Japan Integrated Beverage Strategy

Kirin Brewery considers the above-mentioned changes in the business environment as opportunities and seeks to increase profitability to profit margin levels equivalent to those of global beer makers.

Regarding beer (Figure 2), Kirin Brewery will continue to increase the composition ratio of the highly profitable beer category in anticipation of a future revision to the liquor tax. It will consistently seek to enhance the appeal of the beer category, which is a pillar of its strategy in the 2016 MTBP and attain profit growth even in markets where total consumption is declining. The primary focus of the strategy is to raise the brand equity of Ichiban Shibori, strengthen the craft beer business, and expand the Japanese craft beer market. (Please refer to pages 25 – 26 for Ichiban Shibori and craft beer initiatives.)

With the beer liquor tax on the road to unification, the categories of current beers, Happo-shu and new genre will gradually disappear, and other categories will form. Among these, economy products could be a category that accounts for a certain share of the market. To restore current market share and acquire a future presence, even in the economy category, recovering market share in the new genre category is an urgent task. Kirin Brewery will strengthen Nodogoshi, which has been the No. 1* new genre brand in sales in the other brewed liquors (sparkling) 1 category since its launch in 2005. It will also make the new genre product Honkirin, launched in March 2018, a new pillar brand.

The RTD category, which continues to grow, will become even more important due to rising retail prices for beer, future liquor tax revisions, the diversification of preferences, and changes in lifestyles. In the RTD market, the top brands that account for about 60% of the total market are driving growth and product types are diverse. To increase sales volume in these markets, Kirin Brewery will continue to strengthen its core Hyoketsu and Honshibori brands and also expand its brand portfolio. It will nurture Kirin The Strong, launched in April 2018, in higher-alcohol percentage products, which have a particularly high growth rate among RTDs. Furthermore, Kirin Brewery is taking steps to increase the profitability of the RTD category by building production facilities at the Nagoya Plant, responding to growing demand, and streamlining transportation to the east and west.

* 2005 “Other miscellaneous liquors 2.” From 2006 to 2017, based on taxable quantity shipped of “other brewed liquors (sparkling)” 1
A key strategy for achieving these category and brand strategies is Customer-centered Marketing. In Customer-centered Marketing, Kirin Brewery will focus on brands in which it invests and will continuously create points of contact with focus brands and consumers by working its long-term brand plan. Further, it will market based on customer feelings and behavior at points of contact with the brand. This will enable long-term customer engagement by creating integrated communication that captures the “four moments of truth (Four MOTs)” please see page 26 for a description of the Four MOTs) when customers encounter the brand and strengthening digital marketing that leverages consumer data.

In this way, Kirin Brewery will maximize the marketing return on investment, increase brand equity while reducing sales promotion expenses to secure short-term sales volume, and grow into a highly profitable business.

Kirin Beverage has worked to revitalize in line with its 2016 MTBP to solve the challenge of fully implementing a profit focus, strengthening brand equity, and improving cost structure. Kirin Beverage carried out reforms including the introduction of target controls focused on highly profitable containers, released a new version of Nama-cha in March 2016, captured demand from the hand-brewed tea market, successfully revitalized the brand and reduced supply chain costs. As a result, the profit margin improved from 1.5% in fiscal 2015 to 7.6% in fiscal 2017.

Kirin Beverage, which has steadily resolved these challenges will shift from fiscal 2018 to a stage (Figure 3) of “growth-based profit generation” that will raise the top and bottom lines while increasing the profit margin in preparation for sustainable growth. Its goal is to achieve a normalized operating profit margin of 10% by fiscal 2021. The three pillars of the strategy to achieve this are “growth in existing domains,” “initiatives for new domains” and “development of a sustainable framework.”

1 Growth in existing domains (Figure 4)

The basis for growth is to strengthen brands in the domestic beverages business domain, which is now underway. Specifically, Kirin Beverage will allocate, on a priority basis, marketing investments in the foundational brands of Gogo-no-Kocha, Nama-cha, and FIRE to further enhance the brands’ equity. It will build a robust brand portfolio by building brands in the health, Japanese domestic water, and sugar-free tea categories, where further growth is expected.

Figure 3: Kirin Beverage growth strategy for 2021

<table>
<thead>
<tr>
<th>Year</th>
<th>Challenge</th>
<th>Growth in existing domains</th>
<th>Initiatives for new domains</th>
<th>Development of a sustainable framework</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td></td>
<td>Growth-based profit generation</td>
<td>Development of a robust brand portfolio</td>
<td>Strengthening the business base</td>
</tr>
<tr>
<td>2017</td>
<td>Sustainable “profitable growth”</td>
<td>2018 Normalized OP margin</td>
<td>Approx 8%</td>
<td>2021 Target 10%</td>
</tr>
<tr>
<td>2016</td>
<td>Achieve “profitable growth”</td>
<td>2017 Sustainable “profitable growth”</td>
<td>OP margin</td>
<td>7.6%</td>
</tr>
</tbody>
</table>

Figure 4: Growth in existing domains

<table>
<thead>
<tr>
<th>Category</th>
<th>Brand</th>
</tr>
</thead>
<tbody>
<tr>
<td>Black tea</td>
<td>Kirin</td>
</tr>
<tr>
<td>Carbonated drinks</td>
<td>Kirin</td>
</tr>
<tr>
<td>Specialty drinks</td>
<td>Kirin</td>
</tr>
<tr>
<td>Fruit juice</td>
<td>Kirin</td>
</tr>
</tbody>
</table>

Explore to tap new categories while continuing the advance into the health and well-being, own-brand water and sugar-free tea categories.
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2 Initiatives in new domains
With limited growth expected in the domestic beverage market, we need to plant seeds for the future to achieve sustainable growth. Kirin Beverage will consider all possible new initiatives to expand the world of beverages, including brand alliances and overseas expansion.

2 Development of a sustainable framework
To raise brand equity and further strengthen the profit base, Kirin Beverage will conduct CSV activities (Figure 5), promote greater efficiency, and further reduce costs. Kirin Group’s key CSV Issues of health and well-being, community engagement, and the environment will help strengthen the brand and achieve greater cost efficiency. In addition to addressing issues common to the industry, alliances with competitors to reduce costs that cannot be achieved independently will be actively considered.

As a leading domestic company, Mercian will enhance the appeal of wine and continue to grow by driving market expansion. It will also continue to improve productivity, minimize the impact of fluctuations in raw material prices and exchange rates, and improve profitability.

To enhance the appeal of diverse wines, Mercian will make a selective, focused allocation of resources on brands to be strengthened in each area, while it addresses all areas including fine wine, mid-price range, daily wine domestic production, and daily wine imports. In this way, it will build a highly profitable product portfolio.

In the fine wine domain, Mercian will continue to fortify its flagship brand Château Mercian. The raw grapes for the Japanese wine Château Mercian are cultivated by Mercian or by contract in four Japanese prefectures, and Mercian plans to build two more wineries in the future (Figure 6). Mercian seeks to create Japanese wine brands through community engagement by strengthening its Château Mercian business.

Mercian will also fortify its brands in the mid-price range and daily wine domains and address the polarization of consumption. In mid-price wines, it will maintain its focus on Casillero del Diablo, as well as advertise, promote sales, and develop new products. Daily wine, which is driving the growth of the whole market, will not only boost sales of domestically produced daily wine, but also of imported daily wine, including Chilean wines, which continue to enjoy high growth.

Mercian will work to improve productivity at its factories, headquarters and sales departments, and increase profitability.

Mercian

Market environment
Although an increase in total demand in the domestic alcoholic beverages market is limited, wine, with its diversity and healthy image, is expected to grow steadily over the medium to long term in a category that has grown 1.5-fold over the past 10 years. Wine, which has established itself as a daily alcoholic beverage, is driven by the household market and tends to polarize consumption into daily wine and high-priced/fine wine.

Health and well-being
- In addition to developing products utilizing Lactococcus lactis strain Plasma, provide health value with food for specified health uses and food with function claims
- Focus on developing non-sugar and decaffeinated products

Community engagement
- Expanding our support of Sri Lankan black tea farmers to small-scale farmers, to assist in their efforts to acquire the Rainforest Alliance certification
- Conservation of the water resources of those farmers

The Environment
- Promotion of resource conservation including the reduction of container weight
- Reduction of environmental impact throughout the value chain

Mercian will work to improve productivity at its factories, headquarters and sales departments, and increase profitability.

Figure 6: Creating new Château Mercian wineries