

MARGIN OF SAFETY

BALANCE OF POWER

MANAGEMENT ANALYSIS



MATSUKIYOCOCOKARA & CO.

DISCUSSION MATERIAL FOR FURTHER UPSIDE

2 DECEMBER 2022

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KEY MESSAGE



- Improvements in IR disclosure of integration plans and benefits, expectations associated with the reopening of the company, and attention from the capital markets have contributed to the growing reputation in terms of share price and it has become the no.1 company in its industry in terms of market capitalisation, far ahead of the second company
- The situation is ripe to go on the offensive with high stock prices and conduct M&As through share exchange to secure a dominant position in the industry. However, before taking such action, the company should continue to raise the valuation of the company and obtain a lower cost of capital
- Implementing the industry's first recurring quarterly dividend is worth considering to signal management's confidence in the company's future performance.
- How would appeal points be explained for further growth through integration synergies?
 - ⇒ Horizontal M&A, expansion into healthcare, digital investment, dividend increase
- Turning to the United States...
 - CVS is becoming an integrated healthcare platform with a hub of pharmacies and clinics, as exemplified by the acquisition of Aetna, a major health insurance company (approximately 70 billion yen) in 2017 (advocating the expansion of preventive care and lifestyle disease management services)
 - On the other hand, Walgreens has not been able to capitalize on its scale and has not performed well post M&A but has recently shifted strategies
 - Post-July 2022, the entry into the healthcare space looked like a three-way acquisition battle with Amazon -> One Medical (subscriber medical services), Walgreen -> Carecentrix (home healthcare), CVS -> Signify Health (home healthcare)

MatsukiyoCocokara is a rare company that has the best customer engagement among healthcare providers in Japan, has unparalleled data and has strengths in both the online and offline worlds

YTD STOCK PERFORMANCE



- Since the beginning of the year, MKCC's stock has been the leader in the drugstore industry



YTD PBR



- On the other hand, PBR has jumped from the bottom to the top of the pack and is currently in the middle



MARKET ATTENTION TO MKCC IS STRONG



- The presentation to MKCC got the highest impressions since the establishment of the Hibiki account, demonstrating the high level of attention by the market

Mar 2022 • 31 days

TWEET HIGHLIGHTS

Top Tweet earned 47.6K impressions

ひびき・パス・アドバイザーズ（以下、「ひびき」）は3月11日、株式会社マツキョココカラ&カンパニー（以下、「マツキョココカラ」）の経営陣に対しプレゼンテーションを実施致しました。

pic.twitter.com/e81UgyOGn0

Excerpt from an account with tens of thousands of followers

“I see that Hibiki Path has disclosed engagement materials addressed to MatsukiyoCocokara”

(Omitted)

At the beginning of the article, it says that they are trading cheaply and that the reason for that is the evaluation of the growth rate. Is that true?

(Omitted)

The amount of FCF created with the same profit is about 1.6x higher in Cosmos

That means even if FCF is the same amount and there is no difference in growth prospects, MKCC would need more profit to generate the same FCF which is a 38% discount at 1/1.6 in PER. With the PER I have on hand, there is a possibility that MKCC is traded with higher premium...

The company probably understand that even if they wanted to do it, they cannot act like Apple. I think it is an explanation of measures to grow asset-light and a quantitative impact on the stock price, not a share buyback that relies on CF

CHANGES IN VALUATION



- Achieved No.1 position in Japan in terms of market capitalisation due to integration synergies, disclosure of future roadmap, and expectations of inbound recovery, but it is still not at the highest level of valuation yet
- Looking at ROE, while BS has become larger due to the effect of consolidation, profitability does not appear to have kept pace

As of March 2, 2022

<i>(Yen in Millions)</i>		Revenue	OPM	Equity Ratio	Market Cap	ROA	ROE	PER	PBR	Dividend Ratio	Dividend Yield
3088 MatsukiyoCocokara	556,907	5.7%	71.0%	615,775	6.0%	9.5%	14.2x	1.3x	33.3%	1.6%	
	*5	MK	MK	MC	MC	MK	MK	MC	MC	MK	MC
3141 Welcia	949,652	4.5%	44.6%	634,738	6.8%	16.4%	23.5x	3.3x	21.2%	1.0%	
3349 COSMOS	726,424	4.6%	52.0%	643,880	8.2%	17.2%	25.8x	3.6x	10.2%	0.5%	
3391 Tsuruha	919,303	5.3%	53.6%	455,395	5.5%	12.0%	16.1x	1.8x	30.8%	1.8%	
7649 Sugi	602,510	5.6%	62.9%	404,260	6.4%	11.1%	22.1x	1.9x	23.4%	1.2%	
9989 Sundrug	634,310	5.9%	67.0%	360,124	8.5%	12.7%	14.0x	1.7x	32.3%	2.3%	
Peer Average	766,440	5.2%	56.0%	499,679	7.1%	13.9%	20.3x	2.4x	23.6%	1.4%	
Peer Median	726,424	5.3%	53.6%	455,395	6.8%	12.7%	22.1x	1.9x	23.4%	1.2%	

As of Nov. 30, 2022

<i>(Yen in Millions)</i>		Revenue	OPM	Equity Ratio	Market Cap	ROA	ROE	PER	PBR	Dividend Ratio	Dividend Yield
3088 MatsukiyoCocokara	729,969	5.7%	70.4%	805,123	5.3%	7.6%	21.2x	1.7x	29.6%	1.4%	
3141 Welcia	1,025,947	4.2%	40.7%	631,060	5.9%	13.9%	22.2x	2.8x	23.5%	1.1%	
3349 COSMOS	755,414	3.9%	52.3%	552,800	6.6%	12.8%	23.8x	2.9x	14.5%	0.6%	
3391 Tsuruha	915,700	4.4%	50.8%	430,774	3.9%	9.1%	19.0x	1.6x	50.0%	2.6%	
7649 Sugi	625,477	5.1%	60.8%	377,699	5.7%	9.4%	21.2x	1.8x	27.4%	1.3%	
9989 Sundrug	648,734	5.2%	68.0%	427,939	7.5%	11.1%	17.7x	1.9x	48.3%	2.7%	
Peer Average	794,254	4.6%	54.5%	484,054	5.9%	11.3%	20.8x	2.2x	32.7%	1.7%	
Peer Median	755,414	4.4%	52.3%	430,774	5.9%	11.1%	21.2x	1.9x	27.4%	1.3%	

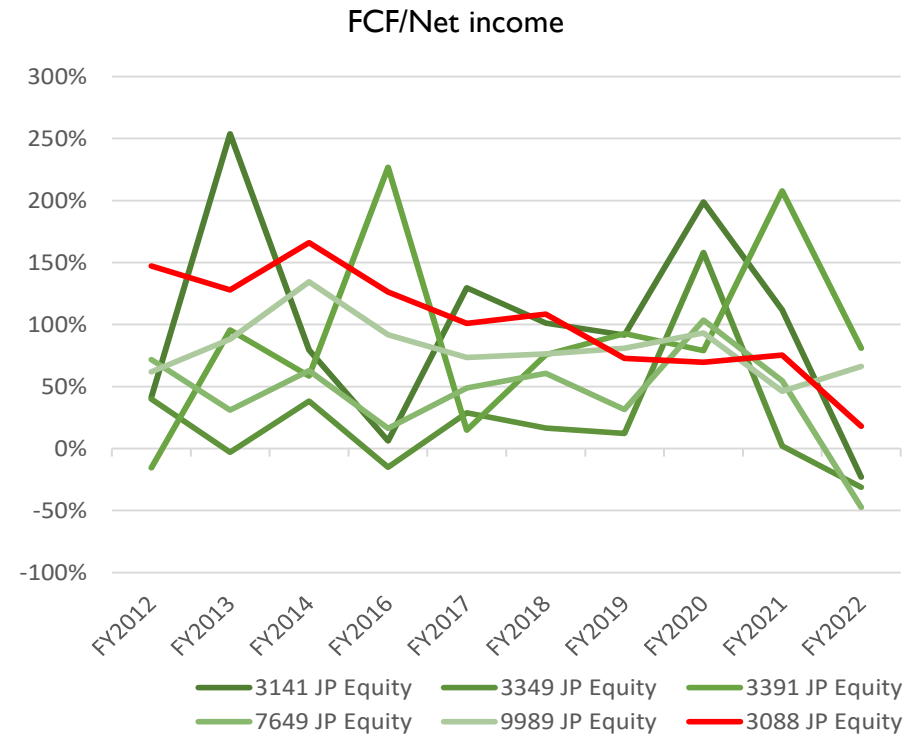
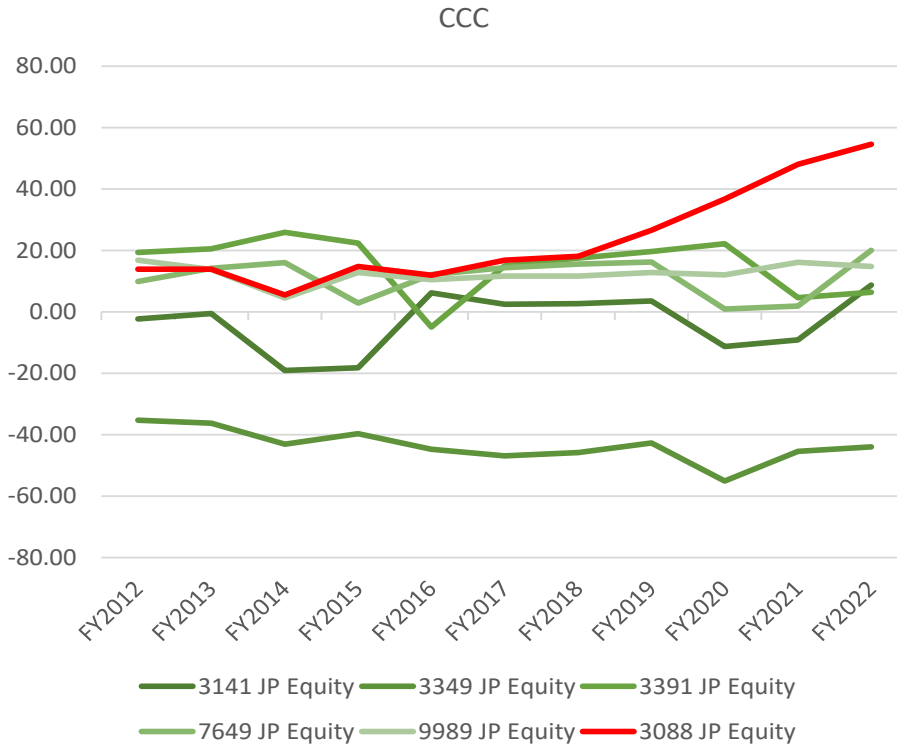
PER	Cost of Equity ⁶	Implied Growth
14x	6.1%	-1.0%
21x	6.1%	+1.4%

Implied growth rate has finally turned positive and is within a reasonable range for a domestic retail business.

DECLINING CASH GENERATION POTENTIAL ?



- Cash flow generation has been declining even before the integration of Cocokara
- It would not be negative if it was based on higher unit cost of inventory and increased customer credit payments



Note: CCC = Cash Conversion Cycle (in days); FCF is calculated by adding back non-cash expenses to operating income after tax and deducting incremental working capital and CAPEX. For FY2022 PL items for Matsukiyo Cocokara, the corresponding half-year figures for Cocokara Fine were added.

Source: Prepared by Hibiki based on Bloomberg and company disclosures.

STOCK PRICE IS IMPORTANT WHEN CONSIDERING M&A



- In the case of a share exchange by a buyer with high PBR, BPS increase in value → Constant PBR and stock price↑
- Cash acquisition will automatically lower PER even if BPS remains unchanged→Undervalued stock price→stock price↑

Company B's B/S			
Assets	100	50	Liabilities
		50	Equity

Your Company's B/S			
Assets	100	50	Liabilities
		50	Equity

Net Income	10
ROE	20%
D/E Ratio	1.0
PBR (input)	1.0
No. of Shares	1
BPS	50
Stock Price	50
PER	5.0
Cost of Equity	20%

Net Income	10
ROE	20%
D/E Ratio	1.0
PBR (input)	2.0
No. of Shares	1
BPS	50
Stock Price	100
PER	10.0
Cost of Equity	10%

i. Stock Swap Case			
Consolidated B/S			
Assets	200	100	Liabilities
		100	Equity

Net Income	20
ROE	20%
D/E Ratio	1.0
PBR (input)	2.0
No. of Shares	1.5
BPS	66.7
Stock Price	133.33
PER	10.0
Cost of Equity	10%

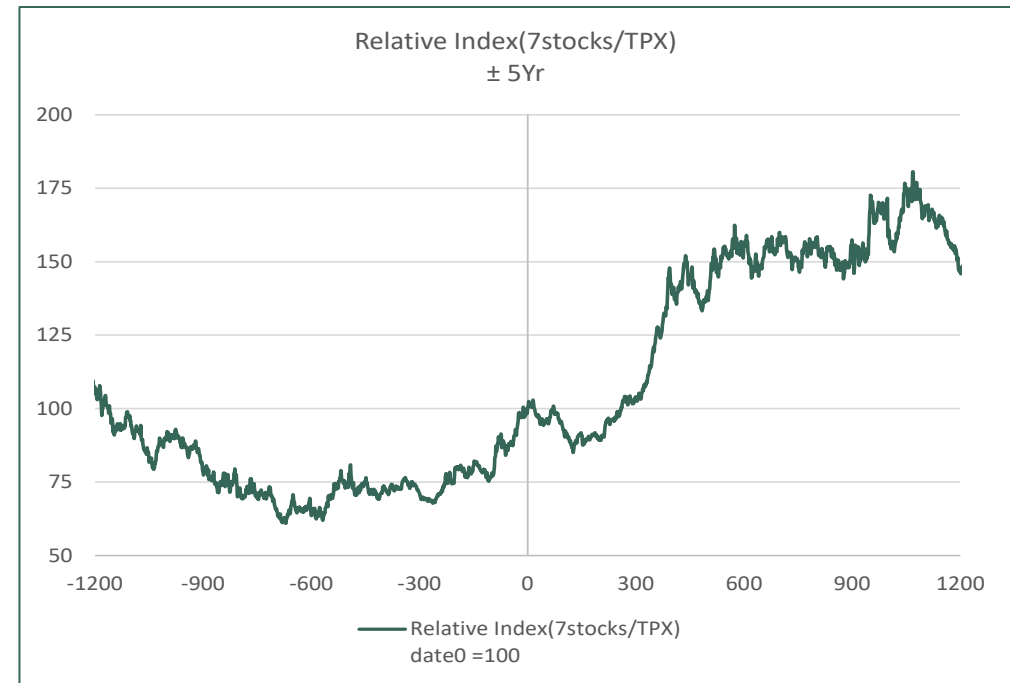
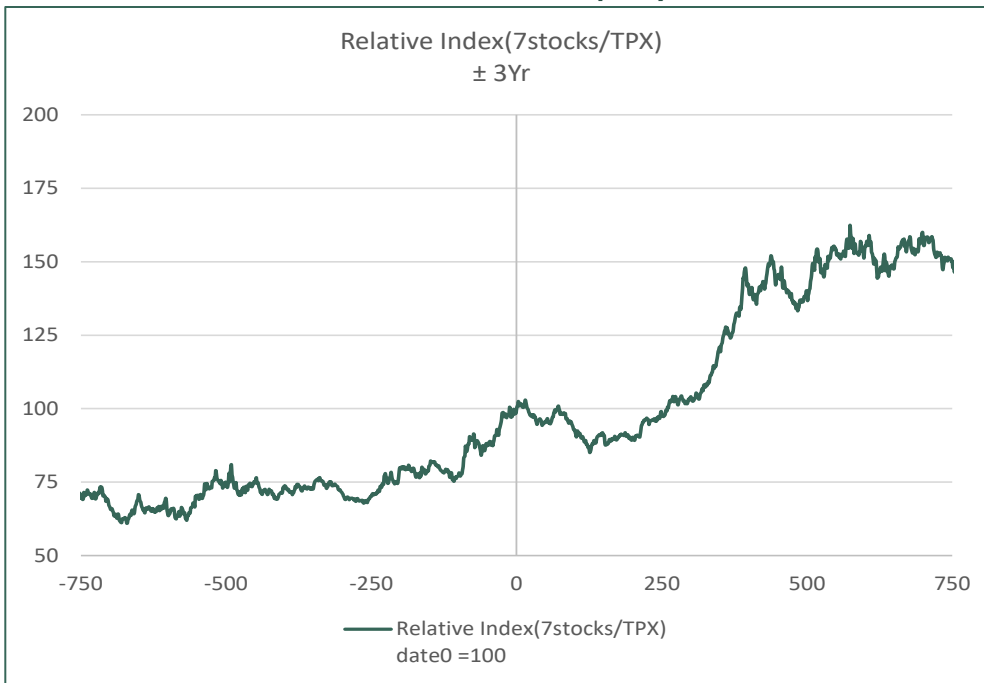
ii. Cash Acquisition Case			
Consolidated B/S			
Assets	150	100	Liabilities
		50	Equity

Net Income	20
ROE	40%
D/E Ratio	2.0
PBR (input)	2.0
No. of Shares	1
BPS	50
Stock Price	100
PER	5.0
Cost of Equity	20%

EFFECT OF QUARTERLY DIVIDENDS



- Below is the consolidated stock price performance of 7 companies that introduced quarterly dividends relative to TOPIX – Outperformed TOPIX by more than 50% over 3 and 5-year timeframes after the announcement (Dividend amount was only slightly positive relative to TOPIX)
- Although individual company circumstances, business performance and industry environment differ, we assume that the general signaling effect of “confidence in future performance” to the market was sufficient → as a B2C company, could there be further effects?



Note: The seven companies covered are Hogi Medical, Comture, Riso Kyoiku, Structural Planning Institute, Aozora Bank, Hikari Tsushin, and GMO Internet.

Source: Compiled by Hibiki from Bloomberg

IS AMAZON PHARMACIES A THREAT?



Online Medical Care	RTC since 2018	○
Online Medical Guidance	From September 2020	○
Electronic Prescription	To be operational from January 2023	○
Refill of Prescription	Available after April 2023	○
Inventory Holding	X	○
Delivery Locations	Scattered	Concentrated
Dispensing	Will the 2024 law be amended to lift the ban on outsourcing?	Concentration in large pharmacies?
Opposing forces	Pharmaceutical Association of Japan	Large PBM
Pharmacy/Population	4.79 (Pharmacies/10k ppl)	0.89 (Pharmacies/10k ppl)
Regulatory Trends	Easing of regulations	Open to New Trends
Amazon Business Partner	Small-Medium Sized Pharmacies	Buyers
Background of Entry	Deregulation	Distortion of profit sharing in PBMs and other industries

Our understanding of Amazon's entry into the pharmacy market

- Amazon does not run pharmacies in Japan. Instead ordering via electronic prescriptions, Amazon demonstrates the value of being able to receive medicines from the comfort of the home
- Besides shipping, there is no significant change in the amount the patient pays
- In Japan. E-prescriptions are not available online and it can only be ordered via fax or in-person

Questions

- Why did Amazon Pharmacy which is said to be a dud in the U.S, decide to launch in Japan at this time when there are many regulations?
- In Japan, even if there is an online option, obtaining medicine from the local pharmacy may be a faster option for the average patient
- Will Japan's dispensing regulations be further relaxed?
- Even if there was a demand for refills, will there be enough users with pain to make a business?
- How far will Amazon expand its territory in the future and how will it impact dispensaries?



US DRUGSTORES ▪ THE FIERCE BATTLE AMONGST HEALTH RETAILERS

APPENDIX



CVS AND WBA'S CURRENT VALUATION



	CVS	WBA
PER	11.3	8.57
PBR	1.87	1.4
EV/EBITDA	9.1	11.2
3 month	0.1%	13.5%
6 month	2.4%	-6.6%
12 month	9.1%	-11.4%

- CVS maintains a higher valuation, however, WBA benefitted from the recent post-COVID recovery
- CVS is able to capture the medical health needs of the public in a broader range of categories (retail, medical, and insurance)
- WBA is undergoing an aggressive business turnaround under the leadership of CEO Roz, who took over last March

WBA SITUATION AS OF NOVEMBER 2022



- 4Q 2022 reached sales of \$32Bn (-3.2%) driven by Boots UK +6.0% and Boots Germany +6.8% - A decision not to sell Boots after a year of consideration (28 June 2022)
- BS Management – Net Debt Equity of 0.43x but goodwill consists of \$33bn which exceeds shareholders' equity by \$3bn. Our guess is that the valuation is negatively impacted by such a risky situation
- Aggressive M&A with Shields and CareCentrix becoming wholly owned subsidiaries. It also spent \$5.2bn to raise its stake in homecare giant - VillageMD from 30% to 63% in October 2021, subsequently, Village MD spent \$8.9bn to acquire a 53% stake in Summit Health, extending its reach in urgent care. Behind the scenes, it sold off its interests in two other companies
- Such a strategy enables WBA to **close the gap with CVS which lags behind in vertical integration**. Whilst heavy-handed, it is able to rapidly maximize shareholder value (Maximising customer acquisition)
- The 2015 horizontal acquisition of RiteAid was heavily criticised by antitrust issues, which likely led to a change in management and a change in strategy

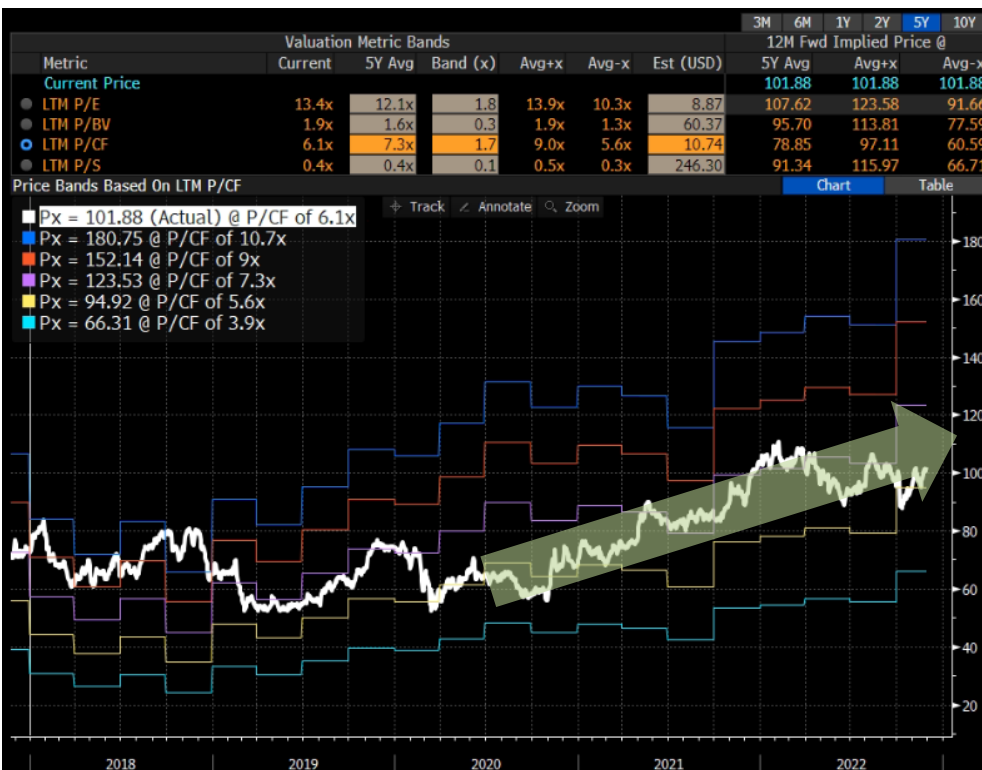


CVS SITUATION AS OF NOVEMBER 2022



- The company has a history of promoting vertical integration rather than horizontal integration ever since before Covid-19 with an eye on advancement of medical care → This may have contributed to the current share price valuation
- Symbolised by the 2018 acquisition of Aetna for \$69bn, the vertical integration of CVS as a medical platform has been successful to some extent. The company is M&A savvy in attracting deals and is daring and aggressive in announcing its desire for M&A in the primary care sector which is the first touch point for patients with health concerns
- In order to make this acquisition possible, it sold Omnicare in October and signify health in November which is viewed as a prerequisite for the acquisition
- In September 2022, it spent \$8bn to acquire publicly traded Signify Health, which has partnered with more than 10,000 clinics across the U.S. and is a pioneer in creating an ecosystem of value-based care catering to lower-income customers as opposed to typical general insurance customers
- The company is conscious of shareholder returns and announced a \$10bn share buyback program on 22 Nov 2022 which represents 7.8% of total outstanding shares and will have an effect of increasing EPS by the same amount
- It showed strong performance in 3Q, with sales +10% YoY and profit margin of 5.2% OPM, an improvement of 0.1% from the previous fiscal year, showing steady progress even under high inflation
- Net Debt/Equity is 0.47x

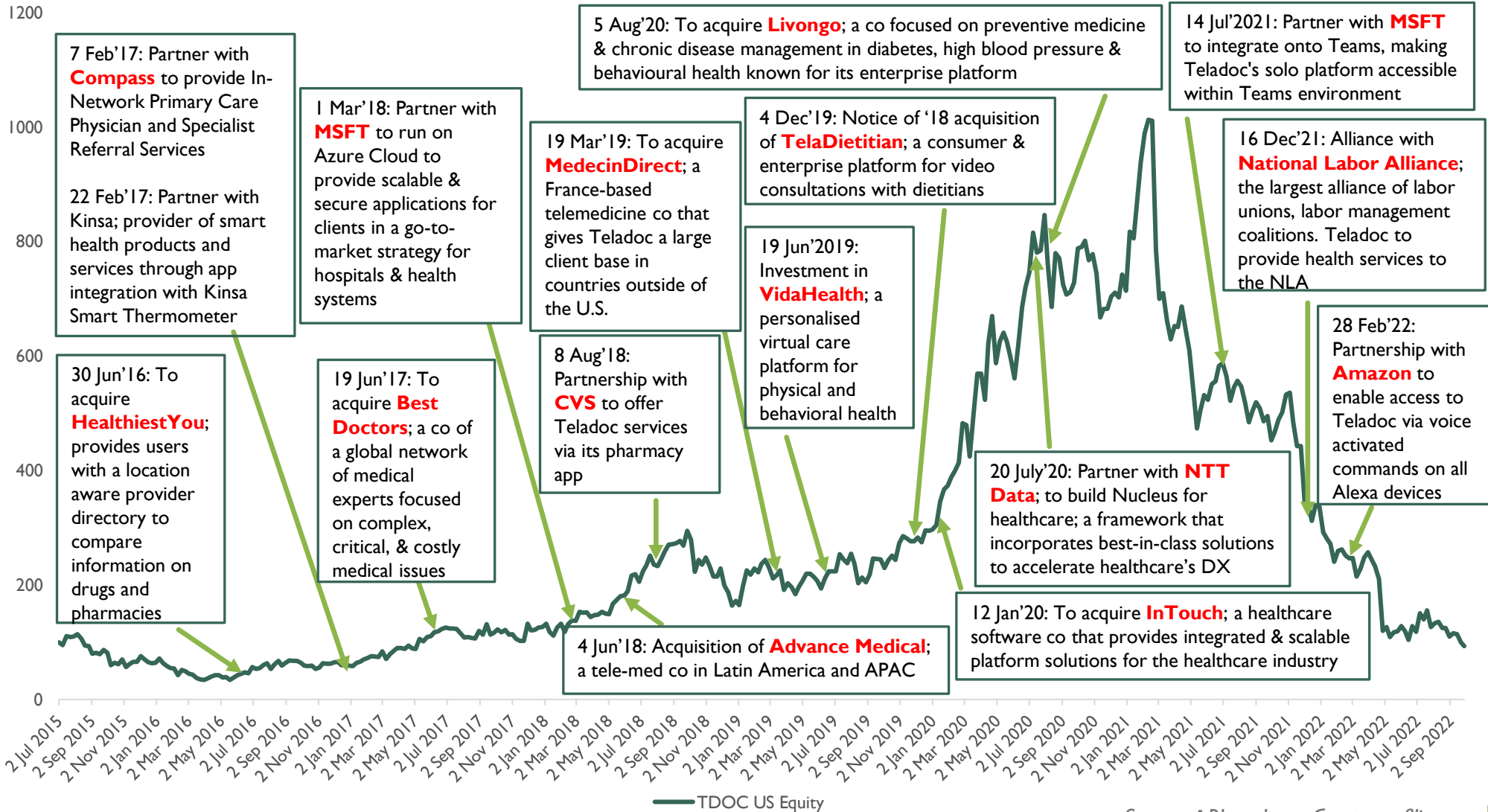
CHANGE IN P/CF BAND (APPROXIMATION OF PER)



CHANGE IN PBR BAND



(REFERENCE) TELADOC NETWORK STRATEGY



— TDOC US Equity

DISCLAIMER



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