

Web Conference for the Results of Operations for the Fiscal Year Ended December 31, 2022  
Key Questions and Answers (Summary)

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Monday, February 13, 2023, 15:15 – 16:15

Responses by:

Kazutoshi Kobayashi, President & CEO

Shinichi Mochizuki, Director & CFO

Hiroko Hanakura, General Manager of IR Department

**1. Why was operating profit of ¥22.1 billion in 2022 almost the same as your initial plan?**

There were contributions to operating profit of about ¥1 billion from yen's depreciation and almost ¥3 billion from measures to hold down the cost of sales ratio by reducing inventories at an overseas subsidiary. As a result, operating profit was about ¥4 billion higher than our revised plan for 2022. After excluding these items, the result is operating profit of around ¥18 billion, which is a more accurate reflection of earnings from our businesses in 2022.

**2. Why are you planning on low profits in 2023 despite your outlook for higher sales?**

The higher cost of raw materials in 2022 will raise the cost of sales in 2023.

In addition, we plan to increase marketing expenses by about ¥10 billion in 2023. The composition of these incremental expenses is 60% for DECORTÉ, 20% for ALBION, 10% for Tarte, and the remainder for prestige brands, primarily SEKKISEI. The 60% share for DECORTÉ includes promotion cost for sales growth in Europe and North America. We view 2023 as a year for laying the groundwork for making investments in brands that we can make stronger. We believe this will result in higher sales and profits from 2024.

Please note that our 2023 operating profit plan of ¥21 billion is about 15% higher than our 2022 operating profit of ¥18 billion after excluding the one-time contributions I mentioned earlier.

**3. What were your sales to foreign tourists ("inbound sales") in Japan in 2022 and what is your outlook for these sales in 2023?**

Sales in this category were ¥5.6 billion in 2022 with ALBION accounting for almost all of these sales. Market conditions are different from 2018 when sales to foreign tourists in Japan peaked. The reason is that people can buy KOSÉ products at duty-free stores in South Korea and Hainan Island too. This change in the business climate is currently having no effect on our performance at this time. Due to the difficulty of determining a sales forecast in this category, we are forecasting 2023 sales to be the same as in 2022.

**4. You said that holding down marketing expenses is one reason that your 2022 operating profit was higher than the revised 2022 plan. In what regions did you hold down these expenses? Also, what are the reasons for higher expenses in 2023. Is it Japan or China?**

In 2022, we held down SG&A expenses in Japan and China. Tarte did not hold down these expenses. In 2023, we again plan to allocate considerable expenses for activities in Japan and China.

**5. Why did DECORTÉ sales increase by ¥2 billion in Japan in the fourth quarter? Also, please provide your 2023 figures separately for Japan and overseas.**

Fourth quarter sales increased because of the popularity of LIPOSOME Cream. In addition, sales of our limited-time-only set combining LIPOSOME Beauty Serum and Cream were higher than we anticipated. In 2023, we will again launch new LIPOSOME products, including an eye serum, and we don't expect as much sales growth as in 2022. As a result, we plan on the DECORTÉ sales growth of 6% in Japan. We have a conservative outlook for DECORTÉ sales in China which means that we expect that Japan will again be the main source of sales growth for this brand in 2023.

**6. What is your assessment of ALBION's current performance and your business strategy for 2023?**

In 2023, ALBION will account for 20% of our planned SG&A expense increase of ¥10 billion. Most of these ALBION expenditures will be in Japan and China. In 2022, ALBION decided to end the EXAGE brand and launched the FLARUNÉ brand. We will continue to step up our activities to promote FLARUNÉ brand in 2023.

**7. On page 17, you said that cosmetaries sales for 2023 are expected to be 1.8% higher than for 2022 due to a negative effect of the termination of some brands. How much will sales increase after excluding the termination of these brands?**

Cosmetaries sales growth of 6.2% in 2022 looks high, but the effective sales increase was 3.6% after excluding the negative effect on 2021 sales of the return of FASIO products due to the rebranding of this brand. We estimate that the termination of the old products reduced cosmetaries sales by 1%. Therefore, when comparing 2022 and 2023 on the same basis, we expect 2023 cosmetaries sales to increase 2.8%. The cosmetaries business is regaining its vitality and posting strong sales, except the in-bath category.

**8. What is your outlook for market growth in Japan in the skin care and makeup categories?**

We expect the overall market in these two categories to achieve mid-to-high single-digit growth in Japan and China. In the United States, although sales will be affected by the health of the economy, we do not anticipate significant growth.

In Japan, we believe that our sales can grow slightly higher than the market at department stores and specialty cosmetics stores, mainly for DECORTÉ. In cosmetaries, KOSÉ Cosmeport products have also posted solid sales in the e-commerce channel. We have had difficulties in the prestige brand and cosmetaries categories. But I think that there is potential for growth if we use the proper methods to sell these products.

**9. What is your view of your profitability in China?**

Our subsidiaries in China, excluding the travel retail category, were profitable in 2022. Our profit margin was in the mid-single-digit range in 2021 and the low-single-digit range in 2022. Travel retail sales have been very strong since the third quarter of 2022. On a yen basis, travel retail sales in China met our plan and had a high profit margin.

**10. Your 2023 outlook for travel retail sales in China and South Korea appears to be low. In both countries, your customers are Chinese. Can't you expect sales growth in both countries if the number of Chinese going on trips increases?**

Our sales and profits in the China travel retail sector were strong in 2022. We think there may be a downturn in 2023 following this performance. In addition, we anticipate even more competition with China in South Korea and expect inventory controls to affect our performance. As a result, our plan is for sales growth of 2% to 5%.

**11. Does your outlook for the travel retail margin reflect your plan to use expenses for the recovery of sales in this market in 2023?**

We expect a small decrease in profit margins in the travel retail category, which is mainly Hainan Island. The end of China's zero-COVID policy will give people more opportunities to shop at stores. Accordingly, we want to be prepared to serve them with the newest sales counters. Furthermore, we plan to use expenses for the resumption of beauty care services and other activities.



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**12. Why were Tarte sales strong in December 2022? Also, why are you not planning on sales growth at Tarte in 2023?**

Throughout 2022, Tarte sales at stores were good but shipments to stores were limited somewhat. In December, there was a large volume of merchandise shipped to stores because of 2022 Christmas season sales that were higher than in 2021. In 2023, we are planning on no sales growth at Tarte because we expect distributors to limit shipments to stores just as in 2022.

**13. What is your outlook for Tarte's earnings in 2023?**

Expenses at Tarte include the cost for gondola display shelves associated with opening more stores in the United States. Furthermore, the cost of labor in the United States is rising rapidly. Higher personnel expenses at Tarte cannot be avoided because this company is increasing its workforce. The company's operating margin hit bottom in 2022 at 10% and we want to raise the margin to a low-teen percentage growth in 2023.

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