Shiseido Company, Limited

2024 First Half Results (January-June)

August 7, 2024

Event Summary

[Company Name]	Shiseido Company, Limited
[Company ID]	4911-QCODE
[Event Language]	JPN
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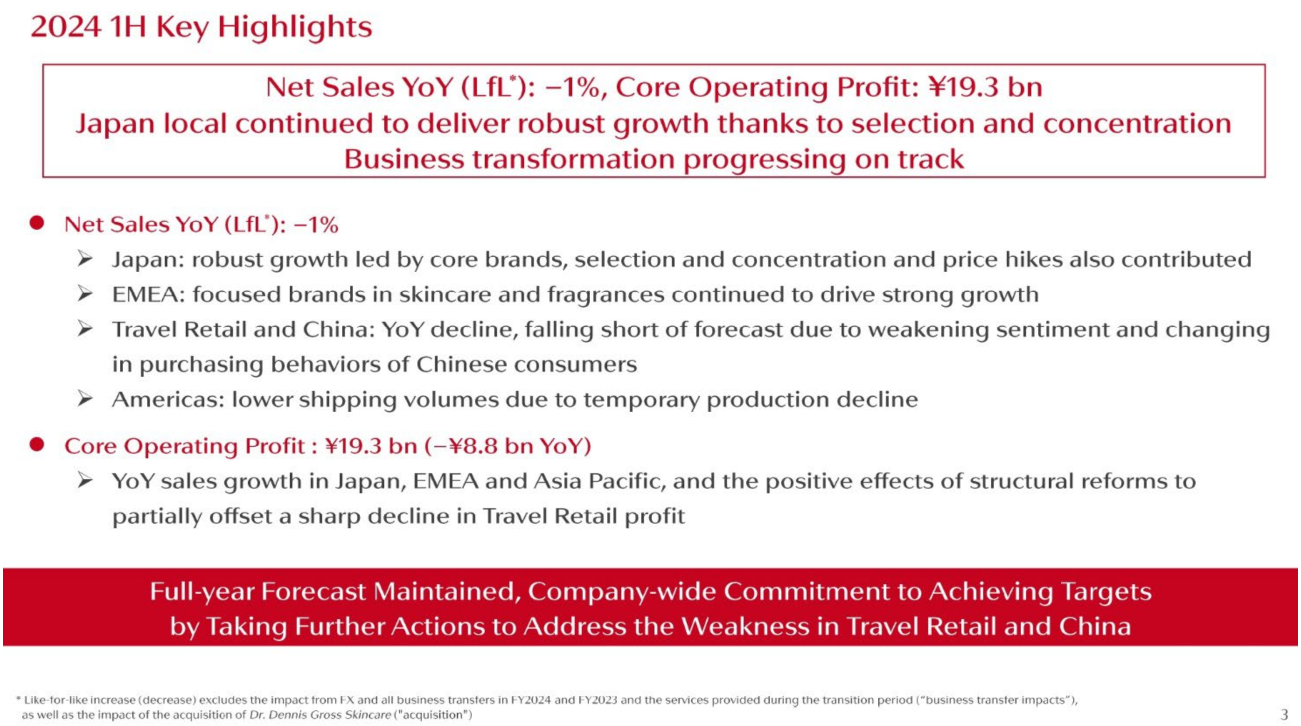
[Event Name]	2024 First Half Results (January-June)
[Fiscal Period]	FY2024 Q2
[Date]	August 7, 2024
[Time]	17:40 – 18:43 (Total: 63 minutes, Presentation: 27 minutes, Q&A: 36 minutes)
[Venue]	Webcast
[Number of Speakers]	4

Kentaro Fujiwara	President and COO
Ayako Hirofuji	Chief Financial Officer
Toshinobu Umetsu	China Region CEO
Yuki Oshima	Vice President, Investor Relations Department

Presentation



Hirofuji: Now, I would like to explain the results for H1 of 2024. Please take a look at page three. First, H1 2024 results. The consolidated net sales for like-for-like basis, excluding the impact of foreign exchange and business transfers, were down 4% in three months from April to June and down 1% in H1. In Japan local, sales continued to grow strongly led by core brands, thanks to tactical investments through selection and concentration. Similarly, in EMEA, strategic investment in focus areas have helped to maintain strong growth in both skincare and fragrances. On the other hand, in the Travel Retail and China, weakening Chinese consumer sentiment and changes in their purchasing behavior were seen as risks in Q1 which became apparent, posting a deeper-than-expected negative results. In the Americas, sales decreased due to lower shipping volumes due to a temporary production decline.

Core operating profit was JPY19.3 billion, a decrease of JPY8.8 billion YoY due to the significant impact of lower profit from Travel Retail, although the decrease was partially offset by a positive impact of fixed cost reduction through structural reforms as well as YoY sales growth in Japan, EMEA and Asia Pacific.

While we are increasingly challenged by the current situation, the full-year forecast remains unchanged. We will take additional company-wide measures to address the weakness in Travel Retail in China and continue to aim to achieve JPY55 billion in core operating profit.

Full-year Forecast Maintained, Company-wide Commitment to Achieving Targets

Strengthen actions aligned with dynamic changes in Chinese consumption
Ensuring profit delivery for medium to long-term success

- ⊖ Sharp deceleration in Travel Retail profitability on the back of changing in purchasing behaviors and weakening sentiment of Chinese consumers
- ⊕ Capture growing demand of Japan inbound tourists
- ⊕ Maximize sales by leveraging the strength of Japan local and EMEA
- ⊕ Further actions added to global cost reduction and profit maximization strategies
- ± FX impact

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H1 results were below expectations for both sales and profit. In Chinese market, due to uncertainty over employment and future drives consumer sentiment for less spending and more savings. This has resulted in a change in purchasing behavior and weakening consumer confidence leading to a significant slowdown in Travel Retail and China. Particularly, since the Travel Retail has high profitability, the decline in sales has also led to a significant drop in profits, deteriorating the so-called regional mix to push down overall profits. However, this volatility in the Chinese market is not a new phenomenon. In order to protect current profits amid this volatility, we will further strengthen measures based on the right understanding of market realities and also promptly formulate and take additional medium- to long-term strategic actions to improve profitability and address fundamental issues. The current negative impact on profits in Travel Retail will be compensated by maximizing the strong local sales in Japan and EMEA, capturing demand from inbound tourists to Japan and company-wide efforts to improve profitability and so on and so forth to achieve our full-year forecast.

2024 1H: Executive Summary

(Billion yen)	2023	% of Net Sales	2024	% of Net Sales	YoY Change	YoY Change %	YoY FX-Neutral %	YoY LfL %[*2]
Net Sales	494.2	100%	508.5	100%	+14.3	+2.9%	−4.1%	−0.5%
Core Operating Profit	28.0	5.7%	19.3	3.8%	−8.8	−31.3%		
Non-recurring Items	−14.4	−2.9%	−22.0	−4.3%	−7.6	-		
Operating Profit	13.6	2.8%	−2.7	−0.5%	−16.4	-		
Profit Before Tax	15.4	3.1%	4.2	0.8%	−11.2	−72.7%		
Income Tax Expense	3.0	0.6%	4.0	0.8%	+1.0	+34.7%		
Profit Attributable to Owners of Parent	11.8	2.4%	0.0	0.0%	−11.7	−99.9%		
EBITDA[*1]	53.2	10.8%	45.5	8.9%	−7.8	−14.6%		

Net Sales:	YoY (LfL[*2]) −0.5%	Japan local continued to drive robust growth from core brands EMEA and Asia Pacific also maintained steady performance Overall, sales declined YoY due to negative growth in Travel Retail, China, and Americas
Core Operating Profit:	YoY −¥8.8 bn	YoY sales growth in Japan, EMEA and Asia Pacific, and the positive effects of structural reforms to partially offset a sharp decline in Travel Retail profit
Non-recurring Items:	2024 −¥22.0 bn	Recognition of structural reform expenses, etc. primarily in Japan and China
EBITDA Margin:	8.9%	

*1 Core Operating Profit+Depreciation and Amortization (excl. depreciation of right-of-use assets) *2 Excluding impacts from FX, business transfer and acquisition

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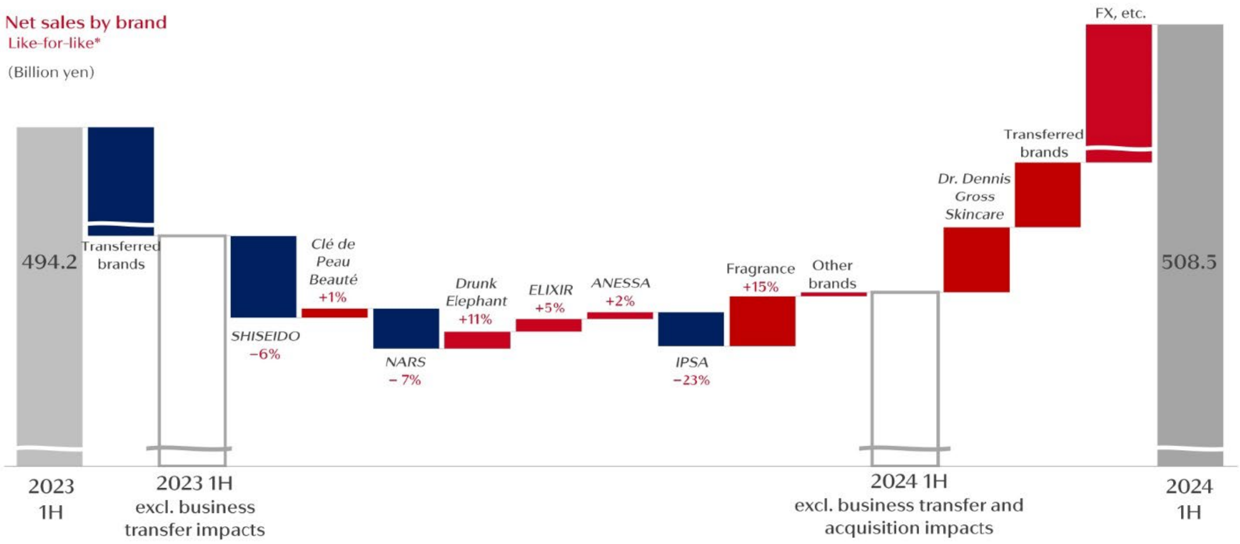
Now page 5, PL summary. Like-for-like net sales and core operating profit are as explained earlier. Operating profit was minus JPY2.7 billion, a decrease of JPY16.4 billion from the previous year. In addition to the decline in core operating profit, non-recurring items were as large as JPY22 billion. The breakdown of non-recurring items of JPY22 billion includes restructuring costs of JPY20.1 billion recognized in Q1 associated primarily with Early Retirement Incentive Plan (ERIP) in Japan. The main items of JPY1.9 billion in Q2 includes restructuring costs related to organizational optimization and store closures in China. Full-year non-recurring items planned at the beginning of the year is JPY30 billion, and there is no significant deviation from this forecast. Profit attributable to owners of the parent decreased JPY11.7 billion to JPY0 billion from the previous year. In Q1, the Company was in the red with profit decline due to a provision of the ERIP. But in Q2, it has returned to the black with profit increase.

Now, you may not be familiar with the term "Interim profit", but there has been a change in the term in compliance with the FIEA, and there is no change in the actual definition or meaning of the previous term "Quarterly profit."

In terms of cash generation capability, EBITDA margin was 8.9%.

Fragrance and *Drunk Elephant* Remained Solid with Strength in EMEA; Sales Stalled Across Other Key Brands, Posting Negative to Single Digit Growth due to Weakness in Travel Retail, China, and Americas



* YoY change (%) for each brand is calculated based on foreign exchange rate assumptions as at the beginning of FY2024, and excludes exchange rate differences, etc.

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Next, page 6 shows H1 sales results by brand. Our fragrance brands led by Narciso Rodriguez and Drunk Elephant continued to perform well, especially in EMEA. On the other hand, all other core brands delivered lower sales or only single-digit growth due to the weakness in the Travel Retail, China and Americas. Brand SHSEIDO was also down 6% globally due to lower sales in China. Conversely, Cle de Peau Beaute which has a large exposure to China like SHISEIDO delivered a year-on-year growth in consolidated sales while maintaining positive growth in China by leveraging the strengths of the high prestige and luxury markets. NARS suffered a sales decline in Travel Retail Asia and lower shipping volumes in the Americas.

Especially from this fiscal year, performance tend to vary depending on the balance of regional sales composition in each brand. However, our strategy to invest in our core brands to nurture brand value remains unchanged. In particular, we will significantly invest in marketing for the SHISEIDO in China, and in the Americas, where sales declined sharply in Q2 so as to win back the consumers and regain our business through strategic marketing investments.

Net Sales: Remained Almost Flat YoY in 2024 1H
Japan and EMEA Achieved Double-digit Growth Offset by Negative Growth in Travel Retail, China, and Americas

	2023 (vs. 2022)					2024 (vs. 2023)		
Like-for-like*	Q1	Q2	Q3	Q4	FY	Q1	Q2	1H
Japan	+8%	+9%	+6%	+17%	+10%	+20%	+7%	+13%
China	−3%	+20%	−9%	−21%	−5%	−3%	−9%	−7%
Asia Pacific	+16%	+12%	+15%	+8%	+13%	+5%	+7%	+6%
Americas	+30%	+18%	+10%	+9%	+15%	+9%	−20%	−5%
EMEA	+22%	+11%	+15%	+26%	+19%	+17%	+6%	+12%
Travel Retail	−4%	−4%	−25%	−43%	−20%	−31%	−15%	−23%
Total	+7%	+10%	−2%	−6%	+2%	+3%	−4%	−1%

* Excluding impacts from FX, business transfer and acquisition

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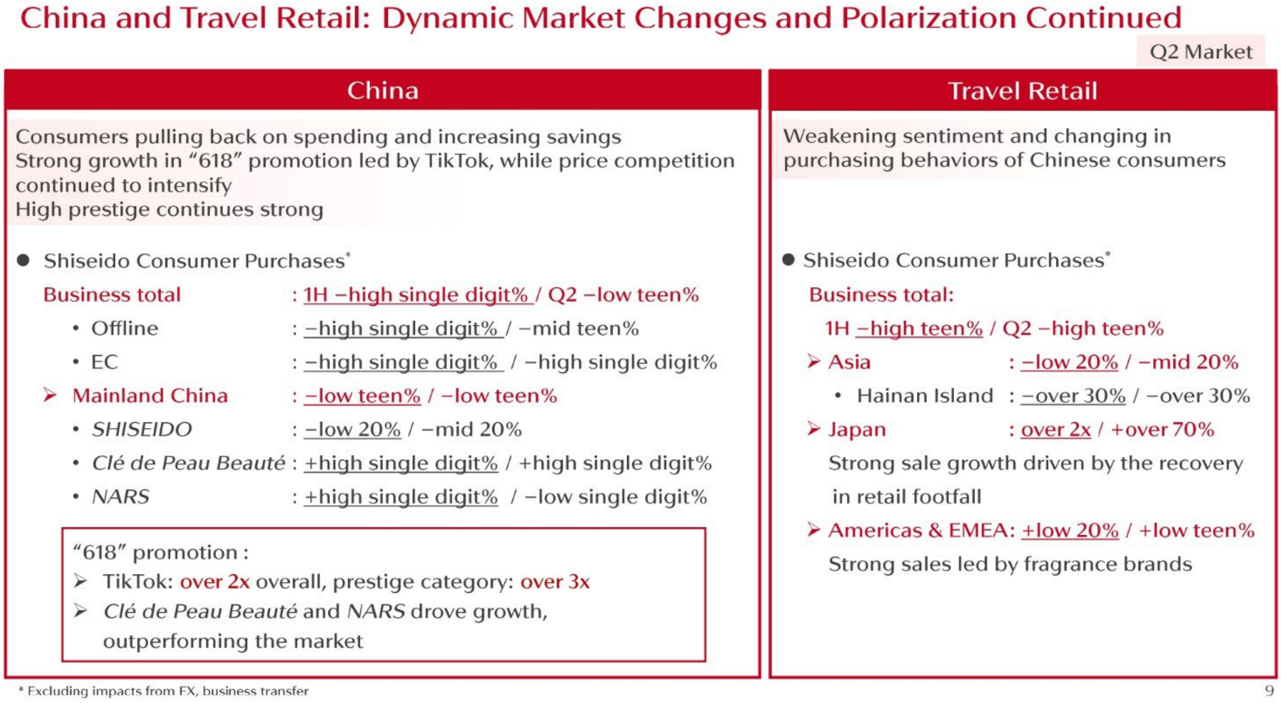
Next on page 7, trends in net sales. In H1 we achieved double-digit growth in Japan and EMEA, but posted a year-on-year decline overall, negatively impacted by lower sales in Travel Retail, China and the Americas. Japan maintained strong momentum with growth of 7% in Q2. While the pace of growth decelerated from +20% in Q1, it was in line with our expectations as there was a rush demand before the price hike in Q1. Actually, we are encouraged by achieving a year-on-year growth of 7% in Q2 and 13% in H1 despite the pullback after the price increase.

Similarly, EMEA maintained double-digit growth in H1 despite the pullback in Q2 due to the advanced shipment in Q1 for the IT system implementation.

In China and Travel Retail, we had anticipated negative growth in Q2, even in our initial plan, due to the high hurdles of the previous year, but the negative growth was deeper than expected due to the changes in China market.

In the Americas, no change in the annual sales plan despite the temporary decline in sales as we expect a turnaround in H2.

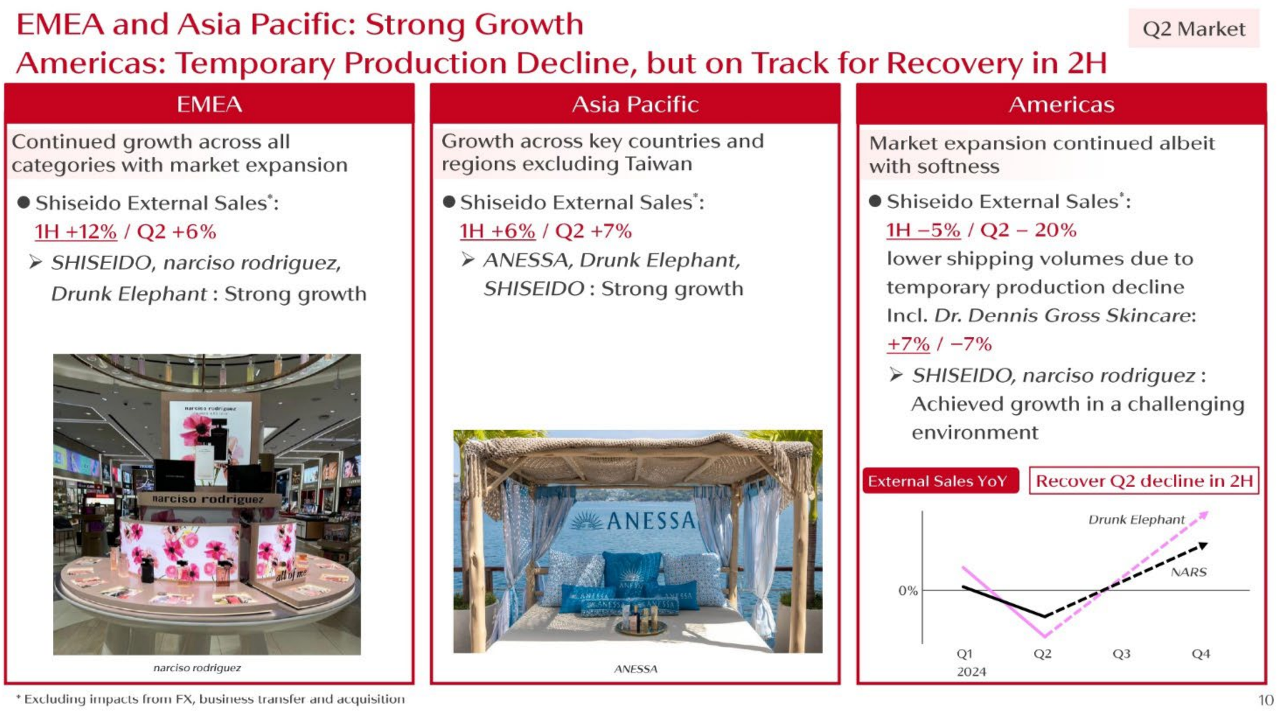
Page 8 is about the Japan Business. The Japan local market maintained growth in Q2, although the pace has decelerated from Q1 due to a high comparison base in the previous year with the downgrade of COVID-19 to Class 5 in May 2023, so we maintained solid trend. In particular, the mid-price range, our largest market, delivered strong growth ahead of the market. The number of inbound tourists to Japan has already surpassed the pre-COV1D-19 level of 2019. While the number of Chinese tourists is still 26% below the level of 2019, our Japan Business continues to see a strong growth in core brands with high teen% and hero products +over 30%, steadily contributing to overall share expansion. The key core brands, Shiseido, Cle de Peau Beaute, and Elixir also drove robust growth on the back of a steady increase in loyal users, increasing their shares in the local market. E-commerce sales also grew at an accelerated pace with over 30% increase in Q2. For inbound, sales growth slowed down in Q2. Although the initially projected annual growth rate of 60% YoY is difficult to achieve, we will make up for this by increasing sales in the local business, which is performing strongly.



Next is page 9, about China and Travel Retail. For the China market, market maturity is progressing amid rising economic uncertainty, resulting in trend for consumers to seek better quality at a more reasonable price. As a result, the discount ratio is getting higher than ever, turning the whole market into price competition. Even in such environment, our policy to avoid being dependent on excessive discounting remain unchanged, and we will continue to strengthen our ability to drive sales by leveraging brand value and not pricing.

As for performance by brand, Cle de Peau Beaute and NARS realized high single digit growth in H1. The high-end categories known as high prestige or luxury continues to perform well. On the other hand, since the treated water impact, brand SHISEIDO is struggling especially and there is a sense of urgency to make a turnaround for the business.

Travel Retail is also facing a difficult situation affected by weakening Chinese consumer sentiment as in the China market. Also, the Travel Retail's price appeal to consumer is diminishing due to the exchange rate fluctuation. In the previous earnings call, we have shared with you that the Travel Retail was expected to turn into positive in May, although the month of May alone was positive in terms of the actual performance of our external sales, although the numbers turned negative again in June, performing lower than expected. On the other hand, Travel Retail in Japan made a significant growth with a recovery in consumer traffic, and the Americas and EMEA achieved strong growth, driven primarily by fragrance brands.



Next is page 10. In the EMEA market continued to grow in all categories and we also delivered double-digit growth in H1, driven by SHISEIDO, Narciso Rodriguez and Drunk Elephant. Skincare and fragrances both benefited from strategic investments in key focus areas. We will continue to strengthen investment in focus areas in H2, including the new product launch for Issey Miyake.

In the countries and regions of the Asia Pacific, the business was negatively impacted by the market slowdown in Taiwan and South Korea, but continued steady performance helped by the growth of other markets such as Thailand.

While we posted negative growth in the Americas, SHISEIDO and Narciso Rodriguez managed to deliver year-on-year revenue growth. Currently, both manufacturing and shipments are recovering and we expect to achieve our initial target on a full-year basis.

COGS Ratio : Steadily Improving as Business Transfer Impacts Diminish
COGS LfL[*1] Ratio: Improved from Q1 Thanks to Lower Inventory Write-offs, Mix Improvement, Price Hikes

	2023 1H	2023 Full Year	2024 1H
COGS	27.6%	26.7%	24.2%
COGS LfL[*1]	23.0%	23.1%	23.6%

1H YoY COGS analysis

(+) Price hike effect and mix improvement

(+) Decline of negative impact from MSA[*2] for business transfers (2023 3.7pts -> 2024 0.6pts)

(+) Impairment losses and structural reform expenses on transfer of Kuki Factory in 2023

(–) Lower production volume

*1 Excluding business transfer impacts and impairment loss, etc. *2 Manufacturing Service Agreement

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Next is page 11, COGS ratio. The bold line is the reported figures based on accounting policies while the dotted line is figures on a like-for-like basis. The one-off factors that had been pushing up the bold line for COGS, such as product supply due to business transfers, impairment loss and structural reform expenses associated with the factory transfer became much smaller this year. Therefore, we expect the gap between the bold line and dotted line will likely continue to narrow going forward.

The COGS on a like-for-like basis shown in the dotted line has steadily improved from Q1 to Q2, primarily attributable to the reduction of allowance for excess inventory write-offs, price hike impact, and the mix improvement driven by higher percentage of sales from skincare brands with high gross profit margins as sales in China tend to increase in Q2 compared to other quarters due in part to the seasonality effects including 618 promotion.

Posted YoY Decline in Profit: Higher Profits Driven by Sales Growth in Japan, EMEA and Asia Pacific, Structural Reforms, Agile Cost Management More Than Offset by Sharp Profit Decline in Travel Retail

Japan : Significant increase in profit, benefitting higher gross profit driven by sales growth with better mix and price hikes
China : Decline in profit partially offset by lower inventory write-offs and structural reform effects including fixed cost reduction
Asia Pacific : Increased by higher gross profit driven by sales growth
Americas: Declined due to lower gross profit driven by sales decline
EMEA: Increased by higher gross profit driven by sales growth
Travel Retail: Declined due to lower gross profit driven by sales decline
Other/ Adjustments: Lower gross profit due to decrease in intersegment sales to the Travel Retail and China, increase in elimination of unrealized profit

(Billion yen)

Core Operating Profit (Core OPM)	2023 1H		2024 1H		YoY
Japan	−3.7	(−2.9%)	7.9	(5.6%)	+11.6
China	5.5	(4.2%)	4.9	(3.7%)	−0.6
Asia Pacific	0.2	(0.7%)	2.2	(5.9%)	+2.0
Americas	4.1	(7.3%)	2.6	(4.3%)	−1.5
EMEA	1.3	(2.2%)	3.7	(5.6%)	+2.5
Travel Retail	15.4	(19.9%)	7.7	(11.5%)	−7.7
Other	−3.4	(−2.5%)	−9.0	(−7.0%)	−5.6
Adjustments	8.6	-	−0.9	-	−9.5
Total	28.0	(5.7%)	19.3	(3.8%)	−8.8

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Next is page 12, core operating profit by segment. Japan marked a significant increase in profit, not just from sales growth but from higher gross profit from mix improvement and price hike. The Japan Business is steadily making its way toward the annual target of over JPY20 billion. While China's like-for-like growth for H1 was minus 7%, we maintained a year-on-year decline in profit to JPY600 million. We will continue to reinforce marketing investment in key focus areas while building a healthy P&L structure by minimizing the impact of revenue decline through fixed cost reduction and structural reforms. Travel Retail, which has the highest profit margin in our business, experienced a significant decline in sales leading to a year-on-year decline in profit. This decline in Travel Retail sales had significant impact on intersegment sales in the Other segment in H1, resulting in a decline of JPY8.8 billion in core operating profit in total. As for the Adjustments, the increase in elimination of unrealized profit drove a year-on-year decline in profit. This is rather technical, but the main factor for this was a significant decline in the inventory levels in the H1 of last year which boosted profitability and we had rebound effect from that this year.

Our Strategic Approach to Chinese Consumers in an Ever-Changing Environment

Building a sustainable profit delivery business model in a moderately growing environment to emphasize quality growth

- **Growth strategy**
  - **Investing in key focus areas, maximize sales in agile growth areas in a weak macro-economic environment**
    - *SHISEIDO* : proactively develop next hero products, enhance strategic marketing investment
    - *Clé de Peau Beauté, NARS,* fragrance brands: continuously enhance
    - Focus on high-function and high-efficacy product categories
    - *Drunk Elephant* : enhance brand awareness, conduct campaigns to appeal functionality, increase collaborative marketing with retailers
  - **Channel strategy for sustainable growth**
    - Driving synergy through an integrated approach
      - Enhance marketing linkage between China and Travel Retail, and define priorities in brands and products
      - Capture growing demand of inbound tourists (Japan's inbound & Travel Retail Japan)
    - Strengthen online platforms with high growth potential, expand our official route to market
    - Differentiation via offline: explore new touchpoint opportunities, launch pop-up stores in tier 3-5 cities
- **Cost Reduction and Profit Boosting**
  - **Optimization of organization structure, closure of unprofitable doors, COGS reduction, selection and concentration of brands**

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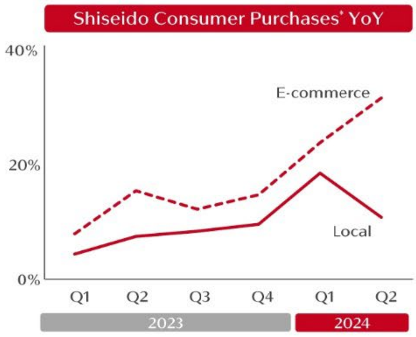
Next is page 13. I would like to explain about the actions taken during H2 to achieve our annual targets. First, the Company's approach to the current challenges in China markets remain unchanged as we will continue to rebuild a business structure that can deliver stable profits and to realize high-quality growth even amidst the moderate market growth. As for the growth strategy, we will maximize sales by strengthening investments in key focus areas that are able to grow in a weak macroeconomic environment. Above all, in SHISEIDO which has the highest sales ratio in the China Business, we will strengthen the brand by reinforcing proactive development and strategic marketing for launching of the next hero SKUs.

In H2, we have renewal plans for Vital Perfection and Future Solution as well as the launch of a new foundation serum - Skin Glow Foundation which have continued to perform well in Japan. Also, we will focus on high functionality product category such as suncare, cream and serum. For Drunk Elephant - launched in April, we will continue to engage in the campaigns to elevate its brand recognition as well as to promote high functionality and efficacy of its products. Furthermore, we will cautiously monitor the Travel Retail market to achieve sustainable growth by executing well-balanced marketing initiatives so that we do not get spiraled into the vicious cycle of excessive price competition. In the off-line channel, we will be launching pop-up stores in regional cities. In terms of profitability, we are making steady progress on strategic initiatives including over 10% headcount reduction in H1 from the last year while taking bold actions to close unprofitable stores since the start of this fiscal year, contributing to the profit during difficult times. We continue our best efforts for stable and sustainable profit delivery.

Japan : Clearer Focus Accelerated Growth, Continue to Strengthen Actions in 2H

- **Local**
  - ➢ Continue to strengthen investments in core brands and hero products
    Increase gross margin through mix improvement
    - Core brands fueled the increase of loyal users, further actions underway in 2H
  - ➢ New market creation through strategic marketing
    - Foundation serum: continued strong performance, more campaigns underway in 2H to solidify its presence as new market for further expansion
  - ➢ Continue strategic price increases
  - ➢ EC sales: 1H +high 20%, accelerating investments & brand expansion



- **Inbound**
  - ➢ Launch of Tourist Marketing Team
    - Capture tourists as a new consumer segment, offering valuable customer experience, enhance brand and product recognition to drive inbound sales

* Excluding business transfer impacts

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Next is page 14, regarding the strategic initiatives for Japan in H2. As explained earlier, in H1 we realized effective sales growth in the local market with steady increase of loyal users in core brands. In H2, we will continue to strengthen investments for core brands to maximize this positive trend. Next, for new market creation, the two products in the category of foundation serum continued to perform well, driven by the marketing communication focused on production technology in April. To ensure this does not become a one-time trend, we aim to establish this category as a new market and expand its size going forward. The EC sales, as shown in the graph on the bottom right, have been exceeding the growth rate of the total Japan local since last year, especially accelerated its growth from Q3 last year. We have made steady progress by completing the renewal of the owned EC site and the launch of SHISEIDO on Amazon and Rakuten in July. We will continue to focus on expanding the EC sales. As for the inbound sales, we have launched the Tourist Marketing Team in July in order to capture demand from inbound visitors to Japan, which is now exceeding the number back in 2019. By capturing travelers as another consumer segment, we aim to drive inbound sales by offering valuable customer experience while enhancing brand and product recognition.

Global Cost Reduction and Profit Boosting

Making steady progress towards achieving benefits of ¥40.0 bn+;
The Global Transformation Committee to make sure the delivery

- 1H Key Actions
  - Japan : COGS reduction by focusing on core brands and hero products; the implementation of ERIP*
  - China : optimization of organizational structure, closure of unprofitable doors, COGS reduction, selection and concentration of brands
  - Global : employee productivity improvement

(Billion yen)	2024		2025	Total
	1H			
Japan	2.0	8.0	17.0	25.0
China	3.0	5.0	3.0	8.0
Travel Retail	0.0	1.0	1.0	2.0
Asia Pacific, Americas, EMEA, Other (Global HQ)	2.0	1.0+	4.0+	5.0+
Total	7.0	15.0+	25.0+	40.0+

* Early retirement incentive plan

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Finally, page 15 is about the global cost reduction and profit improvement initiatives, which we are proceeding as part of the global transformation. We have the annual target of over JPY15 billion this year of which we achieved about JPY7 billion in H1, making steady progress on our initiatives to deliver positive impact. We have implemented the ERIP in Japan, as already mentioned, organizational optimization plan in China as well as the initiatives for employee productivity improvement, which are all progressing on track. Because we are in a tough market condition, we will continue to complete any profit improvement activities that can be done on our own efforts to achieve benefits of over JPY40 billion and further exceeding that to achieve our full-year targets. That is all from me. Thank you.

Vision and Strategic Direction for 2024 and 2025

Executing Business Transformation: Achieving Profitability and Resilience through Growth and Structural Reforms

- Global cost reduction (¥40.0 bn+)
- Complete Japan structural reform and accelerate growth
- Achieve high-quality sustainable growth in China and Travel Retail
- Accelerate growth in Americas, EMEA and Asia Pacific
- Advance growth momentum of core brands
- Enhance gross profit: develop growth drivers to maximize results

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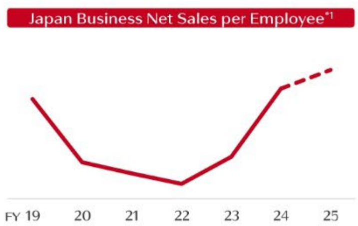
Fujiwara: Now, I will explain our strategy to ensure sustainable growth in the medium to long term. In February of this year, I announced that we will complete our business transformation to achieve sustainable profitable growth and to build a resilient business structure by 2025. As you can see, we defined our objective to achieve the cost reduction of over JPY40 billion globally with a particular focus on completing structural reforms in Japan as our top priority. The next focus is to achieve high-quality growth in China and Travel Retail. For the Americas, EMEA, and Asia Pacific, we will accelerate growth, elevate the growth momentum of core brands, and maximize gross profit.

Japan: Accelerate Progress on "Mirai Shift NIPPON 2025"

- Brand Strategy
  - Selection and concentration of brands and SKUs
  - Strategic price increases
  - New market creation through strategic marketing
- Touchpoint Strategy
  - Strategic collaboration with key retailers
  - Generate synergies in online-offline tie-ups by OMO acceleration
  - Accelerate EC sales growth
- Reinforce inbound marketing
- Steady progress on profitability improvement actions
  - Completed main actions in 2024 1H, ensure full impact from 2H
  - Set to improve organizational productivity after ERIP*2



Remain Committed to the Core OP Target of ¥50.0 bn in 2025

*1 Net Sales in Japan Business ÷ the number of employees in the Japan Business (incl. temporary employees) *2 Early retirement incentive plan

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Please see page 18. As explained by Hirofuji earlier, Japan's business transformation plan "Mirai Shift NIPPON 2025" which we implemented as a top priority is delivering steady results. Among other strategies, the selection and concentration of brands and SKUs and strategic price increases are generating gross profit margins outpacing growth and we will further accelerate these efforts. In addition, to optimize our headcount and achieve growth, we will further create synergetic online-offline business models by strengthening OMO. We will also accelerate the expansion of our loyal user base and build a stronger foundation for growth by further strengthening our digital investments and creating a more integrated customer experience that clarifies the roles of online and offline operations.

Secondly, we see an increase in inbound customers as a new market opportunity for growth. We established a dedicated team for inbound tourism marketing at Shiseido Japan, and they will collaborate with Travel Retail Japan, China, and other regions in Asia to create new growth opportunities in Japanese inbound market and to enhance communication from Japan to the rest of the world. We have made steady progress in improving profitability and the continuous process of productivity improvement and cost reduction has taken root in the organization, which is a big accomplishment. We believe that our process and organizational capabilities to continuously manage progress toward target and immediately consider new ideas when it is not sufficient will enable us to improve productivity in a sustainable manner.

Americas, EMEA and Asia Pacific : Accelerate Growth to Optimize Geographical Footprint

- **Brand Strategy**
  - Strengthen investments with selection and concentration in skin beauty and core brands
  - Accelerate growth of *Dr. Dennis Gross Skincare*, achieve synergy at an early stage
  - Rebuild and enhance fragrance business - Partnership with Max Mara
  - Strategic M&A
- **Building Strong Foundations**
  - Enhance digital investments
  - Strengthen expansion in emerging markets – India, the Middle East and more
  - Evolution of the organizational structure

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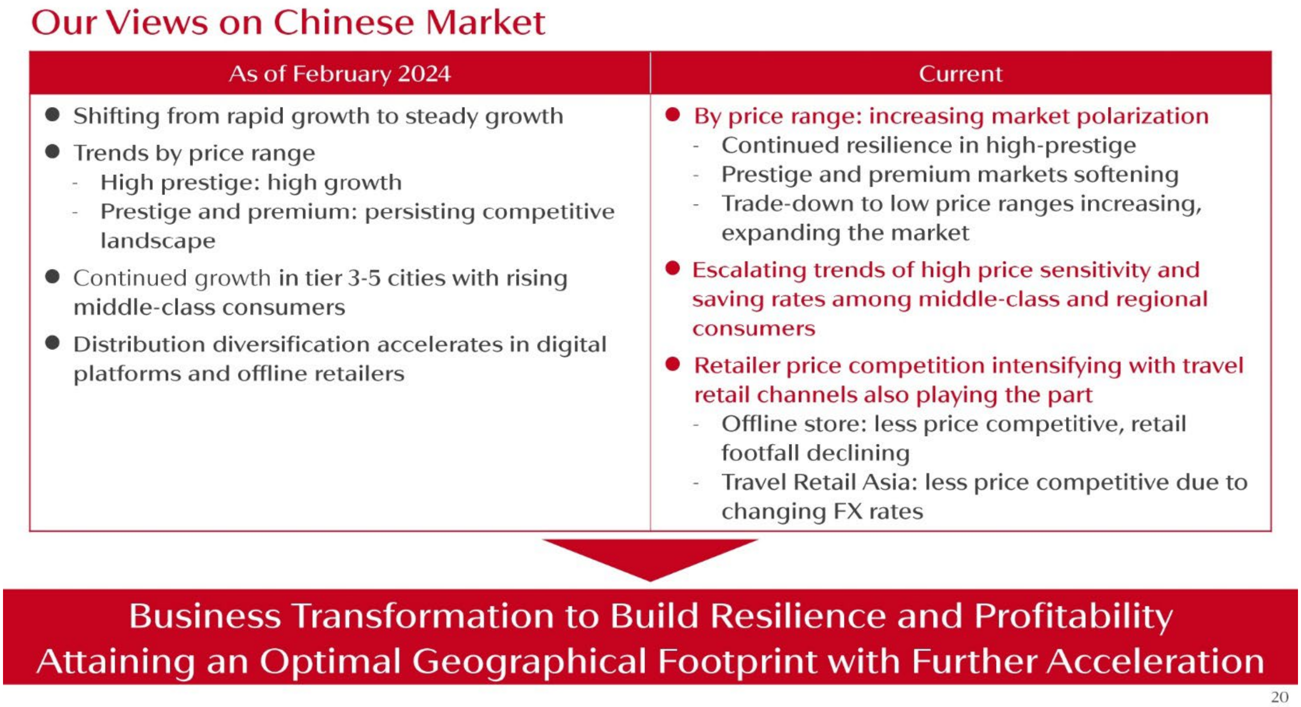
Next, page 19, about the Americas, EMEA, and Asia Pacific. We will execute continuous actions for growth to optimize regional portfolio for the future. In terms of brands, we will strengthen investments in core brands and also reinforce skin beauty category with the addition of Dr. Dennis Gross Skincare in the portfolio intended to accelerate the growth of derma category.

For fragrances, which continues to show solid performance particularly in the EMEA, we will realize growth and maximize profit contribution with the new partnership with Max Mara. We will continue to monitor the market. We will continue to monitor market trends and evaluate the effectiveness and profitability of our strategies while pursuing opportunities for strategic M&As. The market environment changes drastically in these regions, too, and we will aim to realize high growth by expanding our consumer touch points and e-commerce focusing on digital and especially by collaboration with Retail.com. Also, we have completed building the local business foundation in India and Middle East for our future potential market. We plan to make proactive investment to achieve high growth.



Next is page 20. China market continues to be an important market for the Company in the medium to long term. However, given the recent market environment, we must be cautious about our strategies for certain areas in the China and Travel Retail going forward. Key points to mention are the acceleration of market polarization, increased focus on price leading to fierce price competition among retailers with Travel Retail also playing a part in that. In light of these trends, we have determined that we will not only need to review our China and Travel Retail Businesses, but also to rebuild a more resilient organization and profit structure while optimizing our regional portfolio on a global basis.

Tackle Our Fundamental Issues
New Business Strategy to be Announced in late November 2024

- Current issues to be addressed: [external factors] slowdown in Chinese consumer spending, manifestations of risk factors
- Fundamental issues: [internal factors] Company-wide challenges
  - China: build a resilient organization and sustainable profit delivery business model
  - Japan: further evolution of business transformation and continuous improvement of productivity
  - Rebalance sales and profit by region:
    - Scale business by driving growth in Americas, EMEA and Asia Pacific, accelerating expansion in emerging markets - India, the Middle East and more
    - Building an organization capable of profit and cash generation across all regions
  - Brand: rebuild brand portfolio with selection and concentration of brands
  - Innovation: strengthen uniqueness and competitive advantage
  - Enhancing the quality of business management, operational excellence:
    - Human capital : productivity enhancement, aspire to be a top-tier talents and organization
    - Enhance digital capabilities: operational innovation with FOCUS and AI
    - Refine pricing strategy : FX fluctuation, price harmonization between regions
    - Strategic capital allocation, enhance financial discipline for investment decisions
    - Selection and concentration, fully capitalize on our assets to be retained

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Based on the assumption that the market environment will continue to be unstable, we will build business strategies that will enable us to steadily generate profit without being significantly impacted by changes in the market environment.

First, to adopt to changes in the market landscape that we are currently facing, we will continuously make efforts to transform the structures of our China and Travel Retail Businesses in order to generate stable profits. In Japan, on the other hand, we will further advance business transformation to further evolve our new growth model, along with continuous productivity improvement. Globally, in order to resolve disparities in profitability between regions, along with acceleration of growth in the Americas, EMEA, and Asia Pacific Businesses. Moreover, we will review our global operational structure so that we can build an organization capable of profit and cash generation across all regions. As for growth strategy, we will rebuild the brand portfolio through selection and concentration of brands. With respect to innovation, we will be focusing more on enhancing our uniqueness and competitive advantage. We have developed an AI-based value development methodology as a way to accelerate innovation creation. We will continue to position R&D as our competitive advantage and strive to achieve growth through continuous value enhancement and new market creation. We will also aim to improve the quality of business management and to achieve operational excellence as we invest further to human capital along with improved productivity, leveraging digital capabilities. In terms of enhancing quality of business management, we will execute strategic capital allocation, selection and concentration of assets, and make sure to firmly establish across the organization an operational framework for management focusing on cash flow. The details of our new business strategies will be announced at the end of November. That is all for me. Thank you very much.

Question & Answer

Kuwahara [Q]: This is Kuwahara of JPMorgan. Talking about the challenges facing in China or Travel Retail, the business, yes, it is understandable by looking at market trends, but I believe that production decline in the Americas is attributable to internal factors of the Company. How did that affect net sales and core operating profit in H1? Could you please give us more details about the production decline and the degree of its impact?

In your earlier presentation, the Americas and certain of Travel Retail Business and NARS have likely been affected by that, as a result. How is the situation there? At the beginning of the year, 40% of full-year core operating profit of JPY55 billion was expected to be delivered in H1. That was your explanation in the beginning of the year. Also, as a factor for falling short of that expectation, how much of the impact came from the Americas? Thank you.

Hirofuji [A]: Thank you for your question. Before talking about the impact of Americas in terms of the overall sales, on a like-for-like basis, sales in H1 were about JPY18 billion lower than the plan. Among them, the largest are the Americas, China, and Travel Retail in the order. The Americas fell short by a little less than JPY10 billion compared to the plan.

Based on that, core operating profit which was initially expected to comprise 40% of the full-year forecast in H1 and 60% in H2, as you mentioned, actually turned out as JPY19.3 billion versus JPY22 billion in H1. That means approx. JPY3 billion short from our original plan. While it exceeded the plan by a few billion yen in Q1, it fell short by JPY6 billion or so in Q2. By region, core operating profit in the Americas and Travel Retail both fell short of the plan due to lower sales, and China also suffered a decline in revenue. However, in China that was more than offset by the positive impact of cost reduction. And then, the Japan and EMEA exceeded the plan overall. That is an overview for H1 in terms of profitability.

Kuwahara [Q]: Well, thank you for that. So, is my understanding correct that production adjustments in the Americas have occurred due to the implementation of FOCUS in H2 of last year? And if that is correct, considering that the EMEA and other regions or manufacturing sites will also be using FOCUS going forward, that kind of unexpected event may be regarded as a risk. How are you going to manage that?

Fujiwara [A]: Well, first of all, there were two reasons behind production adjustments in the Americas. First is the IT system which had a negative impact on production volume. While it is also attributable to the system to some extent, there has also been a bit of delay in procurement of raw materials which has led to lower production volume. However it has already been recovered and production capacity is now returned to normal level. The FOCUS system launched in the Americas is a core system for the production. This core system that we are implementing globally is rather financial and logistics-oriented systems among FOCUS. We are successfully proceeding with launch of the system, and by the end of this year we will complete the entire process by completing the implementation in Japan.

Therefore, we are on track with FOCUS which has been implemented in regions, but regarding production, we plan to monitor the progress and make sure that there are no defects in production before moving on to other manufacturing plants.

Kuwahara [Q]: Understood. Thank you.

Sato [Q]: This is Sato from Morgan Stanley MUFG Securities. Since Umetsu-san is here with us, I would like to ask about China.

At this point, what is the situation in price competition between retailers? How did it happen? What kind of negative impact does it have for manufacturers? Also, how would you go about allocating the marketing cost for diversifying retailers which used to be focused on major players and Tmall?

In the context where all other companies are garnering lower return or ROI / ROIC from marketing investment, how do intend to improve that going forward so as to achieve and stabilize profitability at a reasonable level in China?

First of all, I would like you to elaborate on the retailers' price competition. Along with that, what kind of actions are you taking in the short term so that the sales will not drop any further in H2? I would like to hear comments from Umetsu-san.

Umetsu [A]: I will answer to your question. My name is Umetsu, I am the CEO of the China region. First of all, the detail and what is happening around price competition amongst the retailers. To simply put it, the consumers are looking for a channel or touch point where they can purchase at the cheapest price more active and more aggressive. Within China, price competition is occurring between offline and online channels. Most off-line retailers, for example, are looking for the cheapest promotional pricing offered as a benchmark in the 618 big promotions.

On the brand side, we all want to protect the price, not willing to do promotional pricing that much. But on the EC, for example, platformers are often sacrifice their margins and issue coupons on their own, that's what's happening. Similarly, offline channels are also sacrificing their margins and offering discounts. That was what was happening in aggressive price competition in China.

Prices on unauthorized e-commerce platform are most widely used benchmark right now. Unauthorized sales prices are the cheapest, so the top KOL and retailers are also trying to meet their targets in line with that.

Similar things are happening in Travel Retail, too. There's the airport duty-free, but there's some operators are also doing e-commerce, and they are offering low price range. The percentage of those sales are increasing as a result.

They also seek more promotional offers by benchmarking the cheapest, unauthorized online price range in China. On the brand side, they want to control prices, so they are making cheaper discounts at their own discretion.

As Hirofuji explained earlier about how Shiseido intends to take action in the short term, when we look at the brands after the Fukushima treated water, yes, it's true that our brand is weakening a little bit due to the impact of the treated water.

We are trying to limit bulk sales or group procurement like B2B2C business that is unique to the China Business as much as possible to take control overall. That is one thing. As if we get more gray market, then, of course, there is a mechanism that the pricing will all drop in unauthorized e-commerce channels, so we are also controlling that as well.

The other thing is that we are trying to narrow down the focus of products in terms of what kind of products we need to do a discount. But there are other brands or products that does not need a discount. For those brands and products that we want to grow, we do not need to do that much discount. We want to balance ourselves so that we can create sales where we do not depend too much on the discount.

That was what Hirofuji was saying about the next future hero SKUs. If we can do that to try to balance ourselves then in both China and Travel Retail, we can achieve benefits, and take a balance between the regular price and the promotion price and be able to control sales in our business overall. That is what we are doing right now.

Sato [Q]: Regarding unauthorized sales prices, I think buyers are bringing those products from somewhere, but they have decreased in South Korea and restrictions adopted in Hainan Island from June last year, so where are they coming from right now?

Umetsu [A]: While they have decreased, there still remains some routes that are unauthorized. In the Travel Retail, in fact, there has been a tendency that sales for consumers outside of airport are increasing. In our case, due to the depreciation of the yen, we see some of them flowing from Japan, although they are not very large in scale. As a result, the total volume is shrinking but in terms of market share, but yet the market share of unauthorized sales is growing.

Sato [Q]: For H2 of China, are you going to focus on the profit?

Umetsu [A]: Overall looking, yes, we are taking actions so that we can increase profitability. For brands that we are able to win, such as Cle de Peau Beaute, NARS, and SHISEIDO which needs quick turnaround, we want to continue to proactively invest.

Sato [Q]: Okay. Thank you very much.

Miyazaki [Q]: Thank you for the presentation. Miyazaki of Goldman Sachs. For Japan local business, I have a few questions. I understand that the business is on track, but what are the factors for e-commerce is growing. Are there any new areas that are growing not sequentially or whether there are other elements, and whether there is a portion where the sales mix of your company is changing by the growth in the e-commerce?

Fujiwara [A]: First of all, we are investing in e-commerce business in Japan. We are generating more retail traffic and e-commerce sales as a result. There are three categories in our e-commerce business. First is Owned.com platform. Overall design is now refreshed to make our platform more convenient for consumers and to enhance consumer experience. Second, we have Pure Play platform like Amazon or Rakuten and all those platforms, and we want to invest in this segment mainly to find new customers. We want to increase sales by acquiring consumers who are mainly using these platforms for shopping. Third, we have Retail.com. Going forward, we intend to strengthen this segment as a key driver of sustainable growth. There are retail.com like a department store or a drug store or our specialty stores that are linked with their own offline stores, and that ratio is not so small, and they are showing highest growth rates among others. We have strengthened this segment considerably by linking offline and online stores, which in turn leads to sustainable growth.

As a result of this effort, the e-commerce ratio is three percentage point increase from the beginning of the year in terms of the sales composition. Going forward, we will accelerate growth to increase that ratio.

Miyazaki [Q]: As a result of such initiatives, are there any changes in ASP or the brand composition? Or are you pursuing any changes that you have not realized yet going forward?

Fujiwara [A]: In terms of brand mix, there will be no big change, in my understanding. We will focus on the core brands. In terms of the profitability, the e-commerce channel profitability is the highest among others. Therefore, we also expect to see a structural mix achieved by changes in a channel mix that allows for higher profitability with an increase in e-commerce sales ratio.

Miyazaki [Q]: Thank you very much. This is clear.

Miyasako [Q]: Hello. This is Miyasako from Mizuho Securities. Since Umetsu-san is here, I want to ask about China. In terms of top-line growth, I was wondering if local players are taking market shares from Shiseido in China. Their strengths are increasing steadily, and that they are also rising both in terms of products and in terms of marketing. How do you intend to grow the top line in the future?

Umetsu [A]: First of all, I would like to share with you that we feel that we need to review our brand portfolio. If we look at the current status, in H1, skincare is on a shrinking trend in high price range above prestige, followed by makeup, and then fragrance which the size is small.

In terms of reviewing our portfolio, In the meaning of portfolio review, while Japanese skincare brands used to be the main drivers of growth in the past in a sense, now we are trying to replace portfolios globally with brands like NARS. In this context, fragrances are also perceived as opportunities for growth. Therefore, one of the ideas is that we will capitalize on growth with a mix portfolio of those brands.

The other is about competition with local brands. We are now looking at all the details of which categories the local brands are winning. For example, in skincare, Shiseido and the Japanese brands were originally strong in lotion and emulsion for basic care. However, after the Fukushima treated water incident, the local brands are really emerging in that space.

With that, we want to foster brands in high functionality and high price range such as Future Solution LX in brand SHISEIDO. Alternatively, we are cultivating high-performance cream and essence, and we are now in the process of formulating a plan that will enable us to figure out the target more efficiently and competing brands for each product by strategically selecting where we can compete more strongly, rather than competing in areas where they have advantages in order to grow our market share. We will achieve growth by combination of these strategies.

Also, the area of our business affected by the competition the most right now is the premium brands, such as Elixir and AUPRES. These kinds of brands used to have a competitive advantage of being a Japanese brand but now it is actually taken over by slightly cheaper local brands. In that segment we need to revisit our product portfolio to identify the product category in which we can win in this market. We need a strategy where we can win in that category, and that is how we are shifting.

Finally, we need to be efficient in our investments, we do need to take another step into the structural reforms. Now, we have the brands and products imported from Japan, but we need to try to take another step to be more localized so that we can be more agile and very competitive against the local brands.

Miyasako [Q]: I believe that Cle de Peau Beaute is doing well in base makeup and facial cleansers, but do you think that trend will continue? Can you share about the strategy for Cle de Peau Beaute?

Umetsu [A]: For the Cle de Peau Beaute brand, as you have mentioned, currently, majority of the sales for Cle de Peau Beaute comes from the base makeup and face care set for new customers and cleansers.

At the same time, there is another luxury line, Supreme Collection in which we are trying to grow and expand over the past several years. If we can successfully expand this luxury line in Cle de Peau Beaute, we can take another step for growth in China markets.

We have just renewal launched an eye cream in Supreme Collection this August. We will continue proactive investment in this product to elevate the overall line driven by this high-performance eye cream, not only in the mainland China, but also in Hong Kong and Travel Retail markets. Cle de Peau Beaute also has Synactif, which is the highest line of Cle de Peau Beaute. Right now, we are solidifying the first stage which means there is room for growth in the second and the third stages for the brand. We will keep up the pace of investment for this brand.

Miyasako [Q]: Thank you.

Yamanaka [Q]: This is Yamanaka from SMBC Nikko. I would like to know the progress on global cost reduction on page 15, and your confident to achieve this target given a weak topline in China, Travel Retail and North America which experienced slower sales than expected in Q2. In H1, you had good progress in Japan and China, so the impact of a slowdown in North America may be not affecting overall achievement of the plan. I just want to know what your expectations are around that.

Hirofuji [A]: At the Q1 results meeting we mentioned that the Global Transformation Committee has realized the effects of around JPY3 billion. We also achieved effects close to that level in Q2, so roughly JPY7 billion in H1. It is working in line with our plan. And then, the Americas currently slowing down, but we do not expect any negative impact of that at the moment. Also, in Q2, we are expecting the positive impact of the early retirement incentive plan in Japan, so we are well positioned to achieve our annual target of JPY15 billion at least, in our view.

However, as I mentioned in the presentation, given the current tough situation, we are preparing for additional actions to be taken right now. I believe that depending on how much we can improve our actions right now and in H2 will be the key to achieving our goals.

Yamanaka [Q]: Understood. So in November, you will come with new strategies for boosting this in a challenging environment, is that correct?

Hirofuji [A]: Yes, your understanding is correct.

Hyogo [Q]: This is Hyogo from Mitsubishi UFJ Trust and Banking. A question for myself. In the medium term, how do you feel a sense of crisis is developed or identified within the Company? I believe that just because you are progressing successfully with cost reduction, that is not the end of the story. I would like to know what kind of discussions are taking place and what kind of challenges are identified within the Company? What is the focus for your ideas for the new strategy at the end of November? Please share your actions or initiatives taken within the Company.

Fujiwara [A]: Just what you have exactly mentioned, the urgency and the sense of crisis within the Company is very high. Yes, this is not something that we could resolve with cost reduction in a short-term.

First of all, when the market situation is very uncertain and very difficult to predict, it has become one of the key themes for us to establish resilient organization by transforming our management or the cost structure. And this is not for China and Travel Retail, which we are struggling right now. And this is not just about Japan currently going through structural reforms, but it is an issue at the global level to create a resilient organization that we can continue to drive profit regardless of how the situation is unstable or uncertain.

And we are obviously aware that we will not be able to grow just by cost reductions and improving efficiency so a growth strategy will be crucial that is a very important challenge in a medium term that we do need to work on. This will not be a growth strategy that reflects the growth of the market to a certain extent, but it should be building on a company-wide view in terms of where we can make the most of our strengths, which we can grow on our own, and where we can make the most of our strengths. I would once again like to assemble a brand portfolio, or even more, a confirmation of the growth areas, and what kind of investment we will make there.

Lastly, we plan to review our organizational capability to execute these strategies. Even if we are able to achieve innovation and make investments, we must have the ability to deliver results to consumers. We also need to assess where we need to develop organizational capabilities to respond to ever-changing environment, as well as the ability to identify where we need to develop capability including digital, in formulating our new management strategies.

Hyogo [Q]: For ROI assessment, is it fully done in a visible manner?

Fujiwara [A]: Yes. For each of the return on investment, especially around marketing, it is all very visible, and we can see all of that. For the capital allocation, we need to look at the return on investment and make it even more visible and not only that, we need to take a step further to make sure we all understand that within the Company.

Hyogo [Q]: Thank you very much.

Hirozumi [Q]: Hirozumi from Daiwa Securities. I would like to confirm your comment on page 7. Did you say that the 7% increase in Japan in Q2 was in line with the market and what is the gap between that and the consumer purchases on page 8 indicates? Also, is 1.3 billion yen core operating profit in Japan Business in line with your estimate? I was wondering if it would be more profitable for some reason, so let me confirm on that.

Hirofuji [A]: To answer to your second question, the core operating profit of 1.3 billion yen is in line with our estimate. And in fact, the inbound sales were not meeting our target. That was offset by sales in Japan local. We also successfully managed to secure profits by the structural reforms. So, we made progress on core operating profit in Q2 and H1 in line with our target.

And your first question is about the customer purchases which was +high teen%. There was a rebound in Q2, as +13% in H1 in external sales reflected an increase in shipment in Q1 before the price hike. That's why there were ups and downs in shipment in Q1 and Q2.

Hirozumi [Q]: So +13% in shipment was in line with the market or underperformed the market?

Hirofuji [A]: We are steadily increasing our market share, and yes, we outperformed the market growth.

Hirozumi [Q]: Understood. In local business, you are achieving quite well, but the inbound a little short for the target. As a result, the core operating profit of 1.3 billion yen is in line with your target.

Fujiwara [A]: Yes, I think your point is that we only generated 1.3 billion yen in Q2, but this is the marketing-related issue of which quarter to invest in, and also some of Q1 profits reflect advance shipments. Therefore, Q1 appears to be making profit slightly more than expected. So, looking at the H1, profits are coming in-line.

Hirozumi [Q]: Understood. Thank you very much.

Oshima [M]: Thank you very much. Now, we would like to close the Q&A session.

Now, we would like to end today's earnings report. Thank you.

[END]

Document Notes

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