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March 8, 2021
DyDo Group Holdings, Inc.

Questions and Answers at Financial Results Briefing

Analyst: I have two questions.

My first question is simple. I'd like to ask about your top-line forecast for the Beverage business in FY2021, in which you forecast growth of 5.9%. Please tell me how you view the assumptions underlying this market. Also, please tell me how you view the assumptions underlying the market by sales channel, especially the vending machine sales channel. Based on that premise, please tell me who you expect DyDo will outperform or underperform the rest of the market.

Second, I'd like to ask about the factors behind the change in operating profit in FY2021 shown on page 30. It says here that smart operations and vending-machine related expenses will be a factor that pushes down profit. I'd like to know how these costs will be in FY2022. I know it's a little early to ask this, but I'd like to know if you think these costs will decline, be maintained, or increase even further. Please tell me your views on vending machine-related operations costs in the next fiscal year onward. That's all.

Takamatsu(President and Representative Director): Thank you. First, I'll answer your question regarding our outlook on the Domestic Beverage business in the current fiscal year. In the industry as a whole, we expect a bounce back from the COVID-19 impact last year. We don't think it will return to the same as before, but for the industry as a whole, we expect an increase of around 2% year on year.

In comparison with that number, we target an increase of 6%, partly reflecting the fact that the impact of COVID-19 last year was relatively modest compared to competitors. That said, we expect a substantially higher sales growth than the growth rate of the overall industry.

By channel, we assume a level roughly on par with the previous year for the distribution channel. Our forecast of 6% growth is an overall growth of 6%, including both distribution and vending machine channels. The biggest point is that we expect an increase of 6% in the vending machine channel.

As for the breakdown of this 6% growth, one of the factors is the effect of an increase in the number of vending machine units in operations. The other factor is the increase in per-machine sales. You can think of this as contributing to roughly half of the increase. As for the increase in per-machine sales, the trend from the past was that sales gradually declined every year even without the impact of COVID-19. However, due to the sharp decline last year owing to COVID-19, we expect a recovery led by the bounce-back from a low year-earlier figure. In addition, we aim for additional contributions from a recovery in per-machine sales at existing vending machines. Further, we consider the impact of an increase in the number of vending machine units in operations compared to the number of units last year. In total, we expect the sales growth to be 6%.

Hasegawa (Corporate Officer, General Manager of Corporate Communication Department): I believe your question was about the smart operation-related expenses that will increase in the current fiscal year, and how those expenses will change in the next fiscal year. As shown on page 30, there is a part that says vending machine-related smart operations, which represent the expenses involved in the attachment of communication equipment. We will complete the majority of installation for direct sales during the current fiscal year. However, the costs associated with Kyoeikai to be incurred in the future are still undecided. In a sense, the increase in costs will peak this year. Stated differently, there is room for costs to decline in the next fiscal year.

On the other hand, the item in which costs are likely to slightly increase further in the next fiscal year onward is depreciation. These costs are associated with the effect of the accounting treatment on the current fiscal year. In the previous fiscal year, we made a change to how the useful life of vending machines is calculated, so costs will bounce back up as that impact drops out. As for the current fiscal year, we expect an increase of JPY600 million. We expect these costs to increase each year by around JPY500 million to JPY600 million from the next fiscal year onward until returning to the original level.

Analyst: Excuse me, Mr. Hasegawa. This may only be a problem that I'm experiencing, but I could barely hear what you said.

Did you say that the smart operation cost, which is the foremost factor, will run its course in the current fiscal year? I also couldn't hear the part about depreciation expenses very well, either. I'm sorry.

Hasegawa: Sorry. The smart operation expenses of JPY539 million are the fees for the attachment of equipment, so we expect these expenses to decline from the next fiscal year onward.

Analyst: So, they will disappear in the next fiscal year onward?

Hasegawa: They will decrease. There are still some vending machines that will require the attachment of equipment in the next fiscal year, so please consider that these costs will decrease. In contrast, please understand that depreciation expenses will continue to increase in the next fiscal year. The increase is attributable to the impact of an accounting treatment related to a change in the number of useful years. Although there is a trend of profit growth in the current fiscal year, please understand that depreciation expenses will increase from the next fiscal year onward because of factors where these expenses will increase each year until returning to their original levels.

Analyst: I see. In that case, when completing the smart operation in the next fiscal year onward and operating at full capacity, what kind of costs do you think will decline?

Hasegawa: The ultimate issue or key that will have the foremost impact is how we deal with the personnel structure involved in operations. To a certain extent, there will be a decrease in personnel expenses due to a natural decrease, and there will also be reassignments in job type. We intend to reassign personnel to jobs aimed at growing the top line to bolster sales, and this will ultimately lead to an improvement in profits.

Analyst: I see. As for other expenses, you mentioned that the company would increase the number of units going forward. Do you expect other expenses to continue to increase at around this pace?

Hasegawa: We expect other expenses to increase by JPY1.2 billion. Part of these expenses come from improvements in the warehouse environment of sales offices. Because these expenses are of such nature, they are transitory expenses that will only be incurred during the current fiscal year.

Analyst: Okay. Thank you. I'd like to ask one additional question in relation to the first question. What is your approximate estimation of the vending machine market for this year? I believe the beverage market will increase by 2%. Do you expect the vending machine channel to grow by around 6% this year? Please tell me the underlying assumption for the vending machine channel in the market.

Takamatsu: We don't have an accurate outlook, or information source, by channel. Essentially, the vending machine channel was heavily affected last year due to the impact of COVID-19. As such, we think the recovery will be larger for the vending machine channel to a certain degree. We think it is probably in between the overall recovery of 2% and our target of 6%. That is our rough estimate, but we currently cannot say anything for certain.

Analyst: Do you take into consideration a larger recovery for outdoor locations, which is the company's strength?

Takamatsu: Yes. At DyDo, the ratio of our vending machines installed in outdoor locations is relatively high. As a result, we saw a relatively modest impact from COVID-19 last year. So, we didn't see a slump last year to begin with. By around the second half of last year, sales had nearly recovered, and this trend has continued so far.

On the other hand, we saw a substantial decline in sales for vending machines in urban areas. There was a slight recovery trend through the end of the year. But due to the reissuance of the state of emergency, sales have dropped sharply once again since the start of the new year. Regarding the urban areas, we would have to look at the development of the COVID-19 situation going forward. But there will also likely be major changes in the movement of people working in urban areas, including the further adoption of work at home. Therefore, we expect sales in urban areas are likely to continue to trend at low levels. Regarding our sales activities and the cultivation of new locations for installation, we intend to shift our focus from urban areas slightly toward the suburbs, and advance efforts by targeting areas where we can expect to capture relatively stable sales.

Analyst: Okay. Thank you very much.

Analyst: I have two questions.

First, when watching the video, I felt the president's confidence and determination toward 2021. I personally got the impression that things are going well internally and positive actions are being taken.

I believe what the president was stressing was that the roadmap toward improving the cash flow of vending machines has become clearer. Specifically, what do you think was the trigger that helped clarify this roadmap? Also, what kind of roadmap has specifically become apparent? Please tell me what kind of thoughts are behind your statement about a clearer roadmap. That is my first question.

Second, I believe you have always been saying in the mid-term business plan, quite simply, that you will invest around JPY30.0 billion to create a new pillar. However, given that the situation is in flux partly due to COVID-19, please share your thoughts one more time regarding the healthcare business, which the company is targeting. That's all.

Takamatsu: Thank you. First, I will answer your question regarding the improvement in cash flows of the vending machine business and the roadmap toward the stabilization of this cash flow. This is the biggest theme of the current mid-term business plan, and there are particularly two initiatives that we have focused on. First, we are working to strengthen our sales capabilities to continue to maintain and enhance the sales foundation of these vending machines. Second, we are working to realize smart operations to create a structure in which this sales foundation will be operated as efficiently as possible.

Regarding the first point, we implemented substantial measures last year to enhance our sales personnel resources for vending machines. We think the results are starting to emerge as a result of efforts we have been making since the past such as follows: reinforcement of various sales capabilities; education and training toward raising productivity; and productivity improvements through process management utilizing SFA and other systems. The reinforcement of personnel through these measures has been a positive factor. In addition, we have been able to make solid progress in increasing the number of newly installed vending machines.

Furthermore, for the whole year last year, I continued to talk of how to seize the changes resulting from the pandemic as an opportunity for new sales amidst the pandemic, and we have been taking action. As I stated earlier, we have continuously maintained our sales activity volume, such as by flexibly changing the target location depending on the flow of people or by switching to online negotiations early on even while face-to-face negotiations were difficult due to the pandemic. We launched an on-line sales team by effectively capturing this opportunity. Since the latter half of last year, I have continued to say that their role is to identify new sales targets and provide leads. We have started these activities from an early stage.

In addition, we have made proposals for a vending machine capable of facial authentication payment in sales negotiations by taking COVID-19 as an opportunity to promote the features of the vending machine, such as being contactless and non-face-to-face. We were also able to make proposals on vending machines that sell masks and sterilization sheets as a public health vendor, and we were able to implement this in a truly timely manner. We have been able to flexibly respond to the changes in consumer needs while strengthening our various sales capabilities, which we have been working on up to now. Correspondingly, we now have an outlook of being able to continue to powerfully promote new sales activities in the future.

Also, to give some detailed information regarding the enhancement of vending machines, another factor to keep in mind is how to reduce the churn of existing customers, in addition to acquiring new customers. Over the past several years, there were factors such as the shortage of an operator workforce in the background. However, the mentality that a shortage of operators permitted a reduction in the number of vending machine units had become pervasive among on-the-ground workers. This situation had resulted in a trend where the number of vending machine units in operation continued to decline. To stem this trend, we worked on conveying to on-the-ground workers one more time the mentality of maintaining our vending machine network, including a change in awareness.

We were also able to substantially decrease the number of vending machines that were withdrawn, which we describe as removals in the material, by providing detailed service and follow-up to existing customers. Regarding your first question about the roadmap becoming clearer, the first point is the strengthening of our sales foundation, which has been apparent in increasing the number of vending machine units in operation, sustaining this trend even during the pandemic, and continuing to increase it at present.

Regarding the other point about smart operations, we have been carrying out tests since the past, but we had partly been experiencing delays in the full-scale rollout. We were finally able to get a foothold in smart operations through tests that we conducted in three sales offices last year. We expanded test operations to a total of five sales offices, including the two additional sales offices at the end of last year in addition to the three sales offices.

We were able to roll out smart operations in a way that smoothly demonstrated the effects of implementation from the initial stages at the sales offices where we newly started tests, based on the results of the tests obtained at the three sales offices at the stage of adding two offices to the existing three offices. As such, we plan to deploy smart operations to all sales offices in around 70 locations this year.

We now have a clearer outlook to an extent about the smooth implementation regarding the introduction plan. Under the current situation, we now have a certain degree of visibility around the roadmap toward establishing this smart operation.

Analyst: I see. Does that mean you had taken active steps in advance, including the cultivation of sales targets online, ahead of others during the pandemic? I believe that is why you were able to secure a solid number of units compared to the rest of the market and also why you mentioned that FY2021 would be a decisive year for the company. While other companies are reducing unprofitable machines, DyDo is making proactive investments and taking steps to survive in the vending machine market. Should I consider this to truly be a touchstone year in which DyDo will demonstrate the directionality of these measures?

Takamatsu: It is as you say. Under the current circumstances, other companies are curtailing their investments. Some companies have made relatively aggressive investments. We would fit in the latter category of having made aggressive investments under the circumstances. This year will be the year in which we implement investments especially related to smart operations. We think a major theme in the current fiscal year will be to carry through with these investments.

Analyst: I see. I understand. Thank you. Please answer my second question.

Takamatsu: This is the question related to an investment of JPY30.0 billion centered on M&A toward building the Healthcare business into a second major source of revenue, correct? We have pushed forward on considerations up to now, but they haven't actually taken shape as results yet. Regarding the projects that have been considered up to now, we have given up on most of the projects because they were too expensive.

We will obviously refrain from implementing projects that cannot be expected to generate solid returns, and consideration will continue to be advanced with thorough discernment of projects. A situation that may have slightly changed due to the pandemic is that there are various moves in the industry to conduct business reviews. In some cases, we think this may lead to projects that are more reasonable than before that come forth. We hope to continue to make consideration of such projects.

On the other hand, partly due to the impact of COVID-19 last year, our operating cash flow has been slightly sluggish. One way to handle new M&A is by using the cash on our B/S. But, in consideration of the situation of our latest operating cash flow, I hope you will understand that we have slightly shifted our stance to one in which we would have to make considerations somewhat cautiously.

Analyst: I think, in that past, you also mentioned, for instance, that you would like to give some consideration to areas surrounding B2B domains that would produce synergies with Daido Pharmaceutical. Is there a need to make any substantial changes in that direction under the current pandemic?

Takamatsu: We are basically considering the same policy as before.

Analyst: I see. I understand. Thank you for your time.