

COMPANY RESEARCH AND ANALYSIS REPORT

AXXZIA Inc.

4936

Tokyo Stock Exchange Growth Market

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■ Index

■ Summary	01
1. Summary of the FY07/22 Q3 cumulative results	01
2. FY07/22 results outlook	01
3. Growth strategy and topics	02
■ Company profile	03
■ Market environment	03
■ Business description	04
1. Main brands and products	04
2. Percentages of sales by channel and their features	05
3. Business model	06
4. Company's strengths	07
■ Results trends	07
1. Summary of the FY07/22 Q3 cumulative results	07
2. Outlook for FY07/22	08
■ Growth strategy and topics	10
1. The effects of the Shanghai lockdown and the measures taken in response	10
2. The White Drink is a candidate to be the third hero product	10
■ Shareholder return policy	11

Summary

In the FY07/22 Q3 cumulative results, sales and profits increased despite the impact of the Shanghai lockdown

AXXZIA Inc. <4936> (hereafter, also “the Company”) is a cosmetics company with high growth potential that plans and manufactures made-in-Japan cosmetics and supplements in the high and medium price ranges, and sells them through e-commerce (hereafter, EC), mainly on the Chinese market. Its main brands are AXXZIA and AGtheory, and the Company has succeeded in making hero products (hit products) of both Essence Sheet, an eye-care product, and AG Drink, a beauty supplement.

1. Summary of the FY07/22 Q3 cumulative results

In the FY07/22 Q3 cumulative results, net sales were ¥5,630mn (up 38.8% compared to the same period in the previous fiscal year, hereafter, year-on-year (YoY)) and operating income was ¥1,097mn (up 10.7%). Due to the impact of the Shanghai lockdown (a city lockdown) implemented on March 28, 2022, the Q3 standalone results were less than forecast, but the Q3 cumulative results were higher than forecast, net sales by 9.1%, and operating income by 7.5%. Due to the impact of the Shanghai lockdown, at the Shanghai subsidiary (XiaoziCosmetic (Shanghai) Inc.), sales to beauty salons decreased, and therefore net sales in April 2022 were significantly less than forecast, by 3.5% (sales recovered to a certain extent in May). For the Company on a standalone basis, cancellations increased on Tmall Global and RED compared to a typical month because of the impact of the suspension of logistics in Shanghai, so sales were below forecast, at 97.1% of the forecast. But sales were strong at the TikTok Chinese main store Douyin (hereafter, TikTok), which was opened as a flagship store in FY07/22. In addition, sales grew on major platforms like Taobao and Tmall Global, and also, the Company succeeded with horizontal business development to platforms (launched stores on TikTok and JD.com (hereafter, JD.com)), which covered for the part that was less than forecast in April. In profits, the Company actively conducted upfront investment in advertising to improve the brands’ name recognition and to expand the sales base, so SG&A expenses increased 68.1%, but there was a rise in gross profit due to the higher sales and operating income increased 10.7%.

2. FY07/22 results outlook

For the FY07/22 consolidated results, the Company considers the outlook for net sales and other results to be uncertain, including due to the impact of the Shanghai lockdown. But the results of 618, which is one of the 3 major EC sales events in China, announced in June 2022 were significantly higher than in the previous year and were also higher than the Company’s initial forecasts, and therefore in July of the same year, it upwardly revised its results forecasts. The upwardly revised consolidated results forecasts are net sales of ¥8,000mn (up 38.2% YoY) and operating income of ¥1,500mn (up 8.5%). Net sales are expected to grow mainly in the Chinese market. The Company is aiming to accumulate sales by deepening its business on the existing EC platforms and also by horizontal business development to TikTok and JD.com. For operating income, its policy is to continue to conduct upfront investment in advertising activities in order to improve the brands’ name recognition and to expand the sales base in the Chinese and Japanese markets, so SG&A expenses will increase. But it is still aiming for higher profits from the effects of the higher sales. The progress rates for the full fiscal year forecasts are slightly higher than in the same period in the previous fiscal year, at 70.4% for net sales (70.1% in the same period in the previous fiscal year) and 73.1% for operating income (71.6%). The Shanghai subsidiary was particularly affected by the Shanghai lockdown implemented on March 28, 2022, but during the current Q4, the effects of the measures in response to it are starting to appear, and while the impact of the lockdown will remain, results are expected to improve. So it can be said to be highly likely that the Company’s full fiscal year results will achieve the upwardly revised forecasts.

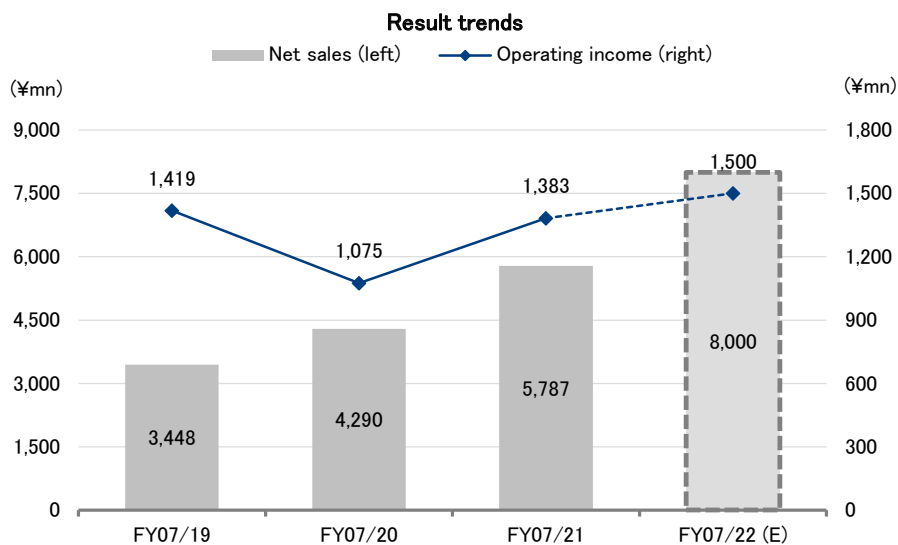
Summary

3. Growth strategy and topics

The Company is strengthening the development of The White Drink as a candidate to become the third hero product after AG Drink and Essence Sheet. Up to the present time, it has positioned White Aminos beauty supplements and sunscreen cosmetics as up-and-coming products and targeted them becoming the third major brand, and then in February 2022, it renewed White Aminos and market launched Venus Recipe The White Drink. It has been well received by customers and in the FY07/22 Q3 standalone results, The White Drink's net sales were ¥120mn, while net sales of whitening-appeal brands as a whole were ¥352mn (¥204mn in the same period in the previous fiscal year) and have become the driver of the rapid growth in this field. The Company is succeeding in increasing sales, such as by creating brand series based on hero products and expanding from beauty drinks to cosmetics, so we shall be paying attention to developments in the future.

Key Points

- In China's EC channel, has succeeded in increasing sales by appropriately using several of the main platforms. In FY07/22, results were strong at the newly opened TikTok flagship store
- In the FY07/22 Q3 cumulative results, sales and profits increased despite the impact of the Shanghai lockdown. Continues to actively invest in advertising and to develop horizontally to channels
- Upwardly revised the FY07/22 results forecasts, including because the results of 618, one of China's three major EC sales events, were significantly higher than in the previous year
- The White Drink, which is a candidate to become the third hero product, has made a strong start



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

■ Company profile

A growth company that develops and manufactures cosmetics and supplement products in the high and medium price ranges and sells them via EC in China

The Company is a cosmetics company with high growth potential that plans and manufactures made-in-Japan cosmetics and supplements in the high and medium price ranges and sells them through EC, mainly on the Chinese market. Its name of AXXZIA is derived from “Women’s XX chromosome,” a symbol of beauty, and the idea of sending the “Beauty of “(ASIA→AZIA)”” from Japan to the world. It is aiming to be a comprehensive beauty solution company that creates beauty and that can provide proposals tailored to customers’ wishes and realities.

Since its foundation, the Company has been led by President and Representative Director Dan Taku. After graduating from China’s prestigious Xiamen University, he completed a post-graduate degree at the University of the Ryukyus. Then, after working as a systems engineer in a listed company, he launched a business in 2003. Subsequently, he accumulated experience including in beauty salon management and imports and exports of beauty devices, and in 2011, he established Orientina Cosme Co., Ltd. for the development and manufacture of cosmetics for beauty facilities (hereafter, salons), and then in 2012, the company name was changed to AXXZIA Inc. A turning point occurred in 2016. The sales launches of the AG Drink beauty supplement and the Essence Sheet eye-care product for B-to-C coincided with the growth of China’s EC market and the Company succeeded in making them hero products. Subsequently, it skillfully conducted brand management, centered on the hero products, and grew to be a company with a lineup of 7 brands and more than 90 items. Also, in 2020 the Company won Rising Enterprise Award 2020 from Tmall, which is China’s largest EC platform. In February 2021 in the 10th year since its foundation, it was listed on the Tokyo Stock Exchange (TSE) Mothers market, and then in April 2022 following the TSE’s reorganization of market categories, its listing was transferred to the Growth market. In April of the same year, it acquired 100% of the shares and made a consolidated subsidiary of Huit laboratories, Inc. At the end of July 2021, the Group had a total of 115 employees, of whom, 73 employees (63.5%) were women. The ratio of women in managerial positions is 48.8% and the ratio of employees who are foreigners is 46.1%, and the Company has vitality through implementing diversity.

■ Market environment

China’s cosmetics market is growing greatly against the backdrop of the improved income level and the increase in the cosmetics population

The scale of the skincare market, which constitutes a large part of China’s cosmetics market that the Company targets, is growing greatly against the backdrop of the improved income level in China due to economic growth and the increase in its cosmetics population. According to the Company, the scale of China’s skincare market was ¥4,178.9bn in 2020 and the forecast five-year average growth rate up to 2025 is 13.3%.

Market environment

In China's cosmetics market, the Company's products are known as made-in-Japan brands from a Japanese cosmetics company. The foundation of this category, which constitutes approximately one quarter of China's cosmetics market, was built over many years by companies such as Shiseido <4911>, Kosé <4922>, and FANCL<4921>, and in particular the functionality of Japanese products is highly evaluated in the skincare field and other fields. The Company competes with groups ranked 4th and lower, such as POLA ORBIS HOLDINGS <4927>. In the Chinese market, brands from Japanese and Western companies tend to be in the medium and high price ranges, brands from South Korean companies in the medium price range, and brands from Chinese companies in the low price range, and their respective positioning is different. Among them, in the medium and high price range categories, there are many companies that rely on retailers, particularly department stores, but the Company is developing its business centered on EC, thereby differentiating itself. The reasons why the Company is focusing on China's EC include that EC is expanding in the distribution channels for China's skincare market, and unlike in Japan where the drugstore is the main sales channel, EC is commonly used in China. Moreover, in the composition ratios of distribution channels for China's skincare market in 2020, EC constituted 40.6% (up from 24.1% in 2016), from which it can be seen that EC is growing significantly.

■ Business description

Is succeeding in increasing sales by properly using several of the main platforms in China's EC channel

1. Main brands and products

AXXZIA is one of the main brands for retailers, mainly of eye products, and the Company has succeeded in making Essence Sheet a hero product. It is a beauty serum that blends multiple beauty ingredients needed for the eyes, and is attached to the skin close to the eyes to provide the area with intensive care. As a result of becoming a hero product in the Chinese market, Essence Sheet's FY07/22 Q3 cumulative net sales were ¥2,510mn (44.6% of Company-wide net sales).

AGtheory, which is the second major brand for retailers, blends cosmetics with AG Drink as the core ingredient, and the Company succeeded in making it a hero product. It then created the AGtheory cosmetics brand series by combining the AG Drink (hero product) with cosmetics based on the same concept to target the existing loyal users of AG Drink. Incidentally, the features of AG Drink, which pursues "anti-saccharification" and has become a hero product, include that it stably ships 10,000 units a month and has a high ARPU (average revenue per user), and its FY07/22 Q3 cumulative net sales were ¥1,852mn (32.9% of Company-wide net sales). The percentage of FY07/22 Q3 cumulative net sales provided by the total sales of the 2 brands of AXXZIA and AGtheory (including AG Drink) was 77.5%.

In addition, the Company has positioned the White Aminos beauty supplement and sunscreens cosmetics to be up-and-coming products and is aiming for them to become the third main brand. The above brands are sold in the Chinese and Japanese markets in the medium and high price ranges (average sales price, ¥5,000 and higher) as B-to-C brands. In contrast to this, "Le Ciel de L'aube," "Aither" and "THE B" are brands sold exclusively to salons (professional field). The brands sold exclusively to salons have been one of the Company's strengths and specialist fields since its foundation, and it sells them in the high price range (average unit price, ¥10,000 and higher).

Business description

The main product lineup



Source: The Company's financial results briefing materials

2. Percentages of sales by channel and their features

The driving force behind the Company's growth is the success of the Chinese market, and in particular, the growth of EC in China. This is clear from the percentages of net sales by region and by channel in the FY07/22 Q3 cumulative results, in which China's EC provided 75.6% (¥4,253mn). Breaking down China's EC, there are sales of the flagship store on Taobao, which is China's largest marketplace-type (C-to-C) EC platform operated by the Alibaba Group (percentage of FY07/22 Q3 cumulative China EC sales, 44.8%) and sales of the flagship store on Tmall Global, which is a B-to-C cross-border EC specialty mall operated by the Alibaba Group (30.5%), and both have high growth potential. RED includes review and comments, the majority of which are by active female users (it is China's version of Instagram) and influencer marketing sales are active on it (8.9%). In addition to these, the video platform TikTok and the EC platform JD.com, on which the Company opened flagship stores in FY07/22, are growing remarkably. Of them, TikTok, which is a SNS specializing in video, is attracting a lot of attention as an influential sales channel (live commerce and interest EC) following its addition of EC functions. It provides 15.7% of total net sales and its presence is increasing as the No.3 platform.

Summary of China's EC platforms on which the Company has opened stores

EC platform	Features	No. of active users	The Company's net sales (¥mn)	% of net sales	YoY
Taobao, etc.	China's largest marketplace-type (C-to-C) platform operated by the Alibaba Group. Individuals can join as sellers and there are many products at reasonable prices.	740mn people	1,905	44.8%	23.5%
Tmall Global	A B-to-C cross-border EC specialist mall operated by the Alibaba Group. Can purchase overseas products while being within China. Japanese products are very popular. It is limited to sales from companies to individuals and transactions are highly reliable.	(Can approach approximately 300 million members of the middle class)	1,299	30.5%	32.2%
RED	Attracted attention as an app on which users can post photographs and comments (China's Instagram). Subsequently added EC functions similar to Amazon. Products are actively sold on it that utilize influencers, mainly skincare, makeup, fashion, and child-raising products.	85mn people (The majority of who are women)	380	8.9%	26.0%
TikTok	An SNS specializing in video operated by ByteDance to which EC functions have been added by DouYin E-commerce. It uses video and live distribution to stimulate the consumers' potential desires for purchases and proposes products that they may want to buy (interest EC), and sales are growing.	Approximately 400mn people	668	15.7%	-
China's EC total			4,253	100.0%	50.4%

Note: The Company's net sales are the FY07/22 Q3 cumulative results. TikTok had no results in the same period in the previous year.

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

Business description

Among the percentages of net sales by region and by channel, the next highest is sales for salons in China at 15.6% (¥875mn). Recently these sales were impacted by the Shanghai lockdown, but there are more than 600 beauty-salon customers and sales are steadily growing. On the other hand, the Japanese market has been impacted by the novel coronavirus pandemic (hereafter, COVID-19) and in particular retail sales have declined, and its percentage of total net sales was 5.5% (¥312mn). In order to improve awareness of its brands in Japan, the Company appointed Taiki Sato and Yusei Yagi of FANTASTICS from EXILE TRIBE as ambassadors of THE B MAISON, a skincare product exclusively sold in salons, and it is working to further increase awareness, mainly through SNS. Other than these, although it has a track record of sales in countries such as Canada, Germany, and Australia, it is currently refraining from active business development, including because of the travel restrictions due to COVID-19.

3. Business model

The Company's business model is optimized for the Chinese market. It is a process divided into four stages: (1) product development, (2) manufacturing, (3) sales, and (4) after-sales support, and each stage of the process has its own features.

(1) Product development

The Company can obtain consumer needs in a timely manner, such as through its strategic collaboration with Tmall and through test marketing with Taobao and others (via KOL (key opinion leaders) and local salons). From among these needs, the Company plans concepts for up to 200 items a year and mass produces around 20 items while repeatedly creating prototypes and conducting quality checks. In the EC channel, evaluations in the market can be confirmed quickly and the timing of reforming or discontinuing a product is also fast. This kind of high-paced release cycle can be said to be factor behind the Company being able to continuously create and develop hero products. Also, another of the Company's strengths is that it conducts in-house all of the functions necessary for cosmetics development, such as formulation development, container development, license confirmation and pharmaceutical affairs. Since making a subsidiary of Huit laboratories, it is able to produce small-lot and multi-variety prototypes, and its policy is to aim to market launch products with a sense of speed.

(2) Manufacture

The Company prioritizes made-in-Japan brands that are highly supported in China, outsources manufacturing to Japanese companies, and thoroughly applies quality-control standards at the same high level as production at its own plants. On the other hand, by making Huit laboratories a subsidiary, it has moved in-house one part of the manufacturing, and as a result it has acquired manufacturing expertise and it is also expected to reduce costs.

(3) Sales

The Company is progressing in parallel online and offline (mainly high-priced items for salons) sales, which contributes to maintaining the brands. For sales channels and sales promotions, it is accumulating expertise in promotions for both the top-down type, centered on Tmall, and the bottom-up type, which mainly utilizes Taobao and RED.

(4) After-sales support

The Company's enhanced customer services have been highly evaluated for each channel. The Chinese market requires that measures be conducted against counterfeit products, diversion and unreasonably low-priced products, but in terms of the Company's initiatives to maintain its brands, it attaches a QR-code security label to all products and numbers them so that buyers can confirm that the product is genuine through numbering, and it has in place a system in which it can respond immediately to a problem at the time of distribution.

Business description

4. Company's strengths

The Company strengths include that it targets the Chinese market and develops products that incorporate the preferences of Chinese people and can sell even medium and high price range products via EC, and that based on these characteristics of China, it utilizes all of the channels in an integrated manner for sales-promotion support and sales. As the Company specializes in China, it can be said to have built competitive advantages over other Japanese companies. In addition, it is utilizing its strengths in relation to China's unique approval system. The Chinese market has its own unique approval system, including requiring approval from NMPA (National Medical Products Administration, China's national food and pharmaceutical supervision and management bureau. Equivalent to PMA approval by the FDA in the United States), and as a result, it can be said that the barriers to enter the Chinese market are high. In response to this, the Company designs products that prioritize ingredients and formulations that the NMPA will approve. As a result, among its products developed for China, 82% have been registered by the NMPA (as of the end of April 2022), and the approval rate in the last 2 years has been 100% (generally, it is 20% to 30%) and its average application period is 3 months (generally, it is 6 months), and it is able to smoothly acquire approvals. Products not approved by the NMPA can still be sold on the Chinese market, but restrictions are placed on advertising for them, so EC stores find it difficult to handle these products.

Results trends

In the FY07/22 Q3 cumulative results, sales and profits increased despite the impact of the Shanghai lockdown. Continued to actively invest in advertising and to horizontally develop channels

1. Summary of the FY07/22 Q3 cumulative results

In the FY07/22 Q3 cumulative results, net sales were ¥5,630mn (up 38.8% YoY), operating income was ¥1,097mn (up 10.7%), ordinary income was ¥1,177mn (up 19.7%), and profit attributable to owners of parent was ¥747mn (up 20.4%). Due to the impact of the Shanghai lockdown implemented on March 28, 2022, the Q3 standalone results were less than forecast (net sales at 96.4%, operating income at 70.5%, and ordinary income at 91.9%). But the Q3 cumulative results were higher than forecast, net sales by 9.1%, operating income by 7.5%, and ordinary income by 19.4%.

FY07/22 Q3 cumulative consolidated results

(Unit: ¥mn)

	9M FY07/21		9M FY07/22			Change		Progress rate
	Results	Ratio to net sales	Forecast	Results	Ratio to net sales	Amount	Ratio	
Net sales	4,057	100.0%	5,162	5,630	100.0%	1,572	38.8%	109.1%
Gross profit	2,843	70.1%	-	4,211	74.8%	1,367	48.1%	-
SG&A expenses	1,852	45.7%	-	3,114	55.3%	1,261	68.1%	-
Operating income	990	24.4%	1,020	1,097	19.5%	106	10.7%	107.5%
Ordinary income	984	24.3%	986	1,177	20.9%	193	19.7%	119.4%
Profit attributable to owners of parent	621	15.3%	642	747	13.3%	126	20.4%	116.4%

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

Results trends

In the overseas cosmetics market, conditions in the future continue to be unclear, including due to the impact of COVID-19. In the Chinese market, logistics were suspended because of the lockdown due to COVID-19, which impacted deliveries and imports and exports of products. The greatest impact was felt by the Shanghai subsidiary, which conducts sales to beauty salons and retailers, and because of the decline in sales to beauty salons, a real-world channel, net sales in April 2022 were significantly below the forecast, by 3.5% (they recovered to a certain extent in May). On a standalone basis, the Company's net sales were below forecast at 97.1%, as on Tmall Global and RED, cancellations increased compared to a typical month because of the suspension of logistics in Shanghai. However, sales were strong at the TikTok flagship store opened in FY07/22. The Q3 cumulative results for China's EC were also strong, apart from in April, and maintained a high growth rate of 50.4% YoY. Sales grew on the major platforms like Taobao and Tmall Global, and in addition the Company succeeded with horizontal business development to platforms (launched stores on TikTok and JD.com), which covered for the part that sales were below forecast in April. In addition, net sales during the period in which 3.8*, which is China's largest EC event, were held, increased 108% compared to the same period in the previous year. By product, sales were strong not only of the main brands, of AXXZIA's Essence Sheet and AGtheory's AG Drink, but also of The White Drink, a renewed version of White Aminos beauty supplement, which contributed to the results.

* One of China's three major EC sales events. It is an EC sales event of women-related products held on March 8 to coincide with International Women's Day. China's other major EC sales events are W11, China's largest EC sales event, held on November 11, which is when China celebrates Singles' Day (the Company's net sales during the period in which the event was held in November 2021 increased 57% YoY), and 618, which is an EC sales event held every year close to June 18 by the Chinese EC site JD.com. It seems that in China's three major EC sales events, the extent of the Company's discounts are small compared to those of other companies.

In profits, the Company actively conducted upfront investment in advertising to improve the brands' name recognition and to expand the sales bases, and as a result, the Q3 cumulative advertising expenses ratio was 19.1%, which was basically in line with the initial forecast of 20% (13.7% in the previous period). Also, payment fees (EC platform usage fees, etc.) increased because TikTok sales increased significantly higher than forecast. As a result of the above, SG&A expenses increased 68.1% YoY, but this was exceeded by the rise in gross profit due to the higher sales, so operating income increased 10.7%.

The results of 618, which is one of China's three major EC sales events, were also significantly higher than in the previous year, so the FY07/22 results forecasts have been upwardly revised

2. Outlook for FY07/22

For the FY07/22 consolidated results, the Company considered that the outlook for net sales and other results was unclear, including due to the impact of the Shanghai lockdown. But when it became apparent that the results of 618, which is one of China's three major EC sales events held in June 2022, were significantly higher than in the previous year and that its results would be higher than the initial forecasts, it upwardly revised its results forecasts in July of the same year. The upwardly revised consolidated results forecasts are net sales of ¥8,000mn (up 38.2% YoY), operating income of ¥1,500mn (up 8.5%) from a detailed forecast of the effects of the increase in net sales and SG&A expenses, ordinary income of ¥1,600mn (up 16.7%) due to the revised outlook for foreign exchange profit/loss, and profit attributable to owners of parent of ¥1,050mn (up 20.9%) following the revision to the estimate of tax expenses.

Results trends

FY07/22 consolidated results forecasts

(Unit: ¥mn)

	FY07/21		FY07/22			Change		Q3 progress rate
	Results	Composition ratio	Initial forecast	Revised forecast	Composition ratio	Amount	Ratio	
Net sales	5,787	100.0%	7,117	8,000	100.0%	2,212	38.2%	70.4%
Operating income	1,383	23.9%	1,466	1,500	18.8%	116	8.5%	73.1%
Ordinary income	1,370	23.7%	1,424	1,600	20.0%	229	16.7%	73.6%
Profit attributable to owners of parent	868	15.0%	930	1,050	13.1%	181	20.9%	71.2%

Note: the FY07/22 revised forecasts are those announced on July 14, 2022. Also, the composition ratios, change, and progress rates are the values in relation to the revised forecasts.

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

Net sales are expected to grow mainly in the Chinese market. The Company is aiming to accumulate sales by deepening its business on the existing EC platforms and also by horizontal business development to TikTok and JD.com. For operating income, its policy is to continue to conduct upfront investment in advertising activities in order to improve the brands' name recognition and to expand the sales base in the Chinese and Japanese markets, so SG&A expenses will increase. But it is still aiming for higher profits from the effects of the higher sales.

The progress rates for the full fiscal year forecasts are slightly higher than in the same period in the previous fiscal year, at 70.4% for net sales (70.1% in the same period in the previous fiscal year) and 73.1% for operating income (71.6%). The Shanghai subsidiary was particularly affected by the Shanghai lockdown implemented on March 28, 2022, but during the current Q4, the effects of the measures in response to it are starting to appear, and while the impact of the lockdown will remain, results are expected to improve. Recently, as previously explained the achievements of the 618 event held from May 24 to June 20, 2022, were announced, and the GMV (Gross Merchandise Volume) of the flagship stores including Tmall Global and RED, increased approximately 86% YoY. The contribution of the results of Huit laboratories, which was made a subsidiary in April 2022, is forecast to be net sales of around ¥150mn and operating income of about ¥3mn. At FISCO, we think that although there is occurring partial confusion in the Chinese economy and to logistics and also some changes, such as to the power map of China's EC platforms, this is not a threat to the growth of the cosmetics EC market that the Company targets and risk is low for the Company, which is developing its business on multiple platforms. Although the pace of growth slowed in the FY07/22 Q3 standalone results, results are trending strongly in the current Q4 and it can be said to be highly likely that the full fiscal year results will achieve the upwardly revised forecasts.

■ Growth strategy and topics

The White Drink, a candidate to be the third hero product, has made a strong start

1. The effects of the Shanghai lockdown and the measures taken in response

China is adopting a zero COVID-19 policy, and due to the spread of the Omicron variant, it implemented a complete lockdown of Shanghai on March 28, 2022 (in practical terms, the restrictions on going outside were lifted on June 1). The lockdown had a directly negative effect on the results of the Company, which mainly develops its business in China, and particularly on the results of the Shanghai subsidiary. Beauty salons and retail shops, which are the Shanghai subsidiary's customers, had to suspend operations, so sales to these real-world channels were greatly affected, with the estimated negative effect on April 2022 net sales being ¥115mn and on the FY07/22 Q3 standalone results being ¥62mn. To prepare for lockdowns in the future, the Company intends to reduce business risk at the Shanghai subsidiary. Specifically, in addition to the previous sales to beauty salons, a conventional real-world channel, it has opened flagship stores on local EC sites in the online channel and is also conducting remote work in the sales department and the management department, and in such ways it has strengthened its approach for risks that threaten business continuity.

On the other hand, EC in China was impacted by the suspension of logistics. From March 28, 2022, deliveries, such as inventory shipments, were suspended in some regions, and in April due to the suspension of the relevant deliveries, there occurred a situation in which consumers did not receive the products they bought on Tmall Global and RED, which resulted in an increase in cancellations compared to a typical month. The negative effect of this was estimated to be ¥13mn in April 2022 (an estimated negative effect of ¥3mn on the FY07/22 Q3 standalone results). To prepare for lockdowns in the future, the Company established a logistics base outside of Shanghai, which started operations in May 2022. It plans to progress additional decentralization in the future and to work to further reduce the risk of a logistics suspension. For EC in China, logistics returned to normal in FY07/22 Q4 and the impact on results has been eliminated.

2. The White Drink is a candidate to be the third hero product

The Company is strengthening the development of The White Drink as a candidate to become the third hero product after AG Drink and Essence Sheet. Up to the present time, it has positioned White Aminos beauty supplements and sunscreen cosmetics as up-and-coming products and targeted them becoming the third major brand, and then in February 2022, it renewed White Aminos and market launched Venus Recipe The White Drink. It has been well received by customers, and in the FY07/22 Q3 standalone results, The White Drink's net sales were ¥120mn, while net sales of whitening-appeal brands as a whole were ¥352mn (¥204mn in the same period in the previous fiscal year) and have become the driver of the rapid growth in this field. The Company is succeeding in increasing sales, such as by creating brand series based on hero products and expanding from beauty drinks to cosmetics, so we shall be paying attention to developments in the future.

■ Shareholder return policy

Is currently prioritizing securing internal reserves, but is expected to pay a dividend in the medium term

The Company's basic shareholder return policy is to strengthen profitability and to continuously and stably pay a dividend. However, it is currently in a growth process and in order to expand the business in the future and to enhance the financial base, it is prioritizing securing internal reserves and has not paid a dividend since it was founded. In the short term, it will utilize the funds acquire through its listing to acquire plant facilities through M&A, so it does not plan to pay a dividend in FY07/22. However, in May 2022 it newly established a shareholder benefits program and every year at the end of July, shareholders holding at least 100 shares will receive a gift of the Company's products depending on the number of shares they hold (100 to 499 shares, products worth ¥3,000; 500 to 999 shares, products worth ¥10,000; and 1,000 or more shares, products worth ¥17,000).

Following the TSE's change of market categories in April 2022, the Company's listing was transferred to the growth market, but it is aiming to be upgraded to the Prime market in the medium term. The Asia market, which has untapped potential, is rapidly growing, so its investment stance at the current term is mainly for the purpose of capital gains. But at FISCO, we expect it to start paying a dividend once it achieves a change of designation to the Prime market.



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