COMPANY RESEARCH AND ANALYSIS REPORT

PIALA Inc.

7044

TSE Mothers

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Summary

Minimal impact by the COVID-19 outbreak, aiming for annual growth exceeding 20% in marketing assistance services that focus on Beauty & Health and food markets

PIALA <7044> (hereafter, also "the Company") focuses on Beauty & Health (below, B&H) and food markets and provides an array of marketing assistance for clients with electronic commerce (EC) operations. It has been achieving growth with a vision as a "Marketing Commitment Company" that makes commitments to KPI from new customer acquisition through cultivation and maximizes marketing effect and uses a performance-based compensation business model. It maximizes marketing effect by identifying consumer concerns that affect purchasing activity and harnessing data that is organized by individual concerns and a related analysis system built from past success cases. The Company has established operations in China, Taiwan, Vietnam, and Thailand too and is assisting Japanese companies with market entries in Asia.

1. FY12/19 results

In FY12/19 consolidated results, the Company reported ¥13,566mn in net sales (+28.2% YoY) and ¥408mn in operating profit (+25.6%), setting all-time highs. The main driver was upbeat momentum in KPI commitment service that uses performance-based compensation, including boosts from creating hit products. Sales from Im Co., Ltd., which enjoyed major success with cosmetics, climbed sharply with a 3.1-fold YoY increase to ¥2,778mn. This business contributed just over 60% of the overall sales gain. Operating margin slightly declined YoY due to higher advertising media costs, a rise in rent related to the headquarters move, and increase in depreciation costs.

2. Medium-term management plan

The Company announced a three-year medium-term management plan that starts in FY12/20. It expects further advances in digital transformation (DX) in the mail-order industry and aims to realize roughly 20% annual growth through promotion of business activities targeting B&H and food markets in Japan and Asia. These segments offer stable demand unaffected by economic fluctuations and have significant growth potential thanks to high cost performance through collection over the Internet and analysis of data on user concerns, the Company's strength, and implementation of marketing measures based on these data. The Company has also started a new service called Knowledge Sharing that promotes optimization of KPI commitments based on sharing knowledge mutually with leading partner businesses (advertising agencies and others) with the aim of accelerating growth. In overseas strategy, it promotes cross-border EC assistance and wholesale operation agency service in B&H and food areas in China, Taiwan, Vietnam, and Thailand. Numerical goals (consolidated) are at least ¥23.5bn in net sales, ¥1.2bn in operating profit, and 5% operating margin in FY12/22.

3. FY12/19 outlook

In FY12/20 consolidated guidance, the Company targets ¥15,865mn in net sales (+17.0% YoY) and ¥531mn in operating profit (+30.1%), projecting continuation of double-digit sales and profit growth. At this point, there is almost no impact by the COVID-19 outbreak. Despite suspending face-to-face real-world promotions and some delays in import approval procedures related to cross-border EC business, impact on overall results is minor. EC marketing remains vibrant in mainstay B&H and food industries, and inquiries for hygiene products and other items have risen. The Company also benefits from decline in Internet advertising media costs amid softer market conditions. As a new initiative, it started marketing assistance for SARABiO Cosmetics, following formation of a capital and business alliance in December 2019, and hopes to create hit products in FY12/20. It has also launched an alliance with a local company to provide marketing assistance services for Japanese products in Vietnam and aims to actively develop overseas businesses.

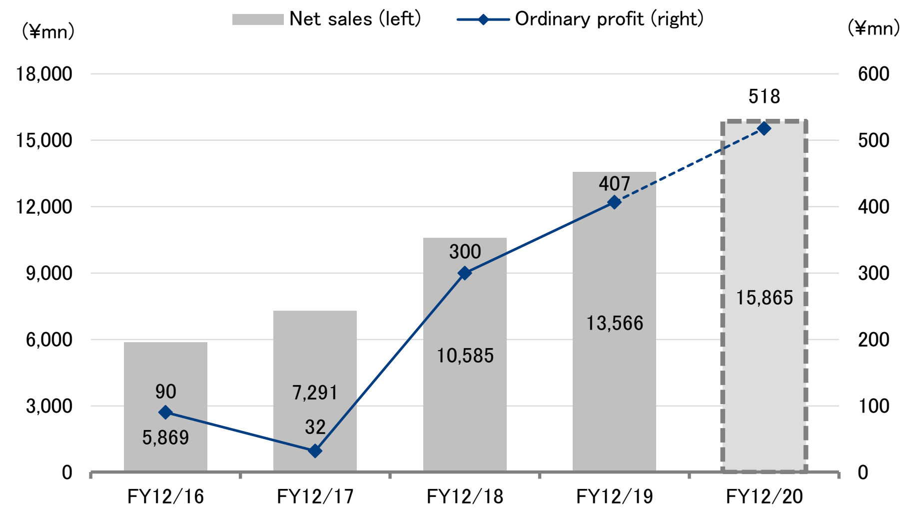
4. Started the "#SAVE YOUR LIFE" project as a response to COVID-19

The Company launched the "#SAVE YOUR LIFE" project with a mission of delivering hygiene products at reasonable prices to as many consumers and medical entities as possible amid persistent hygiene product shortages and inflated pricing due to the COVID-19 outbreak. In May, it started sales on a dedicated EC site of non-woven masks for companies and medical, care, and child-rearing businesses and high-performance KN95 masks for medical, care, and child-rearing businesses. The Company is conducting initiatives that utilize its knowhow cultivated in product development activities and cross-border EC and trade businesses as a firm that provides assistance in the H&B market. It plans to donate some profits to medical entities and others.

Key Points

- Marketing assistance company that specializes in B&H and food industries and provides unique KPI commitment services with a performance guarantee
- Targets roughly 20% annual sales growth and at least 5% operating margin during the medium-term management plan period
- Minimal impact by the COVID-19 outbreak, guides for double-digit sales and profit growth again in FY12/20

Results trend



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

Company overview

Marketing assistance company that specializes in B&H and food industries and provides unique KPI commitment services with a performance guarantee

1. History

The Company traces its roots to the establishment of PIALA Inc. with ¥1mn in capital by Takao Asuka, the current CEO, in 2004. Mr. Asuka had been running the marketing division at major foreign-capital apparel firm Triumph International (Japan) Ltd. before he founded Piala. He is a strongly independent person and wanted to launch his own apparel company. This led to establishment of the Company with three friends from his school years.

The Company initially began with a business model of enclosing ad flyers in paper catalogs based on experience from previous job years. It started Web marketing services in 2008. These include current RESULT EC (EC cart system) and RESULT PLUS (closed affiliate service provider). The Company only outsourced development of the first version of RESULT PLUS service and has developed all subsequent platforms, including RESULT EC and RESULT MASTER, a marketing automation tool equipped with AI (developed in 2012), on its own.

In the rollout of digital marketing assistance services, the Company introduced KPI commitment service that acquires performance income by giving clients its solution services at no charge and committing to results (new customer acquisitions, repeat order acquisitions, etc.) for clients as a way of differentiating itself from the many companies developing and providing these solutions. The Company boosted its reputation with client companies and moved onto a growth trajectory thanks to steadily delivering results, such as selling out products that clients normally sold over a year in three months and fostering hit products.

The Company's business specializes in mail-order companies in B&H and food areas that exhibit high affinity with SNS and other digital media as customer targets. It is also focusing on face-to-face marketing that delivers robust cost performance in these areas and designated roughly 20,000 post offices nationwide as advertising agents to handle demonstration sales, concern consultations, and other activities in September 2018.

The Company is promoting overseas business too, and after establishing a subsidiary in Thailand in 2012, it proceeded in establishing subsidiaries in China in 2013 and Taiwan and Vietnam in 2019. It is focused on marketing assistance for Japanese products in Asian markets.

In apparel business, which was one of the founding aims, the Company ramped up the Marblee brand in 2009, but sold this brand and exited apparel in 2016. It has been expanding business since then through specialization in marketing assistance. PIALA Holding Limited acquired all Company shares in 2012, making a shift to a holding company framework with PIALA Holding Limited as the parent company. Management took this action with the aim of listing its shares on the Hong Kong market because of poor conditions in the Japanese stock market at the time and did not involve any external capital. When Japan's market environment subsequently improved, the Company switched its policy to pursuing an IPO in Japan and hence eliminated the holding company format in 2014. It successfully listed on the TSE Mothers Market in December 2018.

History

Date	Event
March 2004	Established PIALA Inc.to handle advertising agent business and production business (changed the organization to a stockholding company (kabushiki kaisha) in 2005)
September 2008	Started provision of EC system “JOY EC” (now, “RESULT EC”) Started provision of closed affiliate ASP “RESULT PLUS”
October 2009	Started an apparel division in the brand business
April 2010	Started Chinese market entry assistance business
September 2010	Established Marblee Japan Inc.
February 2012	PIALA Holding Limited acquired all Company shares in 2012, making a shift to a holding company framework with PIALA Holding Limited as the parent company
September 2012	Started provision of AI-embedded marketing tool “JOY MASTER” (now, “RESULT MASTER”)
November 2012	Established consolidated subsidiary PIATEC (Thailand) Co., Ltd. in Thailand
January 2013	Absorbed Marblee Japan Inc.
March 2013	Established consolidated subsidiary PG-Trading (HangZhou) Co., Ltd. in China
July 2014	Established consolidated subsidiary PIALab. Inc. in Okinawa
August 2014	Dissolved the holding company framework under PIALA Holding Limited Acquired patents related to unique features “contribution level analysis using attribution scores” and “LTV analysts, etc. for each advertising promotion” in attribution analysis tool “RESULT MASTER”
September 2016	Sold the Marblee apparel brand business operated by Piala
December 2018	Listed shares on the TSE Mothers Market
May 2019	Concluded a strategic business alliance in beauty & health (B&H) and food areas with NTP Corporation, the official Japanese distributor of NetEase News, a media business of major Chinese Internet services firm NetEase, Inc.
July 2019	Established subsidiary PG-Trading (Taiwan) Co., Ltd. in Taiwan
August 2019	Established subsidiary CHANNEL J (THAILAND) Co., Ltd. in Thailand
November 2019	Established subsidiary PG-Trading (Vietnam) Co., Ltd. in Vietnam

Source: Prepared by FISCO from the Company's securities report and Company materials

2. Group framework and business content

(1) Subsidiaries

The PIALA Group consists of the Company and six consolidated subsidiaries. Subsidiary PIALab. Inc., which researches marketing automation, data, and contents and develops application softwares in Okinawa, opened the Tokushima Omotenashi Research Center as a Tokushima branch office in May 2018 and has ramped up call center activities (about 65 employees including part-time workers) at this site. It runs a chat bot service and has started handling some call center operations, which were previously outsourced, internally.

PIATEC (Thailand) Co., Ltd. handles system development and operation, maintenance, and management activities. It transferred Thailand market entry assistance and operation of Japanese food portal video media Channel J to CHANNEL J (THAILAND) Co., Ltd., which was newly established in August 2019 with an aim to strengthen the businesses. Additionally, in China, PG-Trading (HangZhou) Co., Ltd. covers marketing planning, production, design, and advertising operation, and other activities using major EC sites (Tmall/Taobao, etc.), major SNS (WeChat, Weibo, etc.), and other channels. The Company also established subsidiaries for cross-border EC assistance and import consigned sales agent services in Taiwan and Vietnam in 2019. While overseas sales do not have much impact on overall results as they were still at just under 2% in FY12/19, Japanese B&H and food companies are strongly interested in entering Asian markets and the Company moved into these markets with the aim of achieving longer-term growth.

Overview of consolidated subsidiaries

	Investment stake	Business description
PIALab. Inc.	100.0%	System development and call center operation, maintenance, and management activities
PIATEC (Thailand) Co., Ltd.	99.0%	System development and operation, maintenance, and management activities
PG-Trading (HangZhou) Co., Ltd.	100.0%	Marketing planning, production, design, and advertising operation
PG-Trading (Taiwan) Co., Ltd.	100.0%	Cross-border EC import consignment sales agent, logistics assistance, trade, advertising, call center operation, and support
CHANNEL J (THAILAND) Co., Ltd.	49.0%	Cross-border EC import consignment sales agent, logistics assistance, trade, advertising, and media video production
PG-Trading (Vietnam) Co., Ltd.	100.0%	Cross-border EC import consignment sales agent, logistics assistance, trade, and advertising

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

(2) Business description

The Company's Group promotes EC Transformation* for all customers and their related companies with a vision of "Smart Marketing for Your Life (Make your life more satisfactory and convenient by marketing)" and a corporate motto of "all actions create a WIN world." With a mission of creating value by bringing customers into contact with better products to help them enjoy the purchasing activity itself and by maximizing customer satisfaction, the Company provides marketing assistance services that range from new customer acquisition to customer cultivation for clients operating EC sites focused on B&H and food markets as market fields.

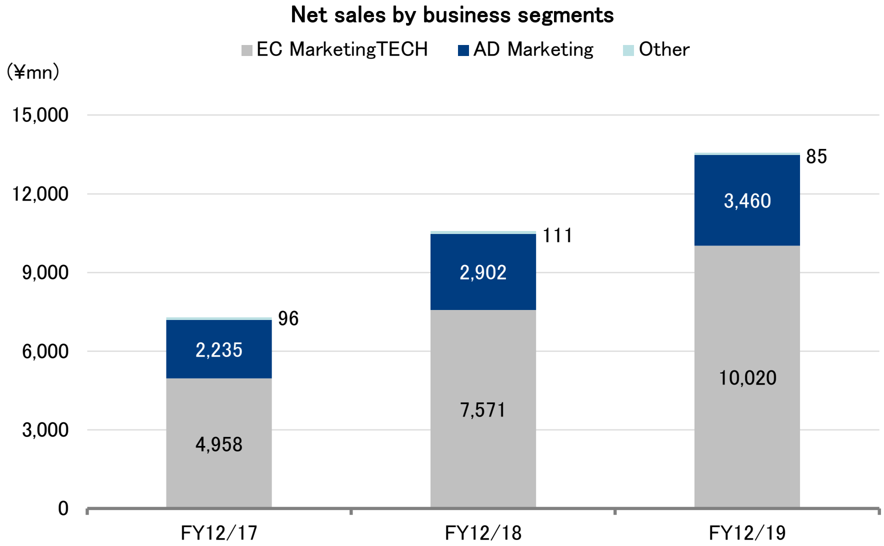
> * This term is a redefined version of "digital transformation," the concept of IT inroads changing people's lives in a positive direction in all respects, applied to the Company's Group business foundation. The EC environment has dramatically progressed over the past few years, including changes in purchasing behavior and communications due to wider smartphone use, SNS utilization, advances in ad technology, and ability to utilize major shopping mall IDs on self-run EC sites. Meanwhile, responses to these changes in the EC environment require corresponding costs and knowledge.

The Company's services consist of EC MarketingTECH* and AD Marketing segments, and EC MarketingTECH is the primary service area accounting for 73.9% of overall sales in FY12/19. The others segment includes sales from wholesale operation agent service for overseas B&H and food areas.

> * This term combines marketing and technology. It refers to optimization of marketing with technology and also technologies that make this possible, including MA tools, EC cart systems, and other solutions as well as DMP and AI.

These businesses focus on B&H and food industries because of the prospect of stable growth in these markets, driven by heightened interest in health and beauty, including anti-aging measures and preventive medicines, as the senior population continues to expand for the time being, in contrast to the downward trend in Japan's overall population. The Company believes it can deliver marketing measures for creating hit products with high reproducibility by analyzing consumer "concerns and purchasing activity" and other big data (DMP (*) by user concern) that it has accumulated up to now and utilizing AI technology. This knowhow differentiates it from rivals and is enabling to sustain growth.

> * DMP (Data Management Platform): This is a platform that manages a variety of information data accumulated online. The DMP enables segmentation of gathered information and supports one-to-one marketing measures tailored to individual customers.

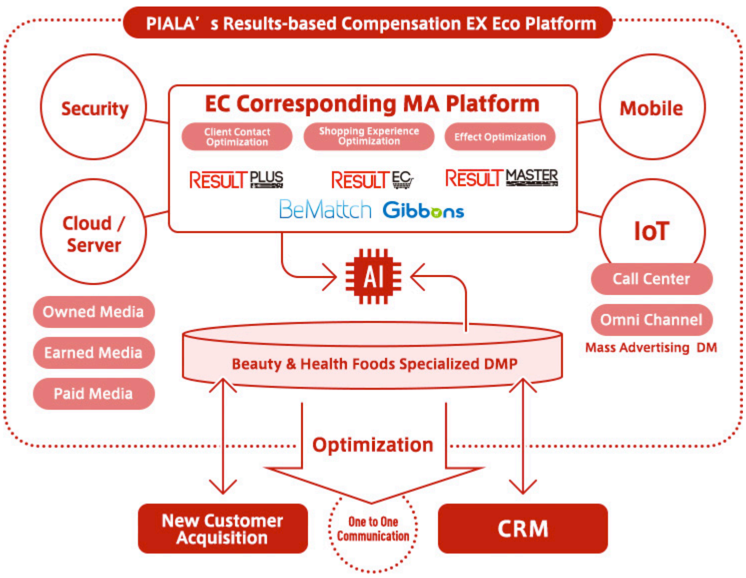


Source: Prepared by FISCO from the Company's financial results and securities report

a) EC MarketingTECH

EC MarketingTECH provides KPI commitment services using the Company's self-developed RESULT series for mail-order companies in B&H and food areas. Clients, the Company, or both sides utilize the DMP that accumulates data by user concerns in B&H and food areas, based on knowhow from cumulative marketing assistance for over 800 companies and proprietary data collection, and the RESULT series, mainly RESULT MASTER equipped with AI functionality. The advantage of data accumulation by user concerns is the ability to offer marketing measures that are most suited to individual customer products using AI because it not only acquires and manages data in real time on characteristics of selected products from data collected by social media, but also adds tags to specific concerns of users, such as "blotches" and "wrinkles." Roughly 80% of new clients are introductions from existing clients, advertising agencies, inquiries, partners, and others.

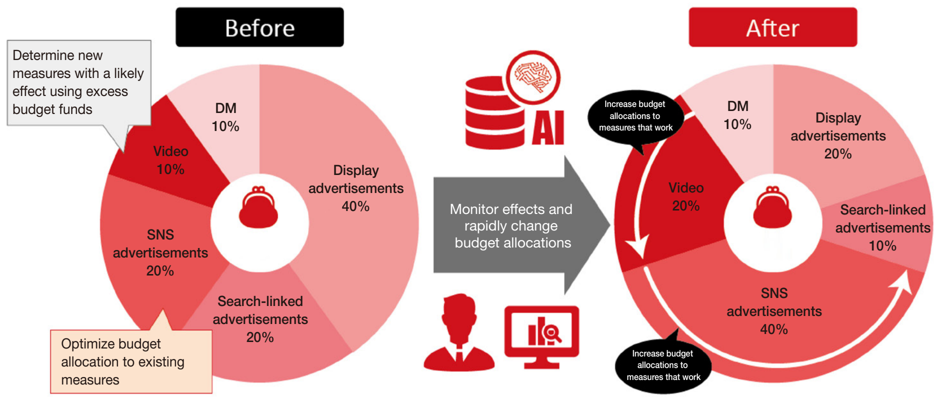
Marketing platform with KPI commitments



Source: The Company's results briefing materials

The Company provides “KPI commitment service” that makes a commitment to results as the basis for compensation in marketing assistance service. KPI commitment, meanwhile, refers to the Company’s guarantee of a “new customer acquisition unit price” incurred to acquire new customer purchases of client company’s products. For example, after initially negotiating with the client and setting a “new customer acquisition unit price,” which serves as the KPI, the Company decides the advertising method, such as targeted media (portal sites, social media, YouTube and other video media, etc.), affiliates, and display ads, based on marketing budget allocation optimized using information from RESULT MASTER and knowhow accumulated on its own (including assessments by people), and places advertisements. The advertising method incorporates new technologies and methods for 10–20% because the Company believes it is important to accumulate data by user concerns on all advertising methods (recently video ads in which Vtubers introduce products via real images have been eliciting a larger response). When new customers purchase client products as a result of these marketing measures, the Company receives performance compensation calculated as “number of new buyers x new customer acquisition unit price” and books this amount as revenue. The rate plan begins at a minimum of ¥500,000 per deal. While the Company also offers a variety of other KPI besides new customer acquisition, such as subscription purchase plan sign-ups, dormant customer buying restarts, and existing customer cultivation, most of its current business utilizes new customer acquisition as the KPI. Customer cultivation KPI has been trending upward recently. In H&B and food industries, where the Company focuses, along with new customer acquisition, customer cultivation is also important. Efforts to cultivate existing customers leverage the Company’s marketing knowhow.

Optimization of budget allocation for KPI commitments



Source: The Company's results briefing materials

From the client perspective, cost performance is confirmed ahead of time because the client only pays a certain predetermined amount for acquisition of a single new customer. Ordinary marketing assistance services decide on a promotion budget and carry out advertising within this framework. Results hence do not attain initial goals in some cases. Cost performance declines if this happens. In KPI commitment service, clients avoid this risk because payments are tied to results (new customer acquisition volume). The format therefore is very accessible to clients as well.

Advertising placement fees for various media comprise the bulk of Company costs and are booked as outsourcing expenses of unit costs. Main media include Google, Yahoo!, LINE, and Facebook. While Yahoo! was at roughly 40% of advertising costs through FY12/18, its share has dropped substantially since December 2018 due to restrictions applied to advertising in the B&H area. Additionally, profit margin fluctuates at the level of individual promotion deals (gross margin ranges from 3% to 30%) because of variation in required costs in the performance-based revenue model. The Company implements measures to mitigate business risk, such as "not guaranteeing the number of customer acquisitions" in KPI commitments and installing a cost-cutting tool for cases in which initially anticipated marketing results have not materialized (when cumulative loss value exceeds a certain level in cases without results after a defined period, etc.) that automatically halts activities. Even when the cost-cutting tool is triggered, the Company retains its trust relationship with the subject client and pursues promotions again using a different product.

b) AD Marketing

AD marketing is marketing assistance service that does not use the RESULT series. It largely covers flyer and pamphlet placement in mail-order company newsletters and products, enclosed concierge service sent to certain users, and DM advertising service. Other services include telemarketing, real event promotions, and buzz marketing utilizing influencers.

The most of this business model charges fixed-value compensation (fees) unrelated to marketing assistance service results. Recently, however, the Company has reached a stage of shifting to KPI commitment service that charges compensation according to results with KPIs based on client issues and budgets.

Results trends

Double-digit sales and profit increases in FY12/19, setting all-time highs again

1. Overview of FY12/19 results

In FY12/19 consolidated results, the Company reported ¥13,566mn in net sales (+28.2% YoY), ¥408mn in operating profit (+25.6%), ¥407mn in ordinary profit (+35.4%), and ¥311mn in profit attributable to owners of parent (+61.8%). Sales rose in a 13th straight year and roughly tripled in the past four years amid rapid expansion. The Company posted all-time highs, including at the various profit levels.

FY12/19 results (consolidated)

(¥mn)

	FY12/18		FY12/19				
	Results	% of net sales	Forecast	Results	% of net sales	YoY change	vs. forecast
Net sales	10,585	-	12,775	13,566	-	28.2%	6.2%
Gross profit	1,869	17.7%	-	2,217	16.3%	18.6%	-
SG&A expenses	1,544	14.6%	-	1,809	13.3%	17.1%	-
Operating profit	324	3.1%	395	408	3.0%	25.6%	3.3%
Ordinary profit	300	2.8%	389	407	3.0%	35.4%	4.6%
Extraordinary loss	-48	-	-	-5	-	-	-
Profit attributable to owners of parent	192	1.8%	273	311	2.3%	61.8%	14.1%

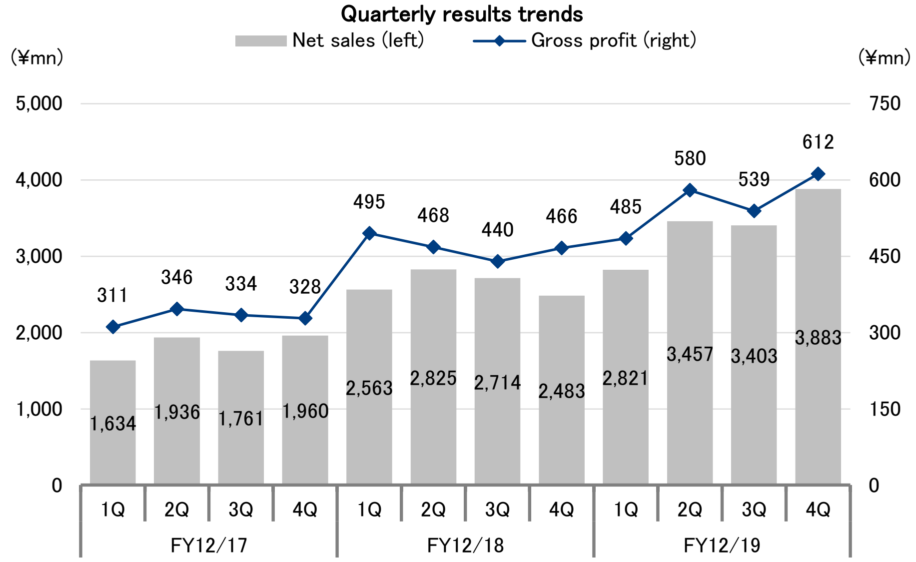
Source: Prepared by FISCO form the Company's financial results

Main drivers are sustained expansion of B&H and food markets in Japan and steady pick-up in marketing measures utilizing the Internet and SNS at mail-order companies. The Company focuses on KPI commitment service in this market environment, and its continuing creating of hit products offers a unique growth source. In FY12/19, Regain Triple Force, a supplement from mail-order sales operator and Daiichi Sankyo Co., Ltd. <4658> group firm Im Co., Ltd. that mainly handles cosmetics and health foods was a major hit, and sales from Im expanded 3.1-fold YoY to ¥2,778mn. Since hits in the B&H market normally last for about three years, we expect strong sales again in 2020. Average sales value per purchase has been steadily rising as well and appears to have climbed by about 1.5-fold over three years.

Gross margin dropped from 17.7% in the previous fiscal year to 16.3%, mainly because of higher advertising media costs and increase in depreciation costs to strengthen EC MarketingTECH capabilities. Even though SG&A expenses expanded 17.1% YoY on higher personnel costs accompanying increase in employees, a rise in rent related to the headquarters move, and upturn in depreciation costs from purchase of non-current assets, the SG&A expenses ratio fell by 1.3ppt due to growth in sales. The number of employees on a consolidated basis at the end of the period increased 31 YoY to 168. Stronger growth in profit attributable to owners of parent is the main source of improvement in extraordinary income.

Looking at quarterly trends, the Company sustained healthy momentum with a 56.3% YoY increase in net sales to ¥3,883mn and a 31.3% gain in gross profit to ¥612mn in 4Q (Oct-Dec 2019).

Quarterly results trends



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

Stable financial conditions with the capital ratio in the 44% range, reached positive retained profit too

2. Financial condition

In financial conditions at the end of FY12/19, the Company reported ¥4,202mn in total assets, an increase of ¥1,089mn from the end of FY12/18, Main changes in current assets were an increase of ¥551mn in trade receivables accompanying sales expansion and an increase of ¥168mn in cash and deposits. Non-current assets changes included increases of ¥72mn in property, plant and equipment related to the headquarters move and space addition, ¥62mn in leasehold deposits, and ¥259mn in investment securities.

Total liabilities rose by ¥764mn from the end of FY12/18 to ¥2,333mn, including additions of ¥365mn accounts payable - trade related to increase in the business volume and ¥411mn in interest-bearing debt. Net assets increased by ¥324mn to ¥1,869mn, mainly on a ¥311mn increase in profit attributable to owners of parent. Retained earnings reached positive territory at ¥205mn.

In management indicators, even though the interest-bearing debt ratio expanded from 29.6% at the end of the previous fiscal period to 46.5% on increase in interest-bearing debt, the capital ratio remained at a stable level of 44.4%, including support from funds raised in the IPO in December 2018. In profitability, while operating margin was low at 3.0%, ROE and ROA stayed above 10%, despite slight declines from previous-year levels, at 18.3% and 11.1%, respectively. Operating margin is unlikely to improve much because of the high percentage of advertising media costs in unit costs. Nevertheless, the Company is targeting increase to about 5% as a near-term goal (and is ultimately aiming for 10%) through improved productivity utilizing AI and sales expansion.

Consolidated balance sheet

(¥mn)

	FY12/17	FY12/18	FY12/19	Change
Current assets	1,418	2,733	3,460	726
(Cash and deposits)	444	1,444	1,613	168
(Trade receivables)	837	1,210	1,762	551
Non-current assets	211	379	741	362
Total assets	1,629	3,112	4,202	1,089
Total liabilities	1,264	1,568	2,333	764
(Interest-bearing debt)	309	456	868	411
Total net assets	364	1,544	1,869	324
(Retained earnings)	-298	-106	205	311
Management indicators				
(Stability)				
Shareholder equity ratio	22.3%	49.6%	44.4%	-5.2pt
Interest-bearing debt ratio	85.1%	29.6%	46.5%	16.9pt
(Profitability)				
ROA	2.6%	12.7%	11.1%	-1.6pt
ROE	19.4%	20.2%	18.3%	-1.9pt
Net sales operating profit margin	0.4%	3.1%	3.0%	-0.1pt

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

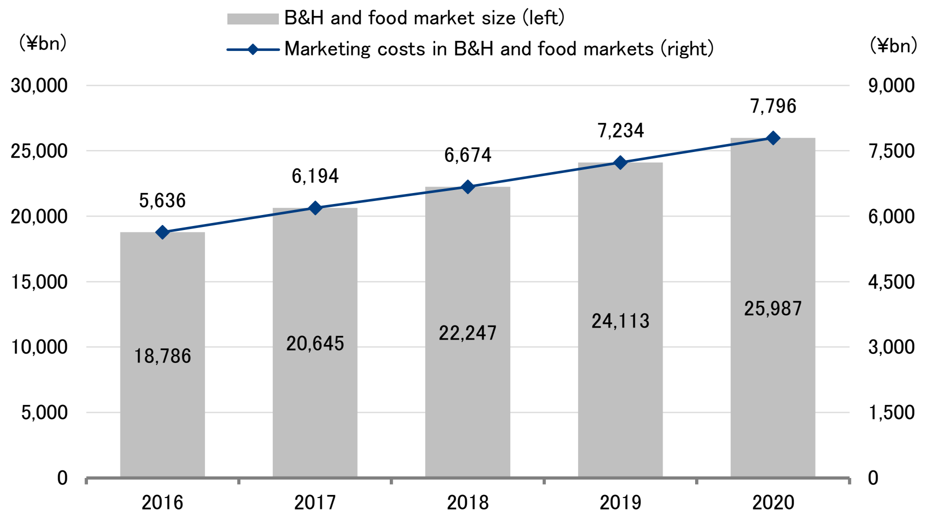
Future initiatives

Stable growth likely to continue in B&H and food markets, tailwind from DX advances in the mail-order industry

1. Market environment

Mail-order and EC market value in B&H and food industry areas targeted by the Company grew from ¥1.8trn in 2016 to ¥2.5trn in 2020 and is likely to sustain stable growth at a rate of around 7% a year. Going forward, it is likely to sustain stable growth in the single-digit range annually against a backdrop of increasing potential customer volume due to aging society advances, growing awareness of health, and widening engagement of women in society. The Company estimates that marketing costs invested by these mail-order and EC companies are about 30% of sales and expects a total market of over ¥700bn for the industry in 2020. In particular, the number of companies putting emphasis on digital marketing measures has risen over the past few years amid EC market expansion and we expect continuation of double-digit growth in the digital marketing segment.

B&H and food market size in mail-order and EC industry

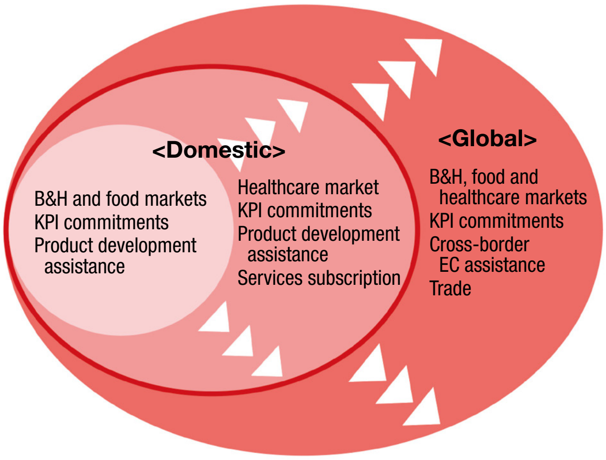


Note: This is a total value for “beauty and others,” “health foods and drugs,” and “food and direct products” markets. The 2018 value is an estimate, and values from 2019 are forecasts. PIALA calculated marketing costs.
Source: Market size prepared by FISCO Inc. from Fuji Keizai’s “Current state of mail-order and e-commerce business and outlook for 2019”

Healthcare industry outlooks indicate rapid expansion in the domestic market from ¥16trn in 2013 to ¥26trn in 2020 and ¥37trn in 2030 as markets for preventive care, health management services, and other areas steadily progress alongside aging society advances. The Company hence intends to bolster marketing assistance for goods and services companies, including preventive medicine.

The global cross-border EC market also continues to grow at an annual rate of over 20% since 2015 against a backdrop of advances in globalization and economic growth in developing countries, and some forecasts project expansion to $994bn in 2020. Additionally, many Japanese companies want to expand sales in China and other parts of Asia. We see large growth potential for the Company with its cross-border EC assistance business.

Medium-term expansion of strategic markets



Source: The Company's results briefing materials

Aims to achieve roughly 20% annual sales growth and at least 5% operating margin in the medium-term management plan

2. Medium-Term Management Plan

(1) Numerical targets and basic policy

The Company announced a three-year medium-term management plan that starts in FY12/20. Numerical goals (consolidated) are at least ¥23.5bn in net sales, ¥1.2bn in operating profit, and 5% operating margin in FY12/22. It intends to allocate ¥1bn over a three-year period as business investments in growth. Other investments are ¥500mn for IT investments (AI investments, business mission-critical systems, etc.) and a ¥1.5bn budget for capital alliances, M&A, and other initiatives.

Numerical targets for Medium-Term Management Plan

	FY12/19	FY12/22
Net sales	¥13,566mn	¥23.5bn or more
Operating profit	¥408mn	¥1.2bn
Operating profit margin	3.0%	5% or more
Business investment		Three-year total
New business investment and internal investment		¥1.0bn
IT investment (AI investment, ERP, etc.)		¥0.5bn
Capital alliance, M&A, etc.		¥1.5bn
Financial strategy	Procuring funds mainly through interest-bearing debt while managing the capital ratio Also reviewing fund procurement from the market as needed for investment projects	
Shareholder equity ratio	40%	
ROE target	20%	

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

The Company seeks high growth with its unique business model of KPI commitment service that leverages its planning capabilities in marketing measures with robust reproducibility and cost performance utilizing data on concerns and adaptability that is capable of providing one-stop services of new customer recruitment, customer cultivation, and overseas initiative assistance. In particular, it plans to place even more emphasis than previously on "consumer concerns (needs)," actively identify products and services that are needed, and implement marketing assistance while jointly developing these products and services in some cases.

One example is the initiative with SARABiO Cosmetics with which the Company formed a capital and business alliance in December 2019. SARABiO is a biotech company with headquarters in Oita Prefecture. It researches hot spring microorganisms and develops, manufactures, and sells skin care products that utilize anti-inflammatory, anti-oxidation, and anti-glycation qualities of "hot spring algae R." Annual sales are just over ¥600mn. Despite having a high repeat rate for its products, marketing was an issue and sales slowed. The Company acquired a 6.8% stake and is handling all of SARABiO Cosmetics' marketing with the hope of realizing a hit with existing products. Furthermore, it intends to pursue joint development of OEM products that utilize "hot spring algae R" technology based on its BEATMAKER service*. It will continue to arrange similar initiatives with other local companies that possess attractive technologies and products.

* This is a service launched in July 2019 that provides support from the customer's product development stage and creates successful products. It uses a business model of free provision of work related to product development and income acquisition through KPI commitment service. The Company aims to absorb development costs by raising the hit rate from about 25% for existing projects to 30-40% through development and sales of carefully selected products with needs. The development period takes about six months to a year, and the Company is currently conducting projects with roughly 10 companies.

(2) Business strategy overview

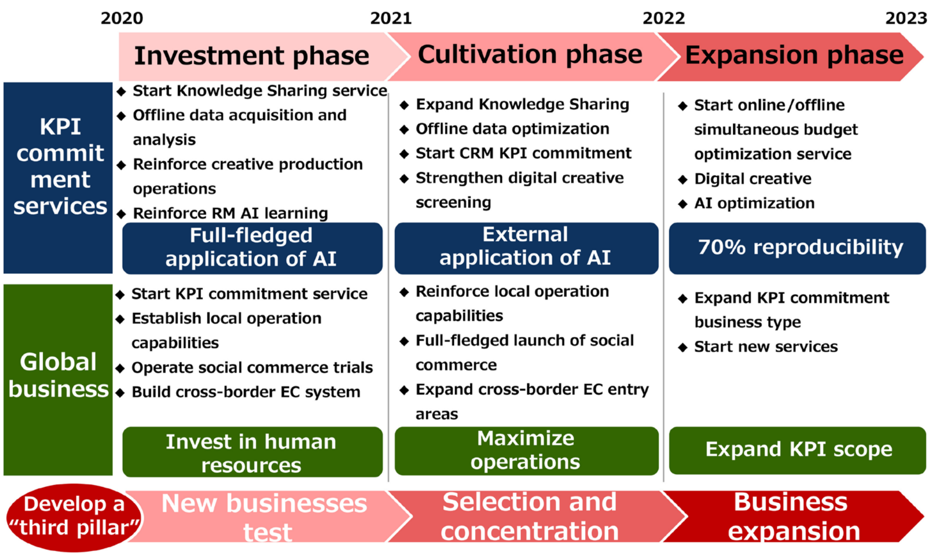
The Company plans to invest ¥1bn over three years (¥500mn in the final fiscal year) in multiple areas that contribute to improved growth potential and profitability, including new businesses. Specific investment themes include promoting OMO*, new business Knowledge Sharing, and AI/RPA development in marketing tech and maximization of site operation, expansion of trade and other related services, and reinforcement of social commerce (collaborating with influencers, etc.) in global solutions. It hopes to broaden the scope of KPI commitment service, accelerate growth, and raise profitability with these investments.

* OMO (Online Merges with Offline): This is a marketing concept of merging online and offline activities. Related measures aim to enhance the user experience by converting all user experiences into data without delineating between the Internet and real world.

The business strategy roadmap for the three years outlines execution of various measures with an investment phase in the first fiscal year, a cultivation phase in the second fiscal year, and expansion phase in the third fiscal year.

Future initiatives

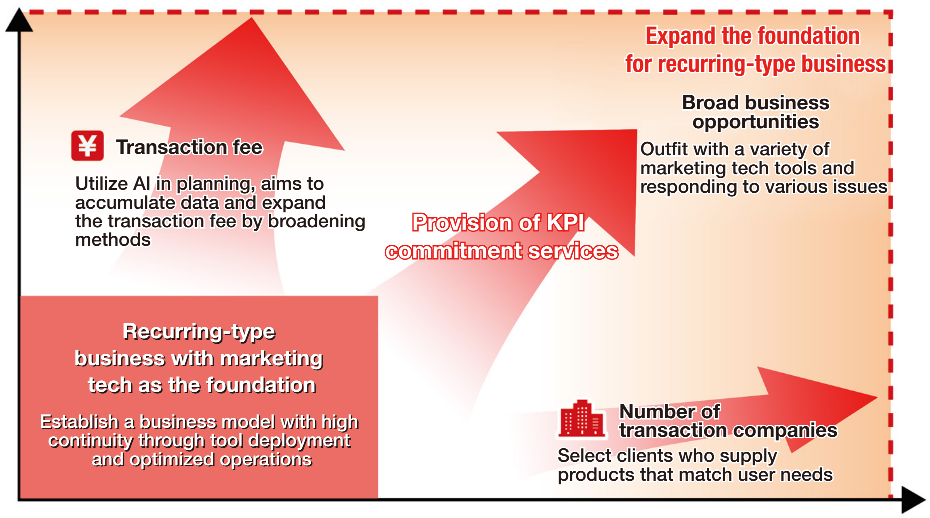
Three-year strategy roadmap



Source: The Company's results briefing materials

KPI commitment service promotes "increase in customer volume x average user spending" by applying "data on concerns x AI," and the Company aims to accelerate growth through expansion of Knowledge Sharing and OMO promotion (digitalization of offline data) as explained below. With AI, it wants to maximize the effect of KPI guarantees and enhance reproducibility by optimizing budget allocation and broadening methods with a combination of multiple technologies and automating the creative area of operations. The Company is developing AI technology while also utilizing technology from other firms. While reproducibility is currently about 30-40%, it hopes to raise the level to about 70% even for new university graduates in three years from now and thereby enhance productivity in the operations division.

Basic growth strategy of KPI commitment services



Source: The Company's results briefing materials

In global business, meanwhile, the Company assists overseas entry mainly for cross-border EC and promotes expansion of B&H specialty wholesale operation agent service. While global business is still only likely to be about 5% of overall sales in FY12/20, the Company wants to increase its share to at least 10% over three years. It intends to establish a highly profitable model through provision of one-stop solutions. It will also pursue new business creation with the aim of cultivating a third major income pillar. Specifically, it will cultivate healthtech-related business that uses proprietary data and marketing tech.

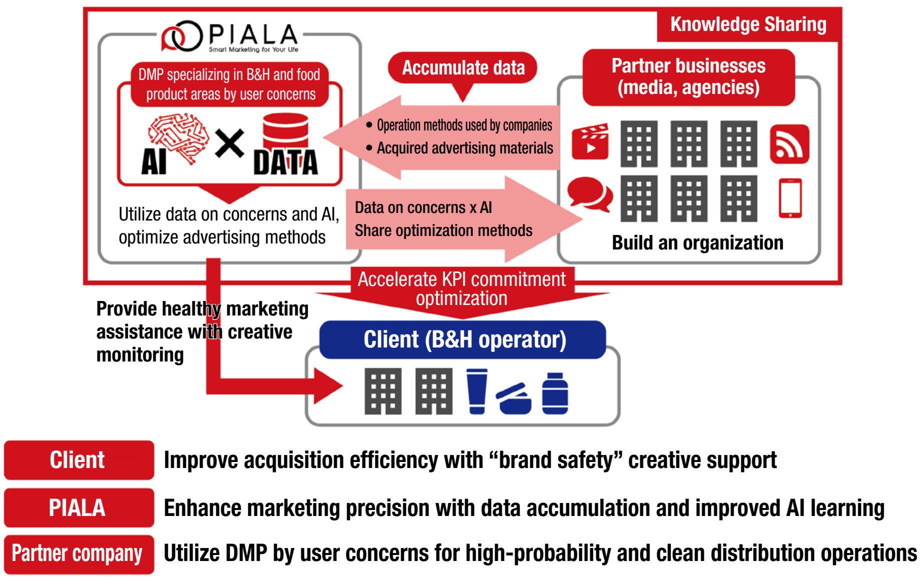
In personnel strategy, it intends to continue to hire about 20 people annually. Since this puts the increase rate in the 10% range, sales and profit per employee should rise. The Company is targeting upstream consultants and engineers as areas for reinforced hiring. It currently has about 10 upstream consultants and will be adding more people in this area over the longer term as a core growth source. The Company also plans to actively hire global human resources in order to expand global business.

(3) Promotion of Knowledge Sharing and OMO

a) Knowledge Sharing

The Company faces a resources issue of not having enough capacity to deal with rapid growth in KPI commitment service inquiries. Knowledge Sharing is a new service that aims to resolve this issue and accelerate growth. The Company hopes to achieve more optimization of KPI commitment service by organizing advertising agencies, peers, and other attractive partners capable of collaborating and mutually sharing knowledge. It promotes faster optimization by opening up the proprietary DMP by user concerns to partners and conducting AI learning together with partner knowhow and data. This initiative seeks to facilitate implementation of marketing measures with about 70% reproducibility by anyone over the medium term. In this service, the Company uses KPI guarantee service contracts with client customers and shares revenue with partners. It is already conducting trial projects with multiple companies.

Knowledge Sharing mechanism



Source: The Company's results briefing materials

b) Promoting OMO

Since the B-to-C market's product purchase ratio through sales at real stores and other non-EC channels is about 94%, this market still offers large opportunities. The Company aims to bolster KPI commitment service in this market through promotion of "data conversion x technology" with real experiences, telemarketing, and other activities. Since 2018, it has been conducting demonstration sales of cosmetics, supplements, and other products at post offices and expanded location scope to major supermarkets, department stores, home centers, bathing facilities, and other sites. The marketing style of collecting data on consumer concerns (knee and lower back pain, etc.) with questionnaires and recruiting purchases by having people actually use products has done well. The Company plans to utilize data obtained from questionnaires in devising measures for existing businesses and in developing healthcare-related business that it aims to pursue as new business. While face-to-face promotions have stopped due to COVID-19 impact, the Company is reviewing promotions and other activities that utilize IT capabilities.

Minimal impact by the COVID-19 outbreak, guides for double-digit sales and profit growth again in FY12/20

3. FY12/20 outlook

In FY12/20 consolidated guidance, the Company targets ¥15,865mn in net sales (+17.0% YoY), ¥531mn in operating profit (+30.1%), ¥518mn in ordinary profit (+27.3%), and ¥351mn in profit attributable to owners of parent (+12.9%), projecting continuation of double-digit sales and profit growth. It projects a 1.4ppt YoY rise in gross margin on increase in the presence of highly profitability services in business mix with an outlook for sustained high growth in KPI commitment services. In SG&A expenses, it expects a 26.0% YoY increase on higher personnel costs and development expenses.

FY12/20 outlook (consolidated)

(¥mn)

	FY12/19		FY12/20				
	Results	% of net sales	1H forecast	YoY change	Full year forecast	% of net sales	YoY change
Net sales	13,566	-	7,505	19.5%	15,865	-	17.0%
Gross profit	2,217	16.3%	-	-	2,811	17.7%	26.8%
SG&A expenses	1,809	13.3%	-	-	2,279	14.4%	26.0%
Operating profit	408	3.0%	169	4.2%	531	3.3%	30.1%
Ordinary profit	407	3.0%	164	0.3%	518	3.3%	27.3%
Profit attributable to owners of parent	311	2.3%	107	-8.8%	351	2.2%	12.9%

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

At this point, there is almost no results impact by the COVID-19 outbreak. Despite suspending face-to-face real-world promotions and some temporary sales suspensions due to supply-chain issues at client companies, the Company has been benefitting from increase in product scope, such as masks and hand gels, and lower media costs amid softer supply-demand conditions in the Internet advertising market. Furthermore, economic fluctuations have less impact on B&H and food segments targeted by the Company. We hence anticipate sustained double-digit growth in FY12/20.

The Company launched the "#SAVE YOUR LIFE" project with a mission of delivering hygiene products at reasonable prices to as many consumers and medical entities as possible amid persistent hygiene product shortages and inflated pricing due to the COVID-19 outbreak. In May, it started sales on a dedicated EC site of non-woven masks for companies and medical, care, and child-rearing businesses and high-performance KN95 masks for medical, care, and child-rearing businesses. The Company is conducting initiatives that utilize its knowhow cultivated in product development activities and cross-border EC and trade businesses as a firm that provides assistance in the H&B market. It plans to donate some profits to medical entities and others.

As new initiatives, besides marketing assistance for SARABiO Cosmetics explained above, the Company formed a business alliance with Son Kim Retail, the retail management company of Vietnamese conglomerate Son Kim Group, in February 2020 to provide sales assistance for Japanese products in B&H and food areas. It also announced plans for product development in the B&H market based on BEATMAKER and selling efforts through Son Kin Group's sales channel.

Son Kim Retail has an EC site, TV shopping business, convenience stores, and other sales channels. The TV shopping business broadcasts to all cities through leading broadcast stations. While it has strong sales capabilities in real-world stores, EC site sales are relatively weak and digital marketing faced issues. The Company aims to support EC sales and offline sales of Japanese companies in Vietnam by providing assistance in digital marketing. It plans to begin sales of about 10 items, including cosmetics, facial care devices, and supplements and is currently working through review procedures for TV shopping. The process takes roughly three months. TV shopping, digital marketing, and other promotions should proceed once it finishes. The Company is working to expand sales of high-quality Japanese products in China, Taiwan, Vietnam, Thailand, and other countries and hopes to become the No.1 marketing assistance company to B&H and food markets for Asia.

Shareholder return policy

Near-term priority on accumulating retained earnings and investing in growth

The Company's shareholder return policy fundamentally targets accumulation of retained earnings needed for future business initiatives and reinforcement of financial standing alongside sustained payment of stable dividends. At this point, however, management expects profit expansion driven by aggressive business investments to enhance shareholder value considering the limited amount of retained profits and other funds for dividends and its current investment phase timing for realizing business growth. From this perspective, the Company retains its stance of not paying a dividend again in FY12/20. It intends to consider shareholder return measures while keeping a balance with retained earnings in light of a comprehensive assessment of profits trends, financial standing, business investment plans, and other aspects.

FISCO

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