

Cosmos Initia Co., Ltd.

8844

TSE JASDAQ

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<http://www.fisco.co.jp>

■ Index

■ Summary	01
■ Company profile	03
1. Company profile and history	03
2. Synergies from partnership with Daiwa House	04
■ Business overview	05
1. The Company's business	05
2. Residential business	06
3. Solutions business	07
4. Construction business and Overseas business	08
■ Medium/long-term business strategy	08
1. Business rehabilitation plan and previous medium-term business plan	08
2. Business environment and basic action plan	10
3. Medium/long-term strategy and image of business scale	11
■ Results trends	14
1. FY3/18 results	14
2. FY3/19 forecast	15
3. Progress versus medium-term business plan 2018	17
■ Shareholder return policy	18
■ Information security	18

■ Summary

Making full use of its expertise in new condominium development, pursuing growth through development and sales of investment properties and apartment hotels

Cosmos Initia <8844> is a mid-tier developer of condominiums and detached housing, specializing in family-oriented condominiums for first-time buyers. Geographically, it operates mainly in the greater Tokyo area and Kinki region. The Company was found in 1969 as a subsidiary of Japan Recruit Center (now Recruit Holdings Co., Ltd.), but is now pursuing its growth strategy as a subsidiary of Daiwa House Industry <1925> and member of the Daiwa House group. The scope of Cosmos Initia's business has broadened over the years as it has gained expertise in different areas and customer needs have grown more diverse. Its business is split into four segments, with its mainstay Residential business (for general consumers) and Solutions business (for businesses) supplemented by a Construction business and Overseas business. In FY3/18, the Residential business accounted for 39% of sales, the Solutions business 47%, the Construction business 10%, and the Overseas business 4%.

Under its Residential business, Cosmos Initia offers various brand lines including its INITIA series of newly built condominiums, COSMOS AVENUE series of new detached housing, and its Renovation series of renovated pre-owned condominiums. The Company has a long reputation for high-quality, customer-oriented service, including after-sale service. At its Solutions business, the Company offers various corporate agency brokerage services, including subleasing of condominiums, office buildings, and other types of properties, sales of investment properties including condominiums and buildings, and consulting services for investment property development. In this area, the Company is distinguished by its professional solutions that draw on the resources of the entire group. The Construction business builds condominium galleries, handles sales of interior design options, and does renovation work in connection with office relocations. The Overseas business has been managing a resort hotel in Australia but, in accordance with the 2018 medium-term business plan, is pulling out of this business in March 2018.

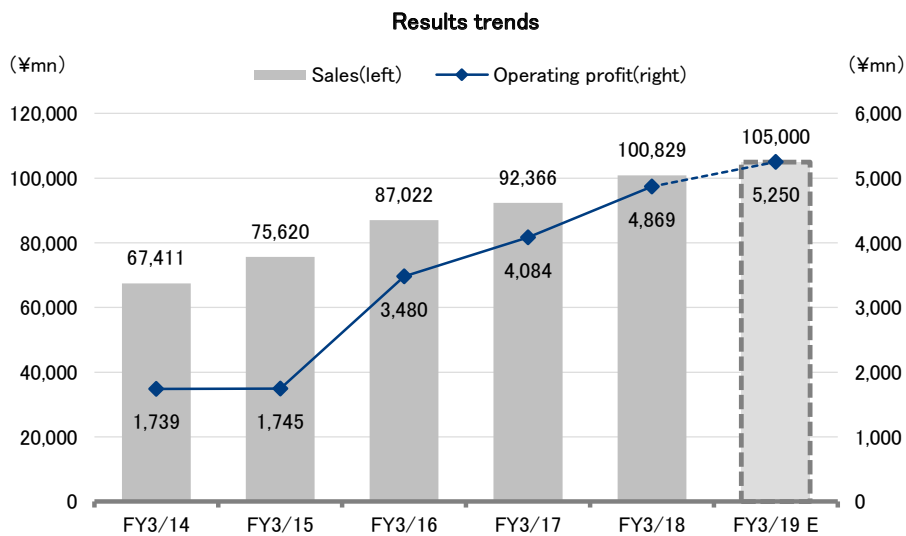
The Company is currently working under its 2018 medium-term business plan to implement initiatives aimed at strengthening its business base and pursuing its growth strategy. The Company has also set forth a medium/long-term business strategy that looks out further ahead of the current medium-term plan, which only runs through FY3/19. At the Residential business, the Company is looking to do more new condominium development work and more renovation work; in addition to its traditional target market, it will also be building housing designed for the so-called "active senior" market. At its Solutions business, the Company is looking to offer a one-stop solutions service for business-use property owners, and is also looking to enter the lodging market for overseas travelers by developing and operating apartment hotels. In terms of sales, the Company envisions total sales of ¥155,000mn in the near future, with some ¥70,000mn of this coming from the Residential business, ¥70,000mn from Solutions, and ¥15,000mn from the Construction and the Overseas business.

Summary

For FY3/19, the Company is forecasting sales of ¥105,000mn (+4.1% YoY) and an operating profit of ¥5,250mn (+7.8%). The gross profit margin is expected to decline as a result of its exit from the high-margin overseas resort hotel management business. In this relation, we note that the operating profit target for FY3/19 under the 2018 medium-term business plan had initially been set at ¥5,000mn but was raised to ¥5,250mn. The cause was a strong performance in the Solutions segment, including real estate for investment among other factors. . The Company also reported that new businesses are getting off to a good start. The Company completed construction of its first condominium complex designed for active seniors (the Grand Cosmo Musashiurawa) in 2016, and has already has tentative plans to build three more properties of this kind through redevelopment projects undertaken in large cities in rural regions. On the apartment hotel development and management front, the Company opened its first facility in February 2018 and as of the April end had a four such properties with a total of 154 guest rooms in operation. Given the progress thus far, it would appear that the Company is finally ready to start expanding these new businesses nationwide.

Key Points

- Mid-tier developer operating mainly in Tokyo area and Kinki region, especially strong in new condominium and investment property development and sales
- Targets under medium-term business plan raised on strong performance of investment real estate business; medium/long-term strategy aiming for sales of ¥155.0bn
- New businesses in condominiums for active seniors and apartment hotels both off to good start



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

■ Company profile

Developer of INITIA brand condominiums and the old Cosmo brand

1. Company profile and history

Cosmos Initia is a mid-tier developer affiliated with the Daiwa House group, focusing mainly on condominiums and detached housing in the greater Tokyo area and the Kinki region. Specializing in family-oriented condominiums for first-time buyers, Cosmos Initia has a very long track record and has brought a cumulative total of more than 100,000 new condominium units to the market. As the needs of customers have grown more diverse and its partnership with Daiwa House has grown, Cosmos Initia has turned itself into a one-stop shop for a wide variety of housing products and services for the general consumer, including new condominiums and detached housing, retail brokerage services, pre-owned condominium purchasing and sales, renovation and remodeling, as well as various after-sale services after the homeowner or tenant moves in. For owners of business-use properties, the Company has also expanded its service menu over the years and now offers a one-stop real estate solutions service, including investment property sales, subleasing of condominiums and office properties, agency services for business-use properties, and real estate consulting. Going forward, Cosmos Initia is looking to continue diversifying its business portfolio away from its past focus on condominium development.

The roots of Cosmos Initia go back to its founding as Japan Recruit Motion Pictures Co., Ltd., a subsidiary of Japan Recruit Center. The Company subsequently switched its business to real estate in 1974. In 1985 the Company changed its Recruit Cosmos Co., Ltd. and was listed on Japan's over-the-counter stock market (now JASDAQ) in 1986. Following a management buyout in 2005, it became independent and it changed its name to Cosmos Initia in 2006, the name it still holds today. Not long after that, however, the real estate market crashed as the collapse of Lehman Brothers shook the financial markets and Cosmos Initia fell victim to its heavy debt load. Having become insolvent, the Company went into Business Revitalization ADR proceedings in 2009, where an agreement was reached on business rehabilitation plan. Cosmos Initia got financial support from its creditors but had to sell off its condominium management company and other assets to Daiwa House. The business rehabilitation plan was finally completed in 2013 as Cosmos Initia paid off the last of the debt covered by the Business Revitalization ADR agreement. Shortly thereafter Cosmos Initia entered into a capital and business alliance with Daiwa House that made it a subsidiary, and it is currently pursuing its growth strategy as a member of the Daiwa House group. Cosmos Initia's mainstay condominium line that now goes under the INITIA brand name used to go by the name of Cosmo when the Company was a member of the Recruit Group.

Company profile

History

History	
June 1969	Japan Recruit Motion Pictures Co., Ltd. is founded in Chiyoda-ku, Tokyo
February 1974	Business objective is changed to the real estate business, and the company name changed to Environment Development Co., Ltd.
May 1974	Sales operations for mid- to high-rise housing begin
June 1977	Osaka Branch (now West Japan Branch) is established and begins sales operations for mid- to high-rise housing in the Kinki region
January 1985	Brokerage Department is established
March 1985	Company name is changed to Recruit Cosmos Co., Ltd. Head office is moved to Chuo-ku, Tokyo
July 1986	Real Estate Rental Business begins in earnest
October 1986	Company stock is listed on the over-the-counter market (now the Tokyo Stock Exchange JASDAQ)
March 1987	All stock for Cosmos Life Co., Ltd. (now DAIWA LIFENEXT Co., Ltd.) is acquired, and entry is made to the real estate management business
January 1990	Cosmos More Co., Ltd., (now a consolidated subsidiary) is established to undertake building and repair work
September 1990	Cosmos Australia Pty. Ltd. is established in Australia Overseas hotels and resorts operations begin
July 1993	The head office is moved to Minato-ku, Tokyo
April 1996	Sales operations of single-family homes begins in earnest
October 1998	Cosmos Hotline is established as a point of contact for customers
June 2005	The Company is spun off from the Recruit Group through a management buyout
September 2006	Company name is changed to Cosmos Initia Co., Ltd. Head office is moved to Chiyoda-ku, Tokyo
April 2009	After becoming insolvent amid real estate market downturn, used Business Revitalization ADR (alternative dispute resolution) proceedings to create business rehabilitation plan
July 2009	Three branches in the Tokyo metropolitan area (Chiba Branch/Yokohama Branch/Northern Kanto Branch) are integrated into the head office
September 2009	All stock from Cosmos Life Co., Ltd. is transferred to Daiwa House Industry Co., Ltd.
January 2011	Number of condominiums sold tops 100,000
July 2011	The head office is moved to Minato-ku, Tokyo.
June 2013	Daiwa House Industry Corp. became the largest stockholder of company and joined the Daiwa House Group
October 2014	Cosmos Life Support Co., Ltd. (now a consolidated subsidiary) is established
May 2016	Establishment of mid-term business plan
December 2016	Cosmos Australia Holdings Pty Ltd (now a consolidated subsidiary) is established
October 2017	Cosmos Hotel Management Co., Ltd. (now a consolidated subsidiary) is established
December 2017	Entered into capital and business alliance with WOOC Co., Ltd. to develop business to revitalize vacant space in rental office buildings and other properties
March 2018	All stock from KBRV Resort Operations Pty. Ltd. held by Cosmos Australia Pty. is transferred. Withdraw from overseas hotels and resorts operations

Source: Prepared by FISCO from the Company's securities report, etc.

Capital and business alliance with Daiwa House Industry

2. Synergies from partnership with Daiwa House

Cosmos Initia has enjoyed the textbook synergies one might expect from its acquisition by Daiwa House in 2013. As a subsidiary of Daiwa House, Cosmos Initia has been able to more easily secure the financing needed to pursue its real estate development business, receiving strong backing from Daiwa House in the form of credit guarantees as well as overall support. And, because Daiwa House makes it a practice to respect the management teams of the companies it acquires, Cosmos Initia has also enjoyed a great deal of autonomy since being acquired, making its own decision about personnel, operations, and even maintaining its stock exchange listing. As this has allowed Cosmos Initia to maintain the continuity in its management team as well as in its branding, which in turn has helped drive the subsequent recovery in sales and earnings. From the perspective of Daiwa House, the acquisition of Cosmos Initia has helped it fill a gap, for even though Daiwa House was already operating in many areas—from detached housing to rental housing, to commercial buildings and construction—prior to the acquisition of Cosmos Initia it did not have much of the presence in the Tokyo area condominium market. With knowledge and experience in the Tokyo, Japan's largest condominium market, Cosmos Initia was a welcome addition to the Daiwa House group that would help it expand its condominium business.

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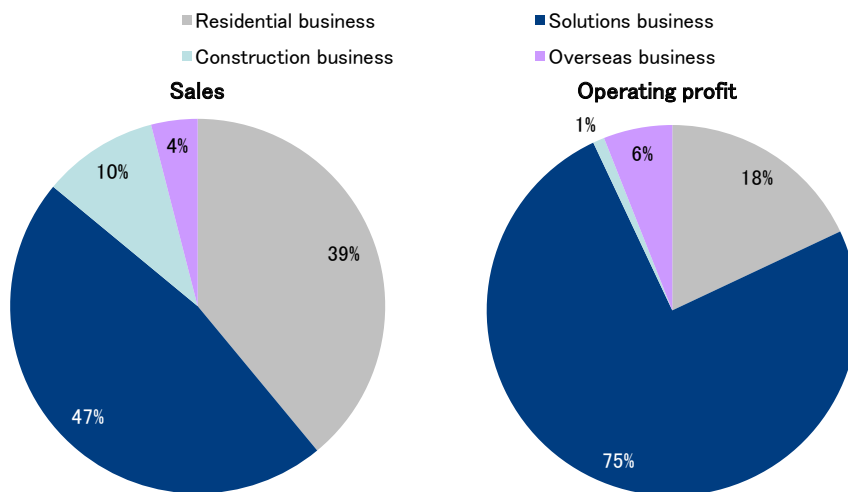
Business overview

Majority of sales and earnings come from two businesses, the Residential business that deals in housing and Solutions business that deals with investment properties

1. The Company's business

Cosmos Initia's primary business is real estate development and sales, but this is broken down further into a Residential business that offer housing products and services for the general consumer and a Solutions business that provides professional services as well as investment real estate and other products to the corporate market. In addition to these two large businesses, Cosmos Initia also has a Construction business and an Overseas business. The Residential business accounted for 39% of sales and 18% of operating profit, the Solutions business 47% of sales and 75% of operating profit, the Construction business 10% of sales and 1% of operating profit, and the Overseas business 4% of sales and 6% of operating profit. The mainstays of the business are the Residential and Solutions businesses, which are primarily managed by the parent company while the Construction and the Overseas businesses are operated by subsidiaries.

Breakdown of sales ratio and operating profit ratio by segment (FY3/18)



Note: All figures prior to adjustments

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

One-stop shop for housing-related products and services for the general consumer

2. Residential business

Cosmos Initia's Residential business does not follow the traditional split between new homes and pre-owned homes, but rather holds itself out as a one-stop shop for housing-related products and services for the general consumer. Its service menu includes its INITIA series of new condominiums and COSMOS AVENUE series of new detached housing, its &Renovation series of renovated, pre-owned condominiums, and retail real estate brokerage services. In FY3/18, new condominiums accounted for 64% of segment sales ratio, new detached housing 12%, renovated condominiums 22%, and retail real estate brokerage services 2%. Cosmos Initia is distinguished by the high proportion of certified first-class registered architects on staff, and its reputation for high-quality, customer-oriented service, including after-sale service.

The new condominiums that account for most of sales at the Residential business go under the INITIA brand name. INITIA condos are aimed at families, their target market being discerning, first-time buyers in their early 30s. As a successful condominium developer of many years, Cosmos Initia has made a practice of listening to customers and so has been consistently able to envision what customers want ahead of time and bring to market condominiums that offer the comfortable living space buyers are looking for. Cosmos Initia's success is evidenced by its long track record that took it over the 100,000 unit mark for new condominiums in 2011 (its 37th year as a developer) and its receipt of the prestigious Good Design awards for 16 years running. In recent years Cosmos Initia has also applied the concept of "spatial quality" to create living spaces that are larger, more enjoyable, and easier to use through innovative designs such as "scenery kitchen" designs that place the kitchen in the center of an LDK condominium and widening entryways to create "welcome halls." In response to the rapidly changing demographics, Cosmos Initia has also started designing condominiums for the so-called "active senior" market.

Although best known as a condominium developer, Cosmo Initia is also a prolific builder of detached housing, having built more than 4,000 units. Applying the same QIT quality control management system to new detached housing that it developed and uses in the construction of new condominiums, Cosmos Initia has been lauded for its service structure that facilitates the formation of communities after people move into new sub-developments by holding ceremonies and other activities until a new community is finally formed. When it comes to renovating condominiums, Cosmos Initia applies the design expertise and skills that it has acquired from years in the new condominium development business and applies it to older condominiums to change ambiance and give it a more welcome feel. In the area of residential-use real estate brokerage services, Cosmos Initia not only helps people with selling properties it also offers services make it easier for homeowners to move to a new home by allowing them to stay in their current and complete the sale only after they buy a new home (katte kara nattoku baikyaku) or, alternatively, buys the condominium from the owner and allows them to stay there while looking for a new place to live (suminagara kaitori).

One-stop solutions service for owners of investment properties

3. Solutions business

The Solutions business is aimed at meeting the needs of owners of investment properties and, with the help of its own and the many professionals in the Daiwa House group, is a one-stop shop for real estate-related solutions services. The service menu includes subleasing of condominiums and office buildings, a real estate brokerage service to handle sales of condominiums, business-use buildings and land, especially the condominiums in the Company's COSMO REID series and office buildings in the REID-C series that were designed specifically as investment properties. Real estate subleasing accounts for 30% of sales ratio at the Solutions segment, investment properties 68%, and real estate brokerage 2%.

Cosmos Initia has been in the property management business for many years, managing the leases of more than 9,500 residential properties as well as a variety of other buildings, including retail store space. Most of its business is accounted for by the subleasing of residential properties, wherein the condominium owner leases his property to the Company who in turn subleases it to tenants. This service offers a great deal of convenience to property owners, as it allows them to avoid the troublesome process of finding tenants, signing rental contracts, renewing contracts, and responding to tenants problems, and also has the additional advantage of signing a one-time leasing agreement that guarantees a safe and steady stream of rental income. The subleasing business also works out well for Cosmos Initia by limiting the business risk that goes along with property ownership while remaining in a position to generate a steady stream of revenues and earnings.

In the area investment property, Cosmos Initia develops smartly style condominiums, office buildings, and commercial properties for sale to investors, and also buys entire old condominium complexes and office buildings that it can renovate, upgrade, bring up to code, and then resell to investors that are looking to generate steady returns by investing in real estate. In this business the Company focuses mainly on properties in central urban districts where demand is high. On the surface, this type of property development and renovation business may appear to very risky. However, thanks to Cosmos Initia's wide-ranging expertise and its targeting of smaller properties (¥200mn to ¥500mn) where there is little competition, it is able to reduce its risk relative to other operators and probably has a distinct advantage over the rest of the industry.

Also included under the Solutions segment is the Company's investment property brokerage service, real estate property development consulting service, and architectural design administration and construction management service. In response to the growing number of foreign tourists visiting Japan in recent years, Cosmos Initia has also started an apartment hotel development and management business, distinguishing its apartment hotel properties with spacious rooms that can accommodate families of four or more and include kitchens versus the growing pipeline of business hotels designed to accommodate one or two occupants per room. With this broad service menu for investment property investors, Cosmos Initia is prepared to provide solutions regardless of the type of property or client.

Cosmos Initia Co., Ltd.

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30-Jul.-2018

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Business overview

As Construction business grows, overseas resort hotel management business is being wound down

4. Construction business and Overseas business

The Construction business is run mainly by Cosmos More Co., Ltd, which builds condominium galleries, handles sales of interior design options for new condominiums, handles repairs and improvements related to office relocations, and builds steel houses and other buildings. Cosmos More is also moving into office design services aimed at creating the maximum value for an office property through smart spatial designs and also has a large-scale building repair business providing service for condominiums operated by Daiwa Cosmos Construction Co., Ltd. The Overseas business consists of Cosmos Australia Pty Ltd. and seven other subsidiaries. In addition to managing a resort hotel on scenic Fraser Island (a World Heritage Site as the largest sand island in the world), located off the coast of the state of Queensland, Australia, the subsidiaries operate other real estate-related businesses in Australia. The resort hotel management business has been profitable recently, but the lack of synergies with the other business and the large impact on results from swings in foreign exchange rates led to a decision to sell off the resort hotel management business in March 2018. As for plans for the Overseas business going forward, the Company said it will be working together with the Daiwa House group on condominium development projects in Sydney, Australia, and is also looking at operating serviced apartments in Australia and New Zealand. In other areas, subsidiary Cosmos Life Support Co., Ltd. provides property management services for condominiums for active seniors.

■ Medium/long-term business strategy

Business rehabilitation plan → previous medium-term business plan → medium-term business plan 2018

1. Business rehabilitation plan and previous medium-term business plan

As mentioned previously when reviewing the Company's history, Cosmos Initia became insolvent in the wake of the financial crisis sparked by the collapse of Lehman Brothers but was eventually turned around under a business rehabilitation plan. After completing the business rehabilitation process, Cosmos Initia became a subsidiary of the Daiwa House group and put together its previous medium-term business plan as it set its sights on growing its business again. Under the medium-term business plan 2018, Cosmos Initia is moving forward with additional initiatives aimed at reinforcing its business base and pursuing its growth strategy. And with its medium/long-term business strategy, it has also given us the business it would like to be in the years after the medium-term business plan 2018 runs out.

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30-Jul.-2018

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Medium/long-term business strategy

During the lead-up to the final approval of its business rehabilitation plan, Cosmo Initia undertook a broad-based restructuring, starting with liquidating certain assets. At that time, it sold the condominium management business operated by subsidiary Cosmo Life Co., Ltd. (now DAIWA LIFENEXT Co., Ltd.) to Daiwa House, and based on financial support such as getting banks to forgive some ¥37.0bn in loans, doing a debt-equity swap worth ¥30.5bn, and getting concessionary repayment conditions on another ¥100.8bn in loans, implementing an extensive and rigorous restructuring. The business rehabilitation plan was completed on schedule in FY3/13, but even though the Cosmo Initia's financials had improved much more than initially expected, its credit standing had not yet recovered to the point where it could expect to raise sufficient capital. Making matters worse, earnings came up short of plan owing to an extraordinary loss booked in anticipation of losses on the future disposal of overseas businesses. In order to regain a credit standing that would allow it to raise the capital need to get back on the growth track, in June 2013 the Company entered into a capital and business alliance with Daiwa House that made it a subsidiary of the Daiwa House group. After joining the Daiwa House group, the Company put together a medium-term business plan that would take it through FY3/16. During that plan, sales on a cumulative basis were slightly less than expected but operating profit, recurring profit, and net profit all finished ahead of plan. With its credit standing greatly improved, the Company was able to increase borrowings again, pushing the total for loans outstanding on its balance sheet at the end of FY3/16 to roughly ¥52.2bn versus its initial target of ¥22.0bn. This allowed it to increase its inventory of properties held for sale (the seeds for future growth) up to ¥67.1bn versus its initial target of only ¥34.0bn. The Company's medium-term business plan 2018 and its medium/long-term growth strategy reflect both past experience as detailed above and its assessment of the current operating environment.

Performance under medium-term business plan versus target

(¥mn)

	Business rehabilitation plan			Previous medium-term business plan		Medium-term business plan 2018		
	FY3/09 results	FY3/13 initial target	FY3/13 results	FY3/16 initial target	FY3/16 results	FY3/19 initial target	FY3/18 results	FY3/19 forecast
Sales	191,616	79,200	85,824	88,000	87,022	105,000	100,829	105,000
Operating profit	-18,207	6,200	2,562	4,000	3,480	5,000	4,869	*1 5,250
Net profit attributable to parent company shareholders	-88,088	5,500	-1,073	3,500	3,639		3,695	4,400
Inventories	168,044	34,400	20,044	34,000	67,101		73,497	
Borrowings	187,766	17,000	5,995	22,000	52,160		58,048	*2 60,000
Net assets	-45,183	19,800	13,109	18,000	19,470	29,000	25,824	

*1 Revised from ¥5,000mn to ¥5,250mn at time of FY3/18 result announcement

*2 Fisco estimate

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

Business environment and basic action plan under medium-term business plan 2018

2. Business environment and basic action plan

Among the many factors influencing the operating environment in Japan at this time are: 1) demographic changes including a growing proportion of the population accounted for by seniors and changes in the number of people per household; 2) a growing need to resolve problems related to vacant properties, reconstruction, and large-scale building repair mansions; 3) a growing secondary market for older homes and buildings that have been renovated; 4) a growing need for property management and inheritance-related planning services; 5) a growing need for energy-efficient and earthquake-resistance homes in response to heightened concerns about the environment and natural disasters; 6) growing awareness of safety and protection features as worries grow about the quality of workmanship and the potential impact of earthquakes; and 7) further growth in demand for lodging from the ongoing rise in inbound tourist traffic and the opening of Tokyo Olympics in 2020. The Company took all of these factors influencing the operating environment into consideration when creating its basic action plan aimed at strengthening its business base and pursuing its growth strategy.

The action plan by segment is as follows. At the Residential business, the action plan calls for 1) more new condominium development projects, increasing renovation of used properties and promoting renovation work, and promoting more after-sale services to create a broad service menu and become a one-stop service provider for housing-related services; 2) stepping up construction of housing aimed at the active senior market and expanding after-sale services for this market; and 3) working together with companies in the Daiwa House group on reconstruction and redevelopment projects. At the Solutions business, the plan calls for 1) creating a one-stop solutions service with a professional consulting group to serve the needs of business-use property owners; and 2) developing more investment properties and increasing inventories of older properties for renovation. 1) At the Construction business, the plan calls for growing existing businesses and expanding further into large-scale building repair mansions. 2) At the Overseas business, the plan calls for continuing to work together with the Daiwa House group on housing development projects in Australia. 3) In terms of new businesses, the plan calls for developing a new business to meet the growing demand for lodging by overseas travelers visiting Japan.

Based on the above expectations with respect to the operating environment and its basic action plan, the Company put together its medium-term business plan 2018 in 2016, targeting sales of ¥105.0bn and an operating profit of ¥5.0bn in FY3/19, and a net debt equity ratio of 1.5x at the end of FY3/19 (with a target for net interest-bearing debt of ¥43.0bn and net assets of ¥29.0bn). The above assessment of operating environment and the action plan under the 2018 medium-term business became the basis for the Company's medium/long-term strategy that was unveiled later with the aim of given investors a picture of the expected size of the business another three to five years in the future.

Medium/long-term strategy incorporates the medium-term business plan 2018

3. Medium/long-term strategy and image of business scale

The medium/long-term business strategy reflects the Company's corporate philosophy of "Next Value For The Customer – Create the next value requested by customer" and, as applied in practice, its CSV* vision statement "Next Good: Give the next answer for God Living" and "Good Society." The medium/long-term strategy serves as a guide to providing solutions to society problems through the products and services the Company offers and, as such, outlines the steps the Company plans to take to create more "Next Good" together with customer and society. The urban living environment, the Company's business domain and the seven characteristics of the operating environment discussed previously are targeted by the medium/long-term strategy, with expansion strategies created for each business according to whether it is considered a flow-type business, a stock type business, or a service business. In accordance with this, the Company was able to project the size of its business in the near future, seeing sales of ¥70.0bn at the Residential business, ¥70.0bn in sales at the Solutions business, and ¥15.0bn in sales at the Construction business and Overseas business for total sales of ¥155.0bn.

* CSV (Creating Shared Value): A differentiation strategy aimed at creating sustainable growth by using the strength of a company to address society problems; said to be an extension of CSR (Corporate Social Responsibility).

(1) Residential business

At its Residential business, the Company plans to offer a broad service menu split between new condominium development (a "flow") and renovation services (utilizing "stock"). It will also offer a wide range of supplemental services to create a one-stop service and increase the profitability. On the new condominium development front, with new developments generally on the decline the Company is looking to capture market share by focusing on locations for condominium and single-family home developments where convenience is a major selling point and further differentiating itself by creating high value-added homes with spatial designs that provide plenty of living space and are highly functional. On the new business front, the Company is looking offer property management and other services to meet the varied needs of the active seniors market. With the help of these initiatives, the Company is aiming to generate ¥50.0bn in annual sales from new condominium development in the near future.

In terms of renovated condominium, the Company will be buying older condominium properties and renovating them to give the interiors the same spatial designs used in new condominiums. The Company is also looking to expand its service that sets up retail agents with renovation construction with the help of its RENONAVI website. In addition increasing the Company's database of information on renovated condominiums on the market, its RENONAVI website provides an analysis of each individual property based on its proprietary housing diagnostic system. With this kind of recurring income-type business, the Company is looking to generate some ¥20.0bn. It is also considering building up its after-sale service menu, such as its *Sugoshikata Concierge* proposal-type support service.

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30-Jul.-2018

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Medium/long-term business strategy

As Japan's population ages we can expect to see a sharp increase in the number of healthy and active seniors. Unfortunately, when most people think about senior-oriented business they wrongly jump to the conclusion that this refers to nursing care and similar businesses, and very few think of businesses that are aimed healthy and active seniors. The Company is stepping into this gap and attempting to address the needs of the market represented by active seniors market by designing condominiums specifically for this market. The Company's GRAND COSMO series are new condominiums designed for active seniors, with features aimed specifically at reducing the burden of housework and physically-demanding tasks. However, unlike serviced units in retirement homes or assisted living facilities, GRAND COSMO condominiums maintain the value of a property in which the residents can live as they please. What distinguishes these condominiums from the average condominium are the various support services (provided by subsidiary Cosmos Life Support) that are readily available to residents to handle medical emergencies, earthquakes, etc., as well as services aimed at helping residents stay in good health and rest at ease. Going forward, the Company is looking to develop this type of active senior-oriented condominiums in government designated cities and cities with at least 400,000 residents, selecting locations within those cities that are convenient from the perspective of everyday living (shopping, hobbies, medical care, travels, etc.). In this venture the Company plans to work together with Daiwa House and fellow Daiwa House group member Fujita Corporation in redevelopment and rebuilding.

(2) Solutions business

The Solutions business is a one-stop solutions service provider with services to cover everything from the initial property purchase, to operations management, to sales. At the same time, the Company is also striving to strengthen synergies among the various business units under the Solutions segment and increase operational efficiency. Investment property development is a flow business, but the Company is not only diversifying its product offering in this area, it is also looking to increase its inventory of used investment properties that it can renovate, reinforce its brand in this market, and develop a new business featuring apartment hotels aimed at meeting the lodging needs of the growing number of foreign tourists visiting Japan. In the near future, the Company is looking for this business to generate annual sales of ¥40.0bn.

In terms of real estate subleasing, the Company is looking to extend its reach from residential properties to buildings, increase the number of unit properties and the square feet under management, and also increase operational efficiency. On the service side, at its real estate consulting business, the Company is working to expand its solutions business that draws on its extensive network, and increase the number of subscribers to its property diagnostic service. Through these efforts the Company is looking to generate sales of ¥30.0bn.

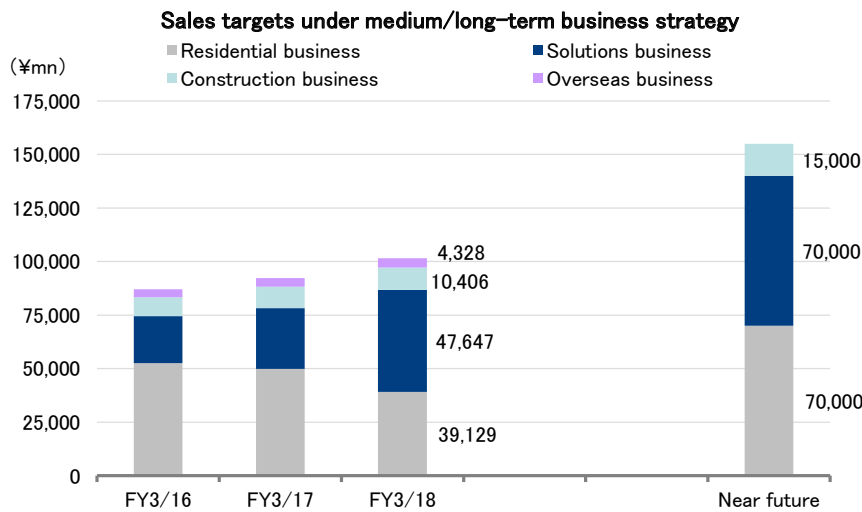
The Company has also moved into the development and management of apartment hotels, drawing upon its expertise in condominium development and management to create the new MIMARU chain of comfortable apartment hotels (complete with hotel management services) for investors. This represents the combination of both a flow business and a stock (recurring income) business, the flow part being the development and the stock part being the hotel management contract. The MIMARU hotels are distinguished by 1) their convenient locations in areas close to major terminal stations in Tokyo, Osaka, and Kyoto; 2) smart designs that evokes Japanese culture and relatively small size, with roughly 40 guest rooms with each room having an average size of 40 square meters; 3) space for bedroom and living & dining in all rooms, as well as a mini-kitchen, cooking utensils, and dining ware, and space enough to comfortably accommodate four or more people; and 4) usually inexpensive rooms charges in Japan of about ¥30,000 per night.

Medium/long-term business strategy

With rooms large enough to comfortably accommodate a party of three to five people, the cost of a night's stay per person comes down to a level that few hotels can match in Japan, so MIMARU apartment hotels will not have much competition. The demand for this kind of hotel is expected to be large because most of the overseas tourists that are expected to come to Japan are coming from other Asian countries and are traveling as a family. One might say that Airbnb and other Vacation Rental operators represent competition, but not only are the types of travelers using Vacation Rental and their motivations quite different, Vacation Rental accommodations cannot come close to the MIMARU apartment hotels when it comes to offering foreign travelers safety, peace of mind, and convenience. And, because MIMARU apartment hotels are a new style of accommodations that promises to appeal to a growing target market, there is an additional advantage of being one of the early movers in the market. Revenues and earnings from MIMARU apartment hotels will come first from the sale after development and then from the hotel management contract. The popularity of this type of hotel is expected to relatively high sales prices. The Company is looking to have 1,500 rooms developed and under management by 2020.

(3) Construction business/Overseas business

At the Construction business, the Company is looking to expand its service menu for residential properties and office buildings, and increase orders for both new construction and repair work on investment properties. At its Overseas business, the Company plans to actively work together with the Daiwa House group in Australia and New Zealand, developing condominiums in Sydney and also participating in a serviced apartment management business. The Company is looking to generate annual sales of ¥15.0bn from the Construction business and the Overseas business in the near future.



Source: Prepared by FISCO from the Company's website, etc.

Results trends

Strong growth leaves FY3/18 results ahead of initial forecast

1. FY3/18 results

For FY3/18, the Company reported sales of ¥100,829mn (+9.2% YoY), operating profit of ¥4,869mn (+19.2%), recurring profit of 4,367mn (+25.4%), and net profit attributable to parent company shareholders of ¥3,695mn (+21.9%). This was the fourth consecutive year that Cosmos Initia reported higher sales and higher earnings and the first time in seven fiscal years that sales topped the ¥100.0bn mark. Compared with the Company's initial forecast, sales came in ¥2,829mn ahead of plan. Thanks to the strong top-line growth and good cost control at the SG&A expense, operating profit came in ¥469mn ahead of plan.

FY3/18 results

	FY3/17	% of sales	FY3/18	% of sales	% change
Sales	92,366	100.0	100,829	100.0	9.2
Gross profit	18,516	20.0	19,487	19.3	5.2
SG&A expense	14,432	15.6	14,618	14.5	1.3
Operating profit	4,084	4.4	4,869	4.8	19.2
Recurring profit	3,482	3.8	4,367	4.3	25.4
Net profit attributable to parent company shareholders	3,030	3.3	3,695	3.7	21.9

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

The Residential business reported sales of ¥39,129mn (-21.6% YoY) and an operating profit of ¥1,142mn (-46.3%), in line with the Company's initial forecast. The sharp decline in sales and earnings was attributed to the drop in sales of new condominium units (down 186 units to 558), a decline in sales of new detached housing (down 13 to 55), and a decline in the sale of pre-owned condominiums that had been purchased for resale (down 103 units to 214). The drop in sales was attributed in part to the Company's insistence on good locations for development projects; together with the rising cost of land at those locations, this limited the number of sites meeting the Company's standards for development projects.

The Solutions business reported sales of ¥47,671mn (+67.3%) and an operating profit of ¥4,862mn (+73.7%). The strong growth in sales and earnings is attributable to high occupancy rates at its condominium subleasing business (where the average vacancy rate declined 0.4ppts to 2.5%), and increases in the number of investment properties sold and the 1.3ppt increase in gross profit margin on those sales. The increase in sales of investment properties reflects the successful preparations made under its previous medium-term business plan to meet the growing demand for investment properties.

The Construction business reported sales of ¥10,406mn (-5.0% YoY) and an operating profit of ¥71mn (-80.3%) as orders for office renovation work declined from elevated levels the previous year and gross profit margin was squeezed. The Overseas business reported sales of ¥4,328mn (+7.3%) and an operating profit of ¥367mn (+20.0%) thanks to a good year at the resort hotel management business in Australia.

Results trends

In keeping with its growth strategy, the Company increased its holdings of properties in all areas, adding to its inventory of investment properties, new condominiums, and the apartment hotels under its new business. And, because it did not depend on borrowing, it was still able to improve the ratio of net debt to equity. The strong demand for investment properties suggests there is not a problem at this time, and the consensus view within the company sees no reason for concern about the operating environment through 2020. Incidentally, the medium/long-term business strategy envisages both the Residential and Solutions businesses being in the scale of ¥70bn, but there is a clear division between the two and the hope is that the Residential business can come back.

Segment sales and operating profit

						(¥mn, %)
Sales (before adjustments)	FY3/17	% of sales	FY3/18	% of sales	% change	
Residential business	49,884	53.5	39,129	38.5	-21.6	
Solutions business	28,502	30.5	47,671	47.0	67.3	
Construction business	10,953	11.7	10,406	10.2	-5.0	
Overseas business	4,032	4.3	4,328	4.3	7.3	
Operating profit (before adjustments)	FY3/17	Profit margin	FY3/18	Profit margin	% change	
Residential business	2,128	4.3	1,142	2.9	-46.3	
Solutions business	2,799	9.8	4,862	10.2	73.7	
Construction business	360	3.3	71	0.7	-80.3	
Overseas business	305	7.6	367	8.5	20.0	

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

FY3/19 forecast prompts upward revision of targets under medium-term business plan

2. FY3/19 forecast

For FY3/19, the Company is forecasting in sales of ¥105,000mn (+4.1% YoY), an operating profit of ¥5,250mn (+7.8%), recurring profit of ¥4,800mn (+9.9%), and net profit attributable to parent company shareholders of ¥4,400mn (+19.1%). The gross profit margin is expected to come down following the Company's pullout from the overseas resort hotel management business, but SG&A expenses are also expected to come down and this together with the growth in sales at the high-margin Solutions business is expected push up the operating profit margin for the Company as a whole and bring operating profit in above the target initially set under the 2018 medium-term business plan.

FY3/19 forecast

						(¥mn, %)
	FY3/18	% of sales	FY3/19 E	% of sales	% change	
Sales	100,829	100.0	105,000	100.0	4.1	
Gross profit margin	19,487	19.3	18,330	17.5	-5.9	
SG&A expenses	14,618	14.5	13,080	12.5	-10.5	
Operating profit	4,869	4.8	5,250	5.0	7.8	
Recurring profit	4,367	4.3	4,800	4.6	9.9	
Net profit attributable to parent company shareholders	3,695	3.7	4,400	4.2	19.1	

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

Results trends

For the Residential business, the Company is forecasting sales of ¥38,000mn (-2.9% YoY) and operating profit of ¥1,250mn (+9.5%). With regard to the operating environment, the Company is looking for new condominium sales to remain in a downtrend but sees sales of new detached housing doubling and sales of pre-owned condominium turning up as well. Near term, the Company appears to be content with just maintaining overall sales at the Residential business at a certain level. For the Solutions business, the Company is forecasting sales of ¥55,100mn (+15.6%) and operating profit of ¥5,560mn (+14.4%) based on its outlook for steady growth in revenues from condominium subleasing and an increase in both the number of investment properties sold and the gross profit margin on those sales. The new apartment hotel development and management business is expected to get into full swing this year, though hotel opening costs will weigh on earnings initially. For the Construction business, the Company is forecasting sales of ¥11,600mn (+11.5%) and a 4.2-fold increase in operating profit to ¥300mn, based on its outlook for improvements in both its order flow and margins. At the Overseas business, following its exit from the resort hotel management business, the Company is forecasting sales of ¥1,100mn (-74.6%) and an operating profit of ¥70mn (-80.9%).

Breakdown of FY3/18 sales and operating profit forecast by segment

(¥mn, %)					
Sales (before adjustments)	FY3/18	% of sales	FY3/19 E	% of sales	% change
Residential business	39,129	38.5	38,000	35.9	-2.9
Solutions business	47,671	47.0	55,100	52.1	15.6
Construction business	10,406	10.2	11,600	11.0	11.5
Overseas business	4,328	4.3	1,100	1.0	-74.6

Operating profit (before adjustments)	FY3/18	Margin	FY3/19 E	Margin	% change
Residential business	1,142	2.9	1,250	3.3	9.5
Solutions business	4,862	10.2	5,560	10.1	14.4
Construction business	71	0.7	300	2.6	322.5
Overseas business	367	8.5	70	6.4	-80.9

Note: Does not include the Other business.

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

Company keeping pace with medium-term business plan as never before

3. Progress versus medium-term business plan 2018

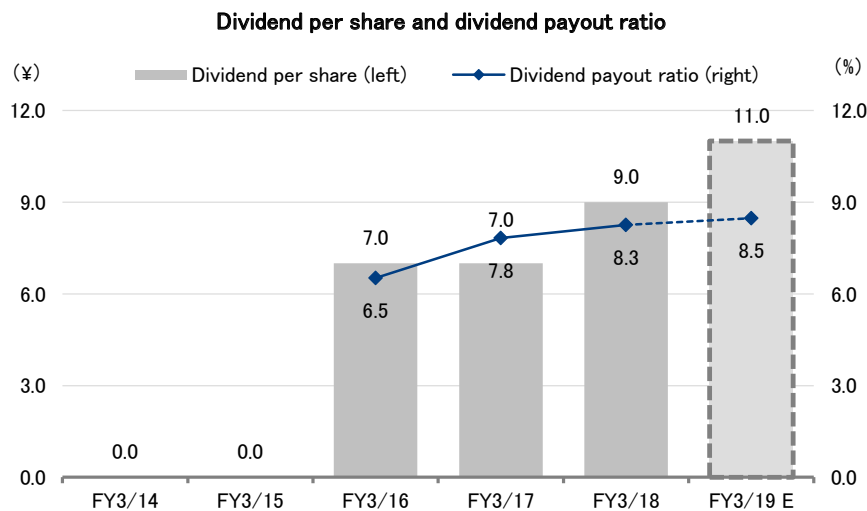
Under its medium-term business plan 2018, the Company initially set a target for FY3/19 sales of ¥105,000mn and operating profit of ¥5,000mn. It also targeted a net debt-to-equity ratio of 1.5x at the end of FY3/19, with a target for net interest-bearing debt of ¥43,000mn and net assets of ¥29,000mn. Results in FY3/18, saw sales hit ¥100,829mn and operating profit ¥4,869mn. Net interest-bearing debt rose to ¥42,706mn and net assets of ¥25,824mn, bringing the net debt-to-equity ratio to 1.7x. This put the Company firmly on track to meet the targets under the medium-term business plan. Indeed, the growth in operating profit was such that the Company raised its operating profit target for FY3/19 to ¥5,250mn.

Looking now at the interim progress under the medium-term business plan 2018, at the Residential business, we find the Company following up the 2016 completion of the GRAND COSMO Musashiurawa condominium complex for active seniors with 2 to 4 additional development plans that represent in cities in regional areas. This is the long-awaited start of a nationwide rollout. The Company has already completed tentative planning for redevelopment projects and also working to respond to the three other brand lines for renovated condominiums. Of these, the INITIA LINE particular has won praise from customers for being easy to picture because renovation gives it a look on par with newly built INITIA condominiums and the and also created synergies with its new condominium construction operations, leading to efficiency gains in both construction and design. The Company says it started getting requests for renovation work from customers last fiscal year.

At the Solutions business, the Company is making rapid progress rolling out its apartment hotel development and management business. Since the February 2018 opening of its first hotel, the 40-room MIMARU Tokyo Ueno NORTH, it has opened three more for a combined total of four hotels and 154 guest rooms under management as of the end of April 2018. The Company is looking to have a total 1,500 rooms under management in 2020, a figure that looks achievable given the total of 931 rooms in the 18 hotels that are either already in operation or under development. For the first three months of operations at its first hotel, the Company reported an occupancy rate of 72% for February, 83% for March, and 89% for April. The average price per room per night during this timeframe was around ¥30,000; the average stay was 2.5–2.6 nights, with an average of 4.2 people per room. Just under 40% of guests were said to be from Taiwan and roughly 10% from Hong Kong; the rest came from a range of countries including Thailand, Japan, the US, and Australia. With these results being closely in line with expectations, the Company is planning to have a total of seven or eight hotels in operation by the end of FY3/19, opening up the possibility that its hotel management business will be in the black as early as FY3/20.

Shareholder return policy

The Company places the highest priority on increasing its enterprise value and distributing profits to shareholders and, in keeping with this, will strive to maintain a stable dividend that both shares profits with shareholders and assures the internal reserves needed to sustain growth. Although its articles of incorporation allow the board of directors to approve the payment of an interim dividend, the Company's dividend policy at this time calls for paying a dividend once a year at the end of the fiscal year. Based on its earnings forecast for FY3/19, the Company expects to pay a period-end dividend of ¥11 per share, an increase of ¥2 over FY2/18. The Company does not have a special benefit program for shareholders.



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

Information security

In the course of its business the Company comes into the possession of personal information of buyers and prospective buyers of new condominiums and detached housing and, as a result, is subject to the Protection of Personal Information Act. In keeping with the Act, the Company has taken all appropriate steps to guard the personnel information in its possession, including establishing a privacy policy and procedures and rules for the handling of personal information. It is also working to fortify its information management structure across the company as a whole, including employee training and the installation of secure entry/exit systems for all offices.



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