COMPANY RESEARCH AND ANALYSIS REPORT

create restaurants holdings inc.

3387

Tokyo Stock Exchange First Section

12-Jun.-2020

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Summary

Multiple acquisitions supported growth in FY2/20, though recorded impairment losses due to COVID-19 impact FY2/21 guidance undecided at this point

1. Company profile

create restaurants holdings inc. <3387> (hereafter, also "the Company") focuses mainly on the operation of restaurants and food courts inside shopping centers, while also developing izakaya (traditional Japanese eating and drinking establishments) and restaurant formats acquired through M&A. One characteristic is that the Company carefully selects locations that attract large numbers of customers, and employs a distinctive multi-brand, multi-location strategy, which involves developing a variety of restaurant formats attuned to specific locations (regional characteristics, customer attributes, competition status, etc.). This strategy has supported the Company's main business. Currently, the Company has 1,149 restaurants*1 in approximately 200 brands (as of the end of February 2020). Moreover, the Company is achieving higher growth by incorporating brands with high growth potential into the Company's own growth profile through aggressive M&A, such as the seafood izakaya chain Isomaru Suisan*2, which has been gaining popularity with its 24-hour operation in favorable station-front locations, by engaging in "Group Federation Management."*3 While impact from the COVID-19 outbreak is a concern at this point, the Company is taking steps to secure surplus liquidity and has not significantly changed the direction of its long-term strategy.

*1 Including all business consignment outlets and franchise outlets (same below)
*2 Developed by SFP Holdings Co., Ltd. <3198> that was acquired in April 2013
*3 The Group's management being advanced by the Company. Up to the present time, it has taken a solar system-type approach to creating synergies between members of the Group, but going forward, it is aiming to evolve to a star cluster-type approach, in which the various companies in the Group pursue synergies with each other.

2. FY2/20 results

In FY2/20 (IFRS basis), the Company reported ¥139,328mn in revenue (+16.8% YoY) and ¥3,483mn in operating profit (-12.4%). Profit fell on higher sales (revenue reached an all-time high). Revenue benefited from contributions by stores that opened in the previous fiscal year from the start of the year. This includes 43 new stores opened during the year, and acquisitions that added 238 stores, which resulted in growth in all categories. Same-store sales were at 99.2% of the year-ago level for the full year, despite impacts from major typhoons and COVID-19 (affected results from mid-February), roughly on track with the plan. In earnings, operating margin dropped to 2.5% (vs. 3.3% in the previous fiscal year), even with improvement in the unit cost ratio, as aggressive impairment losses, including COVID-19 impact, and other factors weakened profit. Nevertheless, we think steady increase in adjusted EBITDA, an important indicator, has positive implications. The Company also strengthened its business portfolio with four acquisitions that had clear aims during the fiscal year, including entry into contract business (such as consignment operation of golf course restaurants), acquisition of regional core cities, and an Italian restaurant in North America.

3. COVID-19 impact

Same-store sales dropped significantly at 60.6% YoY in March 2020 because of shortening hours and suspending operations for some stores in response to the COVID-19 outlook and requests to curtail operations. The Company started large-scale store suspensions in April following issuance of a state of emergency declaration in seven prefectures on April 7 and issuance of a nationwide declaration on April 16. Given these conditions, the Company is facing heavy impacts on earnings and finances, similar to peers, with the prospect of no sales at suspended stores while still incurring fixed costs (store rents, employee personnel costs, etc.) at least until the declaration is lifted. Considering risk of prolonged impact from stay home orders, it is taking steps to secure sufficient surplus liquidity and plans to arrange credit lines worth about ¥30bn in addition to the ¥26.5bn in cash and deposits it held at end-March (consolidated basis). The Company intends to be ready to sustain its business and smoothly resume operations. Meanwhile, it has not decided FY2/21 guidance (undisclosed) yet because of difficulty making reasonable calculations at this point with the COVID-19 outbreak and intends to promptly disclose guidance once such calculations are possible.

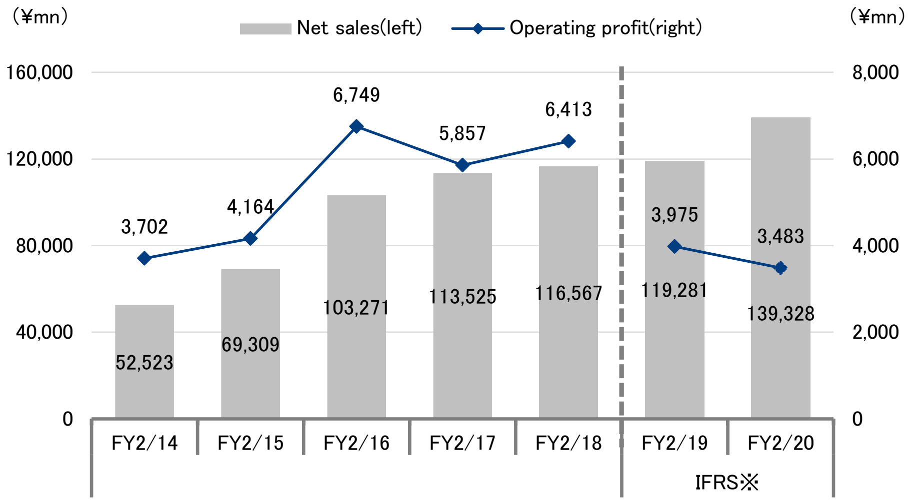
4. Growth strategies

The Company is currently implementing a three-year medium-term management plan that lasts through FY2/22 (a rolling format). There is uncertainty about attaining numerical goals due to COVID-19 impact, however, and it intends to update the outlook once reasonable calculations can be made, just as with FY2/21 guidance. Nevertheless, direction of the longer-term strategy that emphasizes M&A and "Group Federation Management" should not significantly change. In other words, the Company is still aiming for sustainable robust growth through 1) implementing M&A strategy in Japan and overseas, 2) further strengthening its ability to create brands, 3) further evolving Group Federation Management. It also intends to proceed with evolution of the business portfolio, while dynamically responding to changes in the environment, given the possibility of industry reorganization and major changes in consumer behavior after the current situation settles down.

Key Points

- In FY2/20, profits decreased although sales increased
- Multiple acquisitions supported growth in FY2/20, though recorded impairment losses due to COVID-19 impact
- Conducted large-scale store suspensions following the state of emergency declaration accompanying the COVID-19 outbreak and faces major impact on results, though has sufficient surplus liquidity
- FY2/21 guidance and medium-term management plan revisions not decided yet, remains committed to direction of the longer-term strategy that emphasizes M&A and Group Federation Management

Results trends



*Adopted IFRS from FY2/19
Source: Prepared by FISCO form the Company's financial results

Company profile

Implements "Group Federation Management" that pursues a variety of brands utilizing aggressive M&A

1. Business description

The Company mainly have operated restaurants and food courts at shopping centers and has moved into izakaya and other type restaurants acquired through M&A. As a holding company, it brings together 21 consolidated subsidiaries (including 5 overseas companies) (as of end of FY2/20).

The Company carefully selects locations that attract large numbers of customers, and employs a distinctive multi-brand, multi-location strategy, which involves developing a variety of restaurant brands attuned to specific locations (regional characteristics, customer attributes, and competition status, etc.). This strategy has supported the Company's main business. Further, in recent years, the Company is promoting "Group Federation Management," which involves incorporating various brands with high growth potential into the Company through aggressive M&A activities. While COVID-19 is currently weighing heavily on the restaurant industry, the Company's direction of longer-term strategy should not significantly change. As of the end of February 2020, the Company has 1,149* restaurants in approximately 250 brands.

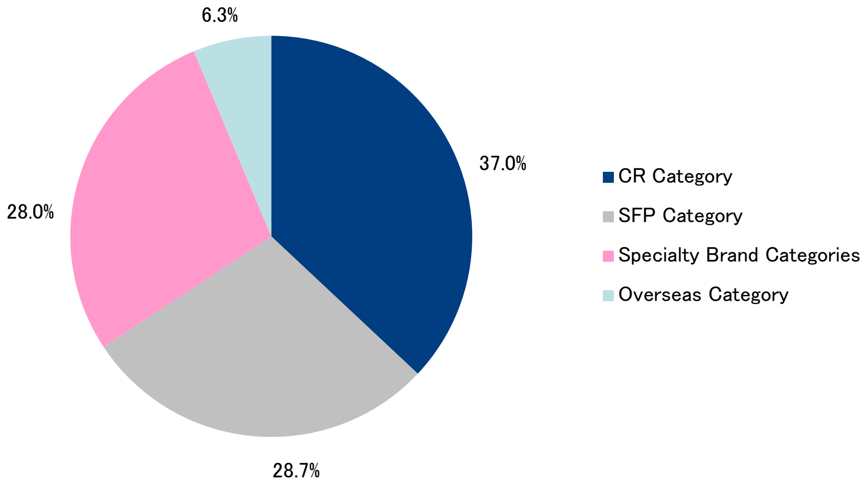
Overview of business categories (as of end-February 2020)

CR Category	It is comprised of the outlets operated by create restaurants (CR), Create Dining (CD), Create Bayside (CB) and create sports and leisure (SL). There were 569 outlets at the end of February 2020. The main brands include Harvest, shabu SAI, Rio Grande Grill, Roast Beef Hoshi, and Desert Okoku.
SFP Category	It is comprised of the restaurants operated by SFP Holdings (SFP), with which the Company entered-into a capital tie-up in April 2013, Joh Smile (JS) and CLOOC DINING (CL). It operates izakaya outlets in urban downtown districts. The Company aims to enter regional core cities with a unique alliance concept. There were 275 outlets at the end of February 2020. The main brands include seafood izakaya Isomaru Suisan, fried chicken wing specialty restaurants Toriyoshi and Toriyoshi Shoten, izakaya Maekawa Suigun, and Karaage Center.
Specialty Brand Categories	It is comprised of KR HOLDINGS (KR), LE MONDE DES GOURMET (LG), eatwalk (EW), YUNARI (YNR), Gourmet Brands Company (GBC), Route 9g(RN), YUZURU (YZ), Kiya Foods (KF), and Icchou (IC). It is mainly focusing on Kagonoya, ICCHOU and Gomasoba YUZURU outlets for roadside locations, developing their respective specialty brands for urban commercial facilities. There were 251 outlets in total at the end of February 2020. The main brands include Japanese restaurants Kagonoya and ICCHOU, Italian restaurants TANTO TANTO, primarily vegetable-based Italian restaurants AW kitchen, Tsukemen TETSU, Café Boulangerie JEAN FRANÇOIS, Singaporean cuisine Hainan Jeefan Restaurants, Gomasoba YUZURU, and udon and soba restaurants Ginza Kiya.
Overseas Category	It is comprised of restaurants operated by the Company's overseas subsidiaries in Singapore, Hong Kong, Taiwan, and the United States. There were 54 outlets in total at the end of February 2020. The main brands include shabu SAI and MACCHA HOUSE, an outlet specializing in matcha green tea. In North America, the Company operates three Japanese restaurants, including sushi restaurant SushiNao and SOBA TOTTO, in New York and newly acquired Italian restaurant Il Fornaio.

Source: Prepared by FISCO from Company materials and interviews

The Company's businesses are divided into four categories: (1) the CR Category, involving the operation of restaurants and food courts with multiple brands mainly at commercial facilities, (2) the SFP Category, involving the operation of izakaya brands, (3) the Specialty Brands Category, involving the operation of various restaurant brands, and (4) the Overseas Category, which involves operation of Japanese restaurants in Singapore, Hong Kong, Taiwan, and so forth. The mainstay CR Category makes up 37.0% of the Company's sales, while the SFP Category makes up 28.7%, the Specialty Brands Category 28.0%, and the Overseas Category 6.3% (as of the end of FY2/20).

Revenue by category (FY2/20 results)

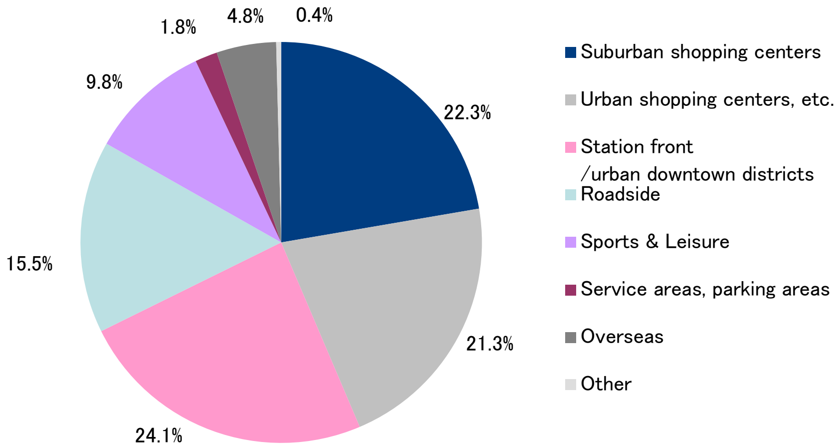


Source: Prepared by FISCO from Company materials

Further, the breakdown of restaurant numbers by location shows 22.3% for suburban SC, 21.3% for urban SC, 24.1% for station front and urban downtown districts, 15.5% for roadside, 9.8% in Sports & Leisure*1, 1.8% for SA/PA*2, and 4.8% overseas; having achieved a good, balanced distribution from the previous concentration in commercial facilities (as of the end of FY2/20).

*1 Consignment operation of restaurants at golf course and theme parks, etc.
*2 Consignment operation of stores in highway service areas and parking areas, etc.

Composition of restaurant numbers by location
(as of the end of February 2020)



Source: Prepared by FISCO from Company materials

2. History

The Company was established in 1997 as the Yokosuka Brewing Company K.K. (the company name was changed to create restaurants inc. in 1999) by Tokuju, K.K., the family business of the Company's current chairman, Hitoshi Gotoh. However, its actual foundation was in 1999, when it took over the operation of five western-style restaurants from Tokuju and started the restaurant business in earnest. In 2000, then employee of Mitsubishi Corporation <8058> and current representative director, president and CEO Haruhiko Okamoto engaged with the Company through an in-house venture scheme, with the Company also receiving a capital investment from Mitsubishi (the capital relationship with Mitsubishi was terminated in 2012). Thereafter, backed by Mitsubishi's reputation and other resources, the Company accelerated its growth by increasing its number of restaurants, mainly opening them in commercial facilities and similar locations. In 2005, the Company listed on Mothers market of the Tokyo Stock Exchange, Inc., changing to the First Section in 2013.

The Company has also been aggressive in M&A, acquiring the Japanese cuisine chain KISSHO in 2007 and shifting to a holding company structure in 2010 to establish a platform for "Group Federation Management." Subsequently, the Company has acquired LE MONDE DES GOURMET in 2012, SFP Dining*1 and eatwalk in 2013, YUNARI and Shanghai Bishoku Chushin Co., Ltd. (company name changed from R21 Cuisine) in 2014, KR Food Service*2 and RC Japan (now Create Dining inc.) in 2015, successively bring them into the Group. SFP Dining was listed on the TSE Second Section in December 2014 (a subsidiary listing). (Its listing was changed to the TSE 1st Section on February 28, 2019). The Company acquired Kiya Foods, Iccho, and other companies in 2019 through a number of M&A.

*1 SFP Dining Co., Ltd. changed its name to SFP Holdings Co., Ltd. in June 2017
*2 KR Food Service Co., Ltd., changed its name to KR Holdings Co., Ltd., in December 2018.

In overseas deployment, the Company started in 2008 by establishing a joint venture with a local company in Shanghai, and among other initiatives went on to establish wholly owned subsidiaries in mainland China in 2010, Singapore in 2011, Hong Kong in 2012, and Taiwan in 2014. While the Company's overseas expansion is still considered to be in the experimental stage, it is preparing the groundwork for a full-fledged expansion in the future. In March 2016 it established a subsidiary in New York also aimed at a US rollout, and in July 2017, it opened NAOKI TAKAHASHI* in New York. In September 2019, the Company added California-based Il Fornaio (America) LLC to the Group, its first major overseas acquisition. The Company completed the exit of all restaurants from China (Shanghai) at the end of August 2017.

* The restaurant name was changed and is currently Sushi Nao.

Corporate characteristics

Possesses a strong brand portfolio with industry development capabilities and robust M&A results

1. Multi-brand, multi-location strategy

The characteristics of the Company's main business are 1) opening restaurants in commercial facilities that attract large numbers of customers (shopping centers, station buildings, etc.) and 2) operating diverse brands attuned to their local environments (regional characteristics and customer attributes, status of competition, etc.). The diversity of these brands, including Japanese, Western, and Chinese cuisine, as well as ethnic food and cafes, enables the Company to open multiple restaurants within a single commercial facility and respond to various needs of the facility owner (developer, etc.). This has worked to the Company's advantage in opening restaurants inside commercial facilities, which typically have a higher barrier to entry. Naturally, there is also a cost factor involved in creating multiple brands attuned to their local environments; however, the capacity to develop brands that use the customer drawing power of favorable locations to maximum advantage is the Company's true worth. The source of its value creation is accumulation of know-how in brand development and operations.

On the other hand, the seafood izakaya ISOMARU SUISAN, developed by SFP which was acquired in 2013, has as a special characteristic in its 24-hour operation in station-front locations populated with convenience stores and drugstores. In challenging fierce competition with street-level locations, the chain deliberately selected high-cost station-front sites due to its insistence on locations that attract large numbers of customers. This may be cited as one reason why the chain has a strong affinity with the strategy employed by the Company thus far. Therefore, it can be seen as an extension of the scope of the multi-location strategy to include the street-level domain, and it could pave the way for future full-scale development of diverse brands among street-level locations in urban downtown districts, in addition to the existing commercial facilities. Furthermore, Japanese restaurant chain Kagonoya, which is operated by KR Food Service acquired in 2015, has stores mainly in roadside locations, and contract business (handled by create sports & leisure), which was acquired in 2019, engages in consignment operation of restaurants at golf courses. The Company is reinforcing location diversity and brand specialization with robust M&A activities.

2. Growth model based on “Group Federation Management”

In addition to organic (internal) growth, the Company’s growth model is one where growth arises by supporting growth through engagement with high growth potential brands via M&A, creating various synergies and providing a platform (support from a funding and management perspective etc.). In the past, the Company expanded its operational base through operating restaurants in commercial facilities and food courts. However, given that it was a growth model that was readily influenced by the commercial facility’s circumstances, along with the shift to a holding company structure, the Company sought to transition to a strategy that aims for autonomous growth via “Group Federation Management.” Understandably, it is recognized the Company succeeded because it had been established from an internal Mitsubishi Corporation venture. Additionally, it was a management style familiar in terms of management resources (with staff etc. that were skilled in business management) and corporate cultural perspective. Furthermore, it was recognized as a partner with which a relationship could be readily formed, and done so with relatively little resistance from capital tie-up partners. For the growth strategy going forward, M&A and “Group Federation Management” (maximizing Group synergies) will be the mainstay in a growth model clearly to the Company’s advantage in a tough operating environment where the domestic market is contracting and affected by labor shortages.

Financial results

Realizing high growth potential and profitability through aggressive additions including M&A

1. “Group Federation Management” progress and results trends

Looking back at results, expansion in restaurant numbers, via new openings and M&A, has been the driver of growth. In particular, the turning point was from FY2/13 with a shift to a new growth strategy through “Group Federation Management.” By realizing high growth potential through bringing a range of formats with growth potential into the Group, while supporting further additions, the Company sought to enhance location diversity and specialty branding. Looking at the composition of restaurants by location, at the end of February 2012, commercial facilities (the total of suburban SC and urban SC) represented 78.4% of overall numbers. However, at the end of February 2020 while representation by commercial facilities had shrunk to 43.6%, a balanced portfolio had been established with station-front locations and those in urban downtown districts (24.1%), roadside locations (15.5%) and Sports & Leisure (9.8%) having been newly added.

Openings and closings (including M&A) and total at the end of period

	New openings	Closures	Acquired via M&A	Total at the end of the period
FY2/14	61	-36	108	514
FY2/15	102	-42	26	616
FY2/16	108	-38	109	795
FY2/17	116	-54	0	857
FY2/18	68	-62	2	865
FY2/19	60	-29	29	925
FY2/20	43	-56	238	1,149

Note: From FY2/15, total at the end of the period includes restaurants where outsourced operations are provided, FC locations, non-consolidated locations and overseas J/V locations.
Source: Prepared by FISCO from Company materials

M&A track record

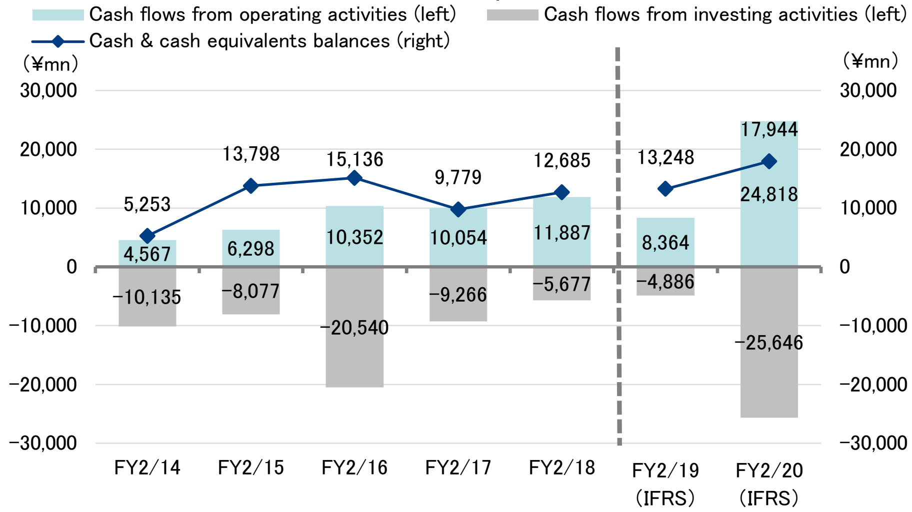
Date acquired	Company name	Main brand(s)	Acquisition price (¥mn)
April 2013	SFP Dining	ISOMARU SUISAN, Toriyoshi Shoten, etc.	6,573
April 2013	eatwalk	AWkitchen, Yasaiyamei, etc.	858
April 2014	YUNARI	Tsukemen TETSU, etc.	1,506
November 2014	Shanghai Bishoku Chushin	Nanxiang Mantou Dian	180
June 2015	KR Food Service	Kagonoya, etc.	14,979
August 2015	RC Japan	Rain Forest Café, etc	65
January 2018	ROUTE9G	Hainan Jeefan Restaurants	Undisclosed
March 2018	Create Bayside	Developing restaurants, etc., under the IKSPIARI brand	Undisclosed
December 2018	YUZURU	Gomasoba YUZURU	Undisclosed
March 2019	Kiya Foods	Ginza Kiya	Undisclosed
March 2019	Joh Smile (M&A by SFP)	Maekawa Suigun, etc.	Undisclosed
July 2019	CLOOC DINING (M&A by SFP)	Karaage Center, etc.	Undisclosed
September 2019	Il Fornaio (America) LLC	Il Fornaio (North America), etc.	8,050
September 2019	create sports and leisure	Operation of golf course restaurants	5,884
October 2019	Icchou	ICCHOU, etc.	7,010

* This is the Il Fornaio (America) LLC acquisition price converted at ¥107/$.
Source: Prepared by FISCO from Company materials

From a financial perspective, the equity ratio, which represents the stability of the financial foundation, achieved a level exceeding 35% by FY2/12. Mitsubishi Corporation's shares were acquired by way of TOB, and as a result of around 80% of those shares being retired, the equity ratio declined to 19.7% at end-FY2/13. In FY2/14, equity was strengthened through the sale of treasury shares and the equity ratio improved to 32.4% temporarily at the end of FY2/15 due to a new share issuance in line with the listing (subsidiary listing) of SFP Dining. The equity ratio dropped again to 24.1% at end-FY2/16 with the acquisition of KR Food Service. Since the Company subsequently carried out major acquisitions, such as Icchou and Il Fornaio, and adopted IFRS accounting (changes the lease accounting standard), equity ratio attributable to owners of parent (corresponds to the equity ratio) was 10.9% at end-FY2/20. Therefore, we think the Company needs to bolster its financial base as it pursues further growth.

In cash flow trends, while cash flows from investing activities steadily exceeded cash flows from operating activities during FY2/14-16 because of aggressive new store openings and M&A activity, these additions fueled earnings growth. The Company temporarily lowered investment cash flow through curtailment of new openings and other measures during FY2/18-19, but then substantially expanded it with multiple M&A deals in FY2/20.

Cash flows from operating activities and cash flows from investing activities, cash & cash equivalents balances



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

Profit fell on higher sales in FY2/20, robust M&A contributed to stronger earnings though recorded impairment losses due to adopting IFRS accounting standards and COVID-19 impacts

2. FY2/20 results overview

In FY2/20 (IFRS basis), the Company reported ¥139,328mn in revenue (+16.8% YoY), ¥3,483mn in operating profit (-12.4%), ¥3,118mn in pretax income (-15.4%), and ¥1,278mn in net income attributable to owners of parent (-3.2%). Profit fell on higher sales (revenue reached an all-time high). While revenue was roughly on track with the plan, profits missed.

Revenue benefited from contributions by stores that opened in the previous fiscal year from the start of the year. This includes 43 new stores opened during the year, and acquisitions that added 238 stores, which resulted in growth in all categories. Acquisitions largely fueled expansion with one company in the CR category (SL) *1, two companies in the SFP category (JS, CL) *2, three companies in the specialty brand category (YZ, KF, IC) *3, and one company in the overseas category (IF) *4. Same-store sales were at 99.2% of the previous-year level for the full year, despite impacts from major typhoons and COVID-19 (affected results from mid-February), roughly on track with the plan. The Company appears to have been successful in revisions and renovations to unprofitable stores and arrangement of suitable personnel operations. Results in store network adjustments during the year were 43 new openings, 238 additions from M&A, 56 closures, 39 format changes, and 38 renovations. Total group store volume expanded substantially to 1,149 stores at the end of February 2020.

*1 create sports & leisure (added to consolidated scope in September 2019)
*2 Joh Smile (added to consolidated scope in March 2019), CLOOC DINING (added to consolidated scope in July 2019)
*3 Yuzuru (added to consolidated scope in December 2018), Kiya Foods (added to consolidated scope in March 2019), Icchou (added to consolidated scope in October 2019)
*4 Il Fornaio (America) LLC (added to consolidated scope in September 2019)

In earnings, the Company kept the personnel costs ratio on par with the previous fiscal year, despite an upturn in average personnel cost, by rigorously controlling shifts, and lowered its unit cost ratio with stable supply of fresh produce and other items and food ingredient consolidation and revisions. Operating margin, however, dropped to 2.5% (vs. 3.3% in the previous fiscal year) due to aggressive recording of impairment losses, including COVID-19 impact, and other factors resulted in a profit decline that came in below guidance. Nevertheless, even though adjusted EBITDA, an important indicator, climbed sharply with a 133.1% YoY increase to ¥25,212mn mainly because of applying IFRS 16 (change in lease accounting), its steady increase excluding the special factor has positive implications.

In financial conditions, gross assets and interest-bearing debt expanded substantially on multiple large M&A deals and application of IFRS 16. While this reduced the ratio of equity attributable to owners of parent (equity ratio) to 10.9% (vs. 22.6% in the previous period), the net D/E ratio (including lease liabilities) expanded to 5.11x (vs. 1.07x in the previous period). However, it is important to recognize that application of IFRS 16 strongly affected the large change in this value*1. The Company has also secured sufficient surplus liquidity, and its net interest-bearing debt to cash flows from operating activities ratio*2 is just 3.36x thanks to robust operating cash flow. We hence are not concerned about financial soundness.

*1 Excluding the impact of IFRS 16 application, the equity ratio attributable to owners of parent (equity ratio) is 17.6%, the net D/E ratio is 1.92x, and the net interest-bearing debt to operating cash flow ratio is 2.80x.
*2 Calculated as net interest-bearing debt / cash flows from operating activities. It is an indicator determining how many years of cash flows from operating activities are required to repay interest-bearing debt, with it generally regarded as of concern if the rate exceeds 10x.

Category results are set out as below.

(1) CR Category

Revenue rose 13.6% YoY to ¥51,843mn, and category CF (*) climbed 10.6% to ¥5,992mn, Both sales and category CF improved. Main drivers of the hefty sales gain were full-year contributions from the 38 stores that opened in the previous fiscal year (including 17 stores from M&A), 15 new stores, and an acquisition (124 SL stores). While same-store sales were also healthy at 99.9% of the year-ago level, this outcome was slightly below guidance because of COVID-19 impact from mid-February. Category CF increased on higher sales, though also undershot guidance.

* Category CF (cash flow) utilizes adjusted EBITDA (operating profit + other operating expenses – other operating revenue including excluding funding revenue + depreciation expenses + non-recurring expense items) (same below).

(2) SFP Category

Revenue increased 6.5% YoY to ¥40,216mn, and category CF slipped 0.1% to ¥4,532mn, roughly on track with guidance. Main sales drivers were full-year contributions from the 18 stores that opened in the previous fiscal year (including 3 FC stores), 11 new stores, and acquisitions (19 JS stores, 22 CL stores). In particular, based on the SFP Food Alliance Concept, the Company added CL to the Group following JS, which finalized a contract in FY2/19. Same-store sales were firm too at 99.0% of the year-ago level. Isomaru Suisan performed well with success in revising unprofitable stores, bolstering operational capabilities, and implementing sales promotion measures.

(3) Specialty Brand Category

Revenue grew 16.5% YoY to ¥39,198mn, and category CF rose 32.5% to ¥2,921mn, roughly on track with guidance. Both sales and CF improved. Main sales drivers were full-year contributions by 25 stores that opened in the previous fiscal year (including 10 stores from acquisitions), 11 new stores, and acquisitions (7 KF stores, 46 IC stores). Same-store sales held up too at 98.4% of the year-ago level. While KR struggled some, bakery and Italian formats generated healthy results. Category CF increased on higher sales.

(4) Overseas Category

Revenue expanded 200% YoY to ¥8,962mn, and category CF used was ¥1,173mn (vs. an ¥89mn deficit). Both sales and CF improved and exceeded guidance. Main sales drivers were full-year contributions by 8 stores that opened in the previous fiscal year (including 2 stores from transfers), 6 new stores, and acquisitions (20 Il Fornaio stores). Il Fornai, the Company's first overseas acquisition, provided a large contribution to category growth. Category CF increased on higher sales.

Overview of FY2/20 results

(¥mn)

	FY2/19 Results		FY2/20 Results		Change		FY2/20 Revised forecasts (dated Oct. 11, 2019)		
	Amount	% of total	Amount	% of total	Amount	Change rate	Amount	% of total	Achievement rate
Revenue	119,281	100.0%	139,328	100.0%	20,046	16.8%	140,000	100.0%	99.5%
CR Category	45,633	38.3%	51,843	37.2%	6,210	13.6%	52,500	37.5%	98.7%
SFP Category	37,751	31.6%	40,216	28.9%	2,465	6.5%	40,000	28.6%	100.5%
Specialty Brand Category	33,659	28.2%	39,198	28.1%	5,539	16.5%	39,500	28.2%	99.2%
Overseas Category	2,987	2.5%	8,962	6.4%	5,975	200.0%	8,500	6.1%	105.4%
Adjustment	-749	-	-893	-	-143	-	-500	-	-
Operating profit	3,975	3.3%	3,483	2.5%	-491	-12.4%	7,500	5.4%	46.5%
Profit before tax	3,688	3.1%	3,118	2.2%	-569	-15.4%	7,000	5.0%	44.6%
Profit attributable to owners of parent	1,321	1.1%	1,278	0.9%	-42	-3.2%	3,700	2.6%	34.6%
Adjusted EBITDA	10,814	9.1%	25,212	18.1%	14,397	133.1%	25,000	17.9%	100.8%
CR Category CF	5,418	11.9%	5,992	11.6%	574	10.6%	6,500	12.4%	92.2%
SFP Category CF	4,538	12.0%	4,532	11.3%	-5	-0.1%	4,600	11.5%	98.5%
Specialty Brand Category CF	2,205	6.6%	2,921	7.5%	716	32.5%	2,800	7.1%	104.3%
Overseas Category CF	-89	-	1,173	13.1%	1,263	-	400	4.7%	293.3%
Adjustment	-1,257	-	10,591	-	11,849	-	10,700	-	-

*The percentages of the total for the category CF (cash flow) are from the percentages of sales per category.
*Category CF = operating profit (Japanese standards) + depreciation expenses + amortization of goodwill + funding revenue + non-recurring expenses items
Source: Prepared by FISCO from Company materials

Financial position at end-FY2/20

(¥mn)

	as of the end of February 2019	as of the end of February 2020	Change	
			Amount	Change rate
Total asset	72,459	149,997	77,538	107.0%
Equity attributable to owners of parent (equity)	16,361	16,289	-72	-0.4%
Equity ratio attributable to owners of parent (equity ratio)	22.6%	10.9%	-11.7%	-
Interest-bearing debt	30,769	101,770	71,001	230.8%
Corporate bonds and loans	29,050	49,774	20,724	71.3%
Lease liabilities	1,718	51,850	50,132	-

* Lease liabilities increased due to the change in lease accounting standards.
Source: Prepared by FISCO form the Company's financial results

The numbers of outlet openings, exits, etc.

	as of the end of February 2019	New openings	Closures	M&A	Transfers, etc. (adjusted)	as of the end of February 2020	Brand conversions	Renovations
CR Category	444	15	24	124	10	569	26	16
SFP Category	239	11	16	41		275	8	15
Specialty Brand Category	208	11	10	53	-11	251	4	6
Overseas Category	34	6	6	20		54	1	1
Total number of group stores	925	43	56	238	-1	1,149	39	38

* Negative value in transfers, etc. due to changes in the business format across periods
* Total number of stores for the entire Group including business consignment stores and FC stores
Source: Prepared by FISCO from Company materials

3. Overview of FY2/20

Looking back at FY2/20 based on trends described above, despite profit decline because of impact from mid-February, albeit limited, by the COVID-19 outbreak and curtailed operations and steep impairment losses booked at period-end, we think the Company's realization of all-time high revenue through various acquisitions and reinforcement of existing stores, besides these setbacks, demonstrates that it is making progress with its strategy, as explained below.

Main activity results

Reinforcing the portfolio with multiple acquisitions

M&A deals are vital to the growth strategy, and the Company had four acquisitions Groupwide in FY2/20. Key points are realization of relatively large purchases and clear aims respectively with acquisitions of new business models (entry into contract business, central kitchen operations, etc.), regional core cities, traditional high-quality brands/cutting-edge MD, and a North American platform. We expect these additions to substantially strengthen the Company's business platform.

(1) create sports and leisure

The Company acquired a portion of restaurants (sports and leisure business) owned by Seiyo Food-Compass Group, which supplies food services a variety of scenes, including employee cafeterias, school meals, and golf course restaurants, on June 26, 2019 (it changed the company name to create sports & leisure after the acquisition). create sports & leisure continues to operate sports business (consignment operation of restaurants at golf courses) and leisure business (operation and facility management of recreational facilities, training centers, and hotels and consignment operation of restaurants at theme parks and commercial facilities). Main aims are 1) full-fledged entry into contract services (consignment operation), 2) further expansion of the golf course restaurant business with the industry's top share (consignment operation), and 3) improvement of business portfolio quality through promotion of consignment-type business that does not involve investment burden (acquisition of stable cash flow). It consolidated this business, which has 124 stores (89 sports business stores and 35 leisure business stores) on September 1, 2019.

(2) Icchou

The Company acquired all shares of Icchou, which operates ICCHOU Japanese restaurants (41 stores) and Yorozu-Ya grilled meat restaurants (5 stores) mainly in the northern Kanto area, on September 2, 2019 (it added this business to consolidated scope on October 1, 2019). Main aims are 1) acquisition of a competitive unique business model cultivated over many years, 2) involvement with operational knowhow for a central kitchen (the Group's first experience), and 3) increase in steady sales and profits by acquiring a large store network with roadside locations.

(3) Il Fornaio

The Company acquired all shares in Il Fornaio (America) LLC, which operates Il Fornai Italian restaurants (20 stores) in North American (California, etc.), on September 12, 2019 (it added this business to consolidated scope on September 30, 2019). Main aims are 1) acquisition of stable income in North American business, 2) collaboration with stores operated by the US subsidiary, 3) rollout of the Group's brands in North America, and 4) building a foundation for aggressive acquisitions of other restaurant brands.

(4) CLOOC DINING

The Company acquired almost all shares of CLOOC DINING, which operates Karaage Center and other restaurants deployed by group firm SFP Holdings in Nagano Prefecture on May 30, 2019 (it added this business to consolidated scope on July 1, 2019). This purchase is part of the SFP Food Alliance Concept promoted by SFP Holdings. Main aims are 1) acquisition of regional core cities, 2) securing personnel, and 3) creating synergies including other alliance partners.

COVID-19 impact and response

FY2/12 guidance undecided (not disclosed)

Securing surplus liquidity to ensure business continuation and putting in place capabilities to support smooth business resumption; FY2/21 guidance undecided (not disclosed) at this point

1. Current situation

Same-store sales dropped significantly at 60.6% YoY in March 2020 because of shortening hours and suspending operations for some stores (*1) in response to the COVID-19 outlook and requests to curtail operations. The Company started large-scale store suspensions (*2) in April following issuance of a state of emergency declaration in seven prefectures on April 7 and issuance of a nationwide declaration on April 16. Given these conditions, the Company is facing significant burden with the prospect of no sales at suspended stores while still incurring fixed costs (store rents, employee personnel costs, etc.) at least until the declaration is lifted. While attention should be given to national and local government subsidies (employment adjustment subsidies, etc.) and additional suspension compensation and rent grace periods, we expect heavy impacts on earnings and finances, similar to peers. The Company intends to curtail personnel, minimize spending, and promote management with as much emphasis on cash flow as possible. It is also taking steps to secure sufficient liquidity to sustain its business and smoothly resume operations.

*1 Shortened hours at 632 stores and suspended operations at 88 stores out of its total 1,150 stores as of end-March 2020
*2 Shortened hours at 224 stores and suspended operations at 863 stores out of its total 1,158 stores as of April 20, 2020

2. Main initiatives

(1) Securing surplus liquidity

Considering risk of prolonged impact from stay home orders following the state of emergency declaration, the Company is taking steps to secure sufficient surplus liquidity and plans to arrange credit lines worth about ¥30bn in addition to the ¥26.5bn in cash and deposits it held at end-March (consolidated basis). Since estimated monthly cash outflow if all group stores experienced long-term suspensions is about ¥3bn, management is putting priority on business survival through arrangement of a financial base that avoids fund liquidity concerns for a certain amount of time.

(2) Store and headquarter initiatives

The Company is strengthening measures to ensure customer and employee safety and reassurance (setting up sanitizer stations, having staff wear masks, ensuring hand-washing practices, etc.) and intends to dynamically implement partial store suspensions and shorter operating hours from the perspective of societal requests (in light of the state of emergency declaration) and reduction of cash outflow. It is also promoting work revisions and temporary layoffs through work sharing and telework at the headquarters.

(3) Return of directors' compensation

Executives decided to voluntarily return some directors' compensation (for a period of six months) considering store suspensions and other current conditions.

* This calls for returning 25% of monthly compensation by executive directors (five people) and 20% of monthly compensation by operating officers (four people).

3. FY2/21 outlook

The Company has not decided FY2/21 guidance (undisclosed) because of difficulty making reasonable calculations at this point with the COVID-19 outbreak and intends to promptly disclose guidance once such calculations are possible.

We believe the entire restaurant industry is facing heavy impact from business suspensions and shorter operating hours. In the Company's case, however, besides having secured sufficient surplus liquidity to continue business and established operations that support smooth resumption of operations, a key point is robust ability to deal with risk through diversification of the business portfolio. Another aspect is the prospect of a growing role (presence) for the Company, which emphasizes M&A as a growth strategy, given the possibility of COVID-19 impact serving as a catalyst of industry reorganization. Since the scenario could change depending on how long the current situation lasts, we think it is important to closely follow progress toward resolving things as well as results trends (quarterly disclosure, etc.).

Growth strategy

Aiming to accelerate growth through M&A and by further evolving the Group Federation Management

1. Medium-term management plan

The Company is currently implementing a three-year medium-term management plan that lasts through FY2/22 (with a rolling format). There is uncertainty about attaining numerical goals due to COVID-19 impact, however, and it intends to update the outlook once reasonable calculations can be made, just as with FY2/21 guidance. Nevertheless, direction of the longer-term strategy that emphasizes M&A and "Group Federation Management" should not significantly change.

2. Direction of the longer-term strategy

The Company has once again indicated the direction of its medium-term growth strategy, which is based on the one hand on its important management issues, which include responding to diversifying customer needs, the intensification of competition including from ready-to-eat meals, and securing high-quality human resources, but also on the other hand, on an environment in which candidates for M&A are increasing, mainly for business succession and fund projects. In other words, its policy is to steer a course for sustainable, strong growth through 1) implementing M&A strategy in Japan and overseas, 2) further strengthening its ability to create brands, 3) further evolving Group Federation Management. In particular, it envisions growth that emphasizes M&A strategy and Group Federation Management (maximizing synergies within the Group). It also wants to achieve further evolution of the business portfolio while dynamically responding to changes in the business environment considering the possibility of major revisions in work style and consumer behavior after the current situation settles down.

(1) Implementing M&A strategy in Japan and overseas

In Japan, the Company's policy is to target companies that possess cutting-edge brands that will enable it to diversify its outlets, and it is aiming to acquire individual assets from a project, regardless of its scale. In particular, in the SFP category, based on the SFP Food Alliance concept, it will work to open outlets of popular brands like ISOMARU SUISAN by progressing M&A for outlets in regional cities. Conversely, for overseas, it is actively progressing the discovery of projects, particularly in North America, centered on the North America Business Investment Promotion Department, which was opened in February 2019. In Asia also, in addition to M&A, its policy is to also consider developments through franchises (FC) and joint ventures (JV).

(2) Further strengthening its ability to create brands

In a situation in which customer needs are diversifying and the pace of change is becoming increasingly fast, we have entered an age in which a company's "ability to respond to change" is being tested more and more. But the Company is constructing a portfolio rich in expertise and diversity and creating a strategy to make it a winner in this age through combining the brand-development capabilities it has cultivated up to the present time with a spirit of taking on challenges.

(3) Further evolving Group Federation Management

The intention is to evolve from the solar system-type approach taken up to the present time, in which the Company played the central role in creating synergies within the Group, to a star cluster-type approach, in which the various Group companies pursue synergies with each other. Specifically, the measures will include 1) developing franchises among Group members, 2) conducting brand conversions across the Group companies, 3) expanding joint purchasing, 4) promoting cooperation between the holding companies, and 5) newly establishing the Group Business Strategy Headquarters*.

> * Some examples of achievements up to the present time include 1) the management of Mr. FARMER (EW) by CR (Kisarazu outlet), 2) the brand conversions from the desert café brand (CD) to a character café brand (CR), and from the Kagonoya brand (KR) to the shabu SAI brand (CR), and 3) joint purchasing of pork (KR and CR) and of wasabi (CR, KR, and SFP). So, a certain level of results has been achieved. Also, the Group Business Strategy Headquarters is newly established in June 2019, and further synergies are expected to be created within the Group in the future.

We think COVID-19 impact might delay progress in the growth strategy, though it is important to prepare for sustainable growth after the situation calms down by thoroughly analyzing the market environment, collecting information, and establishing appropriate systems. In particular, we intend to focus on reinforced collaboration with group companies and movement toward the next M&A deal while closely monitoring post-COVID-19 pandemic work styles, changes in consumer behavior, and other changes in the market environment.

Shareholder returns

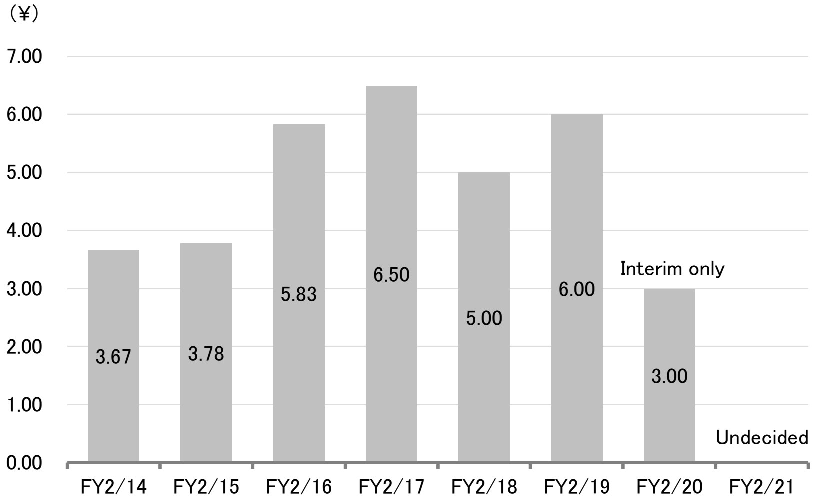
Did not pay a period-end dividend in FY2/20 (only paid a ¥3 interim dividend)
FY2/21 dividend is currently undecided

In the FY2/20 dividend (adjusted for the split (*)), the Company changed period-start guidance (¥3 interim, ¥3 period-end) and did not pay the period-end dividend. This meant it only paid the ¥3 interim dividend. Management has not decided the FY2/21 dividend yet because of COVID-19 impact.

> * Conducted a two-for-one stock split of common shares on March 1, 2020

We think the decision to not pay a period-end dividend because of priority on securing surplus liquidity and building up retained profits was reasonable considering the current situation.

Trends in dividend per share



*Dividend per share after adjusting for the stock split.
* In FY2/15, the consolidated dividend payout ratio decreased because gain on change in equity was recorded under extraordinary income following the IPO of SFP.
Source: Prepared by FISCO from the Company's financial results

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