timeline to start making sales from the first half of the next fiscal year at all. We had planned to incur about JPY2.5 billion in upfront costs in the current fiscal year, but we originally planned to spend more in the second half. This is currently progressing as it should, and we are on schedule for a large amount of this to occur between now and the second half of the fiscal year.
Also, we have had some difficulties with semiconductors over the past few months, but we have managed to make it so that the lack of semiconductors will not hinder our preparations for the equipment.
As I said, we are now preparing both the equipment part and the disposable part, including the start-up of production and QMS (Quality Management System), in order to start recording revenue from the first half of the next fiscal year. We will be using not only in-house production, but also multiple external suppliers, so these members will be working closely with various subcontractors to ensure that we can proceed as planned.
In terms of progress since the last financial results, in Q2, July to September, we completed the submission to the FDA at the end of September. We have now passed a milestone. However, since we are talking about the US, it is going to be the vacation season toward the end of the year, so we will receive the FDA's response before Thanksgiving, the end of this month, and we will be able to proceed with the clearance as scheduled.

Questioner 3: Thank you very much. I would like to ask one more. In terms of the FDA process, is there going to be an advisory committee or something like that this time?

Terumo: I would like the head of the Company to announce the contents of the plan and the status of clearance and how much progress is being made toward that goal when the mid-term plan is announced next month. What I can say now is that we are proceeding smoothly as planned.

Questioner 3: I understand. As I recall, there was a comment at the briefing session 3 months ago that the clinical trial itself was completed several months ahead of the original plan. Is it correct to say that the timing of the FDA application is also slightly ahead of the original plan?

Terumo: Somewhat ahead, or I think we can say that it is almost on schedule.

Questioner 3: I understand. The second question I have is for President Sato. On the slide on page 9 of your presentation, you mentioned some of the drivers in the US market for the next mid-term plan.

I think your gross profit margin is currently around 54% to 55%. Looking at your competitors in the US, their gross margins are in the 60% to 65% range, which is 5 to 10 percentage points higher than yours. Of the several drivers listed on page 9, could you please introduce the product groups that you think will be the biggest drivers to achieve a gross profit margin with your global peers of 60% range?

Terumo: This is generally the case in the US, and not only for the products mentioned here, but also for the products in Terumo's portfolio, which have a relatively higher than average GP. If we can make a positive contribution in this area alone, it will contribute to the improvement of GP.

Questioner 3: As a supplement, if you look at the operating margin, probably in the next 1 to 2 years?

Terumo: If you look at the operating margin, there are many different products. For example, aortic treatment is a product that requires a large amount of SG&A, so you have to see for how the result would be. On the other hand, B2B raw material plasma is such a product that it costs very little in operating profit. Each of them has its own characteristics, but in general, I don't think there are many products in this list that have relatively bad GP.

Questioner 3: I see, I understand. That's all. Thank you.

Questioner 4: Thank you for your explanation. I also have two.
The first one I want to ask is rather short-term of your business, but it is about costs from the current situation to the second half of the year. Transportation costs, labor costs, and of course, inflation, will have an impact on the cost of materials and labor, and in terms of SG&A, logistics costs and labor costs.
I would be grateful if you could explain quantitatively how much of an impact this has had on profits, which have exceeded the plan, in your results up to the second quarter. Also, as we head into the second half of this fiscal year, I am sure that there will be some differences from the plan at the beginning of the fiscal year, so I am wondering if you can help me with some quantitative understanding. This is the first one.

Terumo: The impact on the amount of money is largely influenced by the cost of goods, as you have just explained. I think the level of feeling is in the billion yen level. The biggest part is logistics costs. In terms of logistics costs, the prices in Asia and Europe have risen particularly high, and the impact is expected to be 6 to 10 times higher, which will have an impact of more than billions of yen.
Recently, transportation costs from Asia to the Americas have become more expensive. Normally,

we use ocean freight rates, but as a precautionary measure, we are using air freight, but air freight rates also have been rising recently, so we will take measures in the second half of the fiscal year, taking into consideration the contents.
The price hikes of crude oil and gas are not as large as the logistics costs, but I think that the timing of these price hikes will gradually be delayed and will affect the cost of raw materials. Therefore, in the second half of the fiscal year, the most significant factor will be logistics costs. This is the same situation in the first half of the year. Logistics costs had a major impact. As for raw materials, we have not seen much impact yet.

Questioner 4: Thank you very much. Is it correct to say that the billions of yen means that if you look at it on a yearly basis, compared to what you estimated at the beginning of the fiscal year, the impact will be about that level?

Terumo: Yes.

Questioner 4: I understand. Thank you. Also, I would like to ask you to explain the SG&A ratio for the mid-term, which I think you want us to wait for December. From your explanation, I fully understand that M&A has been successful so far and that there will be many more opportunities in the future. However, as a result, sales have increased and the SG&A ratio has not gone down in the past 5 and 10 years, and the SG&A ratio has always remained flat at around 37% to 38%. Considering the fact that there is still a lot of investment for growth that the president mentioned, I thought that you will continue to build the top line for the next 5 years, and of course, the gross profit margin may increase. While you are building your top line, you are still in a phase where the ratio of SG&A to the Company's capacity to compete on a global scale is not yet at a point where it will drop drastically. If that is not the case, I would like to know about it. That's it for the second question.

Terumo: As you all know, when we expand our business in the US, most of our existing products such as guidewires are not subject to SG&A, so if we increase the number of therapeutic products compared to these products, SG&A will inevitably reach an increasing trend to some extent.
However, even in such a situation, what we are thinking now is that, as I mentioned earlier, we need to manage the cost pressures that are emerging. Therefore, we would like to make great efforts in the direction of selling and managing products more efficiently, as well as reducing head office expenses, et cetera. Since there has been a lot of pressure to do so over the past 5 years, we would like to make great efforts in the direction of reversing this pressure and not increasing it.
This does not mean that we will just sit on our hands and leave SG&A untouched for us to grow; on the contrary, we would like to change the system to one that we can control with a lot of effort.

Questioner 4: I understand. Thank you. That's all.

[END]