NIHON KOHDEN

Second Quarter FY2017 Financial Results Conference Call
Main Question and Answers
(November 9, 2017)

Q1: I would like to know the reason why both sales and profits in the 1st half missed the Company's forecast. Gross profit margin continues to decline every year. I suppose this is because of the unfavorable sales mix of purchased products in the Company's domestic business. Are there any measures being taken to improve the gross profit margin?

A1: Overall sales fell short of the forecast by ¥1.35 billion, roughly half in domestic and half in overseas sales. As for profits, SG&A expenses were in line with our budgets, but the cost to sales ratio of purchased products increased in domestic business. It is one of reasons why the overall cost to sales ratio has risen. One major initiative to improve the gross profit margin is to expand sales of in-house products such as patient monitors. We also aim to improve the gross profit margin of purchased products by introducing high value-added products with exclusive distribution rights. That is why we changed a supplier of warming systems this time.

Q2: LAVITA and Prime Partner are unusual for Nihon Kohden as they are monthly-fee services. What kind of action do you need to take to expand them into the clinic market and how much contribution do you expect from them?

A2: As has been discussed in the revision of medical treatment fees, the government is promoting home care. Along with this, a support structure and infrastructure for home care utilizing ICT will be necessary. Both systems are a new type of business for the Company, but we aim to contribute to the development of home care in this aging society by introducing these systems ahead of competitors. The selling style required is different from the conventional one and the sales contribution of these systems will be small at first, but we aim to expand sales of in-house products by increasing the number of medical devices which can be connected to these systems.

Q3: You explained that cost reduction could not offset the impact of lower selling prices. Please provide the details about falling prices. I would also like to know the reason for the lower gross profit margin despite the increase of overseas sales and consumables which seem to have high gross margins.

A3: As for the changes to selling prices, in addition to the changes in the gross profit margin of purchased products, there was the impact of lower prices required to win orders in some large deals overseas and some information system deals in Japan. Another reason for the lower gross profit margin is increased outsourcing fees for delivery and installation in line with sales growth in the U.S. We recorded the outsourcing costs as sales cost.

Q4: I suppose that the outsourcing fees will rise as the sales in the U.S increase. How do you plan to fix this issue in the 2nd half of this fiscal year? Please also provide details about the support from Headquarters.

A4: Sales in the U.S have grown considerably and installations of patient monitoring systems have become large-scale. Until now, we have dealt with this by increasing the number of service staff, but we were forced to use outsourcing to meet the deadlines this time. We did not have enough staff available. We will strengthen our business negotiation management, scheduling for delivery and delivery structure in the 2nd half of this fiscal year in order to restrict outsourcing fees. We will also send service staff from Headquarters to deal with network construction.

Q5: Despite the number of new products which received CFDA approval, sales in China seemed to be a little bit lower than the Company's expectations. Would you explain the reason and the measures that you plan to take in response from the 2nd half of this fiscal year onward?

A5: Our business in China is on a recovery trend compared to the past few years. Neurology business has been growing as a top brand and sales of defibrillators have been increasing due to the launch of new products. On the other hand, the launch of a new patient monitor did not have a big impact in the 1st half of this fiscal year. Our patient monitor business was sluggish due to the competition with Chinese makers, but orders are increasing thanks to new products. Sales growth in China will accelerate if our patient monitor business grows.

Q6: You explained that you will revise your personnel plan. Are you going to revise the domestic plan or the overseas plan? Do you also intend to change the personnel plans for the next fiscal year and beyond?

A6: We planned to add 250 new employees in our initial forecast, but we revised this figure downward to 150, based on the results of the 1st half of this fiscal year. In the 1st half, the addition of new employees was mainly in Japan as we hired new graduates. In the 2nd half, we will restrict employment in Japan and accelerate hiring overseas. There is no change to the personnel plan for the next fiscal year. In the mid-term business plan, we aim to grow domestic business by an annual average of about 3% and international business by 10%. We will increase staff members in accordance with these targets.

Q7: Will you receive monthly fees from each clinic and nursing care facility which installs LAVITA? Can it be only connected with your products or is it compatible with other makers' products?

A7: LAVITA is a system for clinics which provide home-visit medical care. We will approach not only each clinic but also each local medical association. We will receive fees from clinics or nursing care facilities which use the system. This system uses general communication protocols such as NFC and Bluetooth, so it can be connected with other makers' products.

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