

Processed Foods Business Division

We will execute organization reforms to rise out of low profitability and create a structure that embraces challenges from a customer perspective.

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Business Division



Looking Back on Fiscal 2018

The Processed Foods Business Division posted net sales of ¥353.1 billion and business profit of ¥7.8 billion—which amounted to decreased net sales and increased business profit compared with the previous year—despite increasing personnel and distribution costs and a general slump in the gift market. These challenging factors were offset by growth in demand for core consumer products, such as *SCHAU ESSEN*™, and a shift toward a manufacturing and sales structure emphasizing profit.

Seeking to reinforce profitability by “Strengthen profitability by improving the efficiency of existing businesses,” which is a business policy under Medium-Term Management Plan 2020, the Processed Foods Business Division directed concerted efforts toward improving the gross profit margin through a focus on core brands and raising productivity in manufacturing operations.

Our focus on core brands put the spotlight on *SCHAU ESSEN* and microwave cooking as a new way to enjoy the sausages and also extended the line with new products, including *SCHAU ESSEN*™ *Hot Chili* and *SCHAU ESSEN*™ *Pizza*. We also

worked to improve the segment’s gross profit margin by strengthening promotional campaigns for core products, particularly *Chuka Meisai*™ and *Ishigama Kobo*™. For the enhancement of productivity in manufacturing operations, we reviewed unprofitable product lines and changed operating days at some factories making ham and sausages from 300 days per year to 250 days per year to standardize our manufacturing plan. These efforts led to a cost reduction. From an investment aspect, the installation of a more efficient, labor-saving line for pizza production generated tangible results, and we plan to apply this approach laterally to other factories as a model for success.

In the gift-giving category, sales volume decreased, as price revisions implemented in line with higher delivery charges made consumers feel that other companies’ products were more affordable. Going forward, we will have to redefine our gift strategy, including measures to deal with skyrocketing personnel costs on manufacturing lines and at gift centers.

Environment Surrounding NH Foods Group (Risks and Opportunities)

In addition to issues shared with other domestic operations, such as rising labor and distribution costs due to a shortage of workers, we expect there is risk of increased prices on principal raw materials, sheep casing, and other materials, owing to an imbalance in global supply and demand caused by an outbreak of African swine fever in China. Meanwhile, wider opportunities for growth are expanding,

including demand for quick meal oriented microwavable products, snacks to go with a drink at home, and purchasing by inbound visitors to Japan.

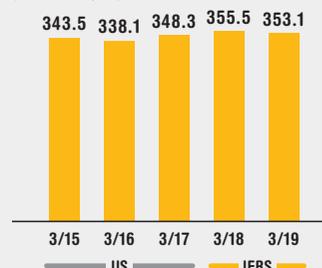
The Processed Foods Business Division seeks to cast off low profitability through such approaches as a review of manufacturing lines and operating costs, and will strive to shape a new food culture with new categories and new hit products.

SHARE OF NET SALES



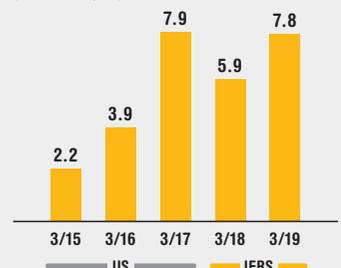
NET SALES

(Billions of yen)



BUSINESS PROFIT

(Billions of yen)



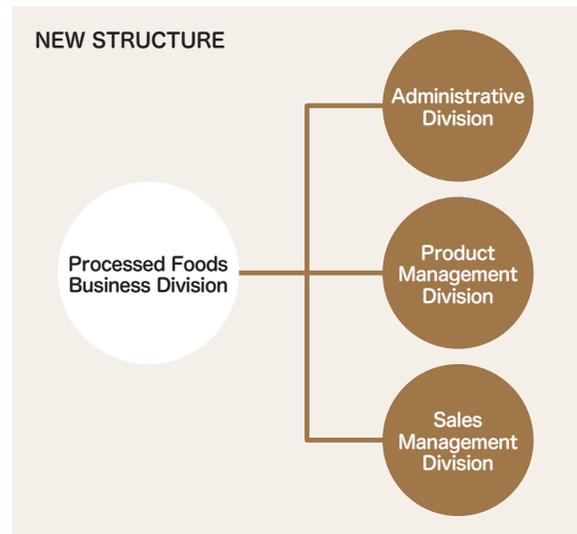
Toward Medium-Term Management Plan 2020 Targets

Restructuring to Cast Off Low Profitability

There was a delay in restructuring the processed foods business, which left the segment with a framework built on conventional concepts and successes of the past. In fiscal 2019, the multi-layered Processed Foods Business Division has been reorganized into three divisions, and, under this new structure, the segment will accelerate decision making and clarify responsibilities and authority, and build a more efficient structure infused with a challenging spirit.

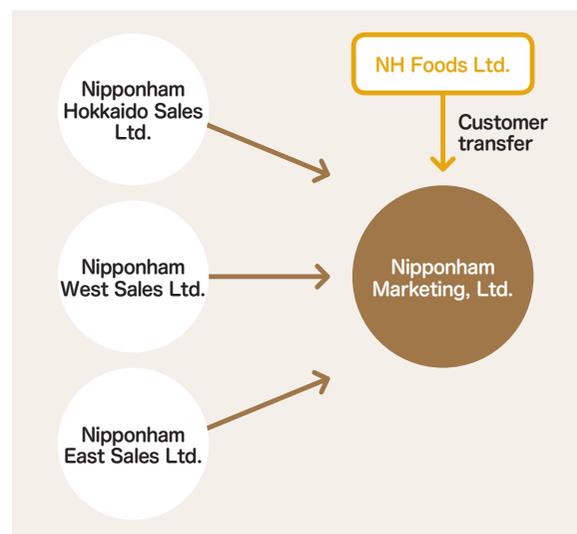
1) Constructively Integrate Ham and Sausages Business Division and Deli and Processed Foods Business Division

Our objective in integrating these two business divisions is to improve productivity by centralizing raw materials procurement and standardizing manufacturing and to reduce costs through the integration of management units. In addition, product development synergies will facilitate mutual use of brands represented by *SCHAU ESSEN Pizza* as well as mutual access to development techniques accumulated over many years. In fiscal 2018, managers in the Ham and Sausages Business Division and Deli and Processed Foods Business Division held concurrent positions in both business divisions, and synergies have already appeared. To further accelerate the process, we will have to hone a sharper competitive awareness and promote greater efficiency and stronger product development capabilities.



2) Stronger Sales Structure

In the sales division, which underpins the business model used for the processed foods business, the sales function that NH Foods and its sales companies had mutually performed was collectively brought under a newly established company—Nipponham Marketing, Ltd.—and, with the transfer of key NH Foods’ customers to the new company, the previously decentralized sales function becomes centralized. We will build a structure that reinforces contact with customers, expands the allocation of brand products, promotes the use of frontline insights in product development, and cultivates new marketing channels, and this will lead to the development of human resources who excel in both product development and sales. In addition, for NH Foods, this structure will turn the sales division into a product development and sales division and enhance the feedback function so that the frontline knowledge of people closest to customers can be applied to the development of new products.



3) Enhancing Efficiency of Staffing Division

By concentrating the marketing function previously executed by each division into one division, we will collectively manage responsibilities and authority for product development and sales promotions and promote effective and efficient campaigns. In addition, the Administrative Division will review business processes and achieve both versatility and specialization to cut costs by about 30%.

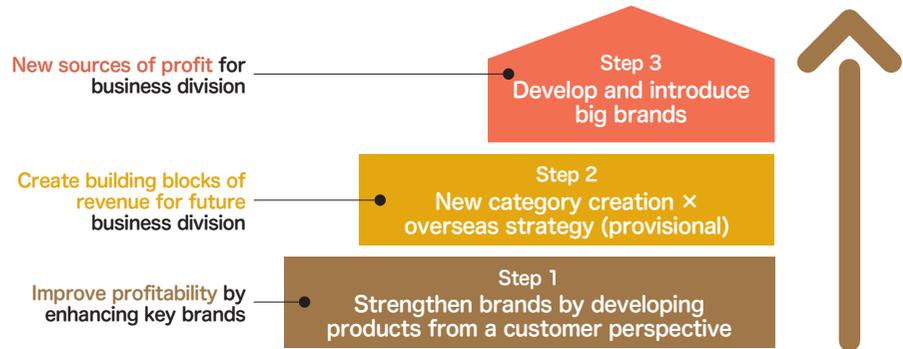
Product Development from Customer Perspective

The Processed Foods Business Division has grown through creativity that translates into hit products and new product categories. But, in recent years, diversifying lifestyles have made it difficult to come up with formulaic hit products. The segment has prioritized efforts to reinforce product development capabilities and will promote reforms in three steps.

In Step 1, we will emphasize brand strengthening through product development from a customer perspective. In Step 2, we will utilize product development capabilities to create new product categories. This will require us to look beyond Japan and select good overseas-made products, which will be the building blocks of stable revenue into the future. In Step 3, we will use these building blocks to cultivate new sources of profits, including wider demand for major brands. For Step 1, which began in fiscal 2018 and is extending through to fiscal 2019, we will launch microwavable

SCHAU ESSEN to meet a growing need for quick cooking options, *SCHAU ESSEN Tray* for sale at convenience stores and aimed at consumers living the single life, and *SCHAU ESSEN Hot Chili* to match current taste trends. We will also capture the interest of new customers, particularly young adults, by complementing existing television commercials with enhanced web-based sales campaigns.

STEPS TO STRENGTHEN PRODUCT DEVELOPMENT CAPABILITIES



Toward a Sustainable Society

Addressing Food Allergies

R&D on foods from a food allergy perspective began in 1996, kindled by customer comments. Nipponham Northeast Ltd., which operates a dedicated factory for products free of seven specified raw materials (milk, eggs, wheat, buckwheat, peanuts, shrimp, and crab) manufactures more than 20 types of products, including ham, sausages, hamburger pate, and bread made with rice flour.

Also, since September 2018, the four companies that make and market similar allergy-friendly foods are collaborating as “Project A”, and working on activities to provide information and raise awareness about food allergies and expand interest in allergen-friendly foods.



Recipes appropriate for people with food allergies are often posted to our website.

Note: See our website for more details.

WEB Allergy-friendly recipes
https://www.nipponham.co.jp/recipes/food_allergy/ (Japanese only)

Toward Medium-Term Management Plan 2020 Targets

Product Launches Matched to Market Needs

To speed up product development, directors and top management of production, sales, and marketing participate in monthly product development review meetings. As a lead-in to cultivate a challenging atmosphere and establish major brands, we hold new product development proposal meetings, involving young members of production and research divisions, and product idea invitation circles to draw up ideas from the sales front line.

For our products launch cycle that used to be twice a year, in March and in August, we have adopted a different approach to deliver more timely responses to market needs and to coincide with the era changeover when Japan's new emperor ascended to the Chrysanthemum Throne in May 2019.

Carving Out New Marketing Channels

To the Group, changes in the market are opportunities for growth, and the Processed Foods Business Division is keen to develop products designed to carve out new marketing channels. In September 2019, we launched *Stock Pork*, a processed meat that can be stored at room temperature, as a stock product for working women and the single segment. In addition to new menu ideas presented at existing sales channels, such as supermarkets, we will utilize other retail networks, such as drugstores and home centers, to draw attention to non-perishable foods, emergency rations, and foods for camping and mountain climbing, as well as the e-commerce channel. We also intend to expand exports.

In other activities, we are involved in collaborative efforts on product development with other companies, and, by creating new products this way, we will create contact points with new customers and raise our brand profile.



Stock Pork, processed meat that can be stored at room temperature

Business model

Development

Toward a Sustainable Society

Reducing Environmental Burden from Packaging

Depletion of resources and issues related to the final disposal sites for garbage as well as the problem of plastics in oceans are topics under a global spotlight. Given greater market awareness, the Group is keen to respond through simplified packaging and other approaches to reduce the environmental burden from containers and packaging. We opted for more lightweight trays and outer wrap for such products as *Chuka Meisai*, *Ishigama Kobo* pizza, and the *Kore wa Benri* series to reduce the amount of plastic used in packaging. We are also contributing to reduced consumption of petroleum and lower CO₂ emissions through the use of biomass packaging made with a certain percentage of plant-based materials for the *Irodori Kitchen* series. Elsewhere, we use recycled PET materials in the packaging for *Kiwami-Yaki™ Hamburger Pate*.

Developing Functional Foods

In response to heightened health needs, we offer the *Healthy Kitchen* series. The ham and bacon in the *Healthy Kitchen ZERO* series has zero carbohydrates* but provides a satisfying texture and a delicious, meaty flavor. The *Healthy Kitchen Green Label* series, a food with functional claims, features gamma-aminobutyric acid (GABA), which benefits the health of individuals worried about high blood pressure.

* Based on Food Labeling Standards. Direct analysis of carbohydrates showed less than 0.5g (per 100g serving), based on Food Labeling Standards, and content is thus listed as zero.

Toward Medium-Term Management Plan 2020 Targets

Improved Business Productivity

From fiscal 2018, we took a revenue emphasis approach to value chains in the processed foods business. To boost productivity, we will work from two sides, seeking to reduce costs and increase gross profit. On the cost reduction front, we will consider asset replacement by investing in laborsaving equipment and abandoning unprofitable lines and apply forward-looking options, such as inspection work using AI. In addition, to deal with rising logistics costs against the backdrop of a labor shortage, we will establish an optimized delivery network based on the wider application of factory direct delivery and joint delivery options.

To increase gross profit, we will strive to offset higher prices on principal raw materials and sheep casing by cultivating new suppliers and reviewing procurement methods to hold down costs. In addition, we will continue to optimize the product mix by introducing new products and extending the selection of brand-based products.



Nipponham Processed Foods Ltd. introduced laborsaving equipment into the pizza line at its Kanto Plant (left) and its hamburger steak line at its Kuwana Plant (right).

Business model

Manufacturing

Toward a Sustainable Society

SDGs Joint Workshop

Targets to achieve Sustainable Development Goals (SDGs) are set for each factory under the Group, and steps are taken at each location toward the realization of a sustainable society, including product development with an SDGs connection, efforts to reduce environmental impact, efforts to create a workplace environment where employees feel motivated, and activities that contribute to the local community. In May 2019, a joint workshop on SDGs initiatives was held at the Kansai Plant of Nipponham Processed Foods Ltd., where participants from three companies and five factories engaged in active opinion exchange and set targets to achieve.



Workshop participants at Nipponham Processed Foods Ltd.'s Kansai Plant

Toward Medium-Term Management Plan 2020 Targets

Thinking Outside the Box

For the processed foods business, which has grown along with successful product development, strong product development capabilities are vital, and this will never change. Cost improvements and greater efficiency are, of course, extremely important, but any progress on these aspects of operations must underpin enhanced product development capabilities.

We have earmarked ¥23 billion for capital expenditures in fiscal 2019, including the greater use of laborsaving features on production lines, construction of a new factory in Hokkaido, and construction of a center to optimize the logistics network. In addition, we will set the stage for developing hit products through such pursuits as the collection of frontline information from sales teams, joint activities with the Lifestyle Research Office, and efforts to encourage young developers to offer ideas.

The Processed Foods Business Division will think outside the box, create categories that shape a new food culture, and establish new brands. This will underpin sustainable growth.



Logistics base with comprehensive low-temperature control features



The *Entier*™ series won a FOODEX Bishoku-Joshi Award 2019 grand prize in the meal category.

Business model

Logistics

Toward a Sustainable Society

Enhanced Logistics Efficiency and Lower Environmental Impact

As the shortage of drivers continues, the Group applies a modal shift and joint delivery to make logistics operations throughout the Group more efficient while reducing environmental impact. At one time, ingredients transported by ship from overseas were discharged at Tokyo and Osaka and then distributed by vehicle to manufacturing points across the country. Now, shipments are discharged at ports close to manufacturing points. Transport from manufacturing points to markets is also changing, with a modal shift from vehicles. In addition, we are promoting joint delivery combining our products with those of other companies.

