

Affiliated Business Division

NH Foods will transition into a manufacturer in the businesses covered by the Affiliated Business Division to promote long-term growth and strive to be an honorable business entity with a sense of presence.

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Executive Officer and General Manager of Affiliated Business Division



Looking Back on Fiscal 2018

The Affiliated Business Division is engaged in businesses across several product groups, mainly marine products and dairy products, and operations hinge on three core companies: Marine Foods Corporation, which specializes in raw fish products for sushi and processed marine products; Hoko Co., Ltd., which handles cheese, canned foods, frozen foods, and freeze-dried foods; and Nippon Luna, Inc., which offers yogurt and lactic acid probiotic beverages.

In the marine products business, sales of sushi toppings—a key category—were up, but sales of products other than sushi toppings stalled, owing to skyrocketing market prices for ingredients and intensifying competition. We streamlined low-profit

products and implemented price revisions and were rewarded with a better profit structure. But the impact of lower sales volume inevitably led to lower profit.

In the dairy products business, sluggish market growth and heightened competition eroded sales of lactic acid probiotic beverages, and with sharply higher expenses for raw materials, personnel, and distribution and start-up costs for a new plant, the business showed a drop in profit.

Consequently, the Affiliated Business Division recorded disappointing results, as sales and operating income dropped year on year, to ¥155.1 billion and ¥400 million, respectively.

Environment Surrounding NH Foods Group (Risks and Opportunities)

In the marine products business, global production and consumption of seafood is increasing, and, in recent years, the aquaculture industry has surpassed the fishing industry. However, in Japan, both production and consumption are on a down-trend. Globally, it will be harder to procure marine raw materials given rising demand, and prices will, undoubtedly, continue to climb. In the dairy products business, the yogurt market had shifted in a favorable direction but this trend may slow. The cheese market is expected to benefit from broader free trade agreement content and remain in a growth mode.

In the marine products business, we aim to improve profits amid skyrocketing raw materials

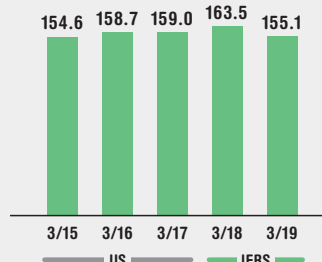
prices by reinforcing procurement capabilities, and we will further implement structural reforms by establishing a raw materials procurement network with locations in Japan and abroad and by leveraging additional business restructuring, including measures to weed out unprofitable products. In the dairy products business, broader free trade agreement content should foster expansion of the snack market, which includes cheese, and the division aims to capitalize on the opportunity. An emphasis will be placed on developing products matched to new trends in the market and evolving customer needs and on making product suggestions more appealing. These efforts will boost sales and underpin an improvement in profits.

SHARE OF NET SALES



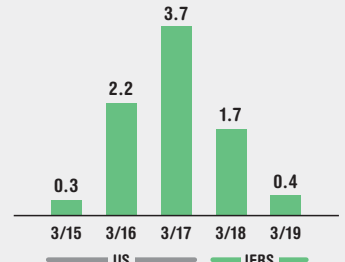
NET SALES

(Billions of yen)



BUSINESS PROFIT

(Billions of yen)



Toward Medium-Term Management Plan 2020 Targets

Reinforce Marine Products Value Chain from Procurement and Supply through to Proposals

For Marine Foods Corporation, the goal is to bolster its marine products value chain, and efforts are being directed toward establishing a raw materials procurement network with locations in Japan and abroad, building a supply structure for company-brand products using its own procurement routes, and strengthening its ability to negotiate business deals with the restaurant market.

Kicking off efforts to establish a raw materials procurement network with locations in Japan and abroad, Marine Foods started purchasing farm-raised salmon from Turkey and engaging in shrimp farming in Thailand. To strengthen procurement in the Far East, the company opened an office in Vladivostok, Russia. The company is also directing efforts toward tuna farming in the Uwakai Sea in addition to domestic *huri* (yellow-tail) farming through joint activities with Yusu Gyogyo Kyodo Kumiai, in Ehime Prefecture. Around autumn 2019, Marine Foods plans to begin domestic sales of farmed shrimp from Thailand and Ehime-raised *huri*.

In efforts to build a supply structure for company-brand products using its own procurement routes, Marine Foods will establish overseas production points, exemplified by the construction of a processing plant in Vietnam. Farmed salmon from Turkey and other raw materials procured through company-carved procurement channels will be processed into sushi toppings in Vietnam. This is one approach to enhancing value chains.

To strengthen its ability to negotiate business deals with the restaurant market, Marine Foods will set up a dedicated team and strive to expand sales mainly by capturing new customers, particularly restaurant chains, a segment of the industry that the company had not really approached before.

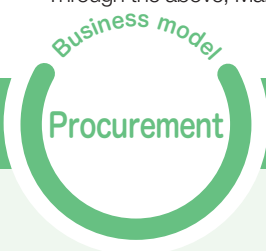
Through the above, Marine Foods will integrate activities from raw materials procurement to menu suggestions and thereby boost total value.



Uwakai fish farm



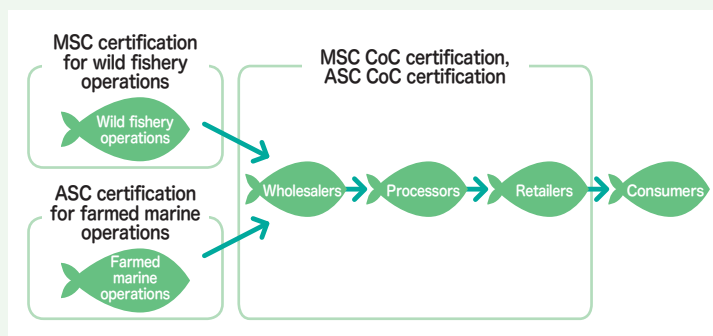
Ehime Uwamaru bluefin tuna



Toward a Sustainable Society

Promoting CSR Procurement

As part of its CSR procurement activities, Marine Foods is working to use sustainable marine resources. In order to enable the processing and distribution of marine products that are in accordance with its receipt of MSC^{*1} certification for wild marine products and ASC^{*2} certification for farmed marine products, in 2018 the company obtained CoC^{*3} certification for some of its seafood. Going forward, in addition to expanding CoC certified seafood, it aims to secure certification for the farmed marine products that are handled by the Group.



*1 This requires certification by a third-party institution based on the "Principles and Standards for Sustainable Fishing" as defined by the MSC (Marine Stewardship Council).

*2 This requires certification by a third-party institution based on the ASC Standards as defined by the ASC (Aquaculture Stewardship Council).

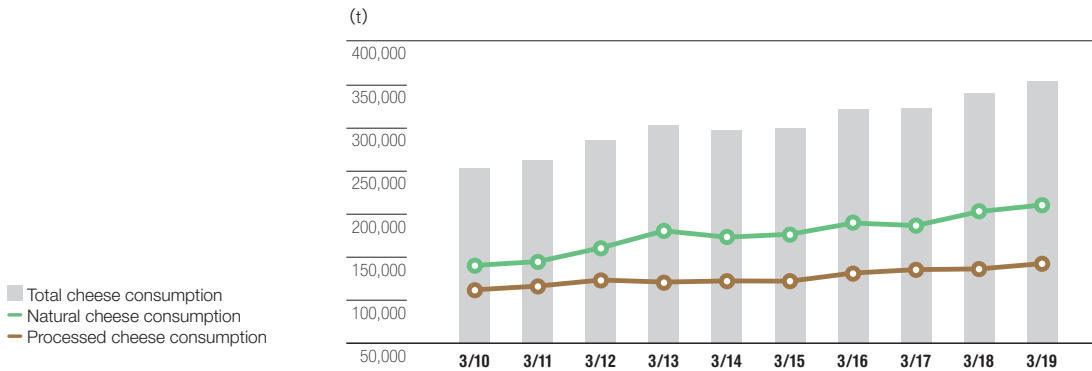
*3 This requires creation and implementation of a management structure that conforms to CoC (Chain of Custody) inspection regulations.

Bigger Share for Cheese Products

Fueled by free trade agreement content, the cheese market is likely to grow. Hoko, with its strength in commercial-use cheese, will capitalize on opportunities to expand sales and capture a larger share of the market.

In raw materials procurement, Hoko will cultivate new procurement points in Europe and North and South America and reduce its reliance on points in Oceania, seeking stability in raw materials procurement. In addition, investment in state-of-the-art facilities using AI and IoT will lead to higher productivity and enhanced cost-competitiveness. An emphasis will also be placed on product development using flexible processing technology, a major strength.

CHEESE CONSUMPTION OVER PAST 10 YEARS



Source: Livestock Industry Department, Agricultural Production Bureau, Ministry of Agriculture, Forestry and Fisheries

Business model

Manufacturing

Toward a Sustainable Society

Reducing Environmental Impact through Printing of Packages

Hoko is aiming to reduce its environmental impact by switching the printing method for the packaging of main products such as its *Rolf Melting Cheese* series to water-based gravure printing. The previous method of oil-based printing uses a large volume of organic solvents, which are a cause of air pollution due to the volatile organic compounds (VOCs^{*4}) they release during the drying process. The switch to water-based gravure printing can reduce the volume of VOCs emitted by around 22%, and the intention is to further expand the number of products for which water-based gravure printing is used.

*4 VOCs include toluene and xylene.



Rolf Melting Cheese

Toward Medium-Term Management Plan 2020 Targets

Reshaping Yogurt Business

Nippon Luna turned in disappointing business results, mainly due to stiffer competition amid sluggish market growth as well as rising costs prompted by the start of operations at a new plant. In fiscal 2019, the company will enhance cost-competitiveness, as the Takasaki Plant moves into full-scale operation. The new plant has an automated, unmanned line, brings container molding in-house, and is equipped with a raw milk ingredients production line. To be better able to offer suggestions to customers, the company will retune its product development structure to match the speed required by major convenience stores. Skyr, a high-protein, zero-fat foodstuff that is a staple food in Iceland, is increasingly gaining popularity in the United States and Europe as a health food. We have been conducting promotional activities ahead of its Japan launch in the spring of 2020 with the aim of creating new value that will resonate with consumers.

Transforming into Honorable Business Entity with Sense of Presence

NH Foods expects investment in the Affiliated Business Division to total ¥4.2 billion in fiscal 2019. In the marine products business, funds have been earmarked to establish joint ventures with local marine products companies, mainly in Thailand and Vietnam, to ensure access to raw materials. In the dairy products business, funds will be applied to improve productivity through upgrades to production equipment for diced cheese and to install equipment for making skyr.

Given the above plans, our approach in the marine products business is not to relax our grip on structural reform but to accelerate business expansion in line with profitability. In the dairy products business, we will seek to create new markets through effective promotional campaigns and expand market share through sharper development and sales capabilities.

In addition, we will vigorously tackle workstyle reform and SDGs and cultivate an environment where employees are excited to come to work and approach their duties with enthusiasm and maintain workplaces that motivate employees.



Toward a Sustainable Society

Environmental Measures at a New Plant

Nippon Luna opened its Takasaki Plant in November 2018 to manufacture items such as yogurt. The plant utilizes a diverse range of measures in order to use energy in an efficient manner, including using waste heat captured from the production lines to heat water in boilers, as well as the installation of an ice thermal storage tank that runs on nighttime electricity and a boiler powered by city gas. In addition, wastewater is treated using equipment that features a special filling material with a high surface area containing micro-organisms, which enables not only more efficient wastewater treatment, but also reduces the volume of sludge produced.



Takasaki Plant, Nippon Luna, Inc.