November 6, 2019

Lion Corporation

Analyst Q&A (Summary)

Nine Months Ended September 30, 2019

Business Performance

Q: To what extent did the pre-tax hike demand surge in Japan affect net sales for the third-quarter, and how did it compare with your expectations?

A: Other factors, such as the introduction of new products, also played a role, so we cannot give an exact figure, but of the ¥7.0 billion year-on-year increase in sales in the Consumer Products business, we estimate that 70%–80% was due to the pre-tax hike demand surge. The surge was slightly smaller than expected.

Q: Have distribution inventories increased in response to the demand surge?

A: We are not aware of an excess in distribution inventories. Shipments from Lion to wholesalers and from wholesalers to retailers since the start of October have not seen greater than expected decreases, either.

Q: What do you expect in terms of recoil from the demand surge?

A: The demand surge before the tax hike in 2014 amounted to approximately ¥13.0 billion (JGAAP). Together with the recoil afterward, on a six-month basis, the net effect on sales was approximately a positive mid-¥2.0 to ¥3.0 billion range. We expect a similar net positive this time.

Q: In the first nine months, how did core operating income compare to your plan? If the demand surge was less than expected, was income, as well?

A: Core operating income for the first nine months reached approximately 75% of our forecast for the full year. While the demand surge was a factor, we regard this progress as within the range of our expectations.

Q: Even though the pre-tax hike demand surge was lower than expected and the business environment in South Korea worsened, income was still on track toward the full-year plan. What made up the difference?

A: Such decreases were absorbed by cost reduction measures and a review of our overall balancing of expenses.

Q: What has caused the decrease in selling, general and administrative expenses, especially marketing expenses? Do you expect these reductions to last?

A: Overall selling, general and administrative expenses have been decreasing due to efforts to increase cost efficiency. Advertising expenses decreased in the third quarter, from July to September, but point-of-sale promotional expenses were increased in light of the pre-tax hike demand surge, leading to an increase in promotional expenses deducted from net sales (a decrease in gross profit).

Q: In the first nine months, approximately how much of net sales was attributable to overseas visitors to Japan?

A: We estimate the figure for the first nine months at just below ¥4.0 billion. We expect it to be around ¥5.0 billion for the full year.

Q: While sales attributable to overseas visitors continued to decline in the first nine months, sales of pharmaceutical products (in which sales to overseas visitors represent a large portion of the total) saw a significantly narrower decline than in the first half and were largely unchanged year-on-year in the third-quarter. I imagine the acquisition of dermatologic agent brands FERZEA and Encron from Shiseido Pharmaceuticals had some effect, but could you tell us more about why this was?

A: Net sales of pharmaceutical products in the first nine months decreased 9.7% year on year. However, excluding the impact of the sale of the insecticide business at the end of last year, net sales decreased only 2.3%, and if just third quarter results are considered, net sales increased 6%. This was due to the pre-tax hike demand surge, the introduction of new products in eye drops, and the acquisition of the FERZEA and Encron brands in August.

Q: The Consumer Products business seems to have a long way to go to in the fourth quarter to meet its annual target. How will you increase sales?

A: To achieve the revised forecast of ¥223.5 billion for the Consumer Products business announced in August, we will need to realize year-on-year sales growth of 1.8% in the fourth quarter. Augmenting the lineup of strong selling new products introduced in the third quarter, we will introduce a number of new products in the fourth quarter, and we expect their performance to be steady.

Q: Has there been any change to the revised forecast for the year-on-year change in annual core operating income published in August?

A: Performance may vary slightly due to changes in the sales mix and fluctuations in raw materials and competition-related expenses, but for the most part we do not expect any major change.

Overseas Business

Q: How were net sales in Lion's four key overseas countries (Thailand, Malaysia, South Korea and China) on a local currency basis?

A: We do not disclose concrete numbers by country. However, sales in Thailand saw a slight increase in the first nine months. Sales in Malaysia saw growth in excess of GDP growth in the first half but then decreased year on year in the third quarter due to recoil from special demand related to local tax reforms implemented last year, resulting in a small year-on-year decrease for the first nine months. South Korea, due in part to the worsening business environment from July onward, sales saw a single-digit decrease across the first nine months. In China, sales growth remains at over 20%.

Q : How much of the ¥2.3 billion year-on-year decrease in the third-quarter net sales in the Overseas segment was due to the results in South Korea?

A : We do not disclose specific figures, but it is quite a large portion of the decrease.

Q : Did third-quarter net sales in South Korea see a double-digit decline?

A : Yes, the third quarter decline was well into the double digits. Our products were not the direct targets of boycotts, but point-of-sale promotions and the introduction of new products were greatly affected.

Q : When do you expect performance in South Korea to bottom out? Do you expect declines to end in the fourth quarter, or will they continue into next year?

A : While our information on the ground indicates that there are signs of improvement, the timing of when performance will bottom out or when it will begin to recover is still in flux.

Q : Was the impact of performance in South Korea a major factor in the decrease in profit in the Overseas business in the third quarter? How do you regard the margins of the Overseas business?

A : The third-quarter core operating income ratio in the Overseas business was 7.6%, down 0.6 of a percentage point year on year. This was due to decreases in sales in South Korea and Malaysia. The ratio for the first nine months was 7.3%, an improvement of 0.8 of a percentage point. Due to such factors as cost reductions for home care products, sales growth in China and growth in the percentage of sales accounted for by personal care, the profit ratio of the segment as a whole continues to improve.