COMPANY RESEARCH AND ANALYSIS REPORT

Qol Holdings Co., Ltd. (Qol)

3034

Tokyo Stock Exchange Prime Market

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Index

Summary

The Company aims for sustainable growth by promoting a differentiation strategy, through strengthening of the Home and Facility Delivery Dispensing Business and DX, and an M&A strategy

Qol Holdings Co., Ltd. (Qol) <3034> ("the Company") is a major dispensing pharmacy chain positioned at No. 2 in the number of dispensing pharmacies and No. 3 in net sales (using data from listed companies). It stands out in its operation of "One-on-one pharmacies" and deployment of "Healthcare pharmacies" through alliances with companies in other industries. In fields other than dispensing pharmacies, in addition to the CSO* Business, it also conducts the Medical Professional Referral Dispatch Business for pharmacists and other medical practitioners, and the Pharmaceutical Manufacturing Business.

* CSO stands for Contract Sales Organization and involves CMR (Contract Medical Representative) dispatch services.

1. In 1H FY3/23, sales reached a record high, although profits decreased

In 1H FY3/23, consolidated financial results were lower than the Company's forecasts (net sales ¥85,000mn and operating income ¥5,000mn), with net sales increasing 0.8% year on year (YoY) to ¥82,459mn, operating income decreasing 3.7% to ¥4,022mn. The factors behind the decrease in profits included a decrease in profit in the mainstay Pharmacy Business due to a resurgence of COVID-19 pandemic causing delays in the conclusion of M&A contracts, a somewhat lower-than-expected number of prescriptions at existing pharmacies, and an increase in pharmacy operation costs for responding to COVID-19; meanwhile, in in the Pharmaceutical Manufacturing Business, operating results decreased, mainly reflecting a deterioration in profits due to a greater-than-expected increase in the raw materials prices. However, net sales continued to renew record highs, driven by growth in CMR dispatches and medical professional referral dispatches. The number of dispensing pharmacies as of the end of FY3/23 increased by 3 stores from the previous fiscal year-end to 837.

2. The Company aims to achieve growth in sales and profits in FY3/23, leaving its initial forecast unchanged

The outlook for FY3/23 results is unchanged from the initial forecast, with net sales to increase 8.3% YoY to ¥180,000mn and operating income to increase 21.8% to ¥12,000mn. In 2H, the number of stores in the Pharmacy Business is expected to expand with progress on M&A negotiations that had been delayed. Furthermore, the Company expects a review of store operations to result in lower costs. The number of new openings of dispensing pharmacies for the full year is expected to be in the range of 10 to 20 pharmacies, with an additional 30 to 70 through M&A. In the Medical Related Business, the CSO Business and the Medical Professional Referral Dispatch Business are expected to continue expanding steadily in 2H, while in the Pharmaceutical Manufacturing Business, a contribution to earnings is expected from the start of sales of a COVID-19 antigen test kit. The Company is making steady progress on its priority measures for FY3/23 of expanding Home and Facility Delivery Dispensing Business sales and expanding services utilizing IT (such as accepting reservations for prescriptions via LINE). Going forward, the Company's policy is to focus on initiatives for increasing the competitiveness and productivity of its dispensing pharmacies.

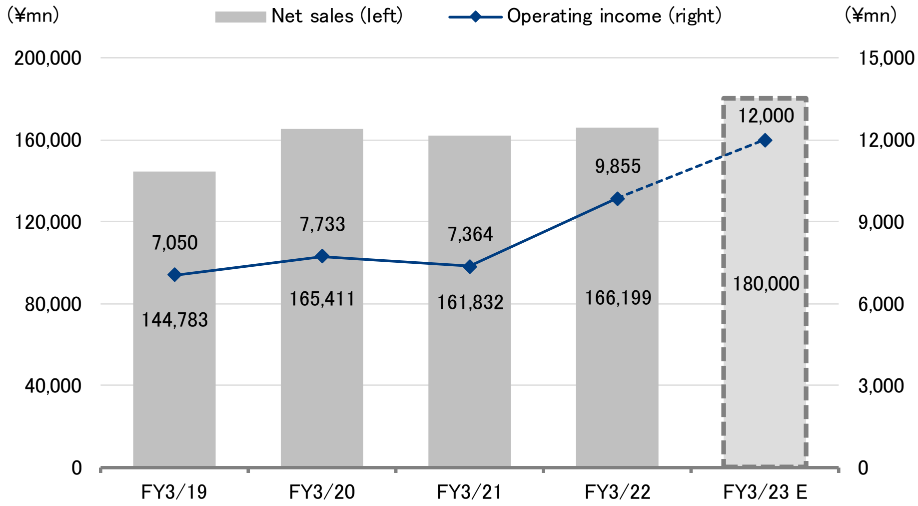
3. Policy of aiming for net sales of ¥300bn driven by the twin axis of the Pharmacy Business and the Medical Related Business

The Company's medium- to long-term growth strategies have remained consistent without changes. In the Pharmacy Business, it is aiming for stable growth by working on expanding scale through strategic store openings and creating value of pharmacies. In store openings, the Company is continuing at the pace of 40 to 90 stores per year including those from M&A, aiming to reach 1,000 stores at an early stage. It also intends to expand its market share by raising added value as part of efforts to strengthen its functions as a primary pharmacy for local communities. In the Home and Facility Delivery Dispensing Business, which the Company is focusing on, the Company will move forward on opening pharmacies specialized for Home and Facility Delivery Dispensing Business in urban areas, aiming for FY3/24 net sales of ¥10bn. Currently there are 15 such pharmacies, but the Company intends to expand this number to 50 over the next few years. This strategy will strengthen earning capability, since the unit price of prescriptions in the pharmacies specialized for the Home and Facility Delivery Dispensing Business is higher than those of general outpatient prescriptions. Moreover, the strategy can also be used to counter the expected emergence of online specialist pharmacies going forward. In the Medical Related Business, the Company will work to deepen specialization in the CSO Business and aims to increase its CMR headcount in the medium term from the current level of around 600 people to 1,000 people while developing high-value-added human resources and considering M&As. Also, in the Pharmaceutical Manufacturing Business, the Company will strive to maximize Group synergies while starting development on new generic pharmaceuticals. Looking ahead, the Company's policy is to expand its business even further through measures such as M&A and strengthening the contract development business. By promoting these strategies, the Company is expected to grow sustainably towards achieving its medium-term targets of net sales of ¥300bn and operating income of ¥25bn.

Key Points

- In 1H FY3/23, the Company updated record high sales due to the recovery of the Medical Related Business, although profits decreased
- In FY3/23, the initial forecast has been left unchanged, and the Company aims to continue renewing record highs
- In the Pharmacy Business, the Company will focus on expanding the number of stores and strengthening the Home and Facility Delivery Dispensing Business, as well as achieving differentiation and strengthening earning capability through the promotion of DX
- CMR dispatches is focusing on the pursuit of specialization and expanding market share, the Medical Professional Referral Dispatch Business is expanding areas and the Pharmaceutical Manufacturing Business is aiming for high growth by utilizing Group synergies

Results trends



Source: Prepared by FISCO from the Company's financial results

Company profile

Under a holding company structure as a major dispensing pharmacy chain, the Company is conducting businesses on the twin axis of the Pharmacy Business and the Medical Related Business

1. History

Chairman Masaru Nakamura founded Qol Co., Ltd. in 1992. Qol Co., Ltd. steadily expanded its dispensing pharmacy network after opening the first pharmacy in Nihonbashi Kabutocho in 1993. In addition to opening its own stories, the Company has been expanding its dispensing pharmacy network through aggressive M&A and also moved into related and peripheral areas, the Company moved into the clinical trial-related business when it established PhaseOn Co., Ltd. in 2003, and established Qol Medis, Co., Ltd. in 2008 to start worker placements and dispatching services business.

Subsequently, the Company organized its businesses into two business segments, the Pharmacy Business and the BPO Business (currently, the Medical Related Business). It then changed to a holding company structure in October 2018 in order to improve management efficiency and to expand the business scope. Following this, the Company changed its corporate name to Qol Holdings Co., Ltd. as a pure holding company, and is leading the Group as a whole toward enhancing corporate governance and formulating the Group's medium- to long-term growth strategy. The Pharmacy Business is conducted by Qol Co., Ltd., and other companies that joined the Group through M&A. In the Medical Related Business, APO PLUS STATION Co., Ltd., conducts the CSO Business, mainly CMR dispatches, while Fujinaga Pharm Co., Ltd., which became as a subsidiary in August 2019, conducts the Pharmaceutical Manufacturing Business. Furthermore, in order to promote the growth of the Medical Professional Referral Dispatch Business for pharmacists and other medical professionals, which had been conducted by APO PLUS STATION, the Company established APO PLUS CAREER Co., Ltd. in February 2020, and transferred the business to it.

The Company is aiming to achieve business growth, while increasing the stability of earnings, by developing its businesses on the twin axis of the Pharmacy Business and the Medical Related Business. The Pharmacy Business is a business that can stably acquire earnings, but it is exposed to the risk of fluctuating earnings due to the government's medical policies (including revisions to dispensing fees once every two years). In a revision year, there may be negative factors in terms of earnings, and the strategy is to stably increase overall earnings by covering these negatives through the Medical Related Business. Looking at the breakdown by segments (1H FY3/23 results), the Pharmacy Business accounts for the majority at 91.6% of net sales and 88.7% of operating income; however, the Company intends to increase the share of the Medical Related Business over the medium to long term.

Pursuing an approach of "One-on-one pharmacies" and "Healthcare pharmacies" through alliances with companies in other industries to increase the number of stores while utilizing M&As

2. Pharmacy Business

(1) Business scale and positioning in the industry

The Pharmacy Business segment mainly involves the management of dispensing pharmacies. Looking at the number of stores at the end of September 2022, 816 (97%) of the 837 stores were dispensing pharmacies, while the remaining 21 were shops located within hospitals. Prescription net sales (dispensing net sales) amounted to about 92% of the segment sales. Remaining sales came from product sales at pharmacies, convenience stores, and shops located within hospitals and sales income for health foods, hygiene items, and other products on Qol's official e-commerce website.

Regarding positioning in the dispensing pharmacy industry, Qol ranks second in number of stores among listed dispensing pharmacy chains after Ain Holdings Inc. <9627> (1,210 stores as of the end of July 2022) and third in net sales after Ain Holdings and Nihon Chouzai Co., Ltd. <3341>. Nihon Chouzai, which is third in the number of stores at 713 (as of the end of September 2022), has net sales that exceed those of the Company because it has developed many pharmacies located adjacent to hospitals, which generate strong sales.

(2) Pharmacy development strategy

A feature of the Company's pharmacy development strategy is that it conducts the business through two formats that are largely different in type. The first type is the "One-on-one pharmacies," and the second type is "Healthcare pharmacies" through business alliances with different industries such as major convenience store operator Lawson, Inc. <2651> and BIC CAMERA Inc.<3048>, and others.

"One-on-one pharmacies" is a concept that defines the fundamental stance in store operations for ordinary QOL Pharmacies. It is also the "core business" in its business model. The key point lies in the close cooperation between the prescribing medical institutions and QOL Pharmacies. Our understanding at FISCO is that the phrase "One-on-one" is used to express the pharmacies' deep, cooperative relationships with medical institutions. From the phrase "One-on-one," the tendency is to imagine a deep relationship between only one QOL Pharmacy and only one prescribing medical institution. But in fact, it seems that in many cases, one pharmacy builds deep cooperative relationships with multiple medical institutions.

In its "One-on-one pharmacies," the Company is aiming to utilize cooperation with medical institutions to realize efficient and low-cost operations, and to invest the results of this into improving services for patients. Specifically, it is aiming to create these pharmacies by adjusting store designs and functions in accordance with factors such as the departments of target medical institutions and the characteristics of each region. The funds for this are generated from the pharmacies' low-cost structures, including more efficient drug inventories, which is one of the benefits of one-on-one management. Based on the concept of "One-on-one pharmacies," the Company positions the creation of pharmacies that are selected by patients for having high utility value as the core of its pharmacy strategy. In addition, the concept of "One-on-one pharmacies," which essentially entails cooperation with medical institutions, can be said to be in line with the Japanese Government's Vision for Patient-centered Pharmacies, which is also an important point for the growth strategy. Moreover, we at FISCO think that the Company's pharmacies will demonstrate their strength in the authorization system for pharmacies with specific functions (details mentioned later), which was introduced in August 2021.

The catalyst for Qol's pursuit of Healthcare pharmacies through alliances with companies in other industries, which is its other format, was a revision to the Pharmaceuticals Affair Law in June 2009 that allows convenience stores, drugstores, supermarkets, and other industry stores to sell OTC drugs as registered businesses. Spurred on by this, it became possible for companies to launch a dispensing pharmacy business, such as in drugstores. As an offensive measure in response to this, the Company entered into business alliances with the two aforementioned companies, and is now proceeding with this initiative.

"One-on-one pharmacies" have somewhat restricted customer scope that enables Qol to improve efficiencies in drug inventory management. "Healthcare pharmacies," meanwhile, target unspecified large number of customers in locations with heavy people flow, so-called foot-traffic pharmacies. While these sites require larger inventory investments and other outlays than the "One-on-one pharmacies," they are likely to attract more customers (and thus receive more prescriptions). Qol positions "One-on-one pharmacies" as the core model and also aims to broaden the customer base through deployment of healthcare.

As a new initiative, the Company has allied with Ryohin Keikaku Co., Ltd. <7453> and started opening stores inside MUJI Stores in FY3/22. Ryohin Keikaku has opened "Machi no Hokenshitsu (town infirmaries)" inside MUJI Stores as a health promotion space that holds periodic health-themed events, offers casual health consultation, and provides a full-line of services covering disease prevention and health maintenance through to pharmaceuticals in order to contribute to the healthy living of local residents. The Company will open dispensing pharmacies as a collaborating partner in this initiative.

As of the end of September 2022, there were 36 healthcare stores in alliance with Lawson, 4 inside BIC CAMERA stores, 2 inside MUJI stores, and a further 2 inside train stations.

Overall image of the pharmacy strategy

Business format	Pharmacy type	Location	Function	Opening method	Degree of focus
QOL Pharmacies	One-on-one	Urban type. Clinic-adjacent	Primary pharmacist and pharmacy function, health support function	Organic, M&A	◎
	Foot-traffic pharmacies		Primary pharmacist and pharmacy function, health support function	Organic, M&A	
	Hospital-adjacent pharmacies	Hospitals of a certain size	Primary pharmacist and pharmacy function, advanced pharmaceutical management function, health support function	Organic, M&A	○
Healthcare pharmacies	Foot-traffic pharmacies	Within shopping districts, within and near to train stations	Primary pharmacist and pharmacy function, health support function	Organic	◎

Source: Prepared by FISCO from Company materials and interviews

Looking at the number of store openings by region at the end of September 2022, Kanto leads with 341 stores (40.7% of the total volume), followed by Kansai with 133 stores (15.9%), and Koshinetsu with 110 stores (13.1%). As store openings have taken place with Tokyo as the area in which the Company was founded, there have been many openings in the Kanto area. Looking at the increases since the end of FY3/17, Kansai has had the greatest increase, with 40 stores, followed by the Kanto regions with 27 stores, Tokai and Hokuriku with 25 stores, and Koshinetsu with 19 stores, suggesting the Company has focused on new organic openings and M&A in major urban areas outside of the Kanto area in the past several years. The focus areas are the Tokyo, Nagoya, and Osaka areas, which have a high population density. Looking at a comparison of the number of stores and population composition ratio by region, the Company has a higher ratio in Kanto, Koshinetsu, and Tohoku and a lower ratio in the Tokai and Hokuriku regions. The Company's priority going forward would seem to be developing the Tokai area, centered on Aichi Prefecture in particular.

Number of stores by region and population composition comparisons

	End of FY3/17	End of FY3/22		End of 1H FY3/23		Increase on end of FY3/17	Population composition
	Number of stores	Number of stores	Composition ratios	Number of stores	Composition ratios		
Hokkaido	10	10	1.2%	11	1.3%	1	4.1%
Tohoku	75	90	10.8%	89	10.6%	14	6.8%
Kanto	314	338	40.5%	341	40.7%	27	34.6%
Koshinetsu	91	110	13.2%	110	13.1%	19	4.0%
Tokai, Hokuriku	45	70	8.4%	70	8.4%	25	14.2%
Kansai	93	133	15.9%	133	15.9%	40	16.3%
Chugoku, Shikoku	51	48	5.8%	48	5.7%	-3	8.7%
Kyushu, Okinawa	17	35	4.2%	35	4.2%	18	11.3%
Total	696	834	100.0%	837	100.0%	141	100.0%

Note: Japan's population composition based on national census data from 2020
Source: Prepared by FISCO from Company materials

Developing the Medical Professional Referral Dispatch Business centered on CMR dispatches, and entered the Pharmaceutical Manufacturing Business through acquisition of a pharmaceutical company in 2019

3. Medical Related Business

The Medical Related Business includes the CSO Business (CMR dispatches), and the CRO* Business (clinical trials support services), which are mainly conducted by APO PLUS STATION; the Medical Professional Referral Dispatch Business (pharmacists, registered sales personnel, public health nurses, nurses, etc.) conducted by APO PLUS CAREER; the medical-related publishing business conducted by Medical Qol Co., Ltd.; and the Pharmaceutical Manufacturing Business conducted by Fujinaga Pharm, which joined the Group in August 2019. Looking at the sales composition ratio, the CSO Business and CRO Business accounts for approximately 60%, while the Medical Professional Referral Dispatch Business accounts for approximately 20%, Pharmaceutical Manufacturing Business for approximately 15%, and the Medical-related Publishing Business accounts for approximately 5%.

* CRO is the abbreviation of Contract Research Organization and refers to assistance business and other services for clinical trials and other activities.

(1) CSO Business and CRO Business

The CSO Business involves recruiting and training MR and dispatching them to the contracted pharmaceutical companies. MR refers to sales representatives for pharmaceutical companies who provide doctors, pharmacists, and others with knowledge and information on the pharmaceuticals that are sold. In recent years, the development trend for new drugs among pharmaceutical companies has shifted from primary medicine (for treatment of lifestyle related diseases, etc.) that targets many customers (medical facilities and doctors) to specialty drugs (anti-cancer drugs, etc.) for which the target customers are limited. Accordingly, there has been an expanding movement toward reducing their in-house MR personnel and switching to CMR personnel.

In this situation, the Company has been leveraging its strengths of recruitment and training capabilities and increasing its recruitment of CMR personnel. At the end of September 2022, it had approximately 600 CMR personnel, which is an industry share of around 15%, and it holds the leading position in the industry for the number of customers as well, with 50 to 60 companies. According to the “2022 Edition MR White Paper” published by the MR Education & Accreditation Center of Japan, at the end of March 2022, there were 3,948 CMRs (increased 25 YoY), who were being utilized by 138 companies as of October 2021 for an MR outsourcing rate of 6.4%. All three metrics represent new record highs.

On the other hand, the CRO Business provides total solutions from planning through to publication for clinical trials and clinical research in the respective fields of ethical drugs, OTC drugs, food, and healthcare. The Company has strengths in clinical trials in the food field, and in the pharmaceuticals field it has experience in dermatology and ophthalmology.

(2) Medical Professional Referral Dispatch Business

This business involves referral dispatches of pharmacists, public health nurses, registered sales personnel, and others. Of these, it mainly conducts referral dispatches of pharmacists. It ranks in the top 10 for the number of dispatched pharmacists in the industry, while it also ranks in the top 3 for public health nurses. In addition, at APO PLUS CAREER, the Company provides pharmacy business succession and management support services and consulting services on health and productivity management for corporations.

(3) Pharmaceutical Manufacturing Business

Fujinaga Pharm is a pharmaceutical manufacturer established in 1941 (founded in February 1924) that mainly covers psychiatry and dermatology fields. It manufactures brand-name drugs Phenobal and Hydantol, generic-drug Fujinaga lithium carbonate, and other products. Its annual sales scale before joining the Group was around ¥1.8bn. But going forward, the policy is to establish its unique position and grow its business by increasing sales for the Group's dispensing pharmacies and strengthening manufacturing facilities.

Business trends

In 1H FY3/23, the Company updated record high sales due to the recovery of the Medical Related Business, although profits decreased

1. Summary of 1H FY3/23 results

In the 1H FY3/23 consolidated results, sales increased while profits decreased, with net sales increasing 0.8% YoY to ¥82,459mn, operating income decreasing 3.7% to ¥4,022mn, ordinary income decreasing 2.3% to ¥4,174mn, and profit attributable to owners of parent decreasing 3.6% to ¥2,366mn. All were lower than the Company's initial forecasts. Although net sales increased for two consecutive periods to renew record highs due to the recovery of the CSO Business and the Medical Professional Referral Dispatch Businesses, in terms of profit, the Company's earnings fell for the first time in two years, albeit slightly, mainly due to a decrease in earnings from the mainstay Pharmacy Business, due to the impact of the COVID-19 pandemic, as well as a deterioration in earnings from the Pharmaceutical Manufacturing Business.

1H FY3/23 results (consolidated)

(¥mn)

	1H FY3/22		1H FY3/23				
	Results	% of sales	Initial forecasts	Results	% of sales	YoY	Compared to forecast
Net sales	81,814	-	85,000	82,459	-	0.8%	-3.0%
Gross profit	10,857	13.3%	-	10,856	13.2%	0.0%	-
SG&A expenses	6,679	8.2%	-	6,834	8.3%	2.3%	-
Operating income	4,177	5.1%	5,000	4,022	4.9%	-3.7%	-19.6%
Ordinary income	4,274	5.2%	5,000	4,174	5.1%	-2.3%	-16.5%
Extraordinary income/losses	6	-	-	-18	-	-	-
Profit attributable to owners of parent	2,455	3.0%	3,000	2,366	2.9%	-3.6%	-21.1%
EBITDA*	6,493	7.9%	-	6,382	7.7%	-1.7%	-

* EBITDA = Operating income + Depreciation + Amortization of goodwill
Source: Prepared by FISCO from the Company's financial results

Looking at the results by business segment, in the Pharmacy Business, net sales increased 0.3% YoY to ¥75,557mn, and operating income decreased 2.4% to ¥5,056mn. Factors behind the increase in net sales included an increase in the number of stores through new openings and M&A in addition to an increase in the number of prescriptions at existing stores and the promotion of the Home and Facility Delivery Dispensing Business, which absorbed the decrease in the unit price of prescriptions. The sales result also reflected growth in sales stores and e-commerce sales. On the profit front, the fall in profits reflected a decrease in technical fee unit prices following a revision of dispensing fees in April 2022 and an increase in the number of people infected with COVID-19 even within the Company due to the arrival of a seventh wave of infections, as well as an increase in expenses for maintaining store operations (around ¥0.15bn, primarily personnel expenses).

On the other hand, in the Medical Related Business, net sales increased 6.6% YoY to ¥6,901mn and operating income decreased 2.6% to ¥645mn. The CSO Business increased sales and profits due to expansion in demand for highly specialized CMRs, while the Medical Professional Referral Dispatch Business also saw sales and profits increase, mainly due to a recover in demand for dispatch of pharmacists. However, in addition to a decline in sales prices due to the drug price revision, the overall segment recorded increased sales and decreased profits due to a decrease in sales and profits in the Pharmaceutical Manufacturing Business caused by soaring prices for active pharmaceutical ingredients and logistical costs.

Looking at factors causing operating results to fall below the Company's forecast, in the Pharmacy Business there were delays in progress on M&A and a slightly lower-than-expected number of prescriptions at existing stores, as well as an increase in personnel costs to respond to the COVID-19 pandemic. Meanwhile, in the Medical Related Business, the Pharmaceutical Manufacturing Business experienced soaring prices for active pharmaceutical ingredients and logistical costs, which also contributed to the downturn in results.

Performance by segment

(¥mn)

	1H FY3/22		1H FY3/23	
	Results	YoY	Results	YoY
Pharmacy Business				
Net sales	75,341	4.2%	75,557	0.3%
Segment income	5,181	63.1%	5,056	-2.4%
% of net sales	6.9%		6.7%	
Medical Related Business				
Net sales	6,473	-4.2%	6,901	6.6%
Segment income	663	-29.1%	645	-2.6%
% of net sales	10.2%		9.3%	

* Net sales shown before deducting inter-segment transactions
Source: Prepared by FISCO from the Company's results briefing materials

A decrease in the unit price of prescriptions resulted in level YoY results for dispensing net sales, however, Home and Facility Delivery Dispensing Business sales increased steadily

2. Trends in the Pharmacy Business

(1) Status of net sales at dispensing pharmacies

In the Pharmacy Business, net sales are comprised of dispensing pharmacies' dispensing sales and product sales such as shops and e-commerce. Looking at the breakdown of net sales for 1H FY3/23, dispensing sales were level with a decrease of 0.1% YoY to ¥69,839mn, but other sales rose 5.6% to ¥5,718mn. Breaking down dispensing sales by store-opening period and format, among the Company's organic openings, sales at existing pharmacies increased 4.7% YoY, or ¥984mn on a monetary basis, while sales at new pharmacies declined 33.8% YoY, or ¥103mn on a monetary basis, due to a lower number of new pharmacy openings compared with the previous fiscal year. For pharmacies acquired through M&A and other methods, although it is difficult to distinguish their results as they are not separated for existing pharmacies and newly opened pharmacies, sales decreased 2.0% YoY, or ¥966mn on a monetary basis.

Details of dispensing pharmacy net sales by opening period and by format

(¥mn)

	1H FY3/22			1H FY3/23		
	Results	Change	Growth rate	Results	Change	Growth rate
Existing pharmacies	21,138	1,190	6.0%	22,122	984	4.7%
Newly opened pharmacies	305	-248	-44.8%	202	-103	-33.8%
M&A, etc.	48,480	2,230	4.8%	47,514	-966	-2.0%
All pharmacies	69,924	3,172	4.8%	69,839	-85	-0.1%

Source: Prepared by FISCO from the Company's supplemental results materials

On breaking down dispensing pharmacy net sales into the number of prescriptions and the unit price of prescriptions, the number of prescriptions increased 4.2% YoY to 7,323 prescriptions, while the unit price of prescriptions decreased 4.2% to ¥9,537. They are affected by other factors such as the opening period and M&A. We will look at these values in detail below.

The change rate in the number of existing pharmacies, which is considered to be close to actual conditions regarding the number of prescriptions, was a YoY increase of 7.3%. This was largely due to a rebound from a lingering trend of people refraining from seeking treatment due to the COVID-19 pandemic in the previous fiscal year. Moreover, the number of prescriptions at pharmacies through M&A, etc. increased by 3.3%, but the number of new pharmacy acquisitions decreased from eight in the previous fiscal year to one, leading to a slowdown in the growth rate. Overall, growth in the number of prescriptions was slower than forecast, mainly due to the impact of the arrival of a seventh wave of COVID-19 infections in the summer and lack of progress on acquisition of stores through M&A. This in turn was a major factor in net sales being lower than forecast.

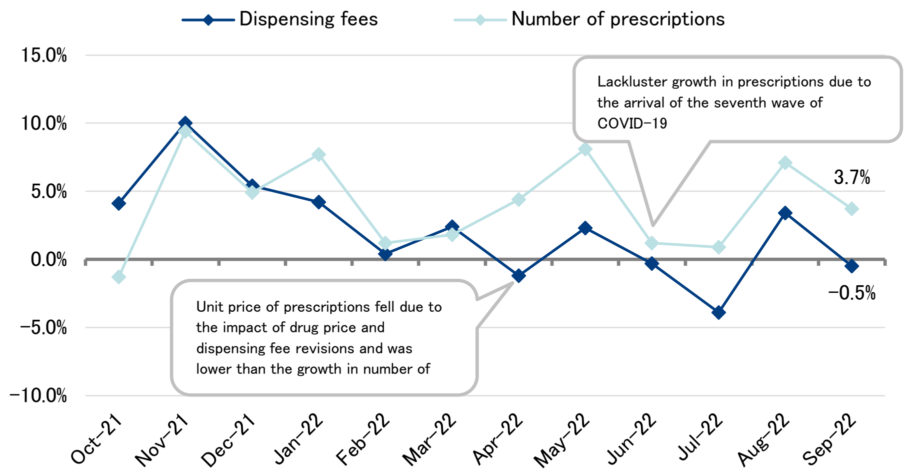
Number of prescriptions by store-opening period and format (details)

(thousands)

	1H FY3/22			1H FY3/23		
	Results	Change	Growth rate	Results	Change	Growth rate
Existing pharmacies	1,960	180	10.1%	2,104	144	7.3%
Newly opened pharmacies	53	5	10.4%	42	-11	-20.8%
M&A, etc.	5,012	332	7.1%	5,175	163	3.3%
All pharmacies	7,026	516	7.9%	7,323	297	4.2%

Source: Prepared by FISCO from the Company's supplemental results materials

Dispensing fees and the number of prescriptions
(compared to the same month in the previous fiscal year, total at all pharmacies)



Source: Prepared by FISCO from the Company's monthly report

On the other hand, the unit price of prescriptions fell by 4.2% YoY overall, including a 2.5% fall at existing pharmacies and a 5.1% fall at M&A and other pharmacies. The main factors were the impact of a drug price revision, in addition to a decrease in dispensing fee unit prices as there was an increase in relatively low-priced prescription drugs such as antipyretics due to the COVID-19 pandemic. However, there was also a slight decrease due to the impact of dispensing fee revisions regarding the unit price of dispensing pharmacy's technical fees.

Unit price of prescriptions by store-opening period and format (details)

(¥)

	1H FY3/22			1H FY3/23		
	Results	Change	Growth rate	Results	Change	Growth rate
Existing pharmacies	10,783	-419	-3.7%	10,510	-273	-2.5%
Newly opened pharmacies	5,671	-5,663	-50.0%	4,785	-886	-15.6%
M&A, etc.	9,673	-208	-2.1%	9,180	-493	-5.1%
All pharmacies	9,952	-301	-2.9%	9,537	-415	-4.2%

Source: Prepared by FISCO from the Company's supplemental results materials

The dispensing pharmacy's technical fees, which are the equivalent of the pharmacy's added value, work on a system in which points are aggregated depending on the level of achievement of predetermined standards. The fees mainly comprise a basic dispensing fee, (categorized by number of prescriptions and concentration ratio around designated medical institutions, etc.), generic drug dispensing premium (categorized by ratio of generic drugs handled), and community support system incentives (categorized by system for contribution to community healthcare, such as home and facility delivery dispensing). Of these, the generic drug dispensing premium and community support system incentives offer different points depending on the quality of each pharmacy's initiatives. With the recent revision, the setting for the basic dispensing fee was changed based on the efficiency of pharmacy management; the standard for the proportion of dispensing volume for the generic drug dispensing premium was increased and the evaluation method revised; and the systems relating to contribution to community healthcare and results-based evaluation system for the community support system incentives were revised. As a result, the unit price for the basic dispensing fee decreased, but technical fee unit prices for the generic drug dispensing premium and the community support system incentives increased.

The revised points categories for the basic dispensing fee have been refined from four categories to five, adding an item of 32 points between 42 points, which is the highest, and 26 points. With the recent revision, for the basic fee of large-scale Group pharmacies*, pharmacies receiving over 85% of prescriptions from designated medical institutions were assigned 16 points, while those with less than 85% received 32 points. As a result, the ratio of the Company's pharmacies receiving 42 points, which was 47.3% in April 2021, decreased to 1.2% in April 2022, while the ratio of pharmacies receiving 32 points, a newly added category, was 47.1%. This was the main reason for the decrease in technical fee unit prices.

* The pharmacies in the same group receiving more than 0.4 million prescriptions a month, or having 300 or more pharmacies in the same group.

The generic drug handling ratio (volume basis) rose slightly from 84.0% for the overall Group as of March 2022 to 84.7% as of September 2022, exceeding the level of 80% targeted by the Ministry of Health, Labour and Welfare. The major factor in this change was the overall Group's leadership in the use of generic drugs in line with Japan's policy on them. With the revision in April 2022, for example the condition for receiving the maximum points has been lifted from the previous condition of 85% or above to receive 28 points to 90% or above to receive 30 points after the revision. The ratio of stores that received 30 points has increased from 18.7% in April 2022 to 27.9% in September, which has contributed to the increase in technical fee unit prices. Furthermore, since the summer of 2021, supply shortage issues caused by misconduct at a generic drug manufacturer appear to have been improving. In FY3/23, the supply shortages caused impacts such as a temporary dip in the productivity of pharmacies; however, since the start of FY3/23 these issues are being resolved.

Regarding the factors behind the increase in community support system incentives, whereas previously there were only two categories: 0 points and 38 points, after the revision, the categories were refined into four: 0 points, 17 points, 39 points, and 47 points. The ratio of the Company's pharmacies receiving the maximum points allocation as of September 2022 was 28.2%. Furthermore, the ratio of pharmacies receiving 0 points decreased from 64.3% in April 2021 to 50.1% in September 2022. The goal with respect to the community support system incentives is to promote stronger functions as a primary pharmacy for local communities, and the Company has also increased the number of pharmacies which acquired the community support system incentives by promoting initiatives for home and facility delivery dispensing. The Company has stated its target is to increase Home and Facility Delivery Dispensing Business sales from approximately ¥5bn in FY3/22 to ¥10bn in FY3/24, and its sales are currently growing steadily, partly driven by an increase in specialist home and facility dispensing pharmacies and key pharmacies.

Basic dispensing fee

Points	End of April 2021	End of April 2022	End of September 2022
42 points	47.3%	1.2%	1.2%
32 points	-	47.1%	47.1%
26 points	0.6%	0.0%	0.0%
21 points	0.0%	0.5%	0.5%
16 points	50.0%	49.1%	48.7%
9 points	2.0%	2.1%	2.5%
Number of pharmacies	782 stores	807 stores	810 stores

Generic drug dispensing premium

Points	End of April 2021	Points	End of April 2022	End of September 2022
28 points	64.7%	30 points	18.7%	27.9%
22 points	18.7%	28 points	51.5%	46.5%
15 points	6.8%	21 points	16.9%	15.0%
0 points	9.8%	0 points	12.9%	10.6%
Number of pharmacies	782 stores		807 stores	810 stores

Community support system incentives

Points	End of April 2021	Points	End of April 2022	End of September 2022
38 points	35.7%	47 points	26.4%	28.2%
		39 points	10.3%	8.6%
		17 points	9.0%	13.1%
0 points	64.3%	0 points	54.3%	50.1%
Number of pharmacies	782 stores		807 stores	810 stores

Source: Prepared by FISCO from the Company's results briefing materials

(2) Store openings and closures and M&A status

The number of stores at the end of September 2022 stood at 834, an increase of just 3 stores from the end of the previous fiscal year. Organic store openings performed strongly with eight stores; but only one store was acquired through M&A as negotiations were prolonged by the COVID-19 pandemic. Considering that in the same period of the previous fiscal year, 12 stores opened organically, while 8 opened through M&A, store opening activity has been somewhat stalled. Nevertheless, M&A negotiations appear to be proceeding steadily, and the Company expects to conclude multiple agreements in the second half of the year. Furthermore, one of the newly opened stores is a collaborative store with Ryohin Keikaku, the second of its kind. In April 2022, the Company opened a store within the "Machi no Hokenshitsu" of MUJI Hiroshima Alpark, one of MUJI store's largest stores.

Store openings and closures status

		1H FY3/22				End of FY3/22	1H FY3/23			
		Opened		Closed	End of 1H		Opened		Closed	End of 1H
QOL Pharmacies		Organic openings	12	1	764	768	Organic openings	8	5	772
		Through M&A	8				Through M&A	1		
Healthcare	Lawson	0		2	36	36	0		0	36
	BIC CAMERA	0		0	5	5	0		1	4
	Ryohin Keikaku	1		0	1	1	1		0	2
	Within train stations	0		0	2	2	0		0	2
Shops		0		0	21	22	1		2	21
Total		21		3	829	834	11		8	837

Source: Prepared by FISCO from the Company's financial results and supplemental results materials

Demand for CMR dispatches and medical professional referral dispatches returns to a recovery path

3. Trends in the Medical Related Business

Within the Medical Related Business, the mainstay CSO Business rebounded to higher sales and profits. CMR dispatch demand began to recover from 2H of the previous fiscal year, and the trend has continued in FY3/23. The number of CMR dispatches remains the same as the previous fiscal year at approximately 600, but with an increase in new specialty drugs that require a high degree of specialization in fields such as oncology and central nervous system disorders, in CMR there has been strong demand for human resources in these highly specialized fields, who have a high unit price, which has led to an increase in the average unit price and a 6.6% YoY increase in net sales.

In the Medical Professional Referral Dispatch Business also, sales and profits have also rebounded to an increase, driven by a recovery trend in demand. Behind this trend is the start of an increase in the number of prescriptions despite a lingering impact from the COVID-19 pandemic, giving rise to a shortage of pharmacists, an increase in demand for registered sales personnel associated with an increase in drugstore openings, and increasing dispatch demand for companies' industrial physicians and health professionals due to increasing interest in health management.

On the other hand, in the Pharmaceutical Manufacturing Business, sales and profits decreased. Downward pressure on earnings came from a decrease in net sales due to drug price revisions and soaring prices for active pharmaceutical ingredients and logistical costs. In the area of raw materials, high prices for lithium used in Fujinaga lithium carbonate tablets, which are an antimanic treatment, had an impact. Lithium is a major raw material for EV batteries, which has sent demand up sharply, and prices increasing rapidly 4 to 5 times from the level on year ago. The Company procured more than usual to respond to the risk of further price increases.

In FY3/23, the initial forecast has been left unchanged, and the Company aims to continue renewing record highs

4. FY3/23 outlook

The financial results outlook for FY3/23 has been left unchanged from the initial forecast, with net sales to increase 8.3% YoY to ¥180,000mn, operating income to increase 21.8% to ¥12,000mn, ordinary income to increase 18.9% to ¥12,000mn, and profit attributable to owners of parent to increase 18.4% to ¥6,500mn. The progress rates for 1H FY3/23 are low, with net sales at 45.8% and operating income at 33.5%, leaving a high hurdle to achieve the forecast. Nevertheless, there are also positive factors, such as expectations for improved productivity in 2H by revising operations at pharmacies, an expected increase in the number of stores through new store openings and M&A, and the start of sales of new antigen test kits for COVID-19. Furthermore, some observers have expressed a view that influenza will spread widely this season, and if this is the case, the number of prescriptions could very well increase a step further. The Company's ability to achieve the forecast is dependent on these trends; however, we at FISCO see plenty of potential for the Company to continue renewing its past record highs at the least.

FY3/23 outlook

(¥mn)

	FY3/22		FY3/23			1H progress rate
	Full year results	% of sales	Company forecasts	% of sales	YoY	
Net sales	166,199	-	180,000	-	8.3%	45.8%
Operating income	9,855	5.9%	12,000	6.7%	21.8%	33.5%
Ordinary income	10,094	6.1%	12,000	6.7%	18.9%	34.8%
Profit attributable to owners of parent	5,489	3.3%	6,500	3.6%	18.4%	36.4%
EBITDA	14,588	8.8%	17,360	9.6%	19.0%	36.8%
Capital investment	1,733	-	1,174	-	-32.3%	-
Depreciation	1,565	-	1,916	-	22.4%	40.5%
Amortization of goodwill	3,168	-	3,444	-	8.7%	46.0%
Profit per share (yen)	149.51		177.02			

Source: Prepared by FISCO from the Company's financial results and supplemental materials

(1) Pharmacy Business

The Pharmacy Business is expected to record increases in both sales and profits. In FY3/23, the forecast for new store openings, an indicator of performance, is for about 10 to 20 organic openings and 30 to 70 openings through M&A. Of the organic openings, five are planned to be in collaboration with other industries or pharmacies within stations. From October 2022 through to November 15, 2022, the Company opened 6 new stores organically and newly acquired 8 stores through M&A*, for a total of 851 stores, an increase of 22 stores compared with the end of the previous fiscal year. Since April 2022, the Company has progressed more or less as planned, with 14 organic store openings, while store acquisitions through M&A number only 9. However, the dispensing pharmacy market will has become stricter in terms of management status due to drug price revisions and so forth, and the pace of store acquisitions through M&A may accelerate going forward.

* The Company acquired all of the shares of Hokusetsu Chozai Co., Ltd. which operates eight stores in Osaka, Hyogo, Nara, and others, dated November 7, 2022.

The number of prescriptions is expected to increase at existing stores by just over 5% YoY. As for the unit price of prescriptions, dispensing fee unit prices are forecast to decrease due to the impact of drug price revisions and the decrease in long-term prescriptions, whereas the unit price of dispensing pharmacy's technical fees is expected to remain level, resulting in a slight decrease in the total. Because of this, the Company expects an increase of about 5% YoY in sales from dispensing fees at existing stores, in addition to an increase in sales through the effects of new store openings and M&A, e-commerce sales, convenience store product sales together with increased sales of OTC drugs. The Company's policy is to increased sales for Home and Facility Delivery Dispensing Business for major nursing care facilities and to strengthen initiatives for individual homes.

Factors increasing operating income are the increase in gross profit due to the increase in dispensing fee revenue in addition to the contribution from increased technical fee revenue from the increase in the number of prescriptions. In addition, with the impact of an increase in infected cases among pharmacists over 1H, personnel expenses increased by more than anticipated; however, for 2H, the Company will enhance cooperation between pharmacies that have established market dominance to create a system that enables employees to respond efficiently to work shifts and so forth in the event that store staff become infected. In this way, the Company is controlling personnel costs. Furthermore, with an eye to increasing work productivity, the Company has started introducing automatic reading devices for prescriptions at busy stores. Furthermore, the number of new graduate pharmacists recruited in spring of 2023 is expected to be around 200, on par with 2022.

(2) Medical Related Business

The Medical Related Business is expected to achieve double-digit increases in sales and profits. The CSO Business and the Medical Professional Referral Dispatch Business are expected to continue to steadily grow sales in 2H, while the Pharmaceutical Manufacturing Business also has potential to increase sales and profits over the full year by starting sales of COVID-19 antigen test kits, for which the Company is currently filing a marketing approval application. The antigen test kits are expected to go on sale in December 2022, with an expected sales scale in the billions of yen.

Regarding CMRs, the aim is to increase their number to about 700 to 800 by the end of FY3/23 from approximately 600 people at the end of the previous fiscal year, and the Company is proactively moving ahead on recruiting and training. In particular, the Company is poised to proactively recruit and train MRs in specialty drugs and other specialized domains where demand is strong, and MRs with high IT literacy.

Medium- to long-term growth strategy and progress

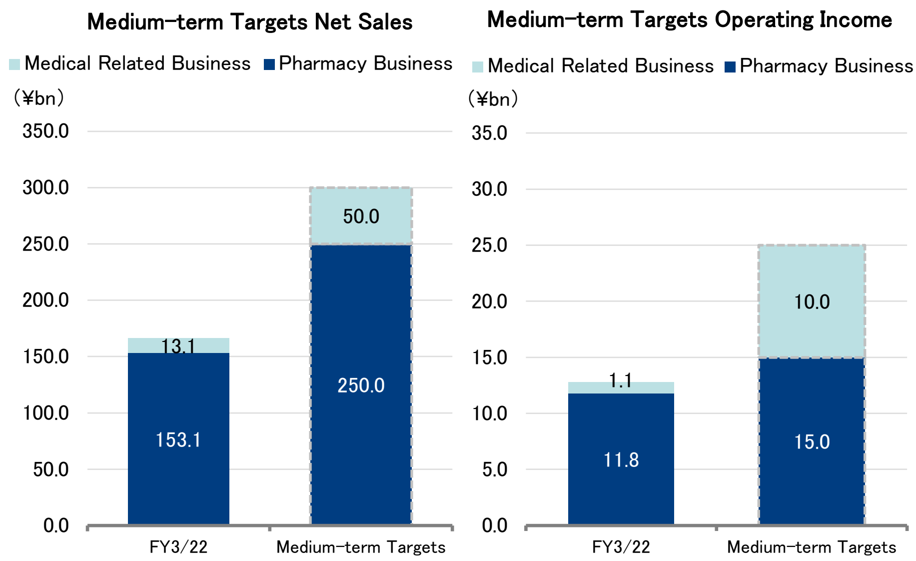
Pharmacy Business and Medical Related Business to expand as the Company aims at achieving the medium-term targets of net sales of ¥300bn and operating income of ¥25bn

1. Overview of the medium-term growth strategy

The Company's medium-term targets and growth strategies to achieve them have remained consistent and unchanged. The medium-term targets are net sales of ¥300bn and operating income of ¥25bn. By business segment, the target for the Pharmacy Business is net sales of ¥250bn, 1.6 times more than FY3/22 and operating income of ¥15bn, 1.3 times, and net sales of ¥50bn for the Medical Related Business, 3.7 times greater than FY3/22 and operating income of ¥10bn, 8.4 times.

For operating income, simple comparisons cannot be made because the holding company and common expenses are not taken into account, but the Pharmacy Business seems to be within range of achieving its target. On the other hand, in the Medical Related Business there is a significant divergence between net sales and operating income and the targets for both, and strategies for each of its businesses will be needed, including consideration of M&A. As a breakdown of the net sales of ¥50bn for the Medical Related Business, the forecast is for the CSO Business and CRO Business and Medical Professional Referral Dispatch Business to achieve a combined ¥20bn and the Pharmaceutical Manufacturing Business and other businesses to make ¥30bn. The strategy is to steadily grow the Pharmacy Business and expand the size and improve the profitability of the Medical Related Business to build a balanced earnings portfolio in the future.

Medium-term targets and ideal business portfolio



Source: Prepared by FISCO from the Company's results briefing materials

The growth strategy for the Pharmacy Business is based on the twin axis of 1) expanding scale through strategic openings; and 2) creating value of pharmacies, with the priority measures for FY3/23 given the themes of strengthening the Home and Facility Delivery Dispensing Business and promoting DX. For the Medical Related Business, the strategy is to achieve high growth by deepening specialization and maximizing Group synergies.

Growth strategies of each business segment and progress are as follows.

In the Pharmacy Business, the Company will focus mainly on expanding the number of stores and strengthening Home and Facility Delivery Dispensing Business, as well as strengthening differentiation and earning capability through promotion of DX

2. Pharmacy Business growth strategy and progress

In the Pharmacy Business, the Company is aiming for growth through the basic strategy of expanding scale through strategic store openings and creating value of pharmacies.

(1) Expanding scale through strategic store openings

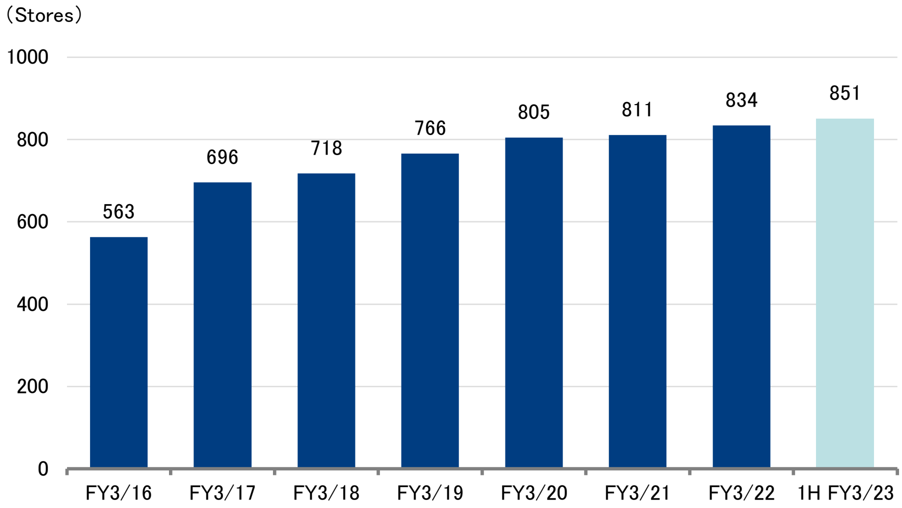
Regarding the number of stores, the Company's target for the time being is to have 1,000 stores though 10 to 20 organic openings yearly and by acquiring 30 to 70 annually stores through M&A. Initially, this achievement was targeted for FY3/23, but as the COVID-19 pandemic has slowed the pace of M&A, the Company expects to achieve its aim by about FY3/25 if maintaining the current pace (or earlier if it is possible to achieve a large-scale M&A). The Company will target openings for areas with large populations, such as the three major metropolitan areas and efficiently expand the number of stores through dominant openings. Similarly for M&A, its policy is to move ahead in main urban areas where it is easy to collaborate with communities.

As for the store format, it continues to open "One-on-one pharmacies" that are its strength and target the same model in M&A. The number of Healthcare pharmacies from alliances with companies in different industries was 45 as of October 30, 2022. Breaking this down, 36 were collaborative stores with Lawson, 5 were pharmacies within BIC CAMERA stores, 2 were pharmacies within MUJI stores and 2 were pharmacies within stations. Among these, due to the improved recognition of the mainstay collaborative stores with Lawson, profitability is also improving. Going forward, the Company will focus on these as a differentiation strategy during the expansion of the Home and Facility Delivery Dispensing Business. Specifically, in combination with visiting drug administration guidance, it has started mobile sales services that deliver OTC drugs and other products to customers' orders for senior facilities such as paid nursing care homes, and having apparently received positive feedback, will expand this service. The services offer high convenience to users by enabling them to purchase daily necessities together with pharmaceutical products, which is a factor that differentiates the Company from its competitors. The opening of the "Machi no Hokenshitsu" store inside a MUJI store has become a distinctive feature of the community-based store, and the Company will increase these openings in the future based on needs.

In other strategic store openings, the Company's policy is to bolster openings of pharmacies specialized for Home and Facility Delivery Dispensing Business, aiming to provide the enhancement of community healthcare called for by the arrival of the super-aging society. Currently, the Company operates a total of 15 such stores, comprising 5 stores with a focus on Home and Facility Delivery Dispensing Business and 10 that specialize in it. The Company will expand the number to 50 stores over the coming years. Within a 16 km radius, which is the condition for medical service fees for pharmaceutical management in home medical care, the Company is expected to have stable sales through agreements with multiple institutions, such as nursing care facilities. At the initial stage of opening such stores, there are upfront costs, as such stores require slightly larger initial investment, such as providing dedicated inventory for at-home and in-facility patients. However, the unit price for prescriptions is around 1.5 times higher (approximately ¥9,500) on average since the medical service fee for pharmaceutical management in home medical care* is added on top. This means that stores become highly profitable if they can secure a number of contracting facilities. In addition, in 2023 also, the media has reported that Amazon Japan G.K. is looking at entering the online pharmacy business, and this could be a counter strategy for this. The company opened its first specialized store (Shakujii Park Store) in 2020, and it has already turned a profit. Looking ahead, the Company is expected to proceed with opening stores in cities that have a minimum level of facilities for elderly people, such as nursing care facilities, present in them.

* Medical service fees for pharmaceutical management in home medical care are added in the amounts of ¥6,500 for one patient in a single building, ¥3,200 for two to nine patients, and ¥2,900 for ten or more patients (up to four times per person per month (for patients with terminal malignant tumors and so forth, twice a week or eight times a month)). There is also an additional ¥150 home visit drug dispensing premium.

Trends in the number of stores

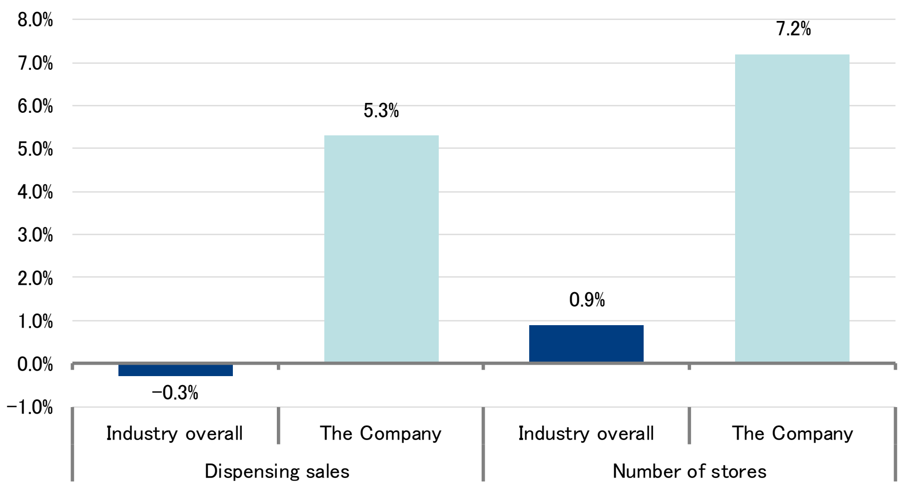


Source: Prepared by FISCO from the Company's results briefing materials

In the dispensing pharmacy industry, in addition to the lifting of the ban on online drug administration guidance in 2020 and the introduction of the authorization system for pharmacies with specific functions in August 2021, electronic prescriptions are scheduled to begin operation from 2023. Looking ahead, as an even greater degree of DX will be required in pharmacy operations, building such systems will require capital capabilities above a certain level, and this is one factor supporting the view that the industry will increasingly become an oligopoly dominated by major corporations. Furthermore, there are approximately 60,000 dispensing pharmacies nationwide, with a market scale of approximately ¥7.7tn in FY3/22. Compared to FY3/16 (market scale ¥7.8tn, number of pharmacies 58,000), the market scale has effectively topped out due to the impact of reducing drug prices, while the number of pharmacies is increasing, albeit slightly, partly due to the opening of drug stores, leading to a more competitive environment.

In this environment, major dispensing pharmacies continue sales growth through expanding the number of stores by organic openings and M&A. The Company is one such company, and the CAGR from FY3/16 to FY3/22 shows dispensing sales grew 5.3% and the number of stores by 7.2%, which significantly exceeds the growth rate of the industry as a whole (dispensing sales -0.3%, number of pharmacies 0.9%). Currently, the total sales of the 10 leading companies in the dispensing pharmacy market are around ¥1.4tn, which converts to a market share of only approximately 19%. Considering that the top 10 companies in the drugstore industry currently have a share of more than 70%, it is highly likely that the major players in the dispensing pharmacy industry will proceed to form an oligopoly going forward. The Company's strategy of expanding store openings, both organically and through M&A, makes sense and we at FISCO believe it is possible for the Company to achieve sustainable growth through the medium-term expansion of store numbers. The Company judges whether or not to conduct an M&A based on strict in-house standards, including the scales of sales, whether or not synergetic effects will be generated, and the investment recovery period.

FY3/16-FY3/22 CAGR



*Number of Qol stores excludes sales stores
Source: Prepared by FISCO from the MHLW's "Trends of Medical Prescription Fees (Computerized Data) in FY2020"

(2) Creating value of pharmacies

As its measures for creating value of pharmacies, the Company has been creating pharmacies that offer high quality sought by the public. For example, as of November 2022, the Company has 157 authorized "health-support pharmacies," which can not only function as primary pharmacies for local communities, but also provide various health-related consultations on matters such as OTC drugs, nursing care, and diet and nutrition. Under the authorization system for pharmacies with specific functions introduced in August 2021, the company has 148 community cooperative pharmacies*1 and 9 pharmacies in cooperation with specialized medical institutions.*2 The system is intended to respond to home medical care, which is becoming an issue in anticipation of the coming super-aging society, and as one of the measures to establish the regional comprehensive care system concept, which includes medical care and nursing care, and to enable patients themselves to choose the pharmacy that is best suited to them.

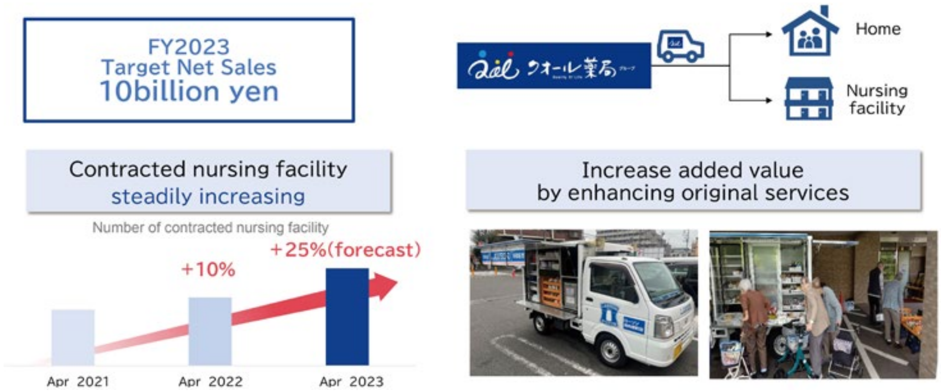
*1 Pharmacies that can respond to hospital admissions and discharges and home medical care in coordination with other medical provider facilities.
*2 Pharmacies that can respond to specialized pharmaceutical management for cancer and other diseases in coordination with other medical provider facilities.

Although profits have currently not been directly impacted by the introduction of this system, we at FISCO believe that there is a possibility of an impact on the calculation of dispensing pharmacy's technical fees when the revisions to dispensing fees are carried out in two years' time. Because of this, the Company plans to move ahead on acquiring authorization going forward. In the future it plans to have all pharmacies receive authorization as either a community cooperative pharmacy or pharmacy in cooperation with specialized medical institutions.

In FY3/23, the Company is also taking measures based on the priority measures of strengthening the Home and Facility Delivery Dispensing Business and promoting DX. According to materials produced by the Ministry of Health, Labour and Welfare, the current home and facility delivery dispensing market scale is estimated to be about ¥310bn, with around 290,000 users. This is still only a small share of the overall dispensing market at around 4%, but from 2025 onward, as the baby boomer generation reaches the age of 75, demand is expected to grow further for at-home medical and nursing care services, and the home and facility delivery dispensing pharmacy market is also expected to continue a period of high growth. Looking ahead, the Company's policy is to focus on both facilities and on individual homes.

As a differentiation strategy for home and facility delivery dispensing, the Company is engaged in working to increase quality through measures such as introducing and utilizing the latest dispensing equipment, introducing barcode management as a countermeasure for preventing administration of the wrong drug, supporting infection-prevention measures, and providing nutrition support by nutritionists. In addition, the Company also aims to grow by providing efficient services for facilities through the opening of pharmacies that specialize in home and facility delivery dispensing and developing original services such as mobile sales services through an alliance with Lawson. The sales target for the Home and Facility Delivery Dispensing Business is ¥10bn in FY3/24, and the Company is forecasting a 25% increase in the number of contracted nursing care facilities compared to April 2021.

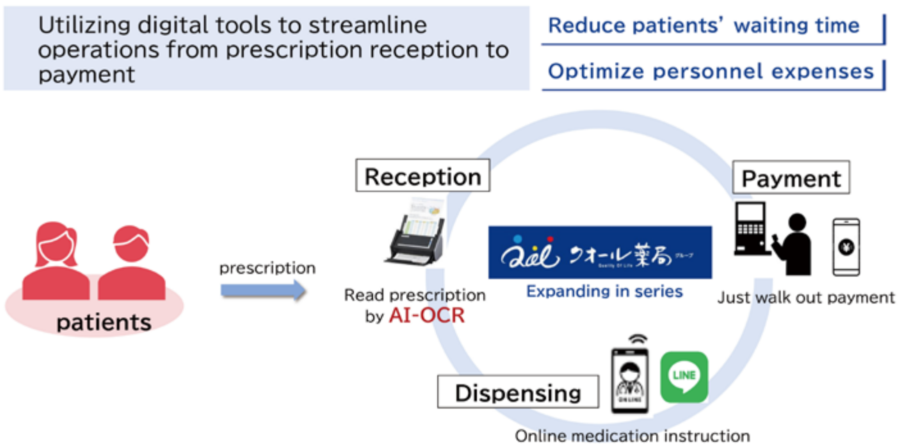
Home and Facility Delivery Dispensing Business



Source: The Company's results briefing materials

Meanwhile, on the other priority measures, promoting DX, the Company is working not only to streamline operations inside pharmacies through the utilization of IT, but also to expand provision of services which lead to shorter waiting times and greater convenience for users by utilizing its LINE official account. Specifically, in April 2022, the Company launched an advanced reservation prescription service using its official LINE account and is also steadily expanding services such as same-day delivery functions, online medicine administration guidance and an automatic data link function with prescription records, etc. These initiatives will help to retain customers by increasing user convenience and lead to an increase in the number of prescriptions. The Company is also currently developing an automatic function for reading prescriptions sent in via LINE. The number of prescriptions handled online has increased two-fold in the year from September 2021 to September 2022, and the Company's strategy is to continue enhancing service functions while retaining customers and expanding sales.

Increase in pharmacy productivity using digital technology



Source: The Company's results briefing materials

CMR dispatches is focusing on the pursuit of specialization and expanding market share, the Medical Professional Referral Dispatch Business is expanding areas, and the Pharmaceutical Manufacturing Business is aiming for high growth by utilizing Group synergies

3. Medical Related Business growth strategy and progress

The Company calls for deepening specialization and maximizing Group synergies as a growth strategy in the Medical Related Business with a policy of expanding sales scale and raising profitability.

(1) CSO Business

The current understanding of the CMR market in the CSO Business is that the main focus of new drugs shifted from primary medicine (drugs for treatment of lifestyle related diseases, etc.) that targets many customers (medical facilities and doctors) to specialty drugs (anti-cancer drugs, etc.) for which the target customers are limited. Amid that shift, the trend of pharmaceutical companies reducing their MR personnel is expected to continue. Meanwhile, demand is growing for highly specialized MR and MR with high IT literacy, and demand for highly specialized CMRs is expected to be solid in such an environment.

Actually, according to the “2022 Edition MR White Paper,” the number of MR personnel in Japan peaked at 65,000 in fiscal 2013 and continues on a decreasing trend, reaching 51,000 in fiscal 2021. On the other hand, according to the “2021 Summary of the CSO Business in Japan” by the Japan Contract Sales Organization Association, the number of working CMRs peaked at 4,148 people in 2014 and declined to 3,110 in 2018, but has since reverted to increasing and in 2021 was 3,424 people. CMRs accounted for 5.0% of all MRs in 2018, and the ratio rose to the highest level on record at 6.4% in 2021. In the United States, which is an advanced country for CMRs, the CMR ratio is 11.2%, while in the United Kingdom it is 14.0%, both in the 10% range. Considering this, there appears to be ample potential for the CMR ratio to increase further in Japan going forward. Nevertheless, considering that there are around 6,500 CMRs among the US population of 58,000 MRs, there is not as much room to increase in terms of absolute numbers, and the demand for specialized CMR human resources is predicted to grow going forward.

Given this situation, the Company’s strategy is to focus on recruitment and training of CMRs specifically for specialized fields where demand is expected to grow and CMRs who are able to cover a wide range of areas, and to aim for growth by expanding its industry share, including through M&As. Specifically, the Company is aiming to increase the number of CMR personnel from the current approximately 600 to 1,000 people and lift its industry share from approximately 15% currently to over 20%. One advantage of the Company’s CSO Business is that it boasts the best staff formation in the industry, with 20 people who conduct MR training. It has a robust educational curriculum that broadly covers everything from basic areas to advanced specialties. In particular, there has recently been strong needs in such fields as oncology, inflammatory bowel disease, central nervous system diseases and COVID-19, and the Company’s expertise in training CMRs in these specialized fields can be considered a strength. In addition, in the CRO Business as well, the Company’s policy is to capture orders in the food field where it has strength, and to promote strengthening of other highly specialized fields.

(2) Medical Professional Referral Dispatch Business

In the Medical Professional Referral Dispatch Business, in addition to expanding dispatch services for medical professionals such as pharmacists, public health nurses and registered sales personnel, the Company is seeking to expand its service lineup to such areas as consulting for business succession for pharmacies and for matters related to health and productivity management for corporations, and its strategy for the future is to diversify its medical professional service and expand the scale of its business by leveraging M&A and the like.

(3) Pharmaceutical Manufacturing Business

The Company decided to enter the Pharmaceutical Manufacturing Business with the aim of becoming a comprehensive healthcare company. Besides being a top-class dispensing pharmacy chain in Japan, it dispatches CMRs for pharmaceutical sales in CSO Business and supports drug R&D activities in CRO Business, etc. By entering the Pharmaceutical Manufacturing Business, the Company is able to provide seamless service in the healthcare field that begins with R&D and extends to manufacturing, sales, dispensing, and services for patients.

For Group synergies, the Company is increasing the number of pharmacies among the Group's dispensing pharmacies that handle products from Fujinaga Pharm. Looking ahead, the Company's strategy is to expand business through capital investment in plants and advancing M&A and the like, while also conducting outsourced manufacturing from major pharmaceutical companies as the next step. Sales scale in FY3/22 were still modest at around ¥2bn, but the Company aims to achieve ¥30bn in the medium term by executing these strategies, and trends going forward will be closely watched.

Income statement and main indicators

(¥mn)

	FY3/19	FY3/20	FY3/21	FY3/22	1H FY3/23
Net sales	144,783	165,411	161,832	166,199	82,459
YoY	-0.5%	14.2%	-2.2%	2.7%	0.8%
Gross profit	17,863	21,094	21,102	23,163	10,856
Gross margin	12.3%	12.8%	13.0%	13.9%	13.2%
SG&A expenses	10,812	13,361	13,737	13,308	6,834
SG&A expense ratio	7.5%	8.1%	8.5%	8.0%	8.3%
Operating income	7,050	7,733	7,364	9,855	4,022
YoY	-22.4%	9.7%	-4.8%	33.8%	-3.7%
Operating margin	4.9%	4.7%	4.6%	5.9%	4.9%
Ordinary income	7,208	8,024	7,403	10,094	4,174
YoY	-22.8%	11.3%	-7.7%	36.4%	-2.3%
Profit attributable to owners of parent	3,908	4,067	3,365	5,489	2,366
YoY	-21.6%	4.1%	-17.3%	63.1%	-3.6%
Split-adjusted EPS (¥)	101.73	107.23	89.55	149.51	64.11
Split-adjusted dividend (¥)	28.00	28.00	28.00	28.00	15.00
Split-adjusted BPS (¥)	1,006.55	1,074.57	1,124.31	1,189.70	1,240.57

Source: Prepared by FISCO from the Company's financial results and supplemental results materials

Simplified balance sheet

(¥mn)

	FY3/20	FY3/21	FY3/22	1H FY3/23	Change
Current assets	45,881	45,499	42,296	37,943	-4,353
Cash and deposits	15,802	19,648	16,685	14,492	-2,193
Notes and accounts receivable-trade, and contract assets	22,862	18,231	17,382	15,260	-2,122
Inventories	5,224	4,854	5,582	5,402	-179
Noncurrent assets	56,976	55,062	53,682	53,080	-602
Property, plant and equipment	13,055	12,730	12,846	13,621	775
Intangible assets	36,642	34,938	33,238	31,806	-1,432
Investments and other assets	7,278	7,393	7,598	7,652	54
Deferred assets	14	9	4	2	-1
Total assets	102,872	100,571	95,984	91,027	-4,957
Current liabilities	38,730	38,709	35,460	31,958	-3,502
Short-term interest-bearing debt	11,626	11,569	8,722	7,662	-1,060
Noncurrent liabilities	23,139	20,026	16,642	13,149	-3,492
Long-term interest-bearing debt	21,024	18,152	14,560	10,618	-3,942
Total liabilities	61,870	58,736	52,103	45,108	-6,995
Total net assets	41,001	41,834	43,881	45,918	2,037
Total liabilities and net assets	102,872	100,571	95,984	91,027	-4,957

Source: Prepared by FISCO from the Company's financial results and supplemental results materials

Cash flow statement

(¥mn)

	FY3/20	FY3/21	FY3/22	1H FY3/23
Cash flow from operating activities	4,468	12,912	10,112	4,711
Cash flow from investing activities	-8,670	-3,065	-3,087	-1,681
Cash flow from financing activities	-225	-6,114	-10,006	-5,223
Cash and cash equivalents at the end of the period	15,766	19,498	16,516	14,323

Source: Prepared by FISCO from the Company's financial results

Returns to shareholders and SDGs initiatives

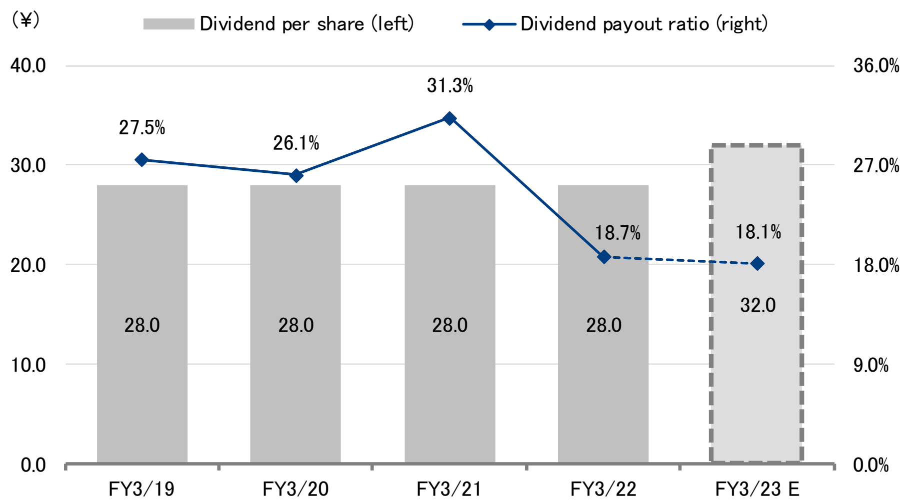
Basic policy is to stable returns to shareholders, as well as introducing shareholder benefits program

1. Shareholder return policy

Its basic policy is to pay stable return of profits to shareholders while also giving consideration to internal reserves for future business development and reinforcement of its management foundation. It does not set an official payout ratio or other standards on dividend. Also, in order to execute a flexible capital policy, the Company considers acquisitions of treasury shares when necessary. Based on this basic policy, in FY3/23, the Company is planning a dividend per share of ¥32 (dividend payout ratio of 18.1%), an increase of ¥4 per share compared to the previous fiscal year. In conjunction with the increase in its retained earnings due to the growth of its results, the Company plans to increase the ordinary dividend by ¥2 per share in addition to paying a commemorative dividend of ¥2 per share to mark the 30th anniversary of foundation in October 2022. The Company has indicated that it intends to maintain the dividend level in FY3/24.

The Company has also introduced a shareholder benefits program. Shareholders registered at the end of March in each year are eligible for the program. Looking at the example of shareholders holding 1 unit of 100 shares, they receive a catalog gift worth ¥3,000 if they have held the shares for less than 1 year, and worth ¥5,000 if held for 1 year or longer. On calculating the investment yield which combines the dividend and shareholder benefits based on the closing share price on November 18 (¥1,158), it is 5.4% if the shares were held for less than 1 year and 7.1% if held for 1 year or longer.

Dividend per share and dividend payout ratio



Source: Prepared by FISCO from the Company's financial results

Content of shareholder benefits

Sustained ownership period	Number of shares owned	
	100-499 shares	500 shares or more
Less than a year	Catalog gifts worth ¥3,000	Catalog gifts worth ¥5,000
One year or longer	Catalog gifts worth ¥5,000	Catalog gifts worth ¥7,000

Source: Prepared by FISCO from the Company's website

2. Initiatives for SDGs

Regarding initiatives for SDGs, the Company established a Sustainability Committee in May 2022, appointing the president and representative director as chair, as an advisory body to the Board of Directors to strengthen activities related to the Group's sustainability. Going forward, the Company plans to move ahead on such activities as sustainability trend surveys, proposals for sustainability-related management strategies, reviews of important issue (materiality), monitoring of progress status and evaluation of achievement status.

As examples of sustainability initiatives, the entire Group is conducting a store greening campaign for store beautification and to promote SDGs. In addition, it has concluded a partnership agreement with the Japan Inclusive Football Federation to support inclusive football associations and soccer teams through lectures and dietary and nutritional consultation given by sports pharmacists with highly advanced specialist knowledge and registered dieticians. Moreover, the Company established Qol Assist Co., Ltd. in 2009, the industry's first special subsidiary with the objective of promoting employment for people with disabilities, and currently more than 50 employees are active in the company, centered on people with severe disabilities engaged in home-based employment.

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