NIHON KOHDEN

Second Quarter FY2022 Financial Results Conference Call
Main Questions and Answers
(November 11, 2022, Tokyo)

Q1: I would like to know the impact on your business of product supply issues due to the shortage of semiconductors in the 1st half of FY2022. Many companies expect to mitigate the impact in the 2nd half of FY2022. How do you see the impact on your business in the 2nd half of FY2022?

A1: We took account of negative impacts of around 4 billion yen on sales and 2 billion yen on operating income, based on the assumption that the product supply issues will continue until the end of the 1st half of FY2022. In the 1st half of FY2022, we estimate that the loss of business opportunities in Asia & Other, Europe, and Latin America amounted to around 1.5 billion yen and the negative impact of delays in supplying new models of mid-range bedside monitors in the U.S. was around 2.5 billion yen. Although the impact of the shortage of semiconductors is reducing, medical equipment companies continue to face difficulty in procuring some parts because of the high-mix low-volume nature of medical equipment production. To minimize the impact on our production and supply, we have continued to increase inventories of finished goods and parts since FY2021. We expect that a risk of delays in supplying some products remains in the 2nd half of FY2022.

Q2: I would like to know the impact on your business of higher prices of components and utility costs in the 1st half and the 2nd half of FY2022, respectively. When do you expect this risk to mitigate?

A2: A negative impact of around 1.5 billion yen on gross profit margin is factored in, based on the assumption that higher prices of components and utility costs will continue until the end of FY2022. In the 1st half of FY2022, higher prices of components had a negative impact of around 0.6 billion yen. We expect this impact to be larger in the 2nd half of FY2022, because we used inventory parts in the 1st half and our sales are highly concentrated in the 2nd half. The impact of component price rises by suppliers is expected to continue, while the impact of components procured at temporarily high prices will be mitigated by inventory digestion in the mid-to long-term.

Q3: I would like to know the reason that the full-year domestic sales forecast has been revised upward by 4.5 billion yen. For which products did sales exceed your expectations? Why did sales of hematology analyzers increase favorably?

A3: Based on the results for the 1st half of FY2022 and recent performance trends, the Company revised upward its FY2022 full-year forecasts. In Japan, sales of Physiological Measuring Equipment such as EEGs and polygraphs for cath lab, and hematology instruments were higher than expected. Sales of installation and maintenance services for medical devices also increased favorably. In addition, we had not incorporated around 1.3 billion yen of COVID-19-related demand in the original forecast for FY2022. Sales of hematology analyzers increased favorably, because opening new clinics, which was put off due to the COVID-19 pandemic, has resumed. MD Linkage, a medical device remote monitoring system for hematology analyzers which provides a value-added service by utilizing IoT, has been well received by many medical institutions.

Q4: What is the outlook for your business environment in 2023? I would like to know the outlook for capital expenditure by medical institutions especially in Japan and the U.S.

A4: In Japan, there have been moves to expand ORs/ICUs and establish HCUs, because new evaluation items for acute care and intensive care have been added in the revision of medical service fees in April 2022. We expect this move to be an opportunity for us to promote our solution proposals. Internationally, there have been moves in each country to strengthen the functioning of their healthcare systems in preparation for the post-pandemic situation. In the U.S., although the risk of supply delays remains, demand for medical devices will also remain steady due to efforts to further strengthen the functioning of the healthcare system. The reactionary decline of COVID-19-related demand has been smaller than our expectation and demand for non-COVID-19-related medical devices has shown a recovery trend. We believe that we have strengthened our business foundation, because the installed base and new customer base of patient monitors and ventilators have expanded due to the COVID-19 pandemic.

Q5: I understand that you are focusing on the U.S. and emerging markets in the mid-to long-term. Would you explain the purpose and the background behind your acquisition of Software Team Srl in Italy?

A5: Both the Company and Software Team reached an agreement on this transaction, because there is a high affinity between the Company’s DHS vision and Software Team’s software. This was also because the Company expects to expand its share of the patient monitoring market, especially in Europe, where demand for digital healthcare is growing. Software Team and Nihon Kohden Europe have had a sales partnership in the European market. This acquisition was promoted by Nihon Kohden Europe and the R&D departments in head office. There is no change in the policy of focusing on the U.S. and emerging markets, which are our key growth drivers in the mid-to long-term.

Q6: Could you explain more details about your syringe pump control software for assisting total intravenous anesthesia? Do you have any competitors and any plans to launch it overseas?

A6: This software can administer a controlled dose of anesthetics using the patient’s vital signs acquired by patient monitors as a guide. We are very excited that this software will contribute to improving medical safety and operational efficiency during surgery. This software covers intravenous anesthetic injected with a syringe pump, but we hope to make additional contributions to the field of anesthesia through further research and development. We will consider overseas deployment after conducting clinical research and establishing the evidence in Japan. We heard that there was an overseas company which developed a system based on a similar concept in the past, but it did not achieve widespread use.

Q7: The in-house sales ratio has continued to be higher than the pre-pandemic level. Do you think that you can keep this level in the future? Do you have any room to further reduce the proportion of third-party products with the aim of improving gross profit margin?

A7: Both in-house sales ratio and gross profit margin has continued at a higher level due to the focus on selling in-house products in Japan and higher overseas sales ratio. One of the basic policies in our Three-year Business Plan is to improve the profitability of existing businesses. We are making steady progress in transformation to a highly profitable structure that can regularly secure a gross profit margin of 50% or more and an operating income margin of 10% or more. In Japan, we focus on selling in-house products and restrain sales of locally purchased products. However, we do not restrain sales of purchased products, because synergistic effects are expected between in-house products and purchased products. To realize our Long-term Vision, we aim to transform our business model from a seller of equipment to a solution provider that helps solve medical issues. We also aim to realize a value creation model that creates value from data. We will further improve profitability by expanding our service business and Software as a Medical Device (SaMD).

Q8: Why will operating income margin improve in the 2nd half compared to the 1st half? Will the cost per unit be lower in the 2nd half than in the 1st half?

A8: Our operating income margin tends to be higher in the 2nd half, because sales are highly concentrated in the 2nd half. Cost per unit also tends to be lower in the 2nd half, because fixed costs such as personnel expenses account for a large percentage of SG&A expenses and sales per employee is higher in the 2nd half.

(End)

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