Message from Director Responsible for Accounting (Chief Administrative Officer)

Review of the Second Year of the Three-year Business Plan, BEACON 2030 Phase II



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In FY2025, the second year of BEACON 2030 Phase II, Nihon Kohden steadily implemented various measures to strengthen its earnings base amid significant changes in the business environment both in Japan and internationally. In Japan, we concentrated on enhancing sales activities which match each market: the acute care hospital market, the small and mid-sized hospital market, and the clinic market. We also focused on strengthening our marketing and service capabilities, creating value which contributed to improving medical safety, patient outcomes, and operating efficiency. While we focused on our consumables and services business, domestic sales decreased by 0.6% from FY2024 due to restraining sales of locally purchased products and lower sales of Abbott products. Internationally, sales in all regions performed favorably, increasing by 13.1% from FY2024. Even excluding the currency effect and the impact of the consolidation of Ad-Tech, the business maintained its underlying growth. In terms of profitability, although higher sales, appropriate pricing, and an improved product mix contributed positively, COGS including the impact of tariffs increased and SG&A expenses also increased due to wage increases, expanded R&D investments, and higher depreciation caused by M&A and capital investments. As a result, operating income decreased 9.5% over FY2024 to ¥18.7 billion, with an operating margin of 8.0% and ROE of 8.1%. In addition, the cash conversion cycle was 215 days, an improvement over FY2024, but did not reach the target of 190 days. Based on these results, we recognize accelerating sales growth, further improving profitability, and enhancing capital efficiency as key issues. Going forward, we will further strengthen our efforts to achieve the Three-year Business Plan by enhancing the profitability of our domestic business while capturing overseas growth opportunities, and by ensuring that management focused on capital efficiency.

Three-year Business Plan, BEACON 2030 Phase II

Based on issues from the previous Three-year Business Plan, we have set three indicators and are implementing six key measures. We aim to achieve each target: a sales CAGR of 5% for "Growth," an operating margin of 15% for "Profitability," and ROE of 12% for "Capital efficiency." To achieve these numerical targets, we implement six key measures, including "Implement the reform of the profit structure," "Introduce Nihon Kohden's own ROIC formula," and "Reduce cash conversion cycle."

1. Implement the Reform of the Profit Structure

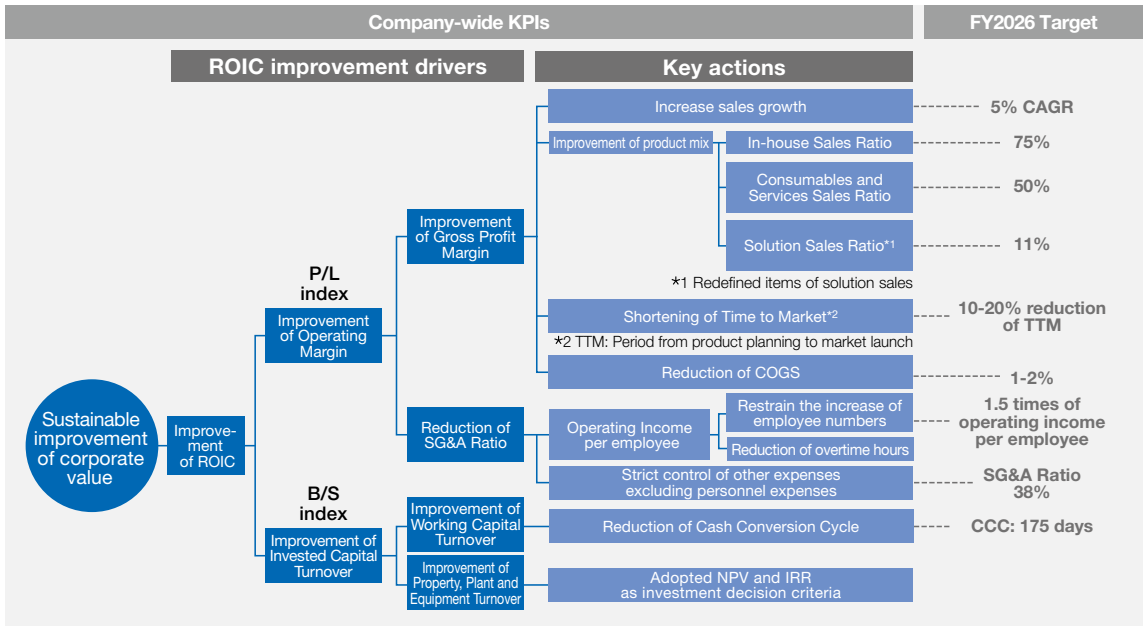
In implementing the reform of the profit structure, we have set a target of improving the operating margin by a total of 5%pt through three pillars: product mix improvement, productivity enhancement, and supply chain optimization (approximately 2%pt, 2%pt, and 1%pt, respectively). In FY2025, we steadily implemented the measures and realized an approximately 3%pt improvement. We currently estimate that approximately 90% of the final target will be realized. In the area of the product mix, we improved gross margin through a shift toward a more profitable product portfolio resulting from strategic reviews of our pricing policies both in Japan and internationally and optimization of the product line-up. In terms of productivity, we achieved operational efficiencies equivalent to approximately 1.99 million hours per year by accelerating the use of digital technologies, including installing generative AI (approximately 2,000 licenses). This enabled us to reduce headcount increases and overtime hours, helping establish a foundation for sustainable productivity improvement. In the area of the supply chain, we steadily reduce the costs of goods sold by further refining the price negotiation process with suppliers and strengthening value engineering in response to the inflationary environment. Going forward, we will further strengthen our earnings capacity through the enhancement and establishment of these measures to achieve sustainable profit growth.

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2. Introduce Nihon Kohden's Own ROIC Formula

To maximize corporate value and shareholder value by achieving the cost of capital-conscious management, we have set Return on Equity (ROE) as a key management indicator and are working to penetrate Nihon Kohden's own Return on Invested Capital (ROIC) formula. Under the Three-year Business Plan, BEACON 2030 Phase II, while positioning it as a phase for accelerating growth investments, we have set improving capital efficiency as a key management theme and aim to achieve both ROIC and ROE of 12%, exceeding our cost of capital. We currently estimate that our cost of capital is around 8%, which is reviewed every year. We have adopted Net Present Value (NPV) and Internal Rate of Return (IRR) as investment decision criteria since FY2022. We set an IRR of 12%, which exceeds our cost of capital, as the benchmark for investment approval. The Board of Directors regularly verifies the progress and results of investment projects above a certain scale to ensure the effectiveness of investment discipline. We are also continuously working to improve ROIC by optimizing capital allocation through improving working capital efficiency, selecting investment projects and managing their execution, and enhancing shareholder returns. Going forward, we will start full-scale calculation and management of Nihon Kohden's ROIC in each subsidiary and accelerate the penetration of ROIC in the entire Group by creating an ROIC indicator dashboard to establish a consistent framework for indicator management from management to frontline operations.

Planned to set KPIs in each subsidiary/division to penetrate Nihon Kohden's ROIC



3. Reduce Cash Conversion Cycle

To reduce the cash conversion cycle (CCC), we have enhanced inventory control and refined supply and demand management mainly at the Production Operations, which was newly established in April 2024. In FY2025, the CCC was 215 days compared to the target of 190 days, as we strategically increased inventories in preparation for the start of operations of PLM/MES* systems and the Tsurugashima Production Center. In FY2026, we will prioritize ensuring a stable supply and secure a certain level of inventory of parts and components, in light of changes in the external environment, including shortages of memory components, higher oil prices, and increasing uncertainty in the procurement environment for parts and components caused by conflicts in the Middle East. From the perspective of improving capital efficiency, we will work to normalize the CCC by continuing to implement measures, including improving inventory turnover and accelerating receivables collection. Inventory control will be enhanced through improved demand forecast accuracy, enabling a better balance between supply and demand. Through these measures, we aim to restore CCC to 195 days by the end of FY2026. Going forward, we will continue to strengthen our sustainable cash generation capability by enhancing working capital management while pursuing the optimal balance between stable supply and capital efficiency.

* PLM: Product Life-cycle Management, MES: Manufacturing Execution System.

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Capital Policy

Nihon Kohden recognizes that the sustainable enhancement of shareholder value is one of management's important tasks and promotes optimal capital allocation under a disciplined capital policy. In distributing profits and dividends, we place emphasis on balancing investments for future business expansion with shareholder returns while securing a sound financial foundation. Specifically, we give top priority in capital allocation to i) investment necessary for future business expansion used in R&D investments, capital investments, M&A or alliances, and development of human resources, and ii) the enhancement of shareholder returns.

Our basic policy on shareholder returns is a consolidated total return ratio of 35% or more. We place emphasis on continuing to increase dividends in a stable manner in line with growth in business performance. Share buybacks are conducted in a flexible manner, taking into account comprehensively our business strategy, investment plans, financial position, and stock price level. Based on these policies, we acquired ¥5 billion of own shares, and the consolidated total return ratio was 70% in FY2025. Going forward, we aim to maximize mid- to long-term shareholder value by enhancing both corporate value through growth investments and shareholder returns.

Cash Allocation Policy

In BEACON 2030 Phase II, we expect to generate cumulative operating cash flow of ¥80 billion or more, which will serve as the source of funding for the optimal allocation between growth investments and shareholder returns. Growth investment including M&A is planned to be ¥30 billion or more, and we ensure that investment decisions place emphasis on capital efficiency. Specifically, we have adopted Net Present Value (NPV) and Internal Rate of Return (IRR) as investment evaluation indicators since FY2022 and set an IRR of 12%, which exceeds our cost of capital, as the investment criteria. Under these policies, we further strengthen our growth foundation by steadily executing investments in areas that are expected to generate synergies with existing businesses, including the consolidation of Ad-Tech as a subsidiary, which has a high affinity with the neurology area, and the consolidation of DOWELL Co., Ltd. as a subsidiary in FY2025. Capital investments are planned to be approximately ¥25 billion. Along with the commencement of operations at the Tsurugashima Production Center, we are enhancing productivity and advancing corporate DX through the implementation and operation of PLM/MES systems. We expect shareholder returns of ¥28 billion or more over three years and will flexibly consider additional shareholder return measures, taking into account the progress of our future investment plans and financial position. By ensuring the execution of growth investments under disciplined investment criteria while optimizing the balance between growth investments and shareholder returns, we aim to improve capital efficiency and maximize mid- to long-term corporate value.

Resilience & Sustainability

The outlook for the business environment surrounding the Nihon Kohden Group remains uncertain due to escalating global protectionism and fragmentation as well as heightened and prolonged uncertainty caused by the impact of geopolitical risks and of policy trends in each country. In Japan, business sentiment in medical institutions remains weak and an increasing number of medical institutions have seen a deterioration in ordinary income due to price and labor cost inflation, while medical institutions strive to implement task shifting and improve their operational efficiency. Internationally, business operations continue to face elevated risks due to tighter regulations and changes in economic conditions in each country. In addition, as improvements in the quality and efficiency of medical care are increasingly required, responding to medical digital transformation, which includes data health, telemedicine, and utilization of AI and ICT, has become essential. In this external environment, establishing robust business and financial foundations that support the stable supply of medical equipment—in other words, strengthening our resilience—is essential for us to achieve sustainable growth. In particular, we will enhance our resilience to changes in the environment by stabilizing the supply chain, strengthening our earnings structure, and advancing our operations through the use of digital technologies. Building on this, we will steadily execute strategic investments for future growth while positioning the enhancement of shareholder returns as an important management policy and pursuing the optimal balance between growth investments and shareholder returns. In addition, we place sustainability management at the core of our corporate value creation, striving to achieve both business growth and the resolution of social issues through healthcare. Even as the external environment remains challenging, we will strengthen our resilience and build a foundation for sustainable growth in an integrated manner. To meet the expectations of all stakeholders, our executives and employees will unite and commit fully to these efforts. We appreciate your continued support.