

Olympus Corporation
FY2021 Earnings Conference Call Q&A (Summary)

(Disclaimer)

For your reference, please find an English translation of the question and answer session at the conference call for financial results for the fourth quarter of the fiscal year ended March 31, 2021 below. This transcript has been edited/modified from the original Q&A conversations for the sake of clarity.

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[Q&A (Summary)]

- Q: ESD's FY2022 guidance appears to be conservative, with the decline in sales in the first half of FY2021 in mind. Some of favorable one-time factors in FY2021 - UK (NHS strengthening healthcare system), Eastern Europe (large-scale projects), Japan (supplementary budget) and China (government support to respiratory products) - can no longer be expected in FY2022. On the other hand, in FY2022, there should be favorable factors such as market penetration of new duodenoscope TJF-Q190V in the US. Can you tell us about the outlook for each region in FY2022?
- A: As you understand, there are positive and negative factors. And also, it depends on market conditions and COVID-19. By region, China's growth rate will be the largest, followed by Europe, and then APAC. Meanwhile, we have cautious views on North America and Japan. In the US, the launch of EVIS X1 is delayed to FY2023, and in Japan we have a cautious view on budget execution at hospitals. Plus, COVID-19 will continue to have a lingering impact throughout FY2022.
- Q: I recognize that TSD is expected to grow significantly in FY2022. While TSD has conducted several M&A deals, I think each of them only makes small contribution in terms of profit. Can you give us a breakdown among existing products, distribution of other companies' products and new products in terms of contribution to TSD's business performance?
- A: Overall demand is recovering with postponed procedures due to COVID-19 coming back, and we will see demand continue to recover throughout FY2022 in a continuation of the trend in 4Q FY2021. The urology segment is expected to continue to perform well as in the previous fiscal year. Lithotripter-related products such as SOLTIVE are growing, and we believe consumables will also contribute to sales in the future. The respiratory segment is also expected to grow, with the acquisition of Veran making a full-year contribution.
- Q: Can you give us risk factors of ESD in FY2022 by region? In Japan, did you pre-empt demand with the supplementary budget in the previous year? In the US, are customers refraining from buying ahead of the launch of EVIS X1 in FY2023? For Europe, is it hard to make an aggressive

plan after strong performance in FY2021?

A: In Japan, the impact of COVID-19 and the postponed resumption of shipping of EDOF scopes are factored in. In the US, many years have passed since the launch of the current GI endoscopy system. Therefore, in this fiscal year, it is difficult to make an aggressive plan prior to the EVIS X1 launch. In Europe, as in Japan, the postponed resumption of shipping of EDOF scopes are factored in. Furthermore, in Europe there were programs that helped customers purchase medical devices in several countries in the previous year, which we recognized as an elevating factor. All in all, the outlook for Europe as a whole is for slight growth. China is expected to continue growing.

Q: Does the suspension of EDOF scope shipment affect whole sales of EVIS X1?

A: EDOF scope is one of the most popular products in EVIS X1, and many customers consider purchasing EVIS X1 including this scope. Consequently, it is assumed that the suspension will affect the shipment of the whole EVIS X1 products, including processors (video system center).

Q: In ESD, operating margin improved significantly in 4Q (3 month). Do you think the 4Q momentum is likely to continue? Meanwhile, China recorded a high growth in 4Q as seen before the pandemic. Do you see demand recovering over there?

A: Although there were favorable supplementary budgets and programs by governments, we think it represents our current earnings power. With regard to the Chinese market, it is strong as a whole, and we are seeing robust expenditures for healthcare.

Q: Given you were negatively impacted by COVID-19 in FY2021, I am just wondering if the operating margin target of >20% in FY2023 is still intact? Looking at FY2022 forecasts, it appears that SG&A costs will grow more than revenue. Does this mean that cost-cutting benefits will not be realized by FY2023 as you assume upfront investments such as Global Business Services (GBS: initiative to outsource routine back-office service)?

A: We aim to transform ourselves from a Japanese precision equipment manufacturer to a global medtech company, and this goal has been set from a long-term perspective. We don't think we can become a leading global medtech company in 3 years, and it is necessary to change our corporate culture and to decisively carry out major reforms. That OPM target is high, but the idea is we should achieve it in 3 years. While the operating margin target is by no means low, the target of >20% has been unchanged at this moment. Despite headwinds, we would like to achieve the operating margin target ambitiously by overcoming them. The fruits of various measures implemented in FY2021 are expected to be materialized. Upfront investments to strengthen our core competence, including recruitment of external talent and investments in infrastructure, are essential. My sense is that awareness and focus on efficiency are becoming established among employees.

Q: How soon do you think those investments will start making a positive impact toward lower SG&A expenses?

A: It is difficult to comment on the absolute amount of SG&A expenses separately. However, I think those investments are contributing to reduce the absolute amount, if not enough to realize operating margin of >20% by themselves. FY2022 guidance includes costs worth about 1-2% of revenue as upfront investments.

Q: I would like to ask about ESD's business outlook in FY2022. Overseas medtech companies have commented that customers tend to purchase capital products when the outlook is bright, even if the current number of procedures is in decline. Please tell us about the sales momentum from January to March, and April, by region.

A: The government programs in Europe and the supplementary budget in Japan led to some preempted demand in 4Q before FY2022, with medical institutions that had been refraining until 3Q making purchases in 4Q. We believe that good momentum is likely to continue in FY2022, but we need to be cautious to some extent. As COVID-19 will continue to impact capex trend, the forecast figures may appear conservative.

April went well as expected, achieving significant growth compared with the same month of the previous year. It was in line with internal plans, although there were some regional variations.

Q: With regard to TSD, we haven't heard much on gynecology, surgical devices and ENT, which are non-core areas other than three focused areas (GI-Endotherapy, Respiratory-Endotherapy and Urology). Are there any decisions waiting in the future?

- A: We have explained in detail about the three focused areas, but we have no particular update for other areas at this moment.
- Q: Gross margin is expected to increase in FY2022. Is this a new product effect?
- A: The main reason are an improvement in factory operation and the absence of voluntary recall costs compared to FY2021. The potential margin impact from new products, including EVIS X1, is not included in the forecasts.
- Q: I have previously heard that there might be a possibility to change the target year while maintaining the operating margin of >20%. Is there any possibility for this?
- A: We have not changed our target at this moment.
- Q: I view TSD's FY2022 guidance as bullish. Is this because TSD is less susceptible to the financial conditions of medical institutions than ESD? What is your premise in terms of recovery in the number of procedures by region?
- A: In FY2021, TSD was significantly affected by the postponement of procedures although there were some regional variations. We don't assume that the number of procedures will completely return to the pre-COVID level in FY2022, but assume that those postponed procedures will gradually come back. Considering the one-time push-up factors that happened to ESD in FY2021, FY2022 will be the year when TSD shows a more remarkable recovery. Revenue of TSD is more likely to be linked to the number of procedures than ESD. We assume strong performance across all regions, not driven by a particular region.
- Q: I have heard that you are thinking to improve operating margin of TSD by improving product mix. Do you have any delay due to COVID-19?
- A: It is difficult to grasp the impact of product mix on margin improvement. We are seeing overall product mix change by business area, though. For example, while the respiratory products have enjoyed special demand caused by COVID-19, there are some clinical areas that are being negatively impacted by a decrease in the number of procedures.
- Q: ESD's business outlook in the US appears conservative in your FY2022 guidance. Is this partly because a change in competitive landscape between re-usable and single-use scopes affected your top-line assumptions?
- A: We think the reason why U.S. revenue declined YoY in FY2021 is COVID-19. Of course, we feel a certain level of competitive pressure, but that is not bringing a serious impact. In the US, the number of endoscope installments increased in FY2021. For FY2022, we don't expect to lose market share due to competition in the US. However, we think that there is a certain amount of refrain from buying new products in anticipation of future launch because customers know that EVIS X1 has already been in place in other regions.
- Q: I think there were cases where medical institutions purchased medical devices ahead of time thanks to government programs and supplementary budgets in FY2021. Do you expect a backlash in FY2022? How long do you expect the backlash to continue?
- A: Since not all the factors mentioned as one-time in this conference call are related to COVID-19, I think there will be a backlash. However, we have modeled our FY2022 plan, taking this into consideration.
- Q: Single-use bronchoscope has been launched in the US. Can you refresh us on your stance on single-use endoscope? Launch schedule in the future?
- A: We recently announced the introduction of single-use bronchoscope in the US. Our leadership in the field of re-usable respiratory endoscope is strong, and we are ready to provide the best solutions that our customers need. This single-use bronchoscope is provided by Vathin and is a premium product for use in endoscopy room that facilitates complicated therapeutic procedures, and we believe it will make a contribution to revenue. This is the first single-use endoscope for us, and we plan to launch a multiple single-use endoscopes in other fields in the future.

(End)