

Pharma Foods International Co., Ltd.

2929

Tokyo Stock Exchange Prime Market

26-May-2023

FISCO Ltd. Analyst

Masanobu Mizuta



FISCO Ltd.

<https://www.fisco.co.jp>

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Summary

A biotechnology company aiming to create pharma foods by fusing pharmaceuticals and foods

Pharma Foods International Co., Ltd. <2929> (hereafter, also “the Company”) is a biotechnology company whose basic policy is to conduct business that contributes to people’s health by aiming to create pharma foods through fusing pharmaceuticals and foods. By focusing on raw ingredients derived from nature and providing proprietary technologies and products that are based on scientific evidence, it is creating food ingredients that clearly function to improve both health maintenance and QOL (Quality of Life).

1. Company profile

With a sustainability vision of meaningful prosperity and health in an era with lives spanning 100 years, the Company seeks to realize a sustainable society in which people are happy and healthy. To achieve this goal, it develops food products, cosmetics, and pharmaceuticals based on scientific evidence and broadly provides them to society in three business, the BtoB business, BtoC business, and Bio Medical business. The BtoB business manufactures and sells functional ingredient products such as PharmaGABA®, and through Meiji Yakuin Co., Ltd., which was made into a subsidiary in August 2021, it manufactures and sells pharmaceutical and non-pharmaceutical products. The BtoC business conducts e-commerce sales and wholesale distribution of supplements, non-pharmaceutical products, and cosmetics that blend the Company’s proprietary functional ingredients. The main product is Newmo® Hair Growth Formula, a hair restoration and new growth stimulant. The Bio Medical business is involved in drug discovery using ALAgene® technology, the Company’s proprietary technology for producing antibodies from chickens, and other technologies.

2. Outline of results for 1H FY7/23

In the Company’s 1H FY7/23 consolidated results, net sales increased 21.9% year on year (YoY) to ¥35,143mn, operating loss was ¥883mn (¥2,032mn profit in the same period of the previous fiscal year), ordinary loss was ¥912mn (¥2,105mn profit), and loss attributable to owners of parent was ¥914mn (¥1,561mn profit). Although net sales increased amid steady growth of the mainstay BtoB and BtoC businesses, the Company recorded losses for each profit type due to ongoing aggressive investment in new product research and development and investment in advertising to promote growth. Meanwhile, looking at quarterly results, the Company recorded losses in 1Q (August–October 2022) due to a significant increase in advertising expenses, but then recorded an increase in net sales in 2Q (November 2022–January 2023) relative to those of 1Q due to factors that include effectiveness of advertising and contribution of new products, thereby culminating in a shift to positive results facilitated by effective use of advertising expenses.

Summary

3. Outlook for FY7/23

For its FY7/23 consolidated results, the Company has maintained its initial forecasts which project net sales to increase by 18.0% YoY to ¥71,000mn, operating profit to increase 10.3% to ¥1,191mn, ordinary profit to edge up 0.3% to ¥1,268mn, and profit attributable to owners of parent to be ¥886mn (loss of ¥374mn in the previous fiscal year). The Company will continue to focus on M&A and building alliances, and intends to establish overseas sites and actively expand, but it plans to offset this by achieving higher sales in all segments. Although the Company recorded losses in 1H, FISCO thinks the Company will most likely attain its initial forecasts considering factors that include the notion that it shifted to positive results in the three months of 2Q in part given the effectiveness of advertising and contribution of new products, and the notion that its advertising expenses in 2H are expected to be lower than the initial estimates.

4. Growth strategy

In its Medium-Term Management Plan 2026, the Company has established “new value creation 1K” as a goal, and through initiatives to create new value (new products, new markets, and a new organization), seeks to be a company with net sales of ¥100.0bn by FY7/26. Regarding its approach to profit levels, it will conduct business development through FY7/26 without concerns over a decline in profit margin each year and intends to expand in scale while boldly taking on risk. The Company is aiming to create a structure that can secure an average operating profit margin of 10%. It has been making progress in reducing its risk of dependence on hit products. For instance, in the BtoC business it has been achieving steady growth with new products that support Newmo® Hair Growth Formula, and in the BtoB business it has been encountering expansion with respect to PharmaGABA® and the CMO*1 business and has launched its new Meiseki Lab product, which is the first in a series of Company’s national brand (NB)*2 products. In the Bio Medical business, expectations for drug discovery and development are rising. Business results for the immediate future may vary depending on the level of investment in advertising, but through new product and new market creation and active business development, FISCO believes the Company has high potential for medium- to long-term growth.

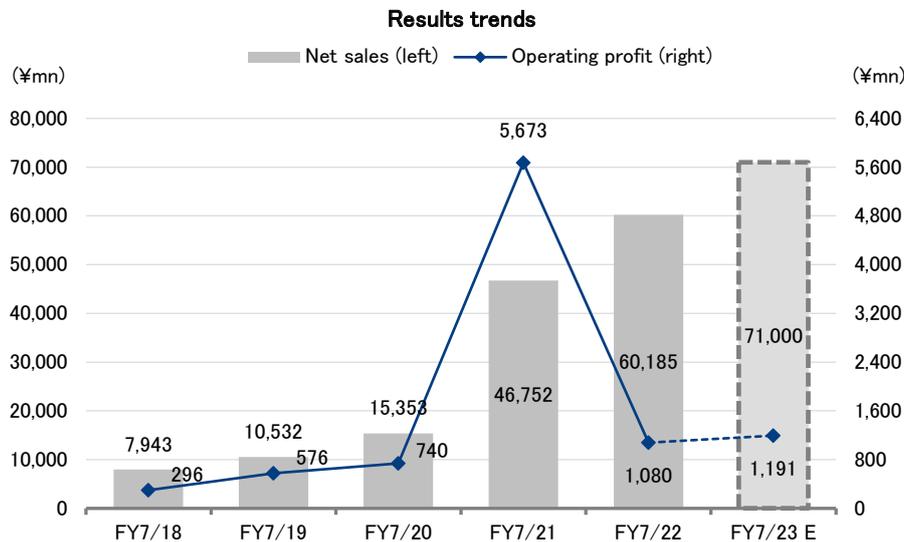
*1 Abbreviation for contract manufacturing organization.

*2 Abbreviation for national brand, and refers to brands associated with the Company’s own products.

Key Points

- A biotechnology company aiming to create pharma foods by fusing pharmaceuticals and foods
- For FY7/23, the forecast for higher net sales and profits remains unchanged, with upside potential brought about by rationalization of investment in advertising
- Aiming for net sales of ¥100.0bn in FY7/26 through initiatives to create new value

Summary



Source: Prepared by FISCO from the Company's financial results

Company profile

Creates food ingredients that clearly function to improve both health maintenance and QOL

1. Company profile

The Company is a biotechnology company whose basic policy is to conduct management that contributes to people's health by aiming to create "pharma foods" by fusing pharmaceuticals and foods. With a development concept of immunity, aging, and the nervous system, three important elements in life activity and health maintenance, the Company examines everyday foods and ingredients like eggs, milk, green tea, rice, and lactic acid bacteria for components that act on these three elements, and by providing proprietary technologies and products based on scientific evidence, it creates food ingredients that clearly have functions helpful to health maintenance and enhancing quality of life.

At the end of 1H FY7/23, the location of the Company's headquarters was in Nishikyo Ward, Kyoto City, and the Pharma Foods International Group consisted of the Company, its five consolidated subsidiaries (PharmaFoods Communication Inc., FUTURE LABO Inc., medi-labo Co., Ltd., Meiji Yakuin Co., Ltd., and PF Capital) and two equity-method affiliates (Benart Co., Ltd., and Onkyo Home Entertainment Corporation). PharmaFoods Communication conducts call center operations for the BtoC business, and FUTURE LABO and medi-labo sell cosmetics, Meiji Yakuin manufactures and sells pharmaceuticals and non-pharmaceutical products. PF Capital (which became a subsidiary following acquisition of the CVC operating company in May 2022) manages the PF Visionary Fund, a limited liability investment partnership established in January 2023.

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Company profile

At the end of 1H FY7/23, total assets were ¥33,875mn, net assets were ¥5,752mn, capital was ¥2,042mn, the equity ratio was 17.0%, and the number of issued shares was 29,074,500 shares (includes 233,970 treasury shares).

2. History

The Company was established as Pharma Foods Research Co., Ltd. in September 1997 in order to develop and sell functional food ingredients, and then changed its trade name to Pharma Foods International Co., Ltd. in October 2004. Regarding the main functional ingredient products, sales of the GABA-containing ingredient PharmaGABA® began in September 2001, the e-commerce sales brand Tamagokichi® and the Tamagosamine® with iHA® formulation supplement were launched in August 2012, and Newmo® Hair Growth Formula, a non-pharmaceutical product formulated with HGP® (Hair Growth Peptide), was launched in November 2018.

In M&As and alliances, the Company concluded capital and business alliance agreements with Sanyo Chemical Industries, Ltd. <4471> in March 2021, and with ROHTO Pharmaceutical Co., Ltd. <4527> in July 2021, respectively. In August 2021, it invested in Ai-BrainScience Inc., which develops a cognitive function diagnosis app, while it also made a wholly owned subsidiary of Meiji Yakuhi. In December 2021, it concluded a business alliance agreement with Onkyo Home Entertainment Corporation (made an equity-method affiliate in May 2022 through third-party allocation of shares) and entered the hearing aid business. The Company obtained the bioscience business (proteome analysis business) of Intégrale Co., Ltd., which possesses top-level results and technological capabilities in protein analysis in Japan, via an absorption-type split in April 2022. Additionally, in July 2022, it made joint investments with ENEOS Holdings <5020> in ENEGGO Inc., which manufactures liquid fertilizers derived from eggs. Most recently, the Company concluded a memorandum of understanding in December 2022 regarding the establishment of a joint venture involving three companies with respect to a health food factory in Vietnam (The MoU pertains to construction of a health food factory in Vietnam, with the intent to make sales through Long Chau Pharmacy; details to be adjusted going forward). The joint venture consists of the Company, FPT Digital Retail Joint Stock Company ("FRT"), owner of Vietnam's major pharmacy chain Long Chau Pharmacy, and Sato Connect Gate Joint Stock Company by VTM Group ("SCG"). In March 2023, the Company concluded a capital and business alliance agreement with LB Co., Ltd., which has strengths in manufacturing yogurt and lactic acid beverages (underwriting of third-party allocation of class A preferred shares).

Regarding shares, the Company listed shares on the Tokyo Stock Exchange (TSE) Mothers Market in June 2006, switched to the TSE Second Section in December 2016, and moved to the TSE First Section in February 2021. It transitioned to the Prime Market accompanying the change in TSE market categories in April 2022.

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Company profile

History

Date	Event
September 1997	Pharma Foods Research Co., Ltd. was established in order to develop and sell functional food ingredients
May 2001	Market launched Ovopron®, a helicobacter pylori chicken egg antibody
September 2001	Market launched PharmaGABA®, an ingredient containing GABA
October 2003	Market launched Pharma Foods Delicious Catechin™, an ingredient containing catechin
October 2004	Changed trade name to Pharma Foods International Co., Ltd.
March 2005	Market launched PF Alpha Lipoic Acid™, an ingredient containing alpha lipoic acid
June 2006	Listed on the TSE Mothers market
October 2006	Market launched Runpep®, an egg white peptides ingredient
April 2007	Established Hiroshima Bio Medical Co., Ltd. in order to conduct an R&D business in the field of blood purification therapy using chicken egg antibodies and to conduct a business for test drugs and reagents (Company's investment ratio: 49%)
February 2012	Launched the Bio Value business
July 2012	Market launched iHA®, a hyaluronic acid production-stimulating ingredient Invested in and made an affiliate of Benart Co., Ltd., which conducts a solar power generation business, in order to enter the renewable energy field (Company's ratio of shareholding: 33.3%)
August 2012	Market launched the e-commerce sales brand Tamagokichi® and Tamagosamine with iHA®
October 2012	Sold some of its shares of Benart (Company's ratio of shareholding: 50%, currently an equity-method affiliate)
September 2013	For the fully fledged development of the drug discovery business, conducted an absorption merger of Hiroshima Bio Medical and established the Bio Medical Department
September 2014	Opened the Company's own call center for the Tamagokichi® e-commerce sales brand
May 2015	Acquired the ISO 9001 quality management system certification
August 2015	Established PharmaFoods Communication Inc. to conduct call center operations for health foods and cosmetics (made a wholly owned subsidiary in December 2018, currently a consolidated subsidiary)
November 2016	To expand the Bio Value business, made FUTURE LABO Inc. a subsidiary (currently a consolidated subsidiary)
December 2016	Listing was changed to the TSE Second Section
October 2018	Concluded a joint research agreement with Mitsubishi Tanabe Pharma Corporation for antibody pharmaceuticals indicated for the treatment of autoimmune diseases
November 2018	Market launched Newmo® Hair Growth Formula, a non-pharmaceutical product formulated with HGP®
January 2021	Concluded an exclusive licensing agreement with Mitsubishi Tanabe Pharma for a new therapeutic antibody to treat autoimmune diseases
February 2021	Listing was upgraded to the TSE First Section
March 2021	Concluded a capital and business alliance agreement with Sanyo Chemical Industries <4471>
July 2021	Concluded a capital and business alliance agreement with ROHTO Pharmaceutical <4527>
August 2021	Invested in Ai-BrainScience Inc., which is developing a cognitive function diagnostic app Made a wholly owned subsidiary of Meiji Yakuin Co., Ltd., which manufactures and sells pharmaceuticals and non-pharmaceutical products
September 2021	Formulated the Agriculture and Nutrition Basic Plan with Sanyo Chemical Industries
December 2021	Concluded a business alliance agreement with Onkyo Home Entertainment Corporation and entered the hearing aid business Entered a new upcycle business using eggshell membranes
April 2022	Obtained the bioscience business of Intégrale Co., Ltd. via an absorption-type split Transitioned to the Prime Market accompanying the change in TSE market categories
May 2022	Made Onkyo an equity-method affiliate
July 2022	Received third-party allocation ENEGGO shares jointly with ENEOS Holdings <5020>
December 2022	Concluded memorandum of understanding related to establishment of a three-company joint venture with respect to a health food factory in Vietnam, between the Company, FRT, and SCG
January 2023	Established PF Visionary Fund, a limited liability investment partnership
March 2023	Concluded a capital and business alliance agreement with LB Co., Ltd.

Source: Prepared by FISCO from the Company's securities report and press releases

Business summary

Develops BtoB business, BtoC business, and Bio Medical business

The Company performs research on pharmaceuticals and functional ingredients that act on immunity, aging, and the nervous system. Based on its research results, it conducts BtoB sales of functional raw materials to food product manufacturers and other companies, engages in the BtoC business in conducting e-commerce sales and wholesale of supplements and cosmetics formulated using the Company's proprietary functional ingredients, and engages in the Bio Medical business in licensing out chicken antibodies to pharmaceutical companies. The Company is a fables company that conducts R&D, marketing, and sales, established manufacturing methods and production process, and monitors health and safety management while contracting out product production to outside manufacturing partners.

Development of pharmaceuticals and functional ingredients that act on immunity, aging, and the nervous system

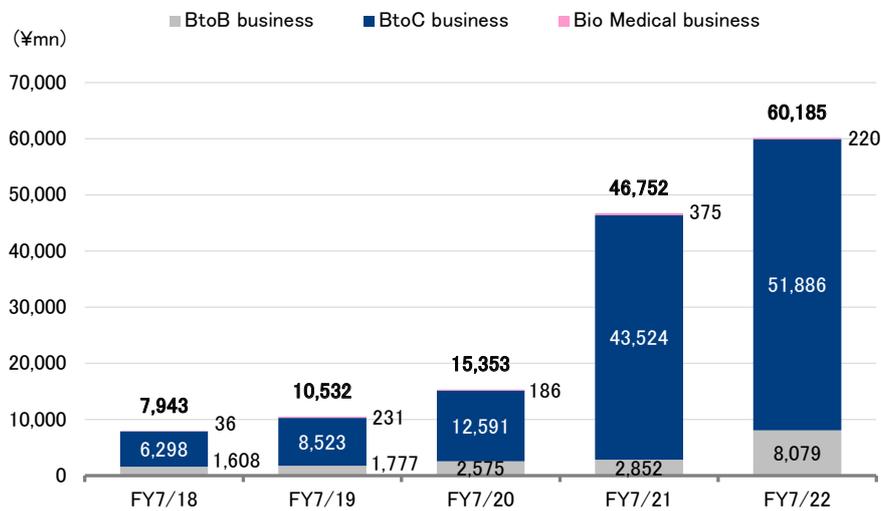


Source: The Company's results briefing materials

Looking at the trends in net sales and operating profit by business segment in the most recent five periods (FY7/18 to FY7/22), in the BtoB business, net sales and operating profit grew steadily alongside the increase in the number of adopting companies. Meanwhile, Meiji Yakuin began contributing to results in FY7/22. In the Integral's BtoC business, Newmo® Hair Growth Formula, which was launched on the market in November 2018, has become a hit product and is contributing greatly to earnings overall. In addition, Meiji Yakuin's Shiboranaite® GOLD also contributed to results in FY7/22. The Bio Medical business is at the development stage and it records lump-sum income relating to joint research and licensing as sales.

Business summary

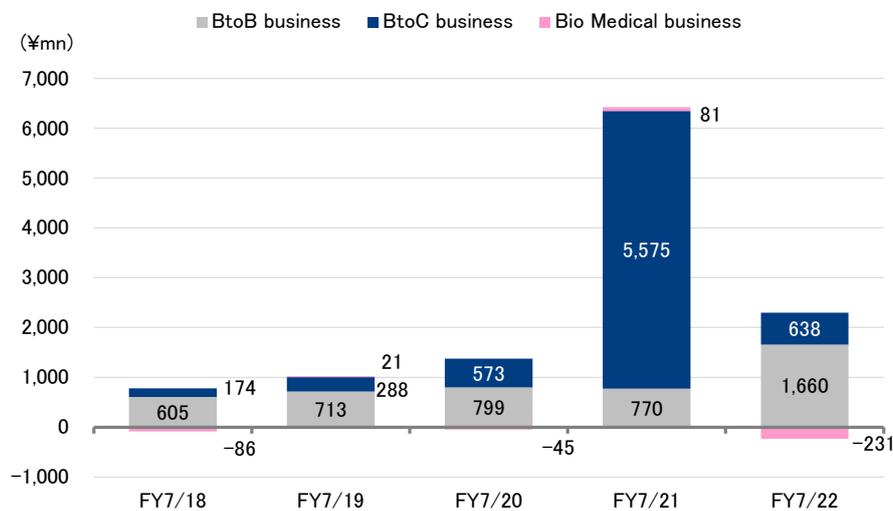
Trends in net sales by business segment



Note: Segment classifications and names changed as of 2Q FY7/22. The Accounting Standard for Revenue Recognition, etc. applied as of FY7/22

Source: Prepared by FISCO from the Company's financial results

Trends in operating profit by business segment



Note: From FY7/19, the Company changed the method of displaying Company-wide expenses and amortization of goodwill to a method displaying the adjustment amounts. Figures for FY7/18 reflect this change.

Segment classifications and names changed as of 2Q FY7/22. The Accounting Standard for Revenue Recognition, etc. has been applied since FY7/22

Source: Prepared by FISCO from the Company's financial results

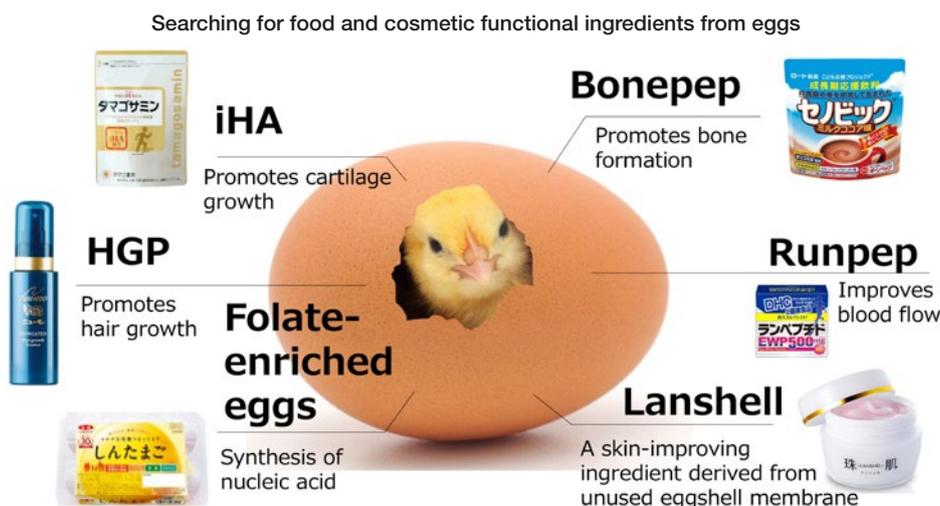
Business summary

Mainstay BtoB business product PharmaGABA® holds top share in GABA production. Contributions also made by Meiji Yakuhin’s CMO and CHC businesses

1. BtoB business

The BtoB business handles R&D and manufacturing of functional ingredients, health foods, pharmaceuticals, and other products and sells them to food and pharmaceutical manufacturers, distributors, and others. The Company’s main functional ingredient products are PharmaGABA®, Bonepep®, Cerepron®, Runpep®, Pharma Biomix, HGP®, iHA®, and Moringa. Additionally, from 2Q FY7/22, Meiji Yakuhin’s contract manufacturing organization (CMO) business and CHC business*, which sells functional foods, pharmaceuticals, and other products mainly in the drugstore channel, as new manufacturing and sales channels, and from FY7/23, the Company’s own brand products have been included. The Company maintains a policy of developing and expanding its own brand products as growth drivers of the BtoB business segment.

* Abbreviation for consumer health care (refers to selling pharmaceuticals, functional foods, and other products at



Source: The Company’s results briefing materials

Trends in net sales by item

	FY7/21				FY7/22				FY7/23	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q
Functional ingredients	334	518	501	754	252	431	391	633	375	440
OEM, NB, etc.	126	179	267	169	252	169	242	261	289	484
CMO						1,672	948	1,021	892	1,104
CHC						869	466	465	312	172
Total	460	698	769	924	504	3,143	2,048	2,382	1,869	2,201

Source: Prepared by FISCO from the Company’s results briefing materials

Business summary

(1) PharmaGABA®

PharmaGABA® is the Company's mainstay product. GABA is a type of non-protein amino acid produced by animals and plants and microorganisms, and is said to act as a neurotransmitter in the brain's inhibitory system. The Company separated the GABA-producing lactic acid bacteria in food and established a method of producing GABA through a fermentation method, which it sells as PharmaGABA®. PharmaGABA® is able to display functional claims, including relieving stress, reducing fatigue, improving blood pressure, and improving sleep quality, and its adoption for foods with functional claims is growing. In the number of GABA notifications in the foods with functional claims system at the end of February 2023, it ranked highest with 837 notifications (Company data) and is maintaining a track record of adoptions. The growing adoptions of GABA by food manufacturers is leading to an increase in orders for PharmaGABA® made by the Company, which holds the top share of GABA.

“PharmaGABA® has also been found to have other effects, including increasing muscle mass, improving cognitive functions, and improving skin elasticity, and the evidence for it is further strengthening. The Company is also selling it overseas and is aggressively expanding sales activities in North America, China, and other regions, and its adoptions are growing. In FY7/23, CENTR in the United States began selling beverages that claim to enhance cognitive function containing PharmaGABA® in California, Texas, and online, thereby marking the first time such beverages have been offered in North America. In South Korea, PharmaGABA® has been adopted by Amorepacific Group's Vitalbeautie brand of beauty drinks. With PharmaGABA® having acquired halal certification, the Company intends to fully launch sales in the Southeast Asian region where there are many Muslim people.

(2) Bonepep®

Bonepep® is a functional ingredient derived from egg yolk protein that was developed as a component to stimulate bone growth. A typical product that adopts it is Senobic sold by ROHTO Pharmaceutical.

(3) Cerepron®

Cerepron® is a functional ingredient derived from yeast as a skin whitening ingredient in food (active yeast extract powder) that can be expected to have skin whitening effects. Demand for skin whitening is increasing particularly in overseas markets, and its adoptions are growing mainly in Southeast Asia.

(4) Runpep®

Runpep® is a functional ingredient derived from egg white protein that was developed to be a component with blood vessel expansion and blood flow improvement effects. It is being adopted for products relating to improving blood flow and reducing exercise fatigue, diet-related products, and male-function products.

(5) Pharma Biomix

Pharma Biomix is a feed supplement to help hens to lay folate-enriched eggs. Within Japan, it has been adopted by JA.Z-TAMAGO. CO., LTD. for its “Shin-Tamago” and “Brown Shin-Tamago” products, and overseas, it has been adopted by Pulmuone Co., Ltd. (Pulmuone) in South Korea for functional eggs.

(6) HGP®

HGP® is a functional ingredient derived from egg yolk protein that was developed as a component that stimulates hair restoration and growth. Research results have been obtained that demonstrate the effects of taking the oral formulation, and it is being adopted by Japanese manufacturers and others.

(7) iHA®

iHA® is a functional ingredient derived from egg yolk protein that was developed as a component stimulating the production of hyaluronic acid. Research results have verified its effects in animal experiments, and it is being adopted for the Company's e-commerce sales products and the products of domestic manufacturers.

Business summary

(8) Moringa

Moringa is known to be a superfood and since ancient times, it has been used as herbal medication in Indian Ayurveda medicine. Research results have shown that it has an anti-aging effect, and it is being adopted for and used to create products in the foods and supplements fields.

(9) OEM and NB business

In OEM business, in addition to selling various functional ingredients, the Company not only conducts outsourced OEM production but also plans and sells products including health foods and supplements that utilize the evidence cultivated in the development of functional ingredients, both in Japan and overseas, as an OEM business.

Under its policy going forward, the Company aims to expand the OEM and NB businesses for its own products as an area of focus, thereby shifting from sales of functional raw materials to sales of end products. In FY7/23, the Company began selling its new Meiseki Lab product, the first in a series of its own NB products, at major convenience stores. The drink, which contains a maximum of 200 mg of GABA, is expected to help maintain people's ability to think logically, which is said to decline with age. In addition, the Company also sells Muscle Lab, which facilitates maintenance of muscle mass, and Sleep-enhancement Drink, which is useful for improving sleep quality, as the second series of products. In March 2023, the Company concluded a capital and business alliance agreement with LB Co., Ltd., which has strengths in manufacturing long-life yogurt and lactic acid beverages. The Company aims to expand its NB business, focusing on major convenience stores and drugstores, particularly through joint development of beverages and other such products using functional ingredients.

As for the OEM business overseas, the Company has achieved expanded adoption of PharmaGABA® in North America and South Korea, and in December 2022 concluded a memorandum of understanding regarding establishment of a three-company joint venture with respect to a health food factory in Vietnam, with FRT, owner of Vietnam's major pharmacy chain Long Chau Pharmacy, and SCG. Whereas this entails construction of a health food factory in Vietnam with plans to make sales through Long Chau Pharmacy, adjustments are to be made going forward concerning details such as scheduling regarding joint venture company establishment and factory construction, as well as the investment ratio.

(10) CMO business

In the CMO business, Meiji Yakuin receives consignments to manufacture ethical pharmaceuticals and OTC pharmaceuticals from pharmaceutical companies. Manufacturing inquiries have been trending upward at Meiji Yakuin following several business suspensions due to legal violations at multiple companies in the domestic generic drug industry.

(11) CHC business

In the CHC business, Meiji Yakuin is selling its brand products to drugstores and other distribution channels. Sales have also risen to cross-border EC distributors in recent years.

Business summary

BtoC business strengthens the product lineup led by Newmo® Hair Growth Formula, with growth in new products as well

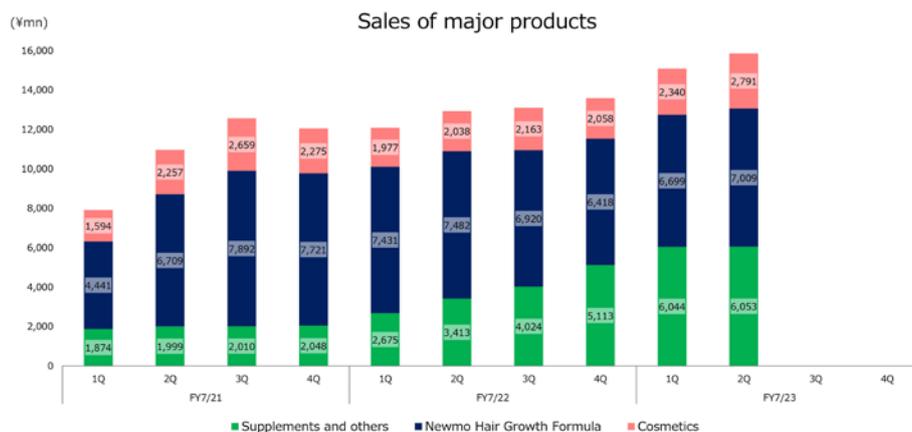
2. BtoC business

As an “invention company’s e-commerce business,” the BtoC business sells health foods and non-pharmaceutical products (under the Tamagokichi®) formulated using the Company’s proprietary functional ingredients and cosmetics (including under the FUTURE LABO brand). Sales methods comprise direct sales to consumers through e-commerce and wholesales to dedicated shopping channels. Furthermore, Meiji Yakuhi’s new repeat e-commerce business has been included from 1H FY7/22.

Main products include Tamagosamin® (iHA® formulation supplement for knee joints); non-pharmaceutical product Newmo® Hair Growth Formula (hair restoration and new growth stimulant); and Tamahada Lanshell® (cosmetic cream formulated from active eggshell membranes), Tamahada Nou Mitsu®, and Derma Qll® (keratin peeling gel) in cosmetics. In February 2021, the Company launched sales of Has V, a schedule III pharmaceutical, as phase 1 of its entry into the pharmaceutical e-commerce market.

By item, Newmo® Hair Growth Formula, which promotes hair growth and restoration, has become a hit product, reaching No. 1 in sales in the hair care market in just two years since its launch and contributing greatly to overall earnings. In addition, the Company has achieved growth also with products such as Eyelash Deluxe WMOA, launched in FY7/22, and its DRcula series of medicated toothpastes. Going forward, the Company intends to expand its product lineup around its mainstay Newmo® Hair Growth Formula.

Net sales by item in the BtoC business



Sales of major products

(¥mn)

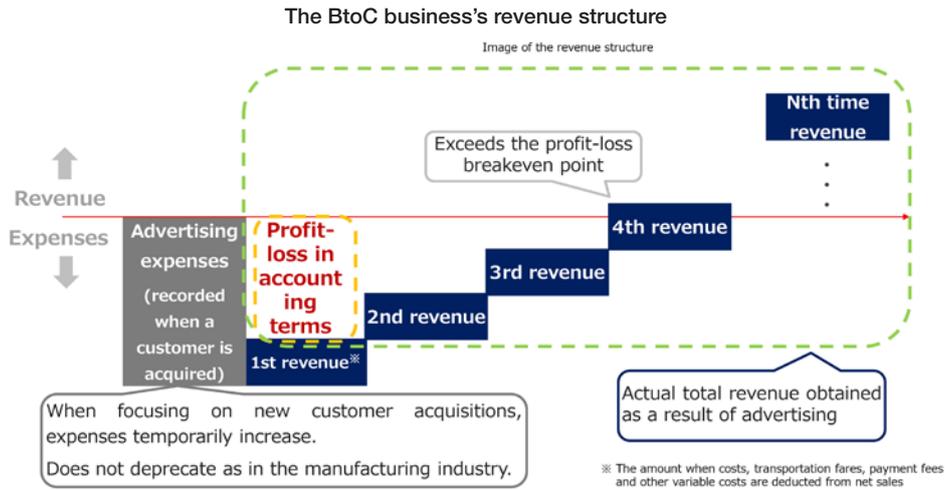
	FY7/21				FY7/22				Current fiscal year	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q
Tamahada Lanshell	118	131	170	127	118	121	238	508	644	856
Color shampoo									324	467
Newmo Hair Growth Formula	4,441	6,709	7,892	7,721	7,431	7,482	6,920	6,418	6,699	7,009
Eyelash beauty serum					74	917	879	922	1,488	1,441
Shiboranaito GOLD					8	652	2,534		2,390	1,840
Lactulose tablets									210	544

Source: The Company’s results briefing materials

We encourage readers to review our complete legal statement on “Disclaimer” page.

Business summary

It is necessary to be aware that the revenue structure of the BtoC business is a structure in which advertising expenses and sales occur in different periods. Specifically, advertising expenses are recorded at the time a new customer is acquired, but net sales are recorded continuously over the regular course. So, when the Company focuses on acquiring new customers, this temporarily causes expenses to increase. However, repeat purchases generated from the base of regular customers give rise to future profits.



Source: The Company's results briefing materials

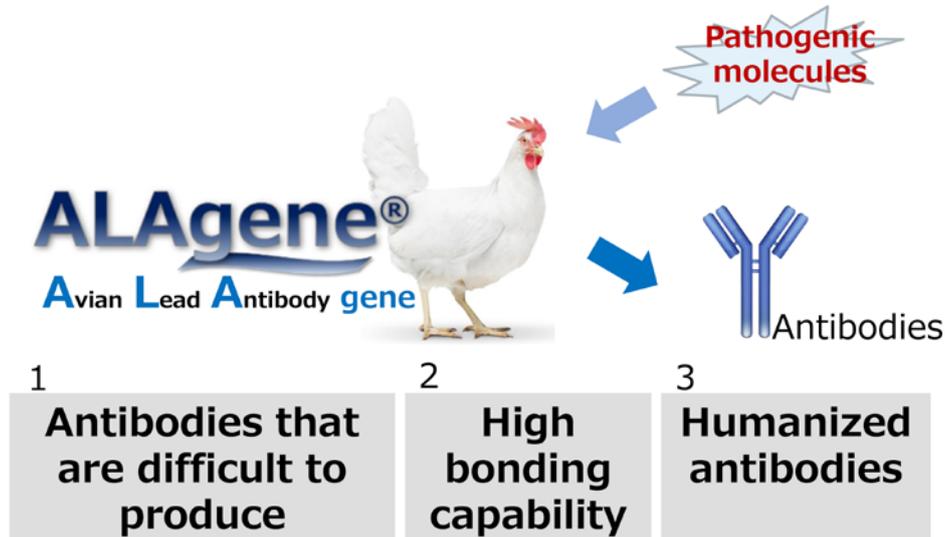
Bio Medical business develops a drug discovery business using its proprietary ALAgene® technology

3. Bio Medical business

The Bio Medical business is a drug discovery business that uses ALAgene® technology, the Company's proprietary technology to produce antibodies derived from chickens, and a technology to develop bioactive peptides derived from chicken egg yolk. Additionally, the Company is developing Intégrale's Bio Science Business (proteomic analysis business), which it assumed in April, 2022.

Business summary

Producing antibody pharmaceuticals from chickens



Source: The Company's results briefing materials

ALAgene® technology is a foundational Company technology that makes possible the production of antibodies for drug discovery target molecules that are difficult to produce using conventional technologies. The Company is using this technology to conduct R&D into antibody pharmaceuticals indicated for patients with autoimmune diseases and malignant tumors. In addition, Reprotite®, a peptide derived from chicken egg yolk developed by the Company, has been successfully isolated and identified as a bioactive material involved in bone formation, and the Company is developing it as an important pipeline candidate. Moreover, by combining ALAgene® technology and proteome analysis technology, whose business has been transferred to the Company, it intends to further strengthen the search for drug discovery targets and their identification in order to accelerate the development of antibody drugs.

Also, based on the technologies obtained from R&D relating to functional ingredients overall, the Company is conducting the LSI (Life Science Information) business, in which external companies outsource work such as analyses and efficacy evaluation tests to the Company. It effectively utilizes its technological capabilities to support the R&D of various manufacturers, mainly in the food industry, including by acquiring and analyzing data on functions, analyzing the components of various ingredients, and creating requests for finished products.

In terms of the business model, the Company progresses development up to the non-clinical trial stage, and from the clinical trials onwards, the pharmaceutical company to which the development-candidate antibody has been licensed-out conducts the manufacture, development and sales. The Company receives license revenue, including joint research lump-sum payments, lump-sum contract payments, development milestone payments, sales royalties after the market launch, and sales milestone payments.

In the Autoimmune Disease Project*, which primarily addresses rheumatoid arthritis, the Company promoted joint research with Mitsubishi Tanabe Pharma Corporation on antibody pharmaceuticals for two years beginning in October 2018, which resulted in concluding an exclusive licensing agreement in January 2021. In addition, in April 2022, the Company was granted a patent in Japan for anti-PAD2 antibodies and in August was granted a patent by the United States Patent and Trademark Office for anti-PAD4 antibodies (already patented in Japan). It is now moving toward licensing out in the next term.

* The autoimmune disease therapy market is over ¥5tn (the Company's estimate).

Business summary

4. Risk factors, feature of earnings, and countermeasures

The risk factors include competition, delays in responding to product development and technological innovation, reliance on specific products, laws and regulations including the Pharmaceuticals and Medical Devices Act and Food Sanitation Act, and the protection of personal information.

Regarding competition, PharmaGABA®, which is the mainstay product in the BtoB business, holds the top share for GABA production, so it appears that there are very few concerns about competition intensifying for the time being.

The risk factors in the BtoC business include the effects of consumer preferences and purchasing trends, the extent of the reliance on specific products, an increase in advertising expenses and sales that are less than forecast. Regarding reliance on specific products, the Company is currently highly reliant on Newmo® Hair Growth Formula, but it is actively promoting the development of new products, including Eyelash Deluxe WMOA, DRcula series, and Shiboranaito® GOLD in an effort to reduce reliance risk by expanding its product lineup. At the same time, with respect to advertising expenses, the Company is working to reduce related risks by responsively controlling the expenses while observing sales, CPO*1, and LTV*2 trends.

*1 Abbreviation for Cost Per Order. It means the amount of advertising expenses required to acquire one customer.

*2 Abbreviation for Life Time Value.

In the Bio Medical business, a long period of time is required from the development of a new drug until its market launch, so there is risk relating to future uncertainty (development delays, discontinuations, etc.). To deal with this risk, when developing a drug's business, the Company cautiously determines factors such as its market potential and the possibility of an actual market launch, and formulates a business plan for it covering a long period of time.

Results trends

In 1H FY7/23, despite losses having been record for each profit type, results turned positive for the three months of 2Q due to factors that include effectiveness of advertising and contribution of new products

1. Outline of results for 1H FY7/23

In the Company's 1H FY723 consolidated results, net sales increased 21.9% YoY to ¥35,143mn, operating loss was ¥883mn (¥2,032mn profit in the same period of the previous fiscal year), ordinary loss was ¥912mn (¥2,105mn profit), and loss attributable to owners of parent was ¥914mn (¥1,561mn profit).

Results trends

Consolidated results for 1H FY7/23

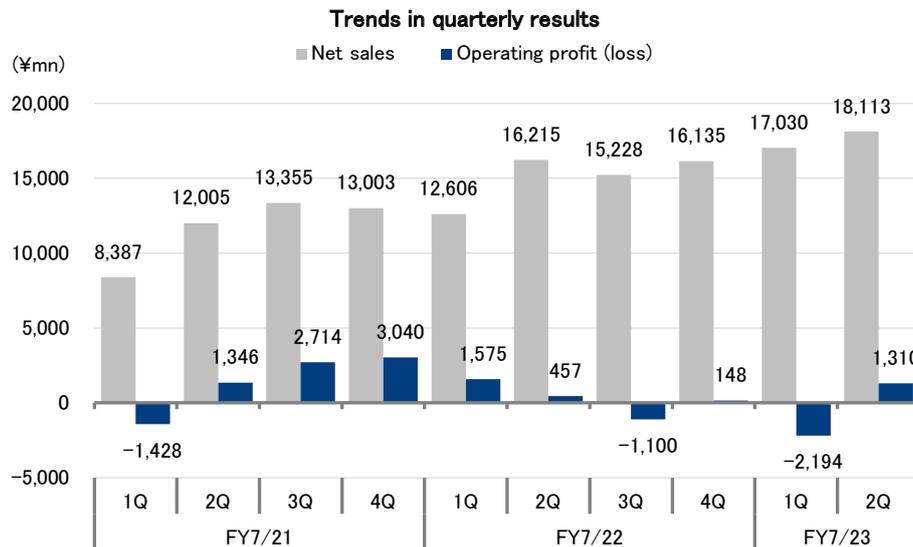
	1H FY7/22		1H FY7/23		YoY
	Results	% of total	Results	% of total	
Net sales	28,821	100.0%	35,143	100.0%	21.9%
BtoB business	3,647	12.7%	4,071	11.6%	11.6%
BtoC business	25,159	87.3%	30,923	88.0%	22.9%
Bio Medical business	14	0.0%	138	0.4%	880.0%
Other (fund management, etc.)	-	-	10	0.0%	-
Gross profit	23,035	79.9%	28,386	80.8%	23.2%
SG&A expenses	21,002	72.9%	29,270	83.3%	39.4%
Operating profit (loss)	2,032	7.1%	-883	-2.5%	-
BtoB business	541	14.8%	700	17.2%	29.5%
BtoC business	2,070	8.2%	-857	-2.8%	-
Bio Medical business	-138	-985.7%	-145	-105.1%	-
Other (fund management, etc.)	-	-	-1	-10.0%	-
Adjustment amount	-440	-	-580	-	-
Ordinary profit (loss)	2,105	7.3%	-912	-2.6%	-
Profit (loss) attributable to owners of parent	1,561	5.4%	-914	-2.6%	-

Source: Prepared by FISCO from the Company's financial results

Although net sales increased amid steady growth of the mainstay BtoB and BtoC businesses, the Company recorded losses for each profit type due to ongoing aggressive investment in new product research and development and investment in advertising to promote growth. Gross profit on a Company-wide basis increased 23.2% YoY, and the gross margin rose 0.9ppt to 80.8%. In addition, SG&A expenses were up 39.4% YoY, and the SG&A expenses ratio gained 10.4ppt to 83.3%.

On a quarterly basis, 1Q (August–October 2022) net sales were ¥17,030mn and operating loss was ¥2,194mn. Meanwhile, 2Q (November 2022–January 2023) net sales were ¥18,113mn and operating profit was ¥1,310mn. The Company recorded losses in 1Q due to proactive investment made in advertising toward growth, but then recorded a 6.4% increase in net sales in 2Q relative to those of 1Q due to factors that include effectiveness of advertising and contribution of new products, thereby culminating in a shift to positive results facilitated by effective use of advertising expenses. SG&A expenses for 1Q were ¥16,020mn, up 75.8% YoY (of which, advertising expenses were up 90.2% to ¥12,800mn), and SG&A expenses for 2Q were ¥13,250mn, up 11.4% (of which, advertising expenses were up 13.0% to ¥10,035mn).

Results trends



Source: Prepared by FISCO from the Company's results briefing materials

2. Trends by business segment

(1) BtoB business

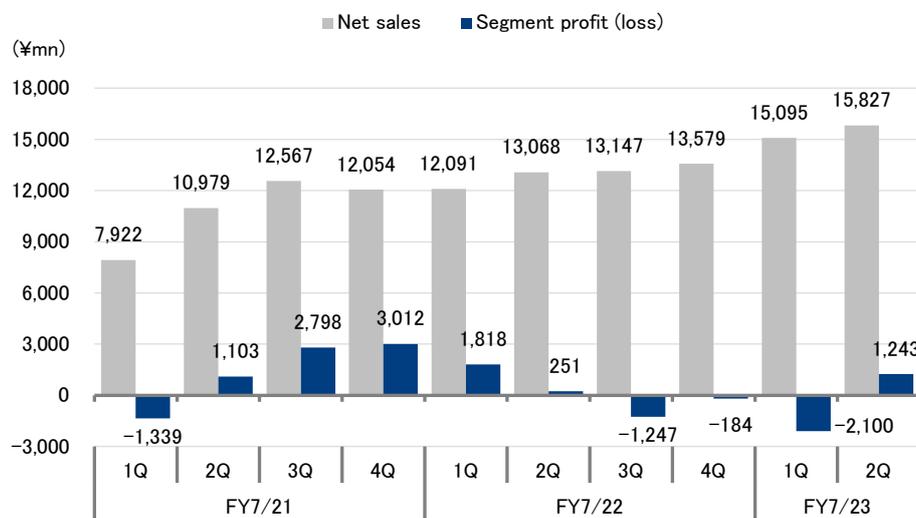
Net sales in the BtoB business increased 11.6% YoY to ¥4,071mn and segment profit rose 29.5% to ¥700mn. As for net sales by item, sales of functional ingredients increased 19.5% to ¥816mn (of which, PharmaGABA® was up 23.6% to ¥564mn), OEM, NB, etc. climbed 83.6% to ¥773mn, CMO business undertaken by Meiji Yakuhiin gained 19.4% to ¥1,996mn, and CHC business decreased 44.3% to ¥484mn. With PharmaGABA®, adoption of GABA by food manufacturers continues to expand and its use also increased in the United States and South Korea. In the OEM, NB, etc. category, there was an increase in sales of private-label brand (PB) hair growth formula to drugstores. In the CMO business, the Company has been striving to improve profit margins by implementing cost pass-through and narrowing down its range of products under contract amid mounting demand for substitute products due to quality issues among generic drug manufacturers. The CHC business encountered a decrease in net sales, but intensified its focus on new branded products for drugstores.

Results trends

(2) BtoC business

The BtoC business reported ¥30,923mn in net sales (up 22.9% YoY) and a ¥857mn segment loss (¥2,070mn profit in the same period of the previous fiscal year). On the sales front, Newmo® Hair Growth Formula continued to perform well, and growth of new products such as Eyelash Deluxe WMOA and those of the DRcula series contributed to results. Meanwhile, the BtoC business recorded a segment loss due to aggressive investment in advertising (up 46.3% YoY to ¥22,771mn). However, net sales set a record high on a quarterly basis in 2Q (November 2022–January 2023) due to the effects of investment in advertising, thereby culminating in a shift to positive results in terms of segment profit.

Trends in quarterly results in the BtoC business

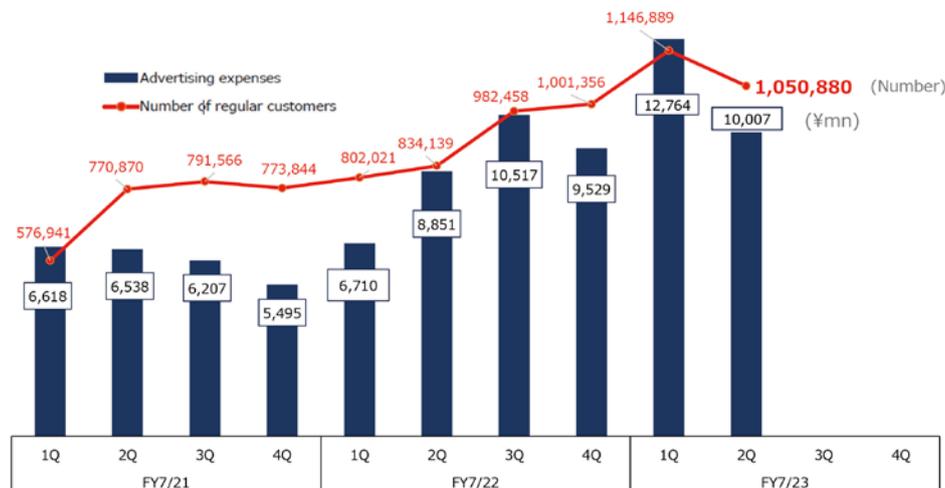


Source: Prepared by FISCO from the Company's results briefing materials

The Company began aggressively investing in advertising for new products while emphasizing CPO, an indicator of customer acquisition efficiency, and LTV, a profitability indicator, and, as a result, the number of regular customers as of January 31, 2023 was 1,050,880 (834,139 at the end of the previous year). Repeat purchases from this customer base continue to expedite profit generation and raise profit levels. Going forward, the Company intends to mitigate risks associated with the advertising expense burden by balancing such expenses while keeping a close eye on sales, CPO and LTV trends.

Results trends

Trends in advertising expenses and number of regular customers in the BtoC business



Source: The Company's results briefing materials

By item, there was steady growth in sales of new products in support of mainstay Newmo® Hair Growth Formula, and Newmo® Hair Growth Formula itself also performed well, with sales hitting ¥13,708mn and volume topping 18 million units (as of December 24, 2022). Other sales were ¥4,230mn attributable to Shioranaito® GOLD, ¥2,930mn for Eyelash Deluxe WMOA, ¥997mn for Newmo® Supplement, ¥969mn for Tamagosamine®, and ¥849mn for DRcula whitening gel.

(3) Bio Medical business

The Bio Medical business reported ¥138mn in net sales (up 880.0% YoY) and a ¥145mn segment loss (¥138mn loss in the same period of the previous fiscal year). The segment did not record lump-sum income relating to joint research and a licensing contract with Mitsubishi Tanabe Pharma, but its Olink Target service for analyzing trace amounts of proteins in the proteome analysis contract services business performed well. The segment seeks to strengthen its new drug development pipeline, particularly with respect to autoimmune diseases and fibrosis, and furthermore aims to acquire new drug modalities enlisting alliances with ventures through subsidiary CVC.

3. Financial condition

At the end of 1H FY7/23, total assets increased ¥2,715mn from the end of the previous fiscal year to ¥33,875mn. This was mainly due to a ¥4,130mn increase in cash and deposits and a ¥943mn decrease in notes and accounts receivable – trade. Total liabilities at the end of 1H FY7/23 climbed ¥4,038mn to ¥28,122mn mainly because of rises of ¥811mn in accounts payable-other related to the increase in advertising expenses and ¥2,000mn in short-term borrowings following implementation of borrowing based on a commitment line agreement enlisting the syndicate method. Total net assets decreased ¥1,322mn to ¥5,752mn due to recording loss attributable to owners of parent and dividends paid. The equity ratio hence dropped 5.7ppt to 17.0%.

Results trends

The Company's overall balance sheet has ballooned as sales have increased sharply, and its equity ratio continues to trend toward a decline, but the Company also continues to expedite profit generation and raise profit levels through aggressive investment in advertising. Moreover, the increase in interest-bearing debt has not been a factor putting pressure on profits. For these reasons, FISCO believes that there are no concerns regarding the Company's financial soundness. In September 2022, the Company concluded a commitment line agreement for a total of ¥7.6bn (three-year agreement) through the Bank of Kyoto <8369>, its main bank, and five regional banks. It can be concluded that this reflects the positive evaluation given to the Company's track record in drug discovery, functional ingredient research and development, and e-commerce sales as well as the high regard the banks have for the feasibility of its Medium-Term Management Plan aimed at expansion in the healthcare domain.

Consolidated balance sheet

	(¥mn)				
	End of FY7/20	End of FY7/21	End of FY7/22	End of 1H FY7/23	Change
Total assets	10,096	20,944	31,159	33,875	2,715
Current assets	7,437	17,933	23,513	26,136	2,623
Non-current assets	2,659	3,010	7,645	7,739	94
Total liabilities	5,188	12,478	24,084	28,122	4,038
Current liabilities	2,837	10,978	22,795	25,283	2,488
Non-current liabilities	2,350	1,499	1,288	2,839	1,551
Total net assets	4,907	8,465	7,074	5,752	-1,322
Shareholders' equity	4,895	8,455	7,024	5,605	-1,419
Capital stock	2,033	2,038	2,042	2,042	-
Equity ratio	48.6%	40.4%	22.7%	17.0%	-5.7pt

Source: Prepared by FISCO from the Company's financial results

Outlook

For FY7/23, the forecast for higher net sales and profits remains unchanged, with upside potential brought about by rationalization of investment in advertising

1. Outlook for FY7/23

For its FY7/23 consolidated results, the Company has maintained its initial forecasts which project net sales to increase 18.0% to ¥71,000mn, operating profit to increase 10.3% to ¥1,191mn, ordinary profit to edge up 0.3% to ¥1,268mn, and profit attributable to owners of parent of ¥886mn (loss of ¥374mn the previous term). While continuing to focus on M&A and alliance-building, the Company plans to establish overseas sites and aggressively expand, but it expects to offset the expenditures by achieving increased sales in all segments. Although the Company recorded losses in 1H, FISCO thinks it highly likely that the Company will attain its initial forecasts considering the notion that it shifted to positive results in the three months of 2Q in part given the effectiveness of advertising and contribution of new products, and the notion that its management team has firmly expressed its commitment to optimizing advertising and improving profit margins.

Outlook

Consolidated outlook for FY7/23

	FY7/22		FY7/23		YoY
	Results	% of sales	Forecast	% of sales	
Net sales	60,185	100.0%	71,000	100.0%	18.0%
BtoB business	8,079	13.4%	8,600	12.1%	6.4%
BtoC business	51,886	86.2%	62,000	87.3%	19.5%
Bio Medical business	220	0.4%	360	0.5%	63.6%
Operating profit	1,080	1.8%	1,191	1.7%	10.3%
Ordinary profit	1,264	2.1%	1,268	1.8%	0.3%
Profit (loss) attributable to owners of parent	-374	-0.6%	886	1.2%	-

Source: Prepared by FISCO from the Company's financial results and results briefing materials

2. Outlook by business segment

(1) BtoB business

In the BtoB business, the Company is forecasting sales of ¥8,600mn, a YoY increase of 6.4%. In functional ingredients, it will strengthen overseas sales and build a production system overseas, with respect to which the Company concluded a memorandum of understanding in December 2022 regarding establishment of a joint venture company with respect to a health food factory in Vietnam. The Company plans to accelerate its shift from functional raw material sales to end product sales and will transition from contract production for private brands to sales of products under its own brands. Most recently, the Company launched sales of its new Meiseki Lab and Muscle Lab products. For mainstay PharmaGABA®, it plans to receive large-scale orders. The CMO business of Meiji Yakuhi is expected to be operating at full capacity.

(2) BtoC business

In the BtoC business, the Company is forecasting sales of ¥62,000mn, a YoY increase of 19.5%. Newmo® Hair Growth Formula is expected to remain firm, with the Company making changes to its advertising. New products such as Eyelash Deluxe WMOA and those of the DRcula series are also expected to continue their growth. Meanwhile, the Company will apparently act in a manner that is responsive to sales, CPO, and LTV trends with respect to advertising expenses.

(3) Bio Medical business

Sales in the Bio Medical business is expected to increase 63.6% YoY to ¥360mn. The Company will expand its contract services for next-generation proteome analysis for major pharmaceutical companies, while moving forward on antibody drug development for new diseases.

Growth strategy

Aiming for net sales of ¥100.0bn in FY7/26 through initiatives to create new value

In its Medium-Term Management Plan 2026, the Company has established “new value creation 1K” as a goal, and through initiatives to create new value (new products, new markets, and a new organization), seeks to be a company with net sales of ¥100.0bn by FY7/26. Looking at a breakdown of this goal, it is targeting ¥70.0bn in growth from existing businesses and over ¥30.0bn from new value creation, and it has committed to an average sales growth rate of 20% or higher and a 20% total payout ratio, including share buybacks, through to FY7/26. Regarding profit levels, the Company will conduct business development through FY7/26 without concern over a decline in profit margin each year and intends to expand in scale while boldly taking on risk. Through this, it is aiming to create a structure that can secure an average operating profit margin of 10%.

1. Creation of new products

For the creation of new products, to create the next hit products to follow up products such as PharmaGABA®, Newmo® Hair Growth Formula, and Derma QII®, the Company is advancing R&D including to develop new ingredients (wine ceramide, Lipi Smart®, sialo sugar chains, egg placenta, and eggshell membrane peptides), new applications and effects (a brain function cocktail theory drink, Moringa, Wellmune, Banafine, and collagen eggshell membrane peptides), and next-generation antibodies. It is also developing products for the scalp and skin field (creating active components for non-pharmaceutical products, hair restorer formulas, wrinkle improvers, egg placenta, and ELLE brand cosmetics), pharmaceutical e-commerce field, and oral care field.

In July 2021, the Company concluded a sales agreement with Mitsui Sugar Co., Ltd. of the Mitsui DM Sugar Holdings <2109> Group for Lipi Smart®, which is a functional foods ingredient that suppresses absorption of triglycerides and contains sesame as a raw ingredient. Through joint development with Mitsui Sugar, the Company has developed a proprietary technology (patent pending) to manufacture Lipi Smart® from sesame. Through this, it launched a product onto the metabolic market for the first time. Most recently, the Company has been encountering growth when it comes to its own NB brand merchandise launched by the BtoB business (Meiseki Lab, Muscle Lab) and new products of the BtoC business (Eyelash Deluxe WMOA, the DRcula series, Shiboranaito® GOLD). As such, FISCO deems that the Company is making favorable progress in the creation of new products.

2. Creation of new markets

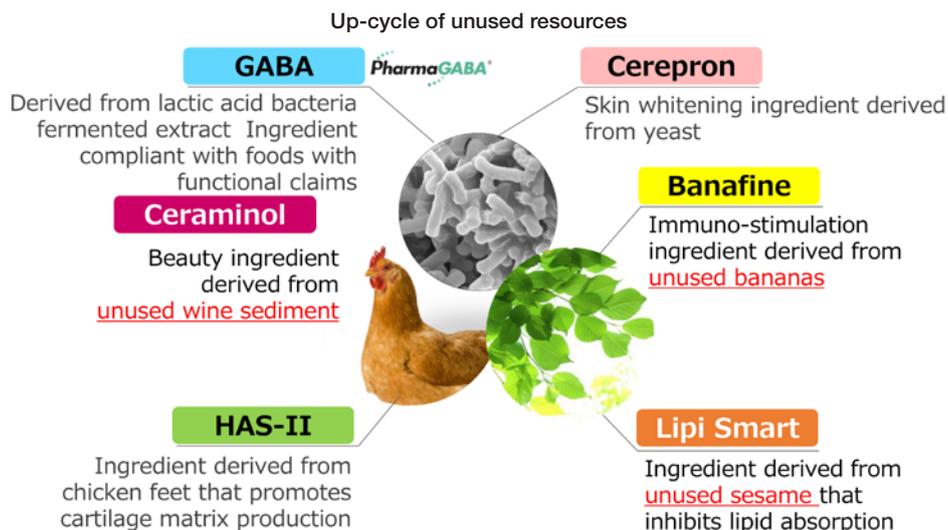
For the creation of new markets, the Company will advance initiatives for the expanding health market, including to strengthen brands and develop overseas markets (US market, China market through cross-border EC, and Southeast Asia market through halal certification), deepen the e-commerce business in the domestic market (develop new products and services that utilize the D2C platform of 1,000,000 people), shift the business orientation from BtoB to BtoC (develop the Company's own brand products for the distribution networks of drugstores and convenience stores), conduct initiatives for SDGs (create upcycle markets for unused resources), and enter the health support devices and medical devices fields (health devices, facial beauty devices, measuring devices, and hearing aids).

Growth strategy

Of these initiatives, to develop the US market, the Company is aiming to acquire GARS (Generally Recognized as Safe) certification from the FDA (US Food and Drug Administration) for PharmaGABA®. By acquiring the FDA's GARS certification, it will widen its current target of supplements to general food and beverages. This will lead to its adoption by major food and beverage manufacturers in the US, which can be expected to result in its rapid growth in the US market. In addition, the Company's efforts in seeking to tap the Southeast Asian market have involved conclusion of a memorandum of understanding regarding establishment of a joint venture company with respect to a health food factory in Vietnam, as mentioned previously. Meanwhile, the Company apparently has its sights set on expanding into Southeast Asian markets other than Vietnam in the future.

Regarding creating an upcycling market for unused resources, the Company intends to harness unused natural ingredients and utilize technology for new value creation from natural products in farming. Specifically, it created the Agri-Nutrition Basic Plan in September 2021 with Sanyo Chemical Industries that integrates the development and technological capabilities of both companies aimed at solving the global farming crisis. The Company has begun verification tests aimed at building a new farming system in Shintomi Town, Miyazaki Prefecture in 2022, and plans to develop high value-added crops with enhanced yields, resilience, and functionality using biostimulants that combine technologies from both companies in 2024, begin sales via the Company's e-commerce sales channel of high-performance health foods and cosmetics made from unused portions of high-value-added crops in 2025, expand target crops and promote sixth sector industrialization and brand formation in 2026, and develop a sustainable farming system in 2030.

The Company also announced its entry into the fiber and plant vitalizing agent markets through advanced utilization of eggshell membranes as a new unused resources upcycling business in December 2021. Through this upcycling, it aims to convert the 260,000 tons of eggshells thrown away annually in Japan into high-value-added products and thereby contribute to the realization of a sustainable society. The Company is currently in negotiations with a major manufacturer looking toward engaging in sales involving Ovoveil eggshell membrane fiber in 2023. In addition, in July 2022, the Company jointly invested with ENESO Holdings in ENEGGO, which manufactures liquid fertilizers from eggs, and signed a business alliance agreement with GreenTechno21 Co., Ltd. and its subsidiary ENEGGO. Through this, it will procure eggshells and eggshell membranes on the largest scale in Japan and work to bolster its chemicals business, which includes eggshell membrane fiber, liquid fertilizers, and other products.



Source: The Company's results briefing materials

Growth strategy

3. Creation of a new organization

For the creation of a new organization, the Company will develop initiatives including conducting reforms for the organizational, personnel, and hiring aspects, such as providing salary levels enabling employees to work with peace of mind and incentives for growth; developing and strengthening the Global Solution Team, including building overseas manufacturing and overseas sales bases; and conducting M&A and entering into alliances. Within these initiatives, the Company will utilize cash on hand and its financing framework for M&A and alliances, and has set its sights on companies with a sales scale of ¥10.0bn in relation to new products and markets. In January 2023, the Company established and initiated operations of PF Visionary Fund, a limited liability investment partnership. The Company will accordingly draw on investments in startup companies in seeking to accelerate innovation in the antibody drug discovery and healthcare business.

4. FISCO's opinion

Because the Company's earnings level has changed substantially on the strength of Newmo® Hair Growth Formula, there are some in the market who believe it is a company whose performance varies depending on hit products and advertising investment in its BtoC business. However, in the BtoC business, new products that support Newmo® Hair Growth Formula are growing steadily, and with PharmaGABA®'s dominant share and expansion of the CMO business in the BtoB business and expectations for drug discovery and development in the Bio Medical business, efforts are being made to reduce the risk of dependence on hit products. Business results for the immediate future may vary depending on the level of investment in advertising, but through new product and new market creation and active business development, FISCO believes the Company has high potential for medium- to long-term growth.

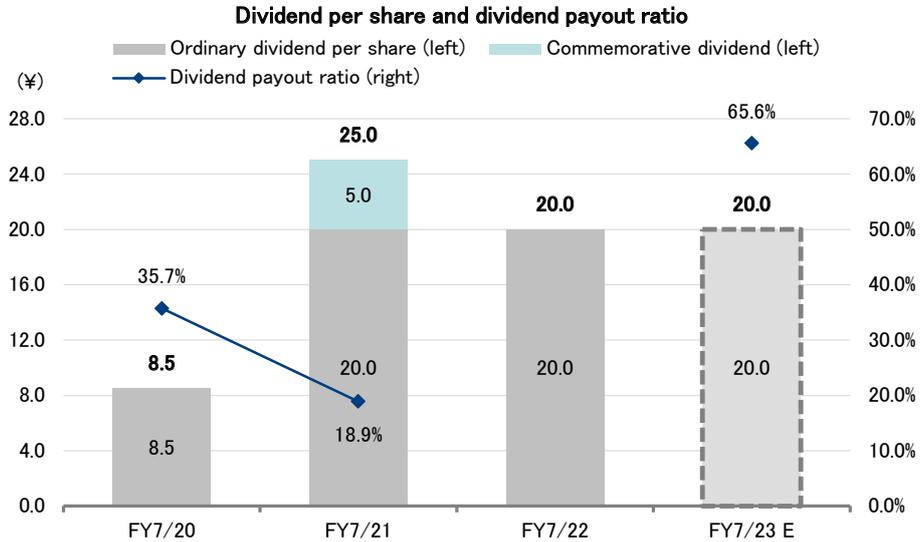
Shareholder return policy

Targets total shareholder return ratio of 20% including acquisitions of treasury shares as shareholder return policy

The Company's basic policy for returning profits to shareholders is, based on its business policy of achieving both corporate growth potential and profitability, to actively return profits to shareholders through dividends and other means, while continuing to expand investment for aspects such as R&D, advertising and M&A. Based on this policy and considering maintaining a balance between investing in growth, securing financial soundness, and strengthening returns to shareholders, it targets a total shareholder return ratio of 20%, including acquisitions of treasury shares.

Based on this policy, in FY7/23 the Company plans to pay an annual dividend per share of ¥20.0, the same amount as the previous fiscal year (dividend payout ratio: 65.6%, total shareholder return ratio: 99.3%). In addition, in order to raise capital efficiency and execute a flexible capital policy based on business conditions, the Company conducts share buybacks, and in October 2022, it acquired 242,200 shares (total acquisition cost of ¥299mn).

Shareholder return policy



Source: Prepared by FISCO from the Company's financial results

Initiatives for ESG and SDGs

As the Company's business itself involves the development and sales of food and cosmetic functional ingredients and products made from naturally derived raw ingredients that relate to people's life activities and health maintenance, its business is consistent with the SDGs. It formulated the Sustainability Basic Policy in December 2021 and is bolstering initiatives in ESG (environment, social, governance) management and SDGs. The Company presents a sustainability vision of meaningful prosperity and health in an era with lives spanning 100 years and intends to make efforts so that its own business growth contributes to realization of a sustainable society as a company that provides comprehensive support in health maintenance. Key issues (materiality) are enhancement of people's QOL, upcycling of unused resources, and respect for diversity. Through its responses to these issues, the Company aims to achieve its sustainability vision and further enhance corporate value.

Joint research on improving cognitive functioning through food was launched in April 2022 with a team of vascular dementia specialists from the National Cerebral and Cardiovascular Center. The research is aimed at removing brain waste, promoting cerebral circulation and activating nerve cells through a "brain function cocktail" that includes GABA. Also, as mentioned above, the Company began a new upcycling business using eggshell membranes, and its eggshell membrane fiber has been drawing attention, being featured on TV programs and the like. The Company also plans to exhibit at the Osaka Pavilion on the theme of "Eggs Save Earthlings" at World Expo 2025 in Osaka, Kansai.



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■ For inquiry, please contact: ■

FISCO Ltd.

5-13-3 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062

Phone: 03-5774-2443 (IR Consulting Business Division)

Email: support@fisco.co.jp