Otsuka Holdings Co Ltd

The 3rd Medium-Term Management Plan
FY 2019 - 2023

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Agenda

- Value Creation Model and Goals
- Position and Performance Targets
- Growth Strategies
  - Pharmaceutical Business
  - Nutraceutical* Business
  - Financial Policy

* (NC) Nutraceutical = nutrition + pharmaceuticals
This diagram shows the essence of management which serves as a basis for Otsuka’s value creation model.

Under our corporate motto, “Otsuka people creating new products for better health worldwide”, we have been creating numerous new forms of value.

Behind our efforts to realize new value creation, there are three phrases that generations of the Otsuka-founding family have left for us as a fundamental guidance.

One is “Ryukan Godou” or “Commitment”, meaning essence and truth can be found only through hard work and execution.

The second phrase is “Jisshou”, or “Actualization”, meaning making achievements by tenaciously accomplishing your role thereby the essence of business can be found.

The third phase is “creativity” which symbolizes our corporate culture of not imitating others and pursuing our original ways to realize what only Otsuka can do in all value chains of business from R&D to marketing.
This is a schematic slide of Otsuka’s original value creation model.

Values are created by turning the social issues into a form of unique business, and, through such efforts, we have been contributing to people’s health worldwide.

Such social contributions of ours find new social issues which are addressed by our value creation undertakings. In this manner, the model has been circulating.

This model can be realized only by adhering to our philosophy represented by phrases of “Ryukan Godou” “Jisshou” and “Creativity” in all phases of discovery of social issues, unique and diverse business operations, new value creation, and social contribution.

In the following slides, I will introduce actual examples of the value creation process which are quite unique and most important.
Unique feature of Otsuka is to connect various businesses, combine assets, pursue true needs from insights, and create new concepts and products by combining technologies and science in an organized fashion.

Furthermore, we have a corporate culture that utilizes such created values for overlapping other businesses to cultivate niche spaces and another new values.

Such corporate culture based on the three ideas of former management leaders that had been passed on from the foundation until today has penetrated into the daily activities of every Otsuka employee as part of our DNA.
Next, I will explain value creation process in our psychiatry and neurology business by presenting an example from the past.

In the 1980’s, we started research activities in the CNS space, trying to prove the hypothesis we set and successfully discovered *Abilify*, which had a new concept of Dopamine D₂ partial agonist.

To maximize the potential of *Rexulti*, we have further expanded its use to the neurological area during the 2nd mid-term plan period and will explore new business opportunities that address unmet treatment needs in the psychiatric and neurological areas.

In the psychiatric area, we are taking on challenges to address other needs related to adherence, namely the development of a long-acting injectable (LAI) formulation and further optimization of treatment with digital medicine, therapeutic apps, and digital health solutions. Otsuka is taking on the challenge of creating new value in areas that are quite different from conventional business models, for which only Otsuka can become value creator.
This is what Otsuka aspires to be.

As a total healthcare company that supports the maintenance and promotion of daily health as well as provides diagnosis and treatment of diseases, we aspire to be an indispensable company that creates original products both in the pharmaceutical and nutraceutical areas to address the unmet needs and yet-to-be imagined needs.
Position and Performance Targets
We have positioned next 5 years as a period to advance to become a world-class total health care company.

We will focus on maximization of existing business value as well as new value creation in our core businesses of pharmaceutical and nutraceutical while being conscious of capital cost in our business operations.
This summarizes the goals of our major initiatives we have set forth to achieve.

As performance target, we aim for a CAGR of 10% or more in business profit growth, which is achievable with steady organic growth of major products and brands of our pharma and NC businesses.

While securing a 10% or more profit growth, we will make aggressive R&D investments, mainly in new drug development to drive revenues in the next management plan period and onward.

As for our business strategy, growth will be accelerated by strategic initiatives for key products and brands.

We will actively carry out strategic plans to nurture next generation products and businesses.

With regard to financial policy, our focus is to attain optimal balance between investments for growth and shareholders return and to secure funds to realize them.
I will talk about our performance targets.

Business profits in FY2023, the last year of the plan, is set at ¥200 billion with CAGR of 10% or more.

We believe this targets are achievable as we have seen strong sales growth of our main products and brands of pharma and NC businesses due to the sufficient investments we have made so far.

We aim for sales of ¥1.7 trillion and business profit before R&D expenses of ¥460 billion, both of which are record highs.

To ensure sustainable growth, R&D expenses are set at ¥260 billion. While continuing aggressive R&D investments, we also set the ROE target to be 8% or more.
The plan is based on the organic growth of existing businesses. In FY2023, the final year, both the pharma and NC businesses are set to make significant contributions to sales expected to reach ¥1.7 trillion, up by ¥408.0 billion.
This shows groups of key growth drivers in the plan.

In the pharmaceutical business, 4 global products, namely, *Abilify Maintena, Rexulti, Samsca/Jinarc* and *Lonsurf*, and new products such as AVP-786, vadadustat, which are expected to be launched during this plan period, will push sales by ¥290 billion in total.

On the other hand, in the NC business, sales of 3 major brands, namely Pocari Sweat, Nature Made, and Nutrition et Sante, and 3 nurture brands, such as products of Daiya Foods, Equelle and Body Mainte will increase by ¥80 billion.

These products are important contributors in the plan as their incremental sales accounts for about 90% of total sales increase of ¥408 billion.
I will explain our aggressive R&D investments to support our new value creation efforts.

Otsuka’s unique business model consisting of two core businesses of pharma and NC allows us to make investments in high-risk pharma business more aggressively while suppressing the overall R&D ratio to total sales.

During this management plan period, R&D expenses are estimated to be around 15% of total sales. In the pharmaceutical business, however, the ratio is expected to be higher and stable at 22%.

We will continue to pursue this unique business model and aim for further expansion through value creation.
Pharmaceutical Business
With the theme of value maximization of existing business and new value creation, we will work on these three targets.
Sales revenue plan of the products that drive our pharmaceutical business growth.

We estimate ¥200 billion in sales after maximizing their values of 4 global products and ¥90 billion sales from new products scheduled to be launched during this period that will further accelerate the growth.

Next, I will explain about them by each therapeutic area.
I will talk about our key strategy on CNS: psychiatric and neurology area.

We have been strengthening our product portfolio and research pipeline not only in the psychiatry area through Abilify but also in the neurological area to expand our CNS franchise.

We will continue with our R&D efforts to contribute to solutions to the unaddressed medical needs in this therapeutic space.

At the same time, we will look into the optimization of medical care and explore establishment of business models to improve adherence by digital solutions and therapeutic app. We will create new values and advance them to a profitable business level as quickly as possible.
Next, I will introduce how we will address the unmet medical needs of dementia of the Alzheimer type and how we will maximize product values.

Patient population of Alzheimer’s disease is estimated to increase along with our aging society.

With this background, behavioral disorders, including agitation, are recognized as major social issues for patients, family members, and healthcare professionals.

Otsuka is taking on the challenge of addressing this issue with Rexulti and AVP-786, two drugs with completely different mechanisms of action.

In one estimate, diagnosed patients with dementia of the Alzheimer’s type in the US will increase to 3.31 million, of which 2.5 million will develop the symptom of agitation.

If 1% of such patients with agitation receive drug treatment, the market size is expected to be $150-200 million.

So our efforts are to address such a big social problem with huge market potential.
This slide shows our aspiration to be the world class player in the CNS space.

In 2013, Otsuka was in the leading position as global player in the CNS in terms of share of sales.

We have a lineup of products and research assets with high potential and we strongly believe we are one of the few companies that will be able to become a top player in this field.

We will continue aggressive investments to enhance our strengths and strongly position ourselves as “Otsuka - the CNS company.”
Next is our strategy in oncology.

Taiho Pharmaceutical has established drug discovery platform and accumulated know-how through advancing biochemical modulation over the past 50 years.

It is proceeding with small molecule R&D activities aiming for co-existence with other anticancer drugs including immunotherapy.

In the discovery of molecular targeting agents, fragment based drug discovery technology by Taiho and Astex is fully utilized. With their technology we will aim for discovery of drugs with innovative mechanisms of action to treat drug resistant cancers.

With small molecule compounds as its main drug class, we are also studying possibility of generating synergies with new modalities such as cancer vaccines, CAR-T, TCR-T, and oncolytic virus.

We will address unmet medical needs capitalizing on our long history of R&D and new drug discovery platform to develop small molecule compounds.
Next, I will explain how we will structure our group organization for business value maximization.

Otsuka Group oncology business has established a strong position in Japan, but has relatively short history overseas where it needs to enhance its presence.

We will set the coming 5 years as a period when we put together all the accumulated assets of Taiho, Astex and Otsuka in drug discovery, clinical development, production and sales to maximize the value of our oncology business.
I will touch upon one drug candidate, TAS-116, which reflects Otsuka’s characteristics in oncology.

Heat shock protein 90 has attracted attention as a drug target, but there have been no drugs launched as its inhibitor.

We tried to determine the potential of this compound through our long-standing R&D knowhow and philosophy of “Ryukan Godou” and continued development tenaciously. As a result, we succeeded in taking this compound to the phase 3 stage for the treatment of a rare disease called GIST (gastrointestinal stromal tumor).

Our business plan is for this compound, in its initial phase, to contribute to a small number of patients, but its potential as a first-in-class drug is huge and our expectations are high. We will focus on the ongoing clinical trials to demonstrate the future potential of the compound.
Next is our strategy for cardio-renal area.

In order to grow Otsuka’s pharmaceutical business and ensure sustainable growth beyond 2030, we need to develop one more core therapeutic area in addition to CNS and oncology. For the expansion of such business, we made many investments during the 2nd mid-term plan period.

Taking advantage of our expertise in cardio-renal area with anti-platelet agent Pletal’s marketing experience in Japan, we have launched Samsca globally.

With the additional indication of ADPKD for Samsca/Jinarc, we are accumulating new expertise in this renal disease area.

In the renal space, we have been making efforts to reinforce our franchise and enrich our pipeline by licensing in vadadustat for renal anemia and acquiring Vistarra.

In addition to the in-licensing efforts, progress has been made for discovering a home-grown drug candidates as well.

In the cardiology space, our main focus is on medical devices.

We have acquired renal denervation system by Recor Medical and unique stent product by Verylan. We are moving ahead steadily with a hope of combining these with our strong assets to build up this business as soon as possible.

In this manner, we will utilize overlapping and derivation of businesses to create a robust business segment.
This shows how we will maximize the value of Jinarc and contribute to ADPKD treatment. We plan to launch multiple initiatives to improve ADPKD treatment and to maximize product value. Our promotional activities include understanding of disease state of rapid progressing patients and disseminating efficacy and safety information of the drug. We will also ensure the safe use of the drug and support patient access to the drug to maximize product value in the U.S.
We will expand our clinical nutrition business globally with high value added products overseas. Together with global expansion and total nutrition management, we set the ambitious target of 18.5% CAGR.

On the other hand, in the challenging market in Japan, we will secure stable profit level and improve existing products with expertise that only Otsuka has and with the development of new technology in these fields, we will expand this business globally in the future.
From now let’s take a look at value maximization of the existing products that support the strategies I have explained.

This shows the sales revenue and SG&A ratio excluding new products to be launched during this plan period.

Our plan is to ensure strong increase in sales of these products while suppressing the SG&A ratio.

Profits to be generated from existing products will be invested in additional indications and marketing activities of new products to boost their sales as quickly as possible to realize sustainable growth.
This is regarding the last theme, innovation creation using unique and diverse research platform.

In this dramatically changing healthcare industry, creation of innovative new drugs is more important than ever.

We will combine drug discovery platform centering on small molecules over the years and cutting edge technology to generate innovation through value creation process based on “Ryukan godou” “Jisshou” and “Creativity”.
Nutraceutical Business
Just like the Pharmaceutical business, we will set value creation and maximization of existing businesses as our main themes and take on the creation of new concepts focusing on business environment changes, challenges to new categories and new areas, and continued efforts to maintain high profit structure.
Fist, sales plan for a group of key drivers.

Our target is to increase sales by ¥80 billion during this five year period.

The increase comes from 3 major brands and 3 nurture brands, each of which contributes to a ¥40 billion sales increase.

From here I will explain our initiatives to develop new concept focusing on changes of business environment.
First, let’s look at the market for health related products Otsuka has special interest in. The global market has been growing with the CAGR of 4.2% between 2014 and 2018, surpassing the growth rate of the pharmaceutical business. So we recognize that we are targeting an attractive market.

In addition, as health consciousness is mounting, the speed of growth of this market is expected to accelerate.
Amid such a health conscious environment, world trends are going through rapid changes. Scientific technology is advancing drastically, which we describe as the 4th industrial revolution as represented by IoT, Big Data, AI, 5G, and robotics.

For example, until recently some diseases would be left unrecognized until diagnostic testing or obvious symptoms appeared, and so many people would just endure the condition if it was not severe.

In the future, signs of the diseases will be captured as digital information and each individual will be able to manage their health proactively.

Despite this vastly changing environment, Otsuka’s business approach remains unchanged. We stick to our corporate philosophy of continued value creation.

To capture the diverse needs in new age, we will make full use of our science and technology established in NC and pharmaceutical businesses to formulate new concepts and thereby contribute to people’s health promotion by offering new values.
Next is our challenge to expansion to new area and category of business.

We will accelerate our global expansion taking advantage of product attributes and characteristics and build a platform to grow 3 major products to ¥100 billion brands and make 3 nurture brands as the next generation brands to support our future business.
I will show you the details on the market environment and growth strategy on each of the major products, *Pocari Sweat*, Supplements and plant-based foods.

First, *Pocari Sweat*:

The sports drink market in the Asia-Pacific region has been expanding with a CAGR of 5.2% between 2014 and 2018. In this health-conscious growing market, we will promote our product concepts through marketing activities unique to Otsuka to enhance brand equity.

In this growing region, the expected CAGR of *Pocari Sweat* in the next five years is 9.4%, surpassing the overall market growth rate.

In addition, we will continue to expand to new areas, mainly in Asia to ensure sustainable growth of the *Pocari Sweat* brand.
Next is our supplement business.

The *Nature Made* business has been expanding mainly in the US. In addition to its market growth, we will grow this business by introducing a new category of personalized vitamins, enabling a platform to raise this business to a ¥100 billion brand.

Another focus of ours is to penetrate product concept of *Equelle*, one of our 3 nurture brands to create a new market not only in Japan but also in North America.

To further develop our business platform, we will evaluate entry into another high-growth market, the Asia-Pacific region.
This is regarding plant-based products of Daiya Foods, one of our new focuses in the NC business.

We are aggressively conducting marketing activities as a category leader to solve health issues of health conscious consumers, mostly of the millennial generation, and expand the market for this type of products.

The plant-based alternative market in the US showed year-on-year growth rate of 20% plus between July 2017 and June 2018. We plan to achieve sales CAGR of 25% in the market, putting efforts in expanding sales channels and product lineup of the core products such as cheese alternatives.

During the 3rd mid-term plan period, we will establish robust platform for this business in North America so that we will be able to expand to new regions as well.
Centering on these growth drivers, we plan to boost the sales of functional drinks and supplements at the same speed as the market growth and sales of functional foods at faster speed than the market growth rate so that we can achieve ¥450 billion sales revenue in the last year of the management plan.
This is the last slide for NC business strategy to explain how to maintain our high profit business scheme.

Through the review of management assets that supported the value chain, we could build a solid business platform and improve the profitability of the NC business, which was the biggest theme for the 2nd mid-term plan for the NC business.

As a result, we are now able to maintain a profitability of 10% or more.

In the 3rd mid-term business plan period, we will promote new products with a new concept, expand our global business footprint, and grow new businesses such as plant-based food products while maintaining a 10% profitability and increasing sales. Thus we will further increase the amount of our business profit.
From here on, I will introduce our financial policy.
In the next 5 years, we will implement business management with a corporate-wide awareness of capital costs.

Here are the 3 key points:

Balancing investments for future growth and shareholders return,

Clarifying main investment areas, and Enhancing management efficiency.
First point is to implement “business management with a corporate-wide awareness of capital costs” throughout the group.

We are going to increase an awareness of capital costs company-wide reflecting business risks and introduce performance evaluation based on capital costs.

As for business and investment strategy, we are going to improve our ROIC on mid-to long term basis by starting ROIC management and investing for new value creation.

With regard to financial policy, we will optimize our capital structure in order to lower our capital costs.

By combining these efforts on business and investment side and also financing side, we are going to maximize Otsuka’s corporate value.
This shows how we are going to balance growth investment and shareholders return. Cumulative operating cash flow in the next five year period is estimated at ¥700 billion to ¥800 billion.

We will make a disciplined use of cash and make each investment decision considering ROIC.

Also we will target an ROE of 8% or more while maintaining a solid financial position.

As for the shareholders return policy, we will maintain stable dividends and consider additional shareholders return depending on our profit growth.
Next I will explain the main areas of investments.

we will consider investments that will generate greater values by combining them with existing assets.

Specifically, we will look for investment opportunities in which we can share assets such as products, technologies, human talents and most importantly Otsuka’s management essence, and that fit our short-, mid-, and long-term strategies.

In the pharmaceutical business, we will invest to reinforce our portfolio and pipeline in the area of our utmost focus, CNS.

Also we will work on enriching our product lineup and pipeline for the Japanese market, which is one of our management issues.

In the NC business, we will make active investments in new businesses focusing on the future social issues.
Next is our effort to enhance management efficiency.

In this plan, for better management efficiency, we will seek standardization of our tasks and improve operational efficiency, reinforce internal control functions, and correspond to regulatory environment.

Specifically, we will move ahead with shared service on a global basis, IT platform unification, promotion of group finances and optimization of procurement function.

We will provide an update on the progress and impact of this initiative at future meetings when we announce our business results.
This is the summary of my presentation today.

Our performance target in this plan is for an annual profit growth of 10% or more.

We will challenge new value creation and maximization of existing businesses for both the pharma and NC businesses.

As financial policy, we set the theme of capital cost–conscious management for better business management in the coming 5 years.

That’s the outline of our 3rd mid-term management plan.

Otsuka celebrates its 100th anniversary during this business plan period. We are determined to continue our efforts to contribute to society through our unique value creation model and its steady implementation.

In the next 5 years, we aspire to play meaningful roles as a unique total healthcare company that contributes to people’s health worldwide.

We would appreciate your expectations to our advance and continued support for Otsuka Group.

Thank you for your attention.