COMPANY RESEARCH AND ANALYSIS REPORT

Sanyei Corporation

8119

TSE JASDAQ

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Summary

Targeting ¥50bn in sales and ¥1.9bn in ordinary income in FY3/19 Expects higher sales and profits in all segments, accelerating rollout of new brands as part of the medium-term business plan and started handling KERBHOLZ, the environmentally conscious brand of watches from Germany

Sanyei Corporation <8119> is a trading company specializing in high-value-added products with a history of over 70 years. It carries a full range of consumer lifestyle products and covers an expansive supply chain spanning manufacturing, imports and exports, wholesale, and retail. It has 19 overseas locations and 83 domestic directly managed retail stores. The Company stands out in terms of its coverage of products with high added value, including the introduction of differentiated European brands to Japan and OEM supply of unique products to customers, such as Ryohin Keikaku Co., Ltd. <7453>, which operates MUJI. It has three main business segments – Furniture and Houseware Business (51.6% of overall sales), Fashion Accessories Business (30.6%), and Home Appliance Business (12.7%).

1. Business description

The Furniture and Houseware Business has been driving the Company's growth in recent years. OEM business is a very large percentage of segment sales at about 94%, and expansion of business at large customers, such as Ryohin Keikaku (MUJI), has been an important factor supporting growth. After reaching ¥27,431mn in FY3/17, sales slipped to ¥23,053mn in FY3/18 due to non-recurrence of spot orders by a major European customer, shrinkage of sales to a US volume retailer, and other impacts, but OEM business should remain the core component. The Company's own MINT e-commerce brand is a fast-growing brand sold via the Company's shopping sites on, Rakuten and Yahoo! and posted a vibrant 1.5-fold increase YoY in FY3/18 sales. At the same timing as expiration of exclusive import agent contracts with two brands (WMF and Silit) in the Furniture and Houseware Business, the Company started handling Villeroy & Boch as a new housewares brand in October 2017. This is a traditional German brand coming up on its 270th year in business. The Company will be booking results for a full fiscal year in FY3/19. We will be looking for steady market inroads of the brand.

Brand business has a substantial presence in the Fashion Accessories Business. The largest brand the Company handles in Japan is BIRKENSTOCK, which makes sandals and comfort shoes with excellent functional beauty and has a tradition of more than 240 years in Germany. It is supported by an enthusiastic fan base. The products are sold via 63 directly managed stores and e-commerce. The Company offers after-sales services because many customer use the products for lengthy periods. The Company opened three stores, including a store at the LAZONA Kawasaki mall, in FY3/18. Although the past boom in BIRKENSTOCK footwear has settled down, the Company has located shops in retail facilities with strong customer draw, and the business performance has been trending firmly. Kipling is a brand of nylon bags that was created in Belgium, and together with the Kipling monkey (its mascot), it is famous throughout the world as a playful, casual brand. The brand operates this business via nine directly managed stores (including the Ginza store and outlet stores) and at about 60 major department stores across Japan. While the appearance of parallel imported products adversely affected results in recent years, the Company's countermeasures are gradually beginning to make a positive effect in FY3/19.

2. Results trends

The Company reported weaker sales and profits in FY3/18 consolidated results with ¥44,692mn in net sales (-10.2% YoY), ¥1,683mn in operating income (-37.8%), ¥1,832mn in ordinary income (-24.8%), and ¥832mn in profit attributable to owners of parent (-41.7%). Sales declined on an increase in the percentage of products in the mature phase of the product lifecycle in Japan and abroad in the OEM business, which accounts for about 70% of overall sales. Additionally, lower sales to a North American volume retailer, non-recurrence of spot orders from a European client in the previous fiscal year, and other factors affected OEM activity in the Furniture and Houseware Business. Even with the sales and profit setbacks in FY3/18, the Company posted its third highest sales and fourth highest ordinary profit in the past 20 years, and has sustained high levels from a long-term perspective.

The Company expects higher sales and profits in FY3/19 consolidated results with ¥50,000mn in net sales (+11.9% YoY), ¥1,900mn in operating income (+12.8%), ¥1,900mn in ordinary income (+3.7%), and ¥1,200mn in profit attributable to owners of parent (+44.1%). It forecasts the largest gains in Furniture and Houseware Business and Fashion Accessories Business. Key anticipated growth sources in the former are overseas OEM business recovery, advances in e-commerce direct-sales MINT furniture, and a full-year contribution from the new Villeroy & Boch brand. The latter’s main drivers should come from reinforcement of special events, besides direct-operation stores, in the BIRKENSTOCK business and a positive effect of measures to deal with parallel imported Kipling products. It might even be possible to attain the medium-term business plan’s goal of ¥2bn in ordinary profit in FY3/19, the second year. Yen appreciation in the first half of 2018 is likely to provide a tailwind.

3. Growth strategy

The Company is currently implementing a medium-term business plan with FY3/18 as the first fiscal year and FY3/20 as the final fiscal year. As a quantitative goal, it hopes to build a foundation to generate at least ¥2bn in ordinary profit on a steady basis by FY3/20. While it missed income targets in FY3/18, the first fiscal year, we think its strategies achieved healthy progress. Under new challenges, it started operations and gained rights to deal with new brands in brand business. In governance, it moved forward with preparations for deployment of a core business system (SAP) and intends to launch it at the parent level in July 2018 and then incrementally deploy it at group companies. This system should help accelerate decision-making and improve business efficiency.

The Company began handling products in Japan from KERBHOLZ, a German brand of watches, in June 2018. KERBHOLZ, which was founded in 2012, sells watches that use wood and other natural materials. Its products are sold at over 350 stores in 10 countries worldwide. The brand stands out with its emphasis on the environment, including use of carefully selected natural materials and contribution of 10% of profits to resource conservation projects. It also offers simple but fashionable forms and has received the GERMAN DESIGN AWARD, a highly respected award in Germany, in two straight years and numerous other awards. The Company plans to start handling products from WOLL, a German brand of cooking utensils, in September 2018. It is making progress with rollouts of new brands.

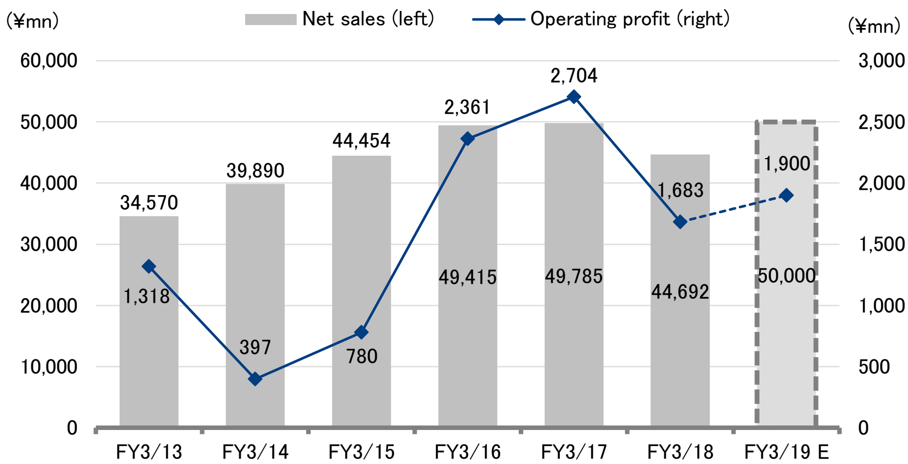
4. Shareholder return policy

The Company paid a ¥160 dividend in FY3/18 (¥60 in 1H and ¥100 in 2H), putting it at a 45.9% dividend payout ratio. It guides for ¥160 in FY3/19 too (¥60 in 1H, ¥100 in 2H) for a 31.9% payout. Stable dividends are an appeal since the Company has continuously raised or maintained its dividend in the past 21 years.

Key Points

- Primarily OEM business in the mainstay Furniture and Houseware Business, with healthy potential for the MINT e-commerce store and new-brand Villeroy & Boch as well
- Targets ¥50bn in net sales and ¥1.9bn in ordinary income in FY3/19, expects higher sales and profits in all segments
- Accelerating rollout of new brands as part of the medium-term business plan and started selling the KERBHOLZ environmentally conscious brand of watches from Germany

Full-year results trends



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

Company profile

A multi-functional trading company specializing in high-value-added products based on the concept of “Bringing fabulous products from the world to the world.”

1. Company profile and history

Established in Osaka in 1946 as an exporter of accessories, the Company has a history of more than 70 years. Today, it carries a full range of consumer lifestyle products and covers an expansive supply chain spanning manufacturing, imports and exports, wholesale, and retail. It has grown to be a multi-functional trading company with 19 overseas locations and 83 domestic directly managed retail stores. The Company stands out in terms of its coverage of products with high added value, including the introduction of differentiated European brands to Japan and OEM supply of unique products to customers, such as Ryohin Keikaku (MUJI). The Company is a global enterprise that manufactures products at overseas sites and sells them in overseas markets, based on the concept of “Bringing fabulous products from the world to the world.”

2. Business composition

The Company operates under the following business segments – Furniture and Houseware Business, Fashion Accessories Business, Home Appliance Business, and Others. The Furniture and Houseware Business mainly procures OEM products for major Japanese and foreign companies, with the proprietary e-commerce brand MINT also gaining momentum. This segment provided 51.6% of overall sales and 58.8% of operating profit in FY3/18. The Fashion Accessories Business covers import sales of brand products with sales rights, such as BIRKENSTOCK (sandals and shoes) and Kipling (bags), and domestic and overseas OEM business. It contributed 30.6% of sales and 27.3% of operating profit. The Home Appliance Business handles OEM product procurement and brand business. Major brands are Vitantonio (cooking appliances) and mod's hair (beauty appliances). This segment generated 12.7% of sales and 11.6% of operating profit. The Others segment handles pet goods and other items and was at 5.1% of sales and 2.3% of operating profit.

Business description and percentages (1H FY3/18)

Business segment	Descriptions of the main businesses	Percentages of net sales	Percentages of operating profit
Furniture and Houseware Business	OEM for Ryohin Keikaku (MUJI) and WMF (kitchen goods manufacturer)	51.6%	58.8%
Fashion Accessories Business	BIRKENSTOCK (sandals) and Kipling (bags) and OEM for domestic and overseas retail stores, etc.	30.6%	27.3%
Home Appliance Business	Vitantonio (cooking appliances) and mod's hair (beauty appliances), and OEM for domestic and overseas manufacturers and retail stores	12.7%	11.6%
Other	Pet merchandise, pets, etc.	5.1%	2.3%

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

The Company has two business models: brand business and OEM business. The brand business mainly promotes wholesale and retail activity in Japan for overseas brands and the Company's own brands. It has a generally higher profitability than the OEM business because it carries excellent brands with strong histories that have not yet been introduced in Japan. The Company aims to expand the brand business from 27.7% of total sales in FY3/18 to about 40% in future years. The OEM business provides various procurement services, such as review of product specifications for products that meet the needs of client companies, plant selection, price negotiation and production schedule adjustment, production management, and export/import and logistics. The Company has strengths in the manufacturing network in Asia built through overseas initiatives over many years and production management by its own staff. Historically, the Company has developed its brand business using the knowledge and experience of overseas business it cultivated in the OEM business, and currently there are synergistic effects in various aspects.

Business model content and composition

	Descriptions of the main businesses	Percentages of net sales
Brand business	Wholesale and retail activity for overseas brands and proprietary brands	27.7%
OEM business	Provide procurement services such as review of product specifications for products that meet the needs of client companies, plant selection, price negotiation and production schedule adjustment, production management, and export/import and logistics	72.3%

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

Business overview

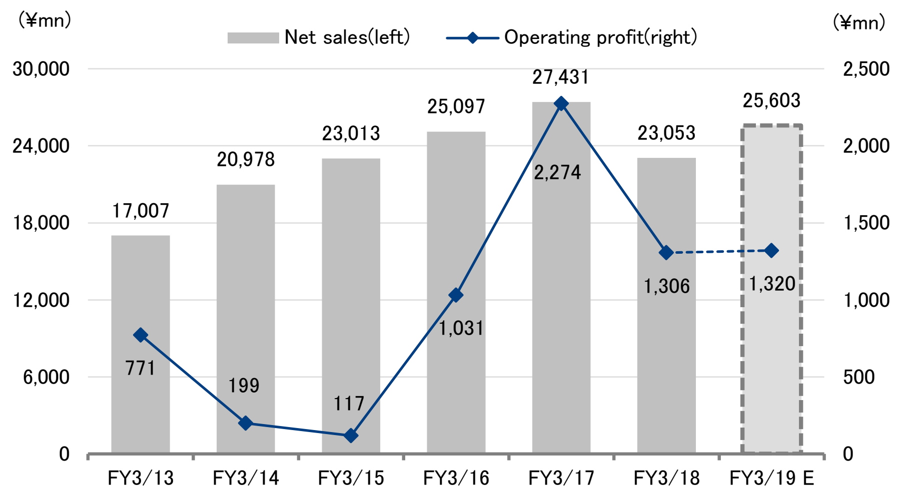
Primarily OEM business in the mainstay Furniture and Houseware Business, with healthy potential for the MINT e-commerce store and new-brand Villeroy & Boch as well

1. Trends in the Furniture and Houseware Business

Furniture and Houseware Business, which employs a business model with OEM at more 90% of sales, has driven the Company's growth in recent years. After expanding from ¥17,007mn in FY3/13 to ¥27,431mn in FY3/17, sales slipped to ¥23,053mn in FY3/18 due to non-recurrence of spot orders by a major European customer, shrinkage of sales to a US volume retailer, and other impacts, but OEM business should remain the core component.

The Company's own MINT e-commerce brand is a fast-growing brand sold via the Company's shopping sites on, Rakuten and Yahoo! and posted a vibrant 1.5-fold increase YoY in FY3/18 sales, albeit at a relatively small scale. At the same timing as expiration of exclusive import agent contracts with two brands (WMF and Silit) in the Furniture and Houseware Business, the Company started handling Villeroy & Boch as a new housewares brand in October 2017. This is a traditional German brand coming up on its 270th year in business. The Company will be booking results for a full fiscal year in FY3/19. We will be looking for steady market inroads of the brand.

Trends in the Furniture and Houseware Business



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

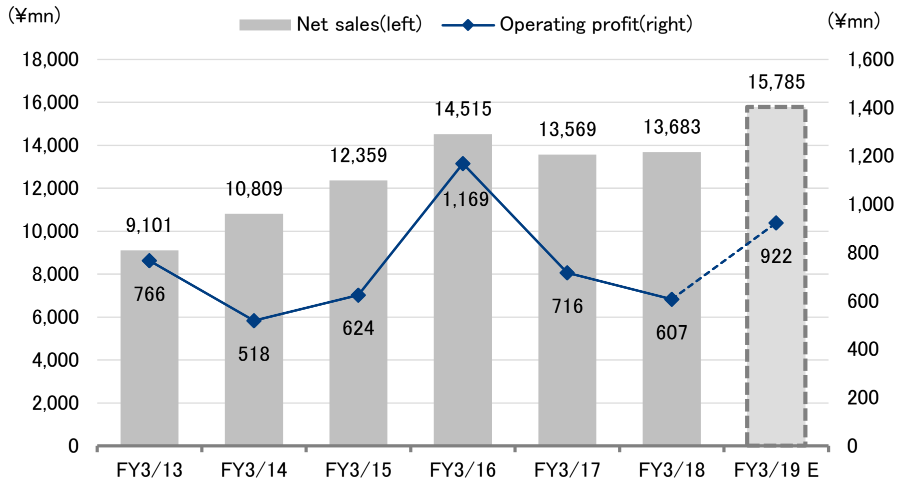
2. Trends in the Fashion Accessories Business

The brand business has a substantial presence of around 50% in the Fashion Accessories Business and exhibits high profitability.

The largest brand is BIRKENSTOCK, which is managed by the subsidiary BENEXY CORPORATION. BIRKENSTOCK provides sandals and comfort shoes with excellent functional beauty and has a tradition of more than 240 years in Germany. It is supported by an enthusiastic fan base even with a price range of ¥10,000 upwards. The products are sold via the 63 directly managed stores and e-commerce. The Company offers after-sales services because many customer use the products for lengthy periods. In FY3/18, the Company opened the Perie Chiba store, the MITSUI OUTLET PARK JAZZ DREAM NAGASHIMA store and the LAZONA Kawasaki Plaza store. Although the past boom in BIRKENSTOCK footwear has settled down, the Company has been able to open stores in customer-attracting commercial facilities, and business performance has been trending firmly.

Kipling is a brand of nylon bags that was created in Belgium in 1987, and together with the Kipling monkey (its mascot), it is famous throughout the world as a playful, casual brand. The brand operates this business via nine directly managed stores (including the Ginza store and outlet stores) and at about 60 major department stores across Japan. While the appearance of parallel imported products adversely affected results in recent years, the Company's countermeasures are gradually beginning to make a positive effect in FY3/19.

Trends in the Fashion Accessories Business



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

Results trends

Sales and profits declined in FY3/18
Impact of the maturing product lifecycles in domestic and overseas OEM businesses

1. FY3/18 results

Looking at the consolidated results for FY3/18, the Company reported declines in sales and profits, with net sales of ¥44,692mn, down 10.2% YoY, operating profit of ¥1,683mn, down 37.8%, ordinary profit was ¥1,832mn, down 24.8%, and profit attributable to owners of parent of ¥832mn, down 41.7%.

Sales declined on an increase in the percentage of products in the mature phase of the product lifecycle in Japan and abroad in the OEM business, which accounts for about 70% of overall sales. Additionally, OEM sales in the Furniture and Houseware Business dropped by ¥4,290mn with major setbacks from lower sales to a conventional volume retailer in the North American market where online sales have taken off and non-recurrence of spot orders from a European client in the previous fiscal year. Brand business sales fell due mainly to the settling down of the BIRKENSTOCK boom and the emergence of Kipling parallel imported goods.

In earnings, gross margin improved 0.8ppt, but gross income contracted due to a heavy impact from weaker sales. While SG&A expenses slightly declined, operating income was down by ¥1,021mn YoY. Furniture and Houseware Business weighed heavily on operating income with a setback of ¥967mn.

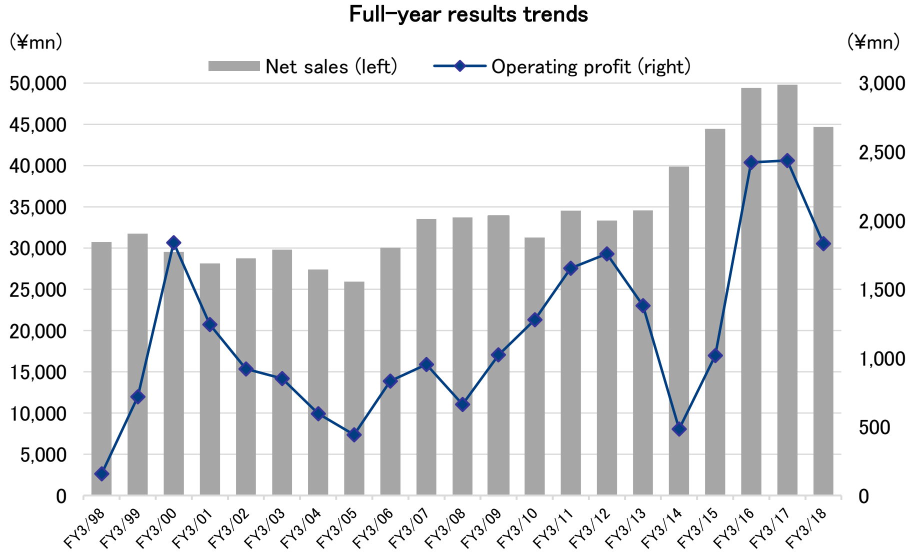
Even with the sales and profit setbacks in FY3/18, the Company posted its third highest sales and fourth highest ordinary profit in the past 20 years and sustained strong levels from a long-term perspective.

FY3/18 results (consolidated)

(¥mn)

	FY3/17		FY3/18				
	Result	% of sales	Initial forecast	Result	% of sales	YoY (%)	vs. forecast (%)
Net sales	49,785	100.0	50,000	44,692	100.0	-10.2	-10.6
Cost of sales	35,826	72.0	-	31,809	71.2	-11.2	-
Gross profit	13,959	28.0	-	12,883	28.8	-7.7	-
SG&A expenses	11,254	22.6	-	11,199	25.1	-0.5	-
Operating profit	2,704	5.4	2,100	1,683	3.8	-37.8	-19.8
Ordinary profit	2,436	4.9	2,100	1,832	4.1	-24.8	-12.7
Profit attributable to owners of parent	1,428	2.9	1,300	832	1.9	-41.7	-35.9

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



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

Expansion of asset scale, sound position with a 51.6% equity ratio

2. Financial position and management indicators

Total asset value rose by ¥2,766mn from the end of FY3/17 to ¥25,823mn, mainly on a ¥1,607mn gain in current assets to ¥18,443mn with higher cash and deposits as the driver and a ¥1,158mn increase in fixed assets to ¥7,379mn largely on higher investment securities.

Liabilities increased by ¥2,136mn YoY to ¥12,385mn. Current liabilities were up by ¥1,842mn primarily on a ¥2,100mn increase in short-term loans. Nevertheless, the addition to short-term loans is a temporary factor related to settlement timing.

In terms of management indicators, the current ratio stood at 183.1% (compared with 204.5% at the end of FY3/17) and an equity ratio of 51.6% (compared with 55.1% at the end of FY3/17), indicating a highly secure financial position.

Consolidated balance sheet and management indicators

(¥mn)

	March 31, 2017	March 31, 2018	Change
Current assets	16,835	18,443	1,607
Cash and deposits	2,859	4,630	1,771
Notes and accounts receivable	6,024	6,615	590
Merchandise and finished products	6,381	6,013	-367
Fixed assets	6,221	7,379	1,158
Total assets	23,057	25,823	2,766
Current liabilities	8,233	10,075	1,842
Notes and accounts payable - trade	2,430	2,267	-163
Short-term debt	2,500	4,600	2,100
Fixed liabilities	2,015	2,310	294
Total liabilities	10,249	12,385	2,136
Net assets	12,807	13,437	629
Total liabilities and net assets	23,057	25,823	2,766
<Stability>			
Current ratio (current assets ÷ current liabilities)	204.5%	183.1%	-
Equity ratio (shareholders' equity ÷ total assets)	55.1%	51.6%	-

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

Outlook

Targets ¥50bn in sales and ¥1.9bn in ordinary income in FY3/19
Expects higher sales and profits in all segments

For FY3/19, the Company forecasts increases in sales and profits with consolidated net sales of ¥50,000mn, up 11.9% YoY, operating profit of ¥1,900mn, up 12.8%, ordinary profit of ¥1,900mn, up 3.7%, and profit attributable to owners of parent of ¥1,200mn, up 44.1%.

The Company expects higher sales and profits in all segments. It forecasts the largest gains in Furniture and Houseware Business and Fashion Accessories Business. Key anticipated growth sources in the former are overseas OEM business recovery, advances in e-commerce direct-sales MINT furniture, and a full-year contribution from the new Villeroy & Boch brand. The latter's main drivers should come from reinforcement of special events, besides direct-operation stores, in the BIRKENSTOCK business and a positive effect of measures to deal with parallel imports of Kipling products.

In the medium-term business plan, the Company hopes to build a foundation to generate at least ¥2bn in ordinary profit on a steady basis by FY3/20. It might even be possible to attain the medium-term business plan's goal of ¥2bn in ordinary profit in FY3/19, the second year. Yen appreciation in the first half of 2018 is likely to provide a tailwind.

Forecast for FY3/19

(¥mn)

	FY3/18		FY3/19			
	Result	% of sales	Forecast	% of sales	YoY	YoY (%)
Net sales	44,692	100.0%	50,000	100.0%	5,307	11.9%
Operating profit	1,683	3.8%	1,900	3.8%	216	12.8%
Ordinary profit	1,832	4.1%	1,900	3.8%	67	3.7%
Profit attributable to owners of parent	832	1.9%	1,200	2.4%	367	44.1%

Source: The Company's results briefing materials

Medium- to long-term growth strategy

Accelerating rollout of new brands as part of the medium-term business plan and started selling the KERBHOLZ environmentally conscious brand of watches from Germany

1. Progress on the medium-term management plan

The Company is currently implementing a medium-term business plan with FY3/18 as the first fiscal year and FY3/20 as the final fiscal year. As a quantitative goal, it hopes to build a foundation to generate at least ¥2bn in ordinary profit on a steady basis by FY3/20. While it missed income targets in FY3/18, the first fiscal year, we think its strategies achieved healthy progress. Priorities are (1) new challenges (development of new business and new clients in OEM business and building a multilayer business model, including M&A, in the brand business), (2) rigorous low-cost operations, (3) further creation of group synergies, (4) promotion of personnel strategy, and (5) proactive governance. While progress differs in each area, the Company believes that it had a smooth start in FY3/18, the first fiscal year. Under new challenges (1), it started operations and gained rights to deal with new brands in brand business. In governance (5), it moved forward with preparations for deployment of a core business system (SAP) and intends to launch it at the parent level in July 2018 and then incrementally deploy it at group companies. This system should help accelerate decision-making and improve business efficiency.

Progress with the medium-term business plan (FY3/18-20)

Priority items	Main progress		Self-evaluation on FY3/18
① Taking on new challenges • OEM business: Develop new businesses and clients • Brand business: Build a multilayer business model including M&As	OEM business	• Preparing new ODM-type business in Europe • Looking for other investment projects	△
	Brand business	• Started handling Villeroy & Boch • Starting new BENEXY business (repair consignments) • Adding multiple new brands (businesses starting in FY3/19)	○
② Rigorously maintaining low-cost operations	Curtailing costs	• Moving the Shanghai office • Moving the Okawa warehouse and consolidating (currently underway)	○
	Business inventory	• Stricter assessment of whether to continue businesses based on the internal Exit rule	○
③ Further creation of group synergies	-	• Revamped the organization to provide guidance on business improvements aimed at raising the profitability of domestic affiliates mainly through Subsidiaries & Affiliates Division	△
④ Promoting human resources strategy	-	• Implementation of a new personnel system	○
⑤ Proactive governance	-	• Proceeding with the core business system (SAP) rollout as planned, decided measures to strengthen governance	○

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

2. Started handling a new brand: KERBHOLZ

The Company began handling products in Japan from KERBHOLZ, a German brand of watches, in June 2018. KERBHOLZ, which was founded in 2012, sells watches that use wood and other natural materials. Its products are sold at over 350 stores in 10 countries worldwide. The brand stands out with its emphasis on the environment, including use of carefully selected natural materials and contribution of 10% of profits to resource conservation projects. It also offers simple but fashionable forms and has received the GERMAN DESIGN AWARD, a highly respected award in Germany, in two straight years and numerous other awards. The Company intends to broaden sales channels to watch shops, multi-brand (select) shops, and lifestyle shops and utilize SNS to raise brand recognition in the Japanese market.

The Company also plans to start handling products from WOLL, a German brand of cooking utensils, in September 2018. It is accelerating rollouts of new brands.

KERBHOLZ

Sanyei Corporation started handling
KERBHOLZ watches from Germany

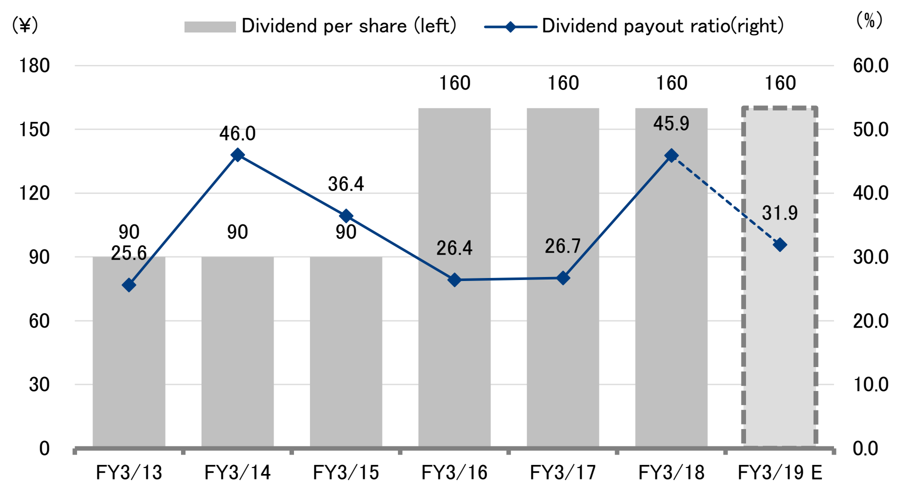
Source: The Company's press release

Shareholder return policy

Forecasting an annual dividend of ¥160 per share for FY3/19, raising or sustaining the dividend for 21 consecutive years, making an attractive stable dividend

The Company has adopted a policy that targets a roughly 30% dividend payout ratio, taking into consideration the need to implement stable, continuous dividends along with securing internal reserves to lay a stronger business foundation. The FY3/18 dividend totaled ¥160 per share with ¥60 in 1H and ¥100 in 2H, which worked out to a payout ratio of 45.9%. It expects to pay an annual dividend of ¥160 per share for FY3/19 with ¥60 in 1H and ¥100 in 2H. The Company has raised or sustained the dividend for 21 consecutive years, making the stable dividend one of its attractive features.

Dividend per share and dividend payout ratio



Note: The FY3/16 dividend included a ¥60 special dividend. The FY3/17 dividend contained a ¥40 dividend commemorating the 70th anniversary.
Source: Prepared by FISCO from the Company's financial results

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