NIHON KOHDEN

Third Quarter FY2017 Financial Results Conference Call
Main Question and Answers
(February 5, 2018, Tokyo)

Q1: I would like to know the reason for the strong domestic sales in the 3rd quarter (three months). Please quantify the contribution of actual demand, if possible.

A1: There are several reasons for strong domestic sales. First, the increase is in comparison with the weak performance in the same quarter of FY2016. Second, hospitals have started to renew equipment which was introduced with the government fund for regional medical care revival plan. Third, large orders are usually concentrated in the fourth quarter, but some of them were advanced into the 3rd quarter this year. The number of hospitals who required deliveries during the New Year's holiday increased as they wanted to avoid the busy April period due to the revision of medical treatment fees. It is difficult to clarify the actual demand, but university hospitals and public hospitals have restrained capex for the past few years. We feel they are now beginning to renew equipment.

Q2: You said that domestic sales grew higher than expected in the 3rd quarter. Which market was stronger than your expectation? Besides, what is your outlook for demand in the private hospital market?

A2: Sales in all markets increased favorably, especially in the university and public hospital market. In the private hospital market and the clinic market, the reorganization of sales operations we conducted in April 2016 continues to have a positive effect. Because private hospitals make quick decisions on capital investment, if there is a positive trend in purchasing equipment to prepare for the medical treatment fees revision, it will happen in the private hospital market in March.

Q3: SG&A expenses including R&D costs seem to exceed the budget. I think the Company is unlikely to meet its full-year operating income target of 15 billion yen. What is the probability of achieving it? Besides, will R&D costs continue to increase considerably in the next fiscal year and beyond?

A3: Although R&D costs exceed the budget, we are restraining personnel cost, expenses, and depreciation. Total SG&A expenses remain within the forecast. Therefore, if we can achieve the sales forecast, we will also be able to achieve the operating income forecast. Because the middle-end bedside monitors which we plan to launch in this fiscal year are some of our main products, development investment of them was greater than expected. At this moment, we think the increase of R&D costs will be smaller in the next fiscal year than this fiscal year. We are working on our plan for the next fiscal year and cannot make any statement about the details at this time.

Q4: Gross profit margin in the 3rd quarter (three months) was 49.1% compared to 49.4% in the same quarter of FY2016. Can you comment on this number? What is your outlook for the 4th quarter gross profit margin?

A4: In the 3rd quarter (three months), the reason for the lower gross profit margin is the increase of large orders combining in-house products and purchased products in the university and public hospital market in Japan. On the other hand, negative impact of outsourcing fees was minor in the 3rd quarter (three months) because it was possible to handle the installation work of patient monitors with internal resources in the U.S. We expect the gross profit margin in the 4th quarter to improve from 45.9% in the same quarter last year, but it would be difficult to achieve a full year gross profit margin of 48.0%.

Q5: You explained that the launch of the middle-end bedside monitors is delayed. Could it have an impact on the 4th quarter sales?

A5: The launch of middle-end bedside monitors will be delayed by a month to the end of February or early March. We expect these new products to fully contribute to sales from April, but the impact of the delay on the 4th quarter sales would be small.

Q6: My understanding is that outsourcing fees in the U.S. will not incur in future because the headquarters continue to send staff to support installation work. Is that right?

A6: As sales in the U.S. are also concentrated in March, support from the headquarters may not be enough and we may need to use outsourcing. We would like to increase the number of service staff in the U.S. subsidiary and strengthen the scheduling management in the next fiscal year. Ideally, they should install products by themselves, without support from headquarters or outsourcing.

Q7: I was wondering if you could give us a sense of the domestic sales growth and outlook for each market in the next fiscal year.

A7: In the mid-term business plan which we started in this fiscal year, our target of domestic sales growth is from 2 to 3%. We would like to aim to grow sales in this range in the next fiscal year too, but first we have to see the result for this fiscal year and the contents of the medical treatment fees revision. We would like to increase our sales in the private hospital and clinic market by strengthening sales activities which are tailored to each market. Besides, replacement demand has finally appeared among university hospitals and public hospitals, so we expect sales to grow steadily from now on. The outlook in each market doesn't seem to be so bad. We are working on our plan for the next fiscal year and cannot make any statement about the details at this time.

(End)