COMPANY RESEARCH AND ANALYSIS REPORT

Estore Corporation

4304

TSE JASDAQ

4-Oct.-2019

FISCO Ltd. Analyst

Hiroyuki Asakawa

FISCO Ltd.

http://www.fisco.co.jp

Index

Summary

Steady expansion of the marketing services business engaged in EC consulting and operations management agency services

Estore Corporation <4304> (hereafter, also "the Company") is a comprehensive provider of e-commerce (EC) support services. After starting from the Systems Business for the provision of ASP services as a framework for EC, it is currently focusing on consulting and operations management agency services to support revenue growth at customer companies. Going forward, the Company plans to strengthen its sales promotion systems.

1. Three EC support businesses: sales systems, marketing services, and sales promotion systems

Since its foundation, the Company's business domain has been providing EC support to companies. After starting with the provision of shopping cart services, the Company has grown by changing the focus of its mainstay business in response to the development and changes of technology and the EC market. With the launch of the sales promotion systems business in 2017, together with sales systems, marketing services, the Company has achieved a structure covering four business domains that support EC.

2. Working to strengthen analogue strategies with a focus on customer contact points and marketing

The Company has established a structure with three businesses as a comprehensive EC support company; however, its business strategy calls for different levels of focus on each business. Looking ahead, the Company is aiming to pursue an analogue strategy, and to strengthen its marketing. Currently, there is an oversupply of information, and the deflationary economy looks set to continue as the population declines going forward. In such an environment, customer contact points are a vital key to effectively selling products, which is to say, the Company recognizes the importance of marketing. Under its business classification, this area comes under the marketing services business, and the specific business operations include consultation and operations management agency services. A distinctive characteristic of the Company's operating strategy is that it seeks to attract new external customers outside of its existing customers (companies that already have Shopserve contracts), and that its target customer scale has shifted towards large customers.

3. Acquisition of new large customers in the marketing services business is on track

Looking back over FY3/19, in the breakdown of net sales by business, net sales in marketing systems declined year on year (YoY), and did not grow as expected in the newly launched sales promotion systems business. Marketing services showed more vigor, with net sales rising 5.2% YoY, but on closer inspection, the Company's efforts to acquire new large customers appear to have stalled, partly due to the impact of organizational restructuring. However, these efforts have gradually been gaining momentum since FY3/19 4Q, and the number of orders acquired has been accumulating steadily since entering FY3/20. Since there is a lag between orders and recording of earnings, 1Q results do not reflect the effect of these large customers, and but the effect is expected to become clear from Q2 onwards.

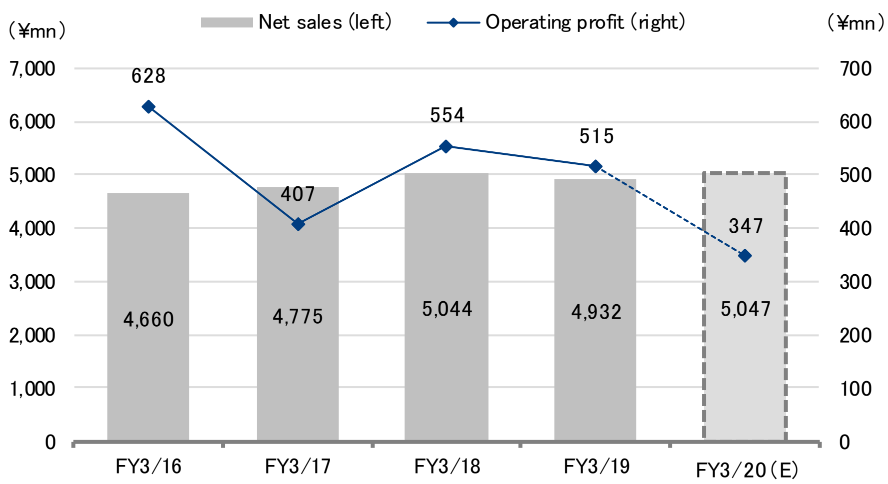
4. Concerns over the impact of consumption tax increase in FY3/20. Full-scale performance growth expected for FY3/21

Meanwhile, it is important not to have excessive expectations for FY3/20 results. In its approach to FY3/20, the Company has forecast conservative net sales and profit after reflecting on the previous fiscal year. The above-mentioned upturn in the marketing services business would ordinarily increase expectations for higher-than-forecast performance, but such optimism should be restrained by concern over the impact of the consumption tax increase scheduled for October 2019. This may have an impact on revenue from fees linked to sales scale, by which the Company receives a fixed portion of customers net sales (classified as sales system flow revenue) and revenue from credit card payment agency commissions. However, these impacts will only be temporary, and if the Company can steadily accumulate contracts from large customers in its marketing services business, we believe it has the potential to make a dramatic leap forward in FY3/21.

Key Points

- Aiming for growth with the themes of “analogue strategy” and “marketing”
- Impact of the consumption tax increase a key concern for 2H. Strong growth in FY3/21 the main focus
- Shareholder benefits dramatically increased from once-yearly dividend of ¥500 to twice-yearly dividends totaling ¥2,000

Results trends



Note: transitioned to consolidated results from FY3/19
Source: Prepared by FISCO from the Company's financial results

Business overview

Steadily strengthening the revenue base and customer base by shifting the focus business every seven years. Completed a comprehensive EC support system with the release of sales promotion systems

Since its foundation in 1999, the Company has consistently developed EC support-related businesses. However, in this process, it has grown while shifting its business focus roughly every seven years to reflect the changes in the business environment and the growth of the Company itself. As each business hit its stride and reached the stage of establishing an earnings base, the Company would use these earnings to expand into creating a new business to contribute to earnings in a repeated cycle. The current year, of 2019, is in the period to shift from the third to the fourth cycle.

Estore's history and the shifts in its business development

Date	Event	Business segment
February 1999	Founded Estore	
July 1999	Started providing the shopping cart service storetool	Systems Business
September 1999	Started providing the web hosting service Siteserve	Systems Business
March 2000	Sales partnership with Osaka Yusen Broadcasting Co., Ltd. (currently, USEN Corporation)	Systems Business / OEM subscriptions
June 2000	Sales partnership with Sony Communication Network Corporation (currently, So-net Entertainment Corporation)	Systems Business / OEM subscriptions
July 2004	Business and capital partnership with TELEWAVE, INC. (currently, iFLAG Co., Ltd.)	Systems Business / OEM subscriptions
November 2005	Established a business alliance with Yahoo Japan Corp. <4689>	Systems Business / OEM subscriptions
November 2005	Established a business alliance with Kakaku.com, Inc. <2371>	Systems Business / OEM subscriptions
January 2006	Started providing the Shopserve comprehensive eCommerce support service under its proprietary domain	Systems Business
November 2006	Launched the product search site Shoppingfeed	Systems Business
June 2011	Converted Precision Marketing, Inc. into a consolidated subsidiary	Marketing Business
July 2012	Established the Sapporo Marketing Factory	Marketing Business
October 2012	Established the shopping site PARK, featuring shopping recommendations issued by "curators" in 34 genres	Marketing Business
October 2013	Started providing the Single Hand simple customer acquisition service	Marketing Business
January 2016	Removed Precision Marketing from the scope of consolidation	Marketing Business
April 2016	Strengthened the Promotions Business sales force	EC Business
August 2016	Shopserve is compliant with Amazon Pay	EC Business
March 2017	Shopserve includes bitcoin payments as standard (provided to 12,500 stores)	EC Business
July 2017	Started providing Estore Compare sales promotion system	Marketing Systems
September 2017	Started providing Estore Query sales promotion system	Marketing Systems
August 2018	Established CrossTrust, Inc. and made it a consolidated subsidiary	EC Business

Note: Segment names are the segment names on the corresponding dates. Currently, the former Systems Business and EC Business have been changed to sales systems business, and the for Marketing Business has been changed to the marketing services business.
Source: Prepared by FISCO from Company materials

(1) 1999-around 2006

The Company's business first started from shopping cart services. After that, it started the provision of rental servers that are needed in order to establish a website, and the rental server business became the main support for the Company's early days. While retaining the rental server business as its core operation, the Company rolled out a series of services needed for conducting EC in addition to its shopping cart services. These paved the way for the Shopserve ASP service providing comprehensive EC support, launched in 2006.

(2) 2006-2012

Over the seven years from 2006, the EC systems business in the form of the Shopserve ASP service providing comprehensive EC support became an earnings source for the Company. Shopserve is an ASP service that provides, as a single service, management of elements such as the store's website, domain, email, payments, ordering, and customers. In terms of its revenue model, the Company collects monthly fees for the usage of the ASP service from customers, so it can be said to be a so-called recurring-revenue type model. Recurring revenue is very effective for stabilizing the management foundation. The Shopserve customer base has steadily expanded and contributed significantly to the Company's growth and management stabilization.

Once the EC systems business hit its stride, the Company began a parallel project of supporting the growth in sales at customer companies and expanding revenue by collecting a fixed percentage of net sales from customers (revenue from fees linked to the sales scale) as payment agency commissions (via store websites on Estore's Shopserve). This type of revenue is described as flow-type revenue and is distinguished from the monthly fees from Shopserve (recurring revenue) in revenue management, even though the revenue comes from the same customers.

(3) 2012-2018

The net sales from existing customers (EC system customers) expanded steadily, with a good compositional balance between recurring revenue and flow revenue. Meanwhile, the Company began strengthening the Marketing Business with an eye to developing it as the core business for contributing to earnings. This involved commercializing the Company's sales promotion support expertise for effectively expanding customers' net sales. The two main points were 1) commoditizing its sales promotion support expertise and policies and acquiring fees from consulting and operations management agency services, and 2) selling these services to customers other than existing customers (EC system customers).

The Marketing Business initially consisted of two businesses, the sales promotions business, which provided consulting and operations management agency services, and the media business, which managed the PARK EC shopping mall. The Company has positioned the sales promotions business as the business domain it should focus on the most. It distinguishes it from the marketing systems business described below and it currently calls it the marketing services business (or sales promotion services). On the other hand, it has positioned the media business as a non-focus business, because it has powerful rivals, like Amazon, and it has fulfilled a certain purpose. As a result, the Company ended the media business on September 30, 2018.

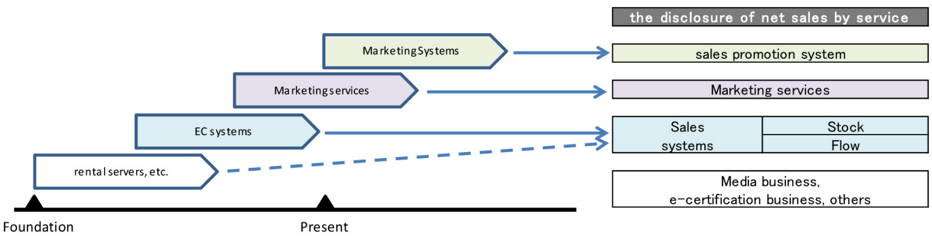
(4) From 2018 to the present day

The marketing services business (sales promotion services business) is provided principally by people; in other words, it is a human work-force service. Therefore, the Company has sought to provide sales promotion services through a system as the next growth driver, and has been working to develop this system. As a result, in autumn of 2017, the Company started providing two software packages: Estore Compare and Estore Query (in some cases, they are collectively referred to as the Back Store Group). This sales promotion systems business is called the marketing system business (or the sales promotion systems business), and in 2018 the Company started full-scale efforts to expand sales of the above two software packages.

After passing through the above-described transition, currently the Company has only one business segment: the EC business. But net sales are disclosed by dividing them into four categories according to the target of the service provision ("sales" or "sales promotions") and the provider and the method of provision ("machinery and software" or "work-force services"). These four categories are sales promotion services (marketing services), sales promotion systems, sales systems, and the media business and others.

Sales systems is further divided into two according to the type of revenue; recurring revenue (system usage fee revenue) and flow revenue (revenue of a fixed percentage of net sales). Also, services in the media business were stopped at the end of September 2018, while the Company has consolidated the subsidiary that conducts the e-certification business. Therefore, the outlook going forward is that this category will change to the e-certification business and others.

Business transition and correspondence relationships for the disclosure of net sales by service



Source: Prepared by FISCO from Company materials and interviews

Medium-term growth strategy and progress

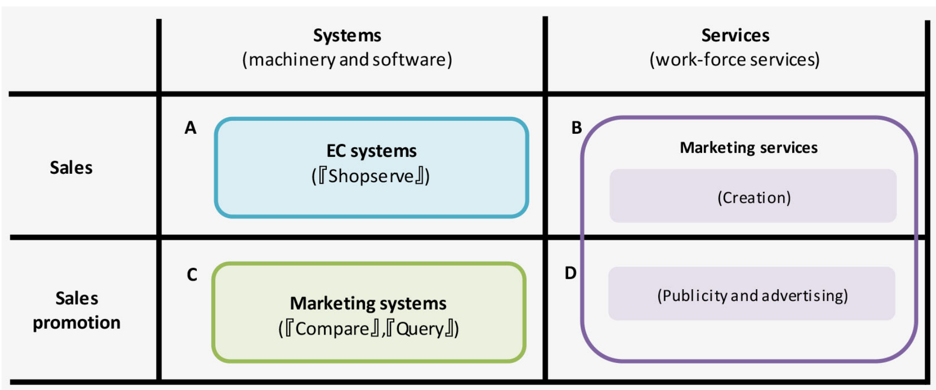
Aiming for growth with the themes of “analogue strategy” and “marketing”

1. Overall image of the growth strategy

(1) Business structure

As noted above, the Company started the sales promotion systems business in 2017, completing a three-business structure comprising the sales system (EC system) business, the marketing services (sales promotion service) business, and the sale promotion system (marketing system) business. These three businesses are presented in four quadrants created from two axes: the sales and sales promotion (marketing) axis and the systems (machinery and software) and work-force services axis.

Business domains



Source: Prepared by FISCO from Company materials and interviews

The Company's growth strategy is, of course, to aim to grow earnings in each of the businesses A to D. But the key point is that A to D do not exist separately (independently) from each other on the same plane, but rather they relate to each other in various ways, such as having causal, substitution, and complementary relations, and they have a three-dimensional and multilayered existence according to their respective relations. Therefore, in order for the Company to grow earnings, of course the various businesses must work together to pursue synergies, but it is also necessary to combine them to reflect changes in the market environment and the changing times, while modifying their contextual relations.

(2) Recognition of the business environment and target direction

After starting with the sales systems business (rental serves, comprehensive EC support service Shopserve, etc.), recently the Company has released its sales promotion systems (E Store Compare and E Store Query) as it makes used of IT and digital technology in its businesses. At the same time, however, the company has positioned its "analogue strategy" at the heart of its growth strategy.

To understand this focus, it is necessary to realize how the Company perceives its own current status. The Company's analysis shows that while the march of the IT society will continue unchecked, the demand side (consumers) has become sated (full) with IT (more precisely, the volume of information provision resulting from the adoption of IT). In this situation, the Company considers that conducting demand prediction using big data and AI will have only limited effectiveness.

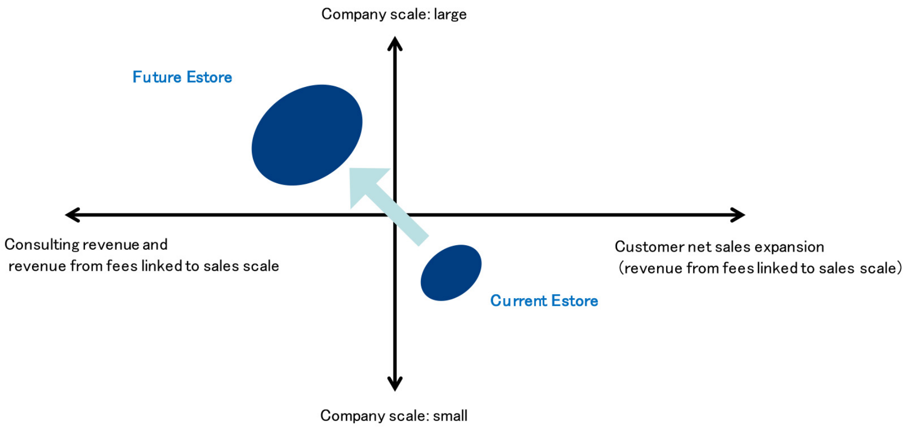
By contrast, the Company considers that an analogue strategy will prove effective. The Company will emphasize building comfortable relationships with its corporate customers and consumers, with just the right amount of distance.

Another very important factor influencing the Company's growth strategy is Japan's deflationary economy. The nation suddenly finds itself a society with a shrinking population, and the generation that experienced the collapse of Japan's asset bubble is gradually decreasing. The Company recognizes that the deflationary economy is therefore going to continue. This is expected to propel a transition from a consumer society that consumes physical things, to a sustainable society that makes physical things last longer. Since it is more difficult to sell products in a sustainable society, it will probably be important for the Company to pursue sales strategies based on relationships with existing companies.

The Company also considers that the deflationary economy will put pressure on companies to change their sales methods. To increase earnings under deflation, the Company predicts that companies will need to shift to sales strategies that do not rely on central locations such as malls, that is to say, direct sales.

Given the above situation and future outlook, it is clear that among the current three business divisions and four business domains, the domain that the Company will focus on especially going forward is the marketing services business. On the other hand, Shopserve within the sales systems business is gradually becoming a non-focus business as it becomes crowded by competition. Sales promotion systems are expected to help making marketing services more efficient, and were originally expected to become a focus field alongside marketing services. However, today the Company's sales promotion systems are often judged to be "premature" and the Company appears to have adopted a policy of not pushing them too hard. The Company has gradually changed its growth direction to stay aligned with the status of society; however considering the above situation, it is changing the size of its target companies from the small and medium-sized firms targets previously to large firms. In addition, in net sales, the Company has previously presented targets mainly around increasing customer sales corresponding to sales system flow revenue (revenue from fees linked to sales scale). By contrast, the Company's policy going forward is to target expansion of consulting revenues in the marketing services business. In consulting also, the target is to expand customer net sales, and as this leads to expansion in revenue from fees linked to sales scale, the Company will be able to increase the volume of its net sales in line with consulting revenue. Furthermore, since the customer who can pay consulting fees are of a certain minimum scale, this policy matches the strategy of targeting large corporations.

Conceptual diagram of growth direction for Estore



Source: Prepared by FISCO from interviews

In an environment that is not conducive to sales of physical goods, the Company will use its accumulated sales promotion expertise as a point of differentiation to supply services mainly to large companies, aiming to expand its business efficiently

2. The marketing services business growth strategy

In the marketing services business, the Company provides survey, analysis, consulting, and operations management agency services, among others, to help customers increase their sales. This service is distinguished by its high reliance on the human work force as it requires human input. This has both positive and negative implications, which will be described later.

The background factors for the Company's decision to strengthen its marketing services, and in particular consulting, is based on its recognition of social trends, the business environment, and other factors mentioned previously. The three elements required for business to succeed are "good products," "good markets," and "good information." However, the current status of these is "oversupply," "declining population," and "information overload." The basis of the Company's strategy for growing sales in this situations is to consider how it optimize distance with its customers. To achieve this, the Company's marketing services business will provide consulting services.

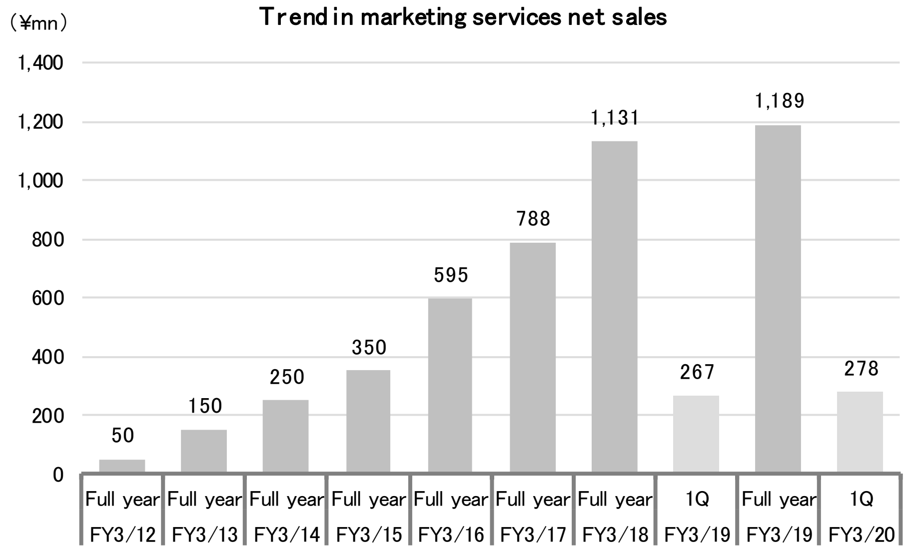
Conceptual diagram of the three elements for a flourishing business and current status

Source: Prepared by FISCO from the Company's Shareholders' Letter (2018)

In marketing services, net sales grew extremely well up to FY3/18, but slowed sharply in FY3/19, with growth declining by 5.2 pp year on year. The main factors reflected are special demand in the previous fiscal year. This refers to unplanned orders, and most of these were orders for strengthening seasonal promotions. When the impact of this special demand is ignored, the Company shows continued double-digit growth. Another factor is that acquisition of new customers has made almost no progress up to the second half of 3Q.

This appears to show the effect of the large-scale organizational restructuring conducted in August 2017. The restructuring was intended to rejuvenate management positions on a Company-wide basis. In FY3/19, the Company created a business plan under the new management and worked on it; however, it seems that some negative aspects of the rejuvenation came to the fore, and results have trended much lower than the business plan.

Acquisitions of new contracts gradually improved in FY3/19 4Q (January to March 2019), and going into FY3/20 1Q, the Company achieved a stable base of contracts. In consulting, the Company is engaged in sales activities that are specialized for acquiring large customers (for example, with an annual contract amount exceeding ¥10mn), with a view to increasing the efficiency of these services, which are highly reliant on the human work force. This also became a factor in the slump in new orders during 2018; however, since 2019, the number of large contracts has been steadily accumulating.



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

The marketing services business is gradually getting on track, but a distinctive feature of this service is its high reliance on the human workforce. On the positive side, it means that the service cannot be easily imitated by other companies. On the negative side, human resources (consultants) require time for acquisition and training, making it difficult to increase capacity. On this point, the Company has consistently invested in human resources while closely monitoring sales growth. To be precise, the Company makes sufficient budget allowance for human resource investment each year in its business plan. Over the past few years, the Company has not progressed as planned on acquisition and development of consultants, so that expenses have effectively been lower than envisaged. As a result, we are unable to view the higher-than-planned profits in a positive light when considering the situation from a long-term perspective.

For FY3/20, the Company is forecasting a decrease in profits, and the human resources issue is also a factor in this. From a medium- to long-term perspective, we would actually consider it a good result if profit declined as planned in FY3/20. We do not believe that the Company can continue to respond sluggishly to this situation. The budget appears to envisage an annual increase of 5 to 10 consultants, and if the recruitment and training proceeds as planned, then we believe the Company will achieve the team that it is aiming for in two to three years. We hope the Company will manage to increase its human resources as quickly as possible while maintaining its selection standards.

Expansion of revenue from fees linked to sales scale, which is linked with the scale of customer net sales, is a core growth strategy. In the very short term, the Company will continue to struggle with the impact of contract cancellations (decline in customer numbers); however, earnings could begin to increase again as early as FY3/21.

3. The sales systems business growth strategy

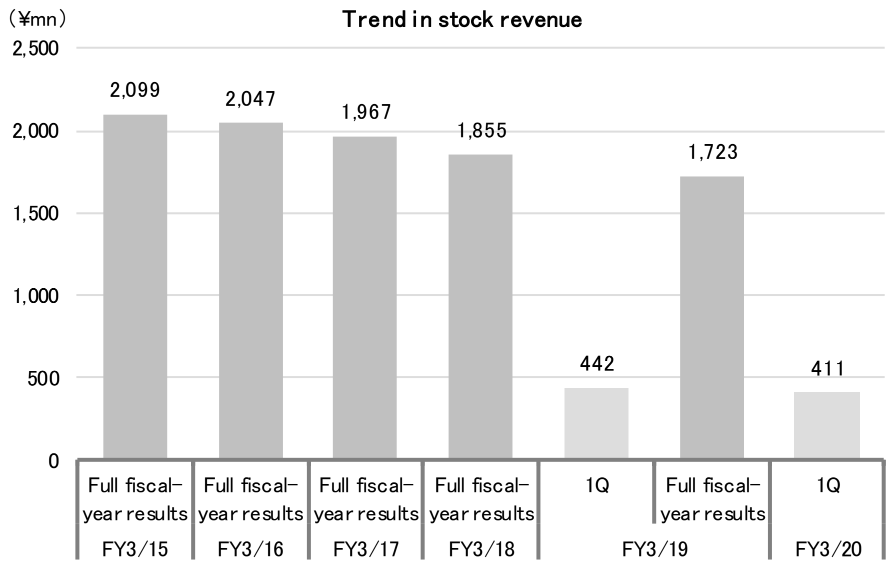
As described in the business overview section, the sales systems business revenues are classified into two types. The first is revenue from the Shopserve ASP service, which provides comprehensive EC support. This is a stock-type business model in which the Company receives monthly usage fees. The other type of revenue is collected as a fixed percentage of net sales conducted via Shopserve as a result of supporting for sales expansion of customer companies (revenue from fees linked to sales scale). This is described as a flow-type business model. The Company manages and discloses its recurring revenue and flow revenue separately.

The Company's recurring revenue has been on a declining trend. The reason for this is that as the Company continues to shift towards large customers, it is experiencing a steady rate of contract cancellations (mainly individual stores and small- to medium-sized companies acquired in the past), which is persistently higher than the rate of new contract acquisitions. This net decline in customer numbers is directly behind the trend of contracting earnings. However, it is consistent with the Companies management stance of "not pursuing contracting customer numbers."

Meanwhile, the Company is working to raise average spend by customer. There are two conceivable approaches to achieving this: raising spend for the same customers without changing their composition, and raising it by changing the customer composition. The Company is currently focusing on the latter. Under the slogan of "shift to good products, good stores," it is progressing the shift to large customers for the acquisition of new contracts.

Acquisition of large customers will not produce much increase in recurring revenue, which is monthly usage fee revenue. This is because the scale of the customer does not have much bearing on the monthly usage fee for Shopserve. However, it does make a significant difference in terms of flow revenue. The shift to large customers can be seen as an effort to change the sales composition of the sales systems business from recurring revenue to flow revenue.

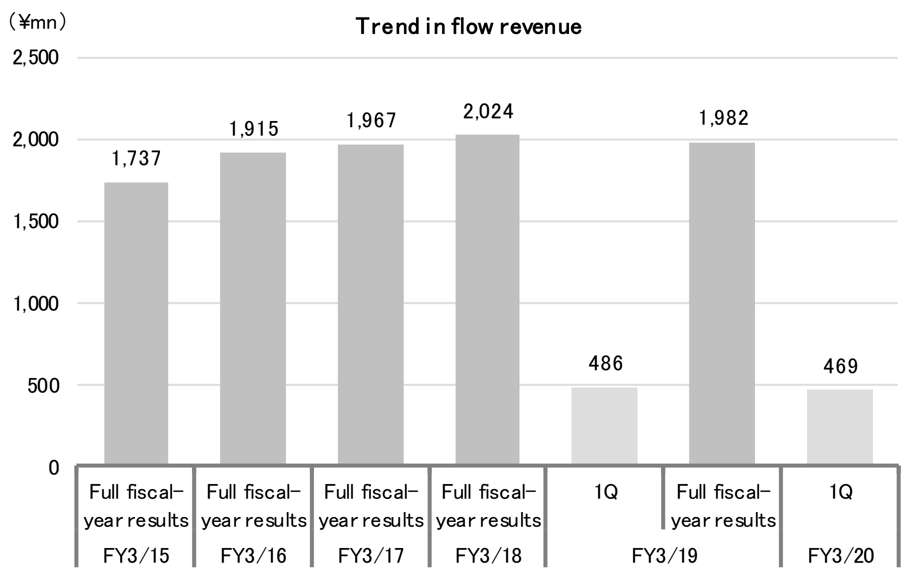
Recurring revenue essentially works to stabilize revenue. The Company itself has previously relied heavily on the stable revenue from Shopserve to support its management base and create resources for next-generation growth investment. The switch in emphasis from recurring revenue to flow revenue may cause concerns from the perspective of management stability, but we understand that the Company has made this management decision based on its expertise and accumulated experience as a result of increasing confidence in growth in sales of customer companies and attendant stable expansion in flow revenue.



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

The Company has thus been expecting growth in flow revenue, but growth began to level out in FY3/17, and revenue has begun to contract in FY3/19. This appears to reflect an increase in the impact of a declining number of Shopserve contract customers, despite steady growth in sales per store.

We expect this declining revenue trend to continue in FY3/20. The reason is that in FY3/19, new acquisitions of large customers were much lower than planned due to the effects of the aforementioned large-scale organizational restructuring. Since the start of FY3/20, however, the number of large customer acquisitions has been growing steadily, and we believe that flow revenue could start to recover and demonstrate YoY growth again as early as FY3/21.



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

Newly released software has been found to be effective, but many have claimed it to be “premature.” For now, the business is expected to continue developing slowly

4. The sales promotion systems business growth strategy

The sales promotion systems business refers to the development and sales of sales promotion support systems, which is to say promotion software. The objective of the business is to expand customers’ sales, which overlaps with that of the marketing business; however, the revenue model is made up of fixed basic monthly fees and a pay-for-use charge according to the number of times the services is used.

By autumn of 2017, the Company launched two Marketing Automation (MA) tools: Estore Compare (“Compare”) and Estore Query (“Query”). Compare is a tool that helps to increase EC website sales by using A/B comparison testing for an EC website to determine in real-time which has the higher conversion ratio (CVR), number of conversions, and life time value (LTV). On the other hand, Query is an email marketing tool for business operators who already have an existing customer base of a certain size. The main feature of the tool is that it can distribute personalized email through refined customer characteristics.

In the sales promotion systems business, fully fledged sales activities only began from FY3/19. Initial sales targeted existing Shopserve customers, and the Company planned to expand sales to external customers while monitoring the status of the initial sales. However, at this stage, sales have been lower than planned. The main factor appears to be the perception that the product is “premature.” In response to the situation, the Company has been proceeding slowly while reviewing the sales cost and target customers during FY3/20 1Q.

As described above, at this stage, the Company has been obliged to review its initial sales strategy. However, we believe there is ample potential to review the efficacy of the strategy over the medium to long term. In the short term, it seems possible that the sales promotion systems could be used to improve internal productivity in the marketing services business, which requires human input. The results could potentially be used to promote the tools and create sales.

Results trends

Upfront investment for strengthening human resources has resulted in lower earnings as forecast

1. Summary of the FY3/20 1Q results

In the Company's FY3/20 1Q results, sales and operating profit declined, with net sales of ¥1,167mn (down 3.2% YoY), operating profit of ¥113mn (down 21.2%), recurring profit of ¥135mn (down 5.7%), and profit attributable to owners of parent of ¥94mn (down 3.4%). The Company transitioned to consolidated results from FY3/19 2Q, so the above YoY comparisons are reference values.

Summary of the FY3/20 1Q results

(¥mn)

	FY3/19			FY3/20				
	1Q results	vs. FY3/19 1Q	Full year	1Q	vs. FY3/19 1Q	vs. full-year forecast	Full year (E)	YoY
Net sales	1,206	-1.0%	4,932	1,167	-3.2%	23.1%	5,047	2.3%
Operating profit	144	33.5%	515	113	-21.2%	32.8%	347	-32.7%
Operating profit margin	12.0%	-	10.5%	9.7%	-	-	6.9%	-
Recurring profit	143	35.1%	582	135	-5.7%	35.2%	384	-34.1%
Profit attributable to owners of parent	97	36.0%	409	94	-3.4%	31.7%	298	-27.2%

Note: The Company transitioned to consolidated results from FY3/19 2Q, so the growth rates for FY3/19 and FY3/20 are reference values.
Source: Prepared by FISCO from the Company's financial results

At the start of FY3/20, the Company announced a forecast for net sales to remain level or rise slightly at ¥5,047mn (up 2.3% YoY), while operating profit was to decline sharply at ¥347mn (down 32.7%). The background to this forecast was a conservative approach to the plan for net sales, based on a fallback from FY3/19. The Company appears to have arrived at this conclusion by considering the status of revenue from Shopserve (sales system, recurring revenue in terms of sales classification), due to ongoing contract cancellations in sales promotion systems, which had started full-scale sales in the previous fiscal year, and onset of a decline in sales system flow revenue due to the impact of shrinking customer numbers, despite growth in sales per store.

The Company's financial results for FY3/20 1Q were in line with forecasts. The sales system recurring revenue declined 7.0% YoY to ¥411mn. This mainly reflected an ongoing decline in customer numbers due to contract cancellations; however, this trend is in line with the Company's strategy as mentioned above. Sales system flow revenue was down 3.4% to ¥469mn. The Company has achieved an 8% increase in distribution amount per store, in line with its targets, but currently the impact of a decrease in customer number has cause a share decrease in sales. In sales promotion systems, net sales were up 35.6% YoY to ¥3mn. The rate of growth is considerable since net sales for FY/19 1Q were just ¥2mn. However, the result is not at all impressive when compared to the original expected performance of several tens of millions of yen for FY3/20 1Q.

In marketing services, net sales were up 4.3% YoY to ¥278mn. It is difficult to evaluate this result. On one hand, the Company has secured revenues, which is good. However, we estimate that the Company had expected a higher level of growth. The reason for this is that the increase for 1Q appears mainly to be due to an increase in revenues from existing contracts with small- to medium-sized companies, and does not reflect revenue from new contracts with large customers.

The Company is clearly making progress on its efforts to acquire new large customers. We observe that several transactions have reached the contract stage. However, there is a time lag between making a contract and recording sales. Therefore, almost nothing has been recorded in the 1Q financial results. We believe this will be resolved as sales are recorded from Q2 financial results and onward.

Breakdown of net sales by business

(¥mn)

	FY3/19						FY3/20	
	1Q results	2Q results	3Q results	4Q results	Full fiscal-year results	YoY growth rates	1Q results	YoY growth rates
Marketing services	267	268	316	338	1,189	5.2%	278	4.3%
Sales systems								
Stock	442	434	427	418	1,723	-7.1%	411	-7.0%
Flow	486	468	567	460	1,982	-2.0%	469	-3.4%
Sales promotion systems	2	3	5	3	13	-	3	35.6%
e-certification, media, others	8	8	2	3	21	-	5	-

Note: The Company transitioned to consolidated results from FY3/19 2Q, so the growth rates for FY3/19 and FY3/20 are reference values
Source: Prepared by FISCO from the Company's financial results

Meanwhile, on the profit front, operating profit for FY3/20 1Q was down 21.2% YoY, in line with the full-year forecasts (down 32.7%). The Company's forecast for a sharp decrease in profit for FY3/20 is due to up-front investments related to human resource acquisition and training. This mainly appears to involve increasing the number of consultant staff for the marketing services business, which is a focus business field. Over the past few years, the Company has created similar budgets and made efforts each fiscal year, but as it has been unable to progress as planned on human resource acquisition, it has continued to record higher-than-planned profits. The decrease in profit for 1Q can be considered a sign that the Company is making good progress on increasing its human resources. In that sense, it is by no means a negative result, and we believe rather that it represents steady progress.

For 2H, concern over the impact of consumption tax increase Large customer acquisitions are a more important focus than short-term performance. Delivery of adequate results in this regard will increase expectations of earning growth in FY3/21

2. Approach for FY3/20 full year

Estore forecasts for a profit decline on increased sales for the full year in FY3/19 with ¥5,047mn in net sales (up 2.3% YoY), ¥347mn in operating profit (down 32.7%), ¥384mn in recurring profit (down 34.1%), and ¥298mn in profit attributable to owners of parent (down 27.2%).

For FY3/20 Q2 onward, no particularly dramatic changes are expected in the business environment, and the Company is expected to continue accumulating its operating results along the same trajectory as 1Q. In its mainstay marketing services business, large contract acquisitions are proceeding as anticipated, or even better, and there actually a growing sense of expectation.

However, there is certainly no question of optimism. The main reason for this is the impacts related to the consumption tax increase. This is not the first consumption tax increase, but based on past experience, the initial reaction is very likely to be a temporary dip in net sales (the net result of rush demand and the subsequent fall back is a negative impact). In addition to the direct impact of a decline in sales, there are also potential impacts on the Company's commission fees from its credit card payment agency system for Shopserve customer companies and service providers stemming from the Ministry of Economy, Trade and Industry-sponsored projects related to cashless payment and consumer returns. The Company will strive to minimize any impacts, but we think that the situation precludes optimism for the time being.

These concerns related to the consumption tax increase are temporary, and we expect their impacts to be dispelled in FY3/21. If the Company can accumulate enough contract with large customers in its marketing services business by then, we believe there is ample potential for a strong surge in earnings in FY3/21.

Income statement

(¥mn)

	FY3/16 full year	FY3/17 full year	FY3/18 full year	FY3/19 full year	FY3/20	
					1Q	Full year (E)
Net sales	4,660	4,775	5,044	4,932	1,167	5,047
YoY	7.5%	2.5%	5.6%	-2.2%	-3.2%	2.3%
Gross profit	1,769	1,548	1,449	1,490	372	-
Gross profit margin	38.0%	32.4%	28.7%	30.2%	31.9%	-
SG&A expenses	1,140	1,141	895	974	258	-
SG&A margin	24.5%	23.9%	17.7%	19.8%	22.1%	-
Operating profit	628	407	554	515	113	347
YoY	12.5%	-35.2%	36.1%	-6.9%	-21.2%	-32.7%
Operating profit margin	13.5%	8.5%	11.0%	10.5%	9.7%	6.9%
Recurring profit	628	401	582	582	135	384
YoY	11.9%	-36.1%	44.9%	0.1%	-5.7%	-34.1%
Profit attributable to owners of parent	420	285	411	409	94	298
YoY	27.3%	-32.1%	44.1%	-0.4%	-3.4%	-27.2%
EPS after adjustment for share split (¥)	78.66	55.32	79.73	79.72	19.81	62.42
BPS after adjustment for share split (¥)	196.74	227.30	283.36	294.15	-	-
Dividend after adjustment for share split (¥)	24.00	24.00	28.00	29.00	-	-

Note: The Company transitioned to consolidated results from FY3/19 2Q, so the growth rates for FY3/19 and FY3/20 are reference values
Source: Prepared by FISCO from the Company's financial results

Balance sheet

(¥mn)

	As of March 31, 2015	As of March 31, 2016	As of March 31, 2017	As of March 31, 2018	As of March 31, 2019	As of June 30, 2019
Current assets	2,797	3,058	3,012	3,568	3,710	3,560
Cash and deposits	2,155	2,385	2,312	2,778	2,977	2,846
Accounts receivable	528	553	575	604	583	549
Fixed assets	511	447	480	411	785	887
Tangible fixed assets	100	82	129	106	106	98
Intangible fixed assets	116	108	103	74	56	50
Investment and other assets	293	256	247	230	622	739
Total assets	3,308	3,505	3,492	3,979	4,495	4,448
Current liabilities	2,098	2,471	2,296	2,490	2,065	1,946
Accounts payable	180	173	190	226	213	196
Short-term borrowings	102	324	-	-	-	-
Deposits held	1,393	1,559	1,740	1,853	1,604	1,529
Fixed liabilities	40	18	22	26	1,025	1,025
Long-term borrowings	24	-	-	-	999	999
Shareholders' equity	1,162	1,012	1,173	1,461	1,402	1,473
Paid-in capital	523	523	523	523	523	523
Capital surplus	539	539	539	539	-	-
Retained profits	2,439	2,759	2,921	3,209	1,203	1,274
Treasury stock	-2,339	-2,810	-2,810	-2,810	-324	-324
Accumulated other comprehensive income	6	3	-0	0	1	1
Stock subscription rights	1	-	-	-	-	-
Net assets	1,170	1,015	1,173	1,462	1,404	1,475
Total net assets & liabilities	3,308	3,505	3,492	3,979	4,495	4,448

Note: transitioned to consolidated results from FY3/19 2Q
Source: Prepared by FISCO from the Company's financial results

Cash flow statement

(¥mn)

	FY3/15 full year	FY3/16 full year	FY3/17 full year	FY3/18 full year	FY3/19 full year
Cash flows from operating activities	678	613	465	691	-26
Cash flows from investing activities	-122	-163	-88	-39	-349
Cash flows from financing activities	-252	-376	-449	-124	513
Effect of exchange rate change on cash and deposits	1	0	-0	-0	-0
Net increase (decrease) in cash and cash and deposits	305	74	-72	527	136
Cash and deposits at beginning of period	2,005	2,310	2,385	2,312	2,840
Cash and deposits at end of period	2,310	2,385	2,312	2,840	2,976

Note: transitioned to consolidated results from FY3/19 2Q
Source: Prepared by FISCO from the Company's financial results

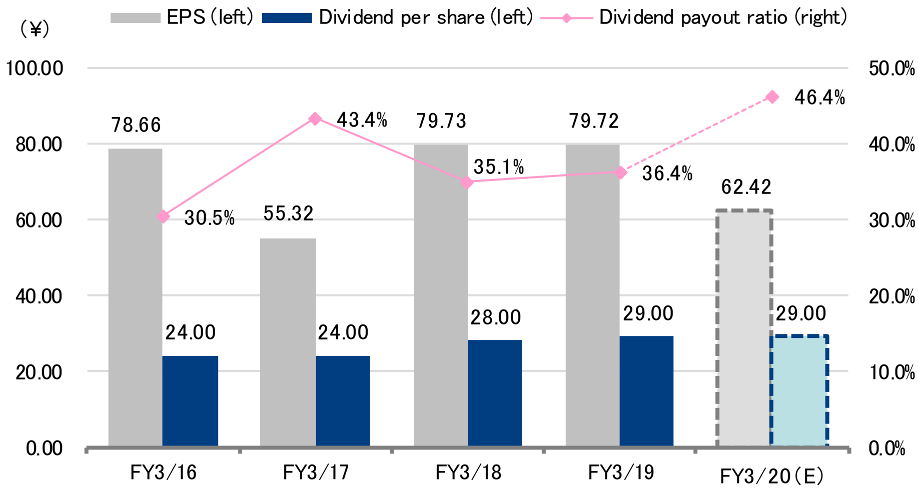
Shareholder returns

FY3/20 dividend expected to be level YoY at ¥29. Shareholder benefits dramatically increased from once-yearly dividend of ¥500 to twice-yearly dividends totaling ¥2,000

The Company basically returns profits to shareholders through dividends. It pays dividends after taking into account a comprehensive range of factors, including business results, financial position, and the need to retain sufficient internal reserves to invest in growth. While it does not formulate an official dividend payout ratio, the foundation of Estore's thinking on the distribution of profits is its basic philosophy of "dividing profits between three groups; shareholders, customers, and staff." In the past also, it has a track record of determining the dividend based on this basic philosophy.

The Company has decided on a dividend of ¥29 for FY3/19, an increase of ¥1 from FY3/18. For FY3/20, the Company has announced a dividend of ¥29 (year-end only), level with FY3/19. Earnings per share (EPS) for FY3/20 calculated using the average number of shares for 1Q was ¥62.42, yielding a dividend payout ratio for FY3/20 of 46.4%.

Trends in EPS, dividend per share, and dividend payout ratio



Note: EPS for FY3/20 calculated by FISCO using the average number of shares during FY3/20 1Q
Source: Prepared by FISCO from the Company's financial results

In addition to cash dividends, the Company also provides a shareholder benefits program. Recently, the Company announced that this program will be enhanced. Up until now, shareholders holding at least one trading unit (100 shares) as of March 31 each year have been gifted a QUO card with ¥500 of value. Now, this gift will be increased to a QUO card with ¥1,000 of value, given twice a year to shareholders as of September 30 and as of March 31. The annual shareholder benefit amount will thus be quadrupled from ¥500 to ¥2,000 per year. This system will be applied from September 30, 2019.

Disclaimer

FISCO Ltd. (“FISCO”) offer stock price and index information for use under the approval of the Tokyo Stock Exchange, the Osaka Stock Exchange and Nikkei Inc.

This report is provided solely for the purpose of offering information, and is not a solicitation of investment nor any other act or action.

FISCO prepared and published this report based on information which it considered reliable; however, FISCO does not warrant the accuracy, completeness, fitness nor reliability of the contents of this report or the said information.

The issuers’ securities, currencies, commodities, securities and other financial instruments mentioned in this report may increase or decrease in value or lose their value due to influence from corporate activities, economic policies, world affairs and other factors. This report does not make any promises regarding any future outcomes. If you use this report or any information mentioned herein, regardless of the purpose therefor, such use shall be made based on your judgment and responsibility, and FISCO shall not be liable for any damage incurred by you as a result of such use, irrespective of the reason.

This report has been prepared at the request of the company subject hereto based on the provision of information by such company through telephone interviews and the like. However, the hypotheses, conclusions and all other contents contained herein are based on analysis by FISCO. The contents of this report are as of the time of the preparation hereof, and are subject to change without notice. FISCO is not obligated to update this report.

FISCO and its affiliated companies, as well as the directors, officers and employees thereof, may currently or in the future trade or hold the financial instruments or the securities of issuers that are mentioned in this report.

Please use the information in this report upon accepting the above points.

■ For inquiry, please contact: ■
FISCO Ltd.
5-11-9 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062
Phone: 03-5774-2443 (Financial information Dept.)
Email: support@fisco.co.jp