COMPANY RESEARCH AND ANALYSIS REPORT

MonotaRO Co., Ltd.

3064

Tokyo Stock Exchange First Section

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Summary

Higher sales for 15 consecutive years and all-time high profits for seven straight years; Kasama DC starting operations in March and likely to lower logistics costs within the year

MonotaRO Co., Ltd. <3064> (hereafter, also "the Company") is headquartered in Amagasaki, Hyogo Prefecture. The Company conducts Online Direct marketing of maintenance, repair, and operating (MRO) products* for plants and construction work and automobile upkeep through the Internet.

* Maintenance, Repair and Operating (MRO) products refers to products used in the manufacturing process such as abrasives, drills, and work gloves, which are for internal use by companies and not for resale.

A key characteristic of the Company's business model is that it sells MRO products at a single price for all customers regardless of their scale or purchase amount. This policy has won the Company strong support from small to mid-size customers, who are usually forced to accept unfair prices from sellers in a conventional market. In this way the Company has established a solid position as a unique Online Direct marketing operator in a niche market. As of December 31, 2016, the number of registered accounts has reached 2.207 million and over 10 million items are sold to these customers.

1. FY12/16 non-consolidated results

The Company maintained strong sales and profit growth rates in FY12/16 non-consolidated results with ¥67,105mn in sales (up 20.7% YoY), ¥9,782mn in operating income (up 32.8%), ¥9,800mn in ordinary income (up 32.5%), and ¥6,631mn in net income (up 40.5%). Both sales and profits surpassed targets updated in October due to robust performance in 4Q. Sales benefited from growth in new customer acquisition aided by aggressive TV commercials and listing advertisements. Weaker growth than expected in average customer spending by existing customers led to the Company reinforcing promotions in 4Q and thereby reviving business. Gross profit improved thanks to optimized procurement, enhanced private-brand and imported products, and reduced import procurement costs due to yen appreciation. SG&A expenses were flat YoY, despite increased investments in efficiency improvements and promotions, with help from efficiency-related savings. On an overall basis, the Company steadily expanded profits by reducing product procurement expenses and controlling costs.

2. Consolidated results outlook

The Company forecasts continuation of strong sales and profit growth rates in FY12/17 consolidated results at ¥84,239mn in sales (up 21.0% YoY), ¥11,596mn in operating income (up 22.2%), ¥11,607mn in ordinary income (up 22.0%), and ¥7,934mn in net income attributable to owners of the parent (up 24.6%). Reaching these targets would extend consecutive increases to 16 fiscal years for sales and eight fiscal years for profits. The business strategy in FY12/17 focuses on enhanced customer convenience by strengthening the supply chain, including operation of the Kasama distribution center (DC), and realization of efficiency reforms and higher sales.

3. Kasama distribution center (Kasama DC)

The Company already completed the Kasama distribution (logistics) center located in Ibaraki Prefecture in February 2017 and is steadily preparing for the site's launch at the end of March 2017. It hopes to double the picking operation efficiency by deploying 160 self-directed delivery robots to conduct efficient picking of the wide range of products. This significantly shortens walking time, which accounted for a substantial amount of past picking time, by having robots bring shelves to workers. It expects to realize logistics cost savings from 2H FY12/17.

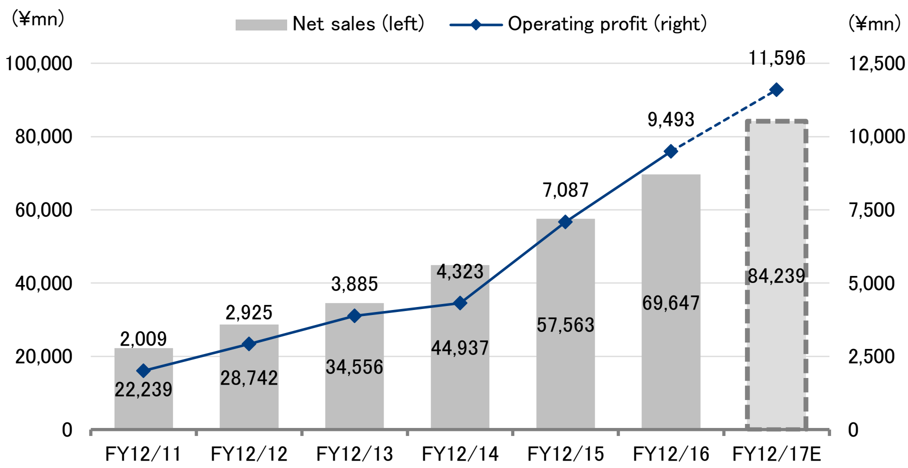
4. System links with large corporate customers

The Company has established system links with purchasing systems of large corporate customers and promoted initiatives to encourage purchasing. At the end of FY12/16, it is collaborating with 309 companies (up 88 companies from the end of FY12/15), and collaboration-related sales steadily expanded to ¥5,500mn (up ¥2,000mn from the end of FY12/15). Additionally, installations of the MonotaRO One Source, the Company's in-house developed system, climbed to nine companies (up five companies from the end of FY12/15). The Company plans to release MonotaRO One Source Lite in March 2017 as a strategy for expanding target customers by simplifying the MonotaRO One Source system and lowering the installation hurdle.

Key Points

- Surpassed targets updated in October due to robust performance in 4Q, higher sales for 15 consecutive years and all-time high profits for seven straight years
- Kasama DC starting operations in March and likely to lower logistics costs as early as 2H FY12/17
- Plans to release MonotaRO One Source Lite for system collaboration with large customers

Trends in sales and operating income



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

Results trends

Surpassed targets updated in October due to robust performance in 4Q, higher sales for 15 consecutive years and all-time high profits for seven straight years

• Review of FY12/16 results (non-consolidated)

The Company maintained strong sales and profit growth rates in FY12/16 non-consolidated results with ¥67,105mn in sales (up 20.7% YoY), ¥9,782mn in operating income (up 32.8%), ¥9,800mn in ordinary income (up 32.5%), and ¥6,631mn in net income (up 40.5%). Both sales and profits surpassed targets updated in October due to robust performance in 4Q. Sales benefited from growth in new customer acquisition aided by aggressive TV commercials and listing advertisements. The new account acquisition pace accelerated from 32,400 accounts/month in FY12/15 to 35,905 accounts/month in FY12/16. Weaker growth than expected in average customer spending by existing customers led to the Company reinforcing promotions in 4Q and thereby reviving business. Gross profit margin improved by 1.4 percentage points thanks to optimized procurement, enhanced private-brand and imported products, and reduced import procurement costs due to yen appreciation. The SG&A expenses ratio was flat YoY, despite increased investments in IT infrastructure and in efficiency improvements at Amagasaki DC and promotions to existing customers, with help from savings in personnel costs and business consignment expenses. On an overall basis, the Company steadily expanded profits by reducing product procurement expenses and controlling costs more than planned.

Non-consolidated income summary

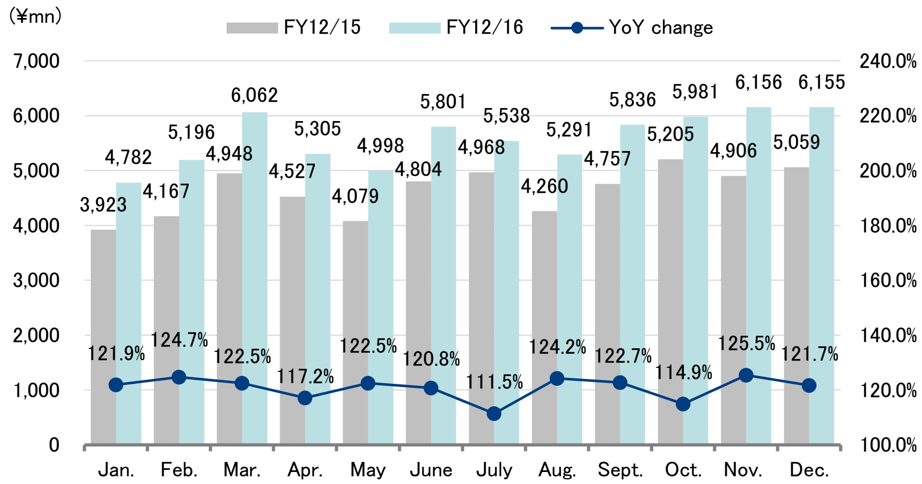
(¥mn)

	FY12/15		FY12/16				Change factors
	Results	vs. sales	Plan	Results	vs. sales	YoY change	
Net sales	55,607	100.0%	66,777	67,105	100.0%	20.7%	· Sustained the new customer acquisition pace with aggressive TV commercials and listing ads · Growth in existing customer sales lower than initially expected → additional promotion benefits surfaced in 4Q
Gross profit	16,957	30.5%	21,333	21,406	31.9%	26.2%	· 1.4pp YoY rise in gross margin · Gain driven by optimized procurement, enhanced PB and imported products and yen appreciation
SG&A expenses	9,593	17.3%	11,670	11,624	17.3%	21.2%	· SG&A expenses ratio unchanged from the previous year · Lowered operation costs at the Amagasaki distribution center with better efficiency · Strengthened promotions and invested in IT infrastructure to sustain growth
Operating income	7,363	13.2%	9,663	9,782	14.6%	32.8%	· 1.4pp YoY increase
Ordinary income	7,398	13.3%	9,667	9,800	14.6%	32.5%	· 1.3pp YoY increase
Net income	4,718	8.5%	6,425	6,631	9.9%	40.5%	· 1.4pp YoY increase

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

Though the Company's monthly results vary, affected by seasonal factors and promotions, there is a general upward trend in sales from January to December as sales to exisiting customers rise each year. The same pattern was apparent in FY12/16. Sales growth held at around 20% YoY through the year.

Monthly sales



Source: Prepared by FISCO from the Company's IR news

For consolidated results, overseas business grew at a healthy pace, and the Company launched efforts in Southeast Asia in FY12/16. The Korean subsidiary actively acquired customers, mainly with listing ads, and broadened the range of products it handles and inventory products, setting the stage for realization of single-month profitability in FY12/17. The Indonesian subsidiary became part of consolidated results in 4Q FY12/16, and royalty income improved as a result of sales growth in the US and Europe of a business entity to which the Company rendered its consulting services.

Business outlook

Aiming for a continued increase in sales for a 16th consecutive year and record profits for a 8th consecutive year

• FY12/17 outlook

The Company forecasts continuation of strong sales and profit growth rates in FY12/17 consolidated results at ¥84,239mn in sales (up 21.0% YoY), ¥11,596mn in operating income (up 22.2%), ¥11,607mn in ordinary income (up 22.0%), and ¥7,934mn in net income attributable to owners of the parent (up 24.6%). Reaching these targets would extend consecutive increases to 16 fiscal years for sales and eight fiscal years for profits. Business strategies include 1) ramping up investments in advertising and other efforts to acquire new customers, 2) continuing promotions to existing customers that were effective in 4Q FY12/16, 3) enhancing customer convenience with a strengthened supply chain, including operation of the Kasama distribution center (DC), 4) promoting correlation with large companies, and 5) pursuing overseas opportunities.

Consolidated operating results targets

(¥mn)

	FY12/16		FY12/17			2Q FY12/17	
	Results	vs. sales	Targets	vs. sales	YoY change	Targets	YoY change
Net sales	69,647	100.0%	84,239	100.0%	21.0%	40,414	21.4%
Gross profit	21,895	31.4%	-	-	-	-	-
SG&A expenses	12,401	17.8%	-	-	-	-	-
Operating income	9,493	13.6%	11,596	13.8%	22.2%	5,393	19.6%
Ordinary income	9,514	13.7%	11,607	13.8%	22.0%	5,399	19.7%
Net income attributable to owners of the parent	6,368	9.1%	7,934	9.4%	24.6%	3,685	23.8%

Source: Prepared by FISCO from the Company's materials

Topics

Kasama DC starting operations in March and likely to lower logistics costs as early as 2H FY12/17

1. Kasama DC operations and improved logistics

The Company already completed the Kasama distribution (logistics) center located in Ibaraki Prefecture in February 2017 and is steadily preparing for the site's launch at the end of March 2017. This large-scale center, which sits on land totaling about 90,000m^2 and has roughly 56,000m^2 in floor space, should contribute along with the Amagasaki distribution center, assuming parallel operation, to expansion of inventory capacity to 500,000 units and support for sales of ¥150,000mn. While the investment totaled ¥8,500mn, including land, building, and initial equipment, the Company selected direct ownership because it has economic advantages over leasing and allows for flexible operational design.

The Company hopes to double the picking operation efficiency by deploying 160 self-directed delivery robots to conduct efficient picking of the wide range of products. This significantly shortens walking time, which accounted for a substantial amount of past picking time, by having robots bring shelves to workers.

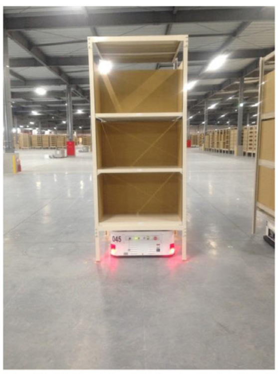
The Company expects to realize logistics cost savings from 2H FY12/17. Logistics costs were at 5.9% of sales in FY12/16, and it projects an upturn to 6.3% in 1H FY12/17, during the transition phase, and 5.4% in 2H FY12/17. This outlook takes into account closure of the existing Tagajyo DC (Miyagi Prefecture) in June 2017 and reductions in personnel expense and business consignment cost ratios (relative to sales) through operating the Kasama DC.

FY12/17 business strategy

◆ New Distribution Center (Kasama DC) to start operation

- Construction to be completed in late February and operations to start in March
- ¥8.5bn investment (land, building, and initial equipment)
- Automated operations to realize higher productivity (improving picking operation by self-directed delivery robots)
- Tagajyo DC in Miyagi Prefecture to be closed in June as Kasama DC starts operations
- Higher productivity enables to lower labor and outsourcing expenses in 2H, and ratio of distribution-related cost to sales to be lowered after launch of operations at Kasama DC

Kasama DC exterior view (Jan. 2017)



Self-directed delivery robot

Source: Reprinted from the Company's results briefing materials

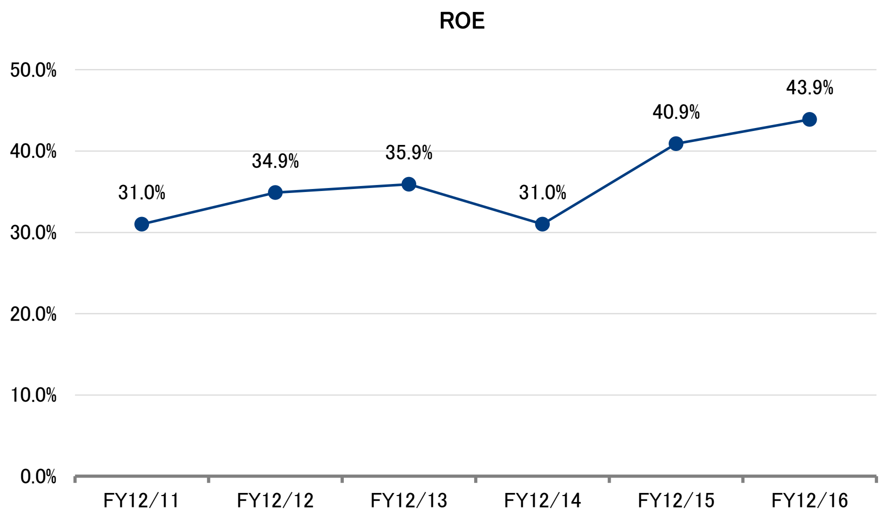
2. Plans to release MonotaRO One Source Lite for system collaboration with large customers

The Company has established system links with purchasing systems of large corporate customers and promoted initiatives to encourage purchasing. At the end of FY12/16, it is collaborating with 309 companies (up 88 companies from the end of FY12/15), and collaboration-related sales steadily expanded to ¥5,500mn (up ¥2,000mn from the end of FY12/15). Collaboration-related sales growth has been exceeding the Company's overall growth rate over the past few years, and sales expanded about fivefold in the four years since FY12/13. Additionally, installations of the MonotaRO One Source, the Company's in-house developed system, climbed to nine companies (up five companies from the end of FY12/15).

The Company plans to release MonotaRO One Source Lite in March 2017 as a strategy for expanding target customers by simplifying the MonotaRO One Source system and lowering the installation hurdle.

3. High-efficiency management with ROE above 40%

The Company is known for high-efficiency management with very strong ROE at more than 30% in the past six fiscal years, including over 40% in the last two fiscal years. Its robust business model has been supporting the steady rise in ROE. The Company achieves high earnings by providing long-tail products, acquiring customer satisfaction through delivery of products that customers want quickly and at reasonable prices, and realizing cost savings with scale benefits from sales growth and utilization of IT. We think the Company should sustain high ROE as long as it can continue to refine this business model.



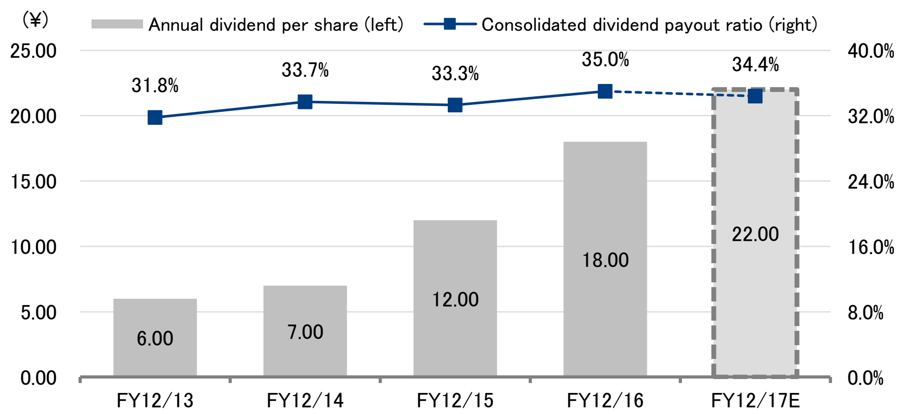
Source: Prepared by FISCO from the Company's financial results

Shareholder return policy

Keeping the dividend payout ratio at 30% or above, targets a ¥22 dividend in FY12/17

The Company's policy on dividends is to pay a stable dividend in accordance with its operating results. The Company sharply raised the FY12/16 dividend to ¥18 (up ¥6 YoY) at ¥9 in 1H and ¥9 in 2H. For FY12/17 the Company is projecting another dividend increase to ¥22 per share, comprising a 1H dividend of ¥11 and a 2H dividend of ¥11, due to a target increase in profit for the year. The dividend payout ratio has been maintained at the 30% level over the past four years, and is projected to maintain the same level for FY12/17 at 34.4%. The Company offers shareholder benefits in the form of private brand product gifts of a ¥3,000 in value for each shareholder holding 100 or more shares at the end of the fiscal year (December 31).

Dividends and consolidated dividend payout ratio



Source: Prepared by FISCO from the Company's financial results
Note: The Company conducted 2-for-1 stock splits in FY12/13 and FY12/15, which have been reflected retroactively.

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