Terumo Corporation
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Q&A Session at the Financial Results Briefing for the First Half of FY23

Outlined below are the Q&As from the financial results briefing on November 14, 2023.

Hidemaru Yamaguchi: This is Yamaguchi. I have only one question.

I am wondering if there was a temporary factor that contributed to the large increase in operating profit.

Could you please explain the details of this and whether it was included in the original forecast?

Kenichi Hata, IR Terumo: Maybe you are looking at page seven. This is, let's look at the front of it, there is a waterfall chart for YoY in Q2, right? In Q2, the shape of the market is much better than in Q1, which means that the price increase is having an effect, and although it was pointed out to us in Q1 that the progress of SG&A was very high, the pace of this is also slowing down.

So Q2 was very much better in YoY form compared to Q1, but once you look at the cumulative total for Q2 on page six, the profit margin effect is still negative 7.

Other than that, we are making very good progress compared to the plan for the fiscal year relatively speaking, but this minus 7, just this box, that is the next page, the full-year forecast of 58, and the explanation of whether we will really reach H1 with a minus at the turnaround point now, that was the seventh page.

Now, what you just pointed out is probably in the lower right corner. I am saying that this will happen in Q4 because there was a very large one-time increase in Q4 last year, so if you look at YoY, it will be a major factor in H2 and will be a factor in the increase in profit versus the previous year.

Therefore, if prices are still negative in H1 but will become positive in the future, profits will increase in H2, and since inflation has already reached a high level in H2 of last year, if you look at YoY, it will not be negative anymore. Rather, freight costs and the like will loosen up, which will turn out to be a positive.

In addition, as noted here, we are actively engaged in global bidding for transportation costs, and we are actively consolidating contracts on a global basis to significantly reduce the freight rate. This is both air and sea freight.

The positive effects of these measures will appear in H2 of the fiscal year, so when we look at the YoY results, we can see that the profit improvement measures will make a greater contribution in H2 of the fiscal year than in H1. We are now implementing measures to improve earnings at a rate that will surpass the JPY5.8 billion mark for the full year. So this will be all right and it is what I wanted to say.

It was a bit too long. Sorry.

Yamaguchi: Thank you very much. Sorry for asking a bit of a bad question. Thank you.

On page four, under operating profit, it says double-digit increase due to one-time gains, and there is a significant gap between operating profit and adjusted operating profit, isn't there? The story of what this is.

Hata: Last year, there was a loss on the sale of a business, Harvest, which we bought, which was a loss of about 35, and this year, on the contrary, there was a positive gain of 13 on the sale of OTB shares, so the swing is JPY5 billion or JPY6 billion, which is taken as an adjusted item. So, there is a major twist in the OP and AOP. It means it is twisted in a good way.

Yamaguchi: Thank you. That’s all.

Motoya Kohtani: This is Kohtani of Mizuho Securities.

Only one question, so since President Sato is here, I would like to ask him.

I am very grateful to you for showing us the pipeline of solutions in this presentation, but I wanted to ask you various questions, such as what criteria you used to select the pipeline and why stent grafts were not included, if I narrow it down to one, honestly, the one that surprised me the most was the Japan-US DSS.

The reason for this is that, although the market size in Japan and the US is 80 billion, it is probably overwhelmingly in Japan, while the US has not used IVUS and OCT to a great extent until now, and it is because of, after all, government reimbursements for medical treatment and other such entanglements.

Moreover, the product offered by Boston, a competitor, is more of a combination of IVUS and FFR, another mechanism, so I thought it must be quite strong, but since this is a pillar of growth, why do they come to use IVUS and OFDI in the US as well? I would like to know why the stent grafts is not included as well.

Sato, President and CEO Terumo: As for what we have introduced so far, the fact is that we dare to omit it because it is a restatement. Therefore, since we have limited time, we decided to focus on and introduce only six items, which are as new as possible.

However, Rika continues to be listed because of customers' strong interest in them. In that sense, of course, we count stent grafts and other products as factors that will boost the growth of GS26 and beyond, but this time, we will focus more on the TIS business and introduce a few new items, such as those that you have expressed an interest in as a few new topics.

I would like Hata to fill in some of the details. As for DSS, imaging itself has entered a new phase. As you mentioned, IVUS used to be a uniquely developed market in Japan, and the size of the market was almost entirely larger in Japan. Statistically speaking, the combined size of both markets is about the same, and I believe that we are headed for an era in which the US market will grow more than Japan.

As I mentioned earlier, the importance of intravascular imaging in this treatment, or rather the evaluation of its effectiveness in treatment and long-term performance, is increasing, and we believe that we are finally heading toward an era in which such intravascular imaging will be used in the United States.

Especially, if we add these products this time, we will be starting from scratch, since we have never introduced IVUS or OFDI in the US. We have existing products as well as imaging products, so I believe that we will be able to expand our business in the US. However, since we have not only imaging products but also existing products, we believe that there is a lot of room for growth in the US.

Hata: The growth rate in this slide is actually a bit of a sneaky way of taking it, taking only the US, but Japan, as you know, is already saturated. Conversely, if IVUS is replaced with this product, insurance will be doubled, so in real terms, sales will increase despite the replacement of IVUS. What we are trying to do in Japan and the US is the same product, but the strategy is a little different.

The US is now on par with Japan and will eventually overtake it, so our strategy is to join the market with strong Boston and Philips.

Kohtani: The IVUS has a very beautiful image, and I have seen it used in various live demonstrations. I think there are many people who think that it would be better to have FFR or something like that together, but do you have anything that can compete with that?

Hata: You say Japan and the US, first of all, Japan, and we will replace it here. Since we are here, the US is positioned to enter as well. I understand what you are saying.

Kohtani: I see. Thank you very much.

Takahiro Mori: I am Mori from Nomura Securities. Thank you.

Please go to page eight of Mr. Sato's slide. I think that diabetes management had a very important place in GS26, but now that CGM is gone, how should diabetes be positioned in GS26?

For example, are you going to stop devoting resources here and position it in the same way as CDMO, which I think has an insulin patch here, or are you not giving up on that yet and are you aiming for growth with diabetes? Please tell us about this diabetes and how it is now changing its position in GS26.

That’s all.

Sato: Diabetes, needless to say, is a disease that we will continue to focus on, and it remains an attractive market in terms of market size and growth rate. That doesn’t change for us.

Looking at Terumo's current products, pipeline, and technologies, we have a good lineup of products, so we do not think that we are going to scale back or withdraw from our diabetes business with this CGM decision.

As you just pointed out, however, CDMO and diabetes overlap in some areas, and we will continue to focus on diabetes in the future, including the product lines related to diabetes in the field of CDMO, as we are sure that they will emerge from such areas.

Mori: Hypothetically, for example, GLP-1 is highly effective, and if it were given to healthy people, it would be more effective in preventing heart function, liver, kidneys, and so on. If so, do you think that the global demand for GLP-1 products will increase and that your company will be responsible for CDMO there, or is such a scenario conceivable as a business related to diabetes?

Sato: In our short experience of the past five years, we have seen a continuous battle against new drugs like the one you just mentioned, and new machines have both positive and negative effects. We would like to keep a close watch on the situation and try to use the new machines in both aspects.

Mori: Thank you. That's all.

Tomoko Yoshihara: I'm Yoshihara, UBS Securities. Thank you. Since President Sato has given us so much information, I would really like to ask him a question, but since the number of questions is limited to one, let me ask you about the financial results.

With regard to your results for H1, especially operating profit, whether adjusted or ordinary operating profit, how did it compare to the Company's internal plan? If possible, I would be happy to hear by department.

In addition, on page seven of the first slide, the itemized section on page seven that Mr. Muto explained, is it correct to assume that this was already included in the plan at the beginning of the fiscal year, including the global bidding for transportation costs?

The Company plan for the full year remains unchanged, but the assumed exchange rate has changed considerably. How should we think about it? I would appreciate it if you could reiterate your company's approach, if any, to this kind of foreign exchange assumption when you revise your results.

Hata: First of all, about the last part of your question about foreign exchange assumption, unchanged. Now, to your first question, excluding foreign exchange, progress is on schedule. We had originally anticipated that shipments of CDMOs with higher margins, such as VC Square and CDMOs with higher margins, would be higher in H2 than in H1, as a result of actions to improve earnings, such as price increases. This is as expected. For that, we are about halfway through the progress, which is good.

This is due to the fact that the core part of the business was very strong, such as getting more bids than expected in one quarter at the BCT for blood. So, on the way, by company and segment as you asked, blood is progressing faster than expected.

Cardiac and Vascular is, well, as you can see. Although it looks like a dent because of the impact of some foreign exchange stock, H2 will be fine, and I believe we will be able to achieve 24% and AOP margins for the full year.

As for MCS, the progress is not bad, and it is very good because the price increase will contribute to another margin improvement in H2.

The reason why we did not make an upward revision to the top line, for example, is that the upward movement is almost entirely due to the exchange rate. In our case, in the case of the dollar, if it goes to the bottom, it becomes neutral, so profits, conversely, if you look at it at the end of H1, the effect of the exchange stock rather eats away at the flow and has a negative effect on it.

So, going forward, we are still looking to see if we can enter another round of foreign exchange stock, as the yen has been moving a bit weaker since closing H1. Therefore, we can already see that revenue and profit will be on the rise, but our current stance is that we are not touching them at this time in order to determine the extent of the upward swing.

Instead, most of the top line has shifted due to the exchange rate, so if you look at the sensitivity behind it, you can see how much it has shifted. Together with that, it means that the Company still leaves it.

I hope I answered your question.

Yoshihara: Thank you very much.

As you mentioned earlier about the access bid in China, could you please add any changes in the business environment in H2 that you did not anticipate at the beginning of the period?

Hata: I should have told you by the way now. There are some very good things happening, but one concern is China's VBP. I have heard that China, which is currently suffering from financial difficulties due in part during COVID-19, is trying to raise financial resources by expanding the scope of the VBP at any cost.

Finally, the Henan Province group bidding, and bidding began in September in 20 provinces in all, including Henan Province. The effect will finally begin to appear in September. Since we have a strong share of access to the market, we are trying to minimize the negative impact through lobbying activities and the like.

For the most part, if we follow this assumption, we will be within our original forecast, so there will be no footprint compared to the forecast. This will probably be determined at the next closing of accounts in December, so either way, we will be talking about JPY1

billion or JPY2 billion, and that is one of the reasons why we decided not to revise upward this time.

Yoshihara: Thank you very much.

Ryotaro Hayashi: Thank you very much. I am Hayashi from Morgan Stanley MUFG Securities. I am participating by phone. Since you mention that we are allowed to ask one question, I would like to ask about the impact of the anti-corruption movement in China.

Your explanation says that the impact on revenue was minimal, but is it your understanding that the number of cases has decreased or that there was a negative impact? In this context, how is it that the impact on revenue has been so minimal? Various companies have commented on this point, so I would ask for your company's viewpoint as well.

Hata: Thank you for the question.

Our conclusion is that there is no impact. There was no impact on the top line, and there was little impact on the number of cases. This is what we are hearing from the local staff.

Normally, the number of cases would drop in Q2 because of the summer season, but this has not been the case this time, so the local staff increasingly evaluated that the number of cases didn't drop, thanks to the implementation of the anti-corruption campaign. So, if you look at our top line in China, we were in very good shape.

However, going back to Ms. Yoshihara's question mentioned earlier, the VBP for access will start in December, so we are already experiencing a bit of a holding-off buying right now, so I think Q3 will be a bit lower, but I do not see any impact from anti-corruption.

Hayashi: Thank you. From me, it is simply that one point. Thank you.

Mie Yamazaki: I'm Yamazaki from Mitsubishi UFJ Morgan Stanley Securities. Thank you.

I would like to ask you about the pipeline Mr. President mentioned in his presentation, but from what you have said, I understand that there are several businesses that are likely to start generating sales in the next fiscal year.

In terms of the contribution to revenue here, I would like to confirm whether GS26 will continue to generate such revenue but at a considerable cost or whether a certain scale of revenue and profit can be expected in the next fiscal year and beyond. Thank you.

Sato: I'll let Hata fill in the details, but in general, of course, it includes revenue that comes from GS26, but I still think the overall impact will be Beyond GS26. If we look at the five-year term of Beyond GS26, most of them will catch up properly in terms of revenue, so I think the growth will be balanced in that context.

However, some of them, such as Rika, for example, as we have just informed you, will be ahead in costs for the first few years, so there are some concerns as you mentioned, but on the other hand, DSS and Reveos will continue to grow in a rather balanced manner. I see these and other things as being balanced over the 5-year term.

Hata: If you look at the list, again, areas like B2B with pharmaceutical manufacturers have very large upfront investments, so there is not much contribution to revenue, at least within GS26. I think that would be Beyond GS26.

On the other hand, when sales of conventional devices, such as DSS and BCT Reveos, start to increase, which is during GS26, the effect on margins will begin to appear at the same time, so the lead time for the effect on profit improvement is a mixture of various things.

Yamazaki: Thank you very much.

Shinnosuke Tokumoto: This is Tokumoto from Nikko Securities. Thank you.

As we move toward GS26 and the achievement of the medium-term management plan, you have been explaining various initiatives to improve profitability, and I have been wondering if progress has been made in the current situation. I would be very interested to know if there are any areas where improvements in margins that can be expected during the period of this medium-term plan are ahead of schedule, any other areas where the effects may manifest themselves more than expected, and if there are any responses or shades of gray now that the new medium-term plan has actually been running for a few years.

That is all from me.

Hata: The price increase, which is the centerpiece of this fiscal year, is to rebound from the effects of inflation, which was stronger than expected by GS26, so we are trying to

rebound from it as quickly as possible and will complete 12 billion this fiscal year. This is not the effect of raising prices at this rate every year, YoY, so once this is done, this is an inflation support and we are doing this as a short-term solution.

In order to achieve the 20% OP of GS26, Alzheimer's disease and Rika, which I introduced today, must be launched in earnest. I think it is still possible that the GS26 will be moved up. Although there are signs of this in Rika, I think it is best to look at the GS26 period to be sure.

Tokumoto: Do you have any update on the effects of the Costa Rican production transfer?

Hata: This is also the first year that the reduction effect will finally exceed the cost to close in this fiscal year, so from the following fiscal year onward, only the effect will be seen, so the amount of revenue contribution will certainly increase.

We have a plan to transfer this to Costa Rica in phases one, two, and three, so if you just look at the amount, it will certainly be a stair-step up. We are assuming that this will be the case, but we are not sure if that would be an advance or not.

Tokumoto: I understand. Thank you.

Hata: So, next will be Mr. Yamaguchi, and then Mr. Kohtani.

Yamaguchi: Thank you very much.

As for plasma innovation, you quoted CSL's comments, but of course, some of the work is left to CSL, but how many centers are currently operating? I understand that there are a little over 10 centers. Please update the information if there is any.

Hata: It's 17 now. We will start negotiations on various aspects toward the end of the year, so we will hold off until then, and we may not see much increase during the year.

Yamaguchi: I see. You are going to negotiate whether or not you can go for it around one to three next year, right? Is that something like the start of a ramp-up?

Hata: Yes. The target is to agree on a schedule for that ramp-up by the end of the year.

Yamaguchi: I see. I understand. Thank you. That’s all.

Hata: Now, Mr. Kohtani, please.

Kohtani: I would like to ask about the CDMO pipeline. Maybe this is what you showed us in your mid-term management plan. I have a vague recollection, but I think it mentioned something about cancer or something like that. You didn't write Alzheimer's, of course. Of course, if you write it down, it would be easily discovered since there are only three drugs available.

I would like to ask you, on page four, I think you mentioned that a new overseas contract may or may not be finalized. Was that part of what was indicated in the mid-term plan or is it something new?

Since you mentioned it, I think it will probably be of a certain scale, but I was wondering if you have already entered the US market with this new product, since a biosimilar called Hulio is already being sold in the US. I was wondering if that is what you meant. Or is it correct that the implication you are saying is that the US company will really sign the contract to do it?

Hata: The classification of domestic and overseas is based on whether the pharmaceutical manufacturer is a domestic manufacturer or not. Therefore, even if we are working with a domestic manufacturer and that manufacturer has already released a product in the US, such as Hulio, we categorize it as domestic.

So, this overseas is really the first case that we have longed for with an overseas pharmaceutical manufacturer, and it will be as early as this year. I can't tell you the region yet, but we are still discussing whether or not we will release a press release when the contract is signed, so I really mean an overseas pharmaceutical manufacturer.

Kohtani: On this slide, there is a K-Pack Needle, PLAJEX, and an insulin pump called Medisafe With, but I'm really curious about this device on the far right, which I don't think is commercially available. What is the relation with this?

Hata: This is an image. Sorry, because we have various things, drug delivery devices, and I mean that we will utilize these things and do deals with foreign drug makers, and we don’t mean any of these.

Kohtani: But is my understanding correct that the device on the far right will eventually be released officially? This was developed in Japan, I believe, at one point. I think the development was stopped for a moment.

Hata: I can't even say that this is the case here, but it's all possible, and it's written like this.

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Kohtani: I understand very well. Thank you.

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