COMPANY RESEARCH AND ANALYSIS REPORT

SFP Dining Co., Ltd.

3198

Tokyo Stock Exchange Second Section

23-May-2017

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Summary

Profit lower, despite increased sales, in FY2/17 owing to inclement weather and weakness at new suburban stores
Changing the store opening policy to existing store reinforcement and new business development

SFP Dining Co., Ltd. <3198> (hereinafter, also "the Company") mainly operates seafood izakaya ISOMARU SUISAN, a popular restaurant format open 24 hours a day located next to train stations and in urban commercial districts (street-level stores). It has achieved robust profitability and growth thanks to a unique income model that takes maximum advantage of customer draw from highly attractive store locations. SFP Dining had 207 stores with 11 formats (also 5 franchise stores) as of end-February 2017. ISOMARU SUISAN is the largest format at 150 stores, and stores are concentrated with 193 stores in Tokyo metropolitan area (including 127 stores in the prefecture). SFP Dining has recently been ramping up Toriyoshi Shoten (chicken restaurants), using the same income model as ISOMARU SUISAN, as a second brand.

In FY2/17, net sales increased 13.4% to ¥35,957mn* while operating income dropped 7.8% to ¥3,307mn. Profit was lower despite positive sales growth. Sales advanced to an all-time high, but both sales and profits missed guidance. The Company benefited from full-contribution of stores added in the previous fiscal year and new openings in FY2/17 (40 stores), though same-store sales came in below guidance at 92.4% of the FY2/16 level (vs. 96.0% in guidance). Business slowed considerably at suburban stores that are vulnerable to economic trends.

* SFP Dining changed the fiscal year from FY2/16, and the comparison covers results for the period from March 1, 2015 to February 29, 2016 (unaudited so simply reference values).

SFP Dining intends to revise the store opening policy and also bolster existing stores and develop new businesses in light of its assessment of various issues. For store openings, it has switched direction to curtailing new suburban stores that do not attract much new customer inflow and are easily affected by economic trends and putting emphasis on openings in commercial districts again. In reinforcement of existing stores, it is renovating stores to bolster customer draw and deploying tablets to raise average customer spend. These initiatives appear to be having some effect recently. In new business, it opened the first Toragoro store, which makes and sells gyoza, utilizing the Company's unique income model in Shinjuku and is enjoying a healthy start.

The FY2/18 guidance projects higher sales and profits with a 2.9% YoY rise in sales to ¥37,000mn and a 1.3% gain in operating income to ¥3,350mn. The Company's moderate growth outlook, compared to prior momentum, stems from concentrating business resources in existing store reinforcement and new store development. SFP Dining plans to pursue stronger growth again from FY2/19. In FY2/18, it assumes 20 new stores and same-store sales at 97.1% of the FY2/17 level.

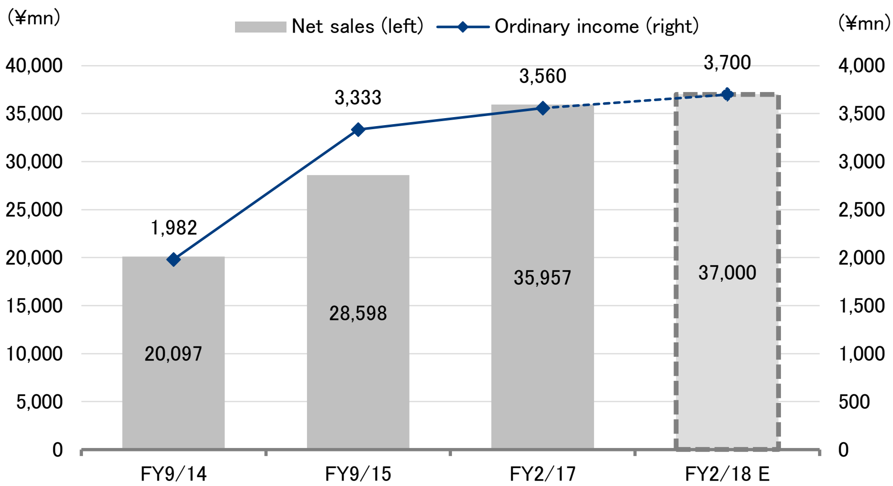
SFP Dining released a new three-year medium term management plan that reflects the impact of revisions to store opening policy and temporary flattening of FY2/18 results. While the Company's previous medium term management plan factored in store additions at a pace of about 40 stores a year, the updated plan lowered overall results growth because of the revision of the FY2/18 opening plan to 20 stores. However, the Company remains committed to opening stores at a pace of about 40 stores per year from FY2/19. Its final-year FY2/20 goals are ¥47,000mn in net sales (14.3% three-year average growth rate) and ¥4,700mn in ordinary income (14.9%).

We think SFP Dining can attain medium term management plan goals, despite revisions to store opening policy, because it has considerable room to open ISOMARU SUISAN and Toriyoshi Shoten stores. The upbeat start for the new Toragoro format is a positive factor too. While income trends are likely to flatten in FY2/18, this is important timing for accelerating growth from FY2/19. We will be closely monitoring outcomes from existing store reinforcement (such as renovations and tablet deployment) and advances in new businesses (Toragoro and others).

Key Points

- Profit declined in FY2/17, despite higher sales, mainly on weakness in suburban store activity
- Income trends likely to temporarily flatten in FY2/18, though SFP Dining aims to restore stronger growth from FY2/19 through revision of store opening policy, existing store reinforcement, and new business development initiatives

Results trends



Note: FY2/16 not shown because it was an abnormal period of just five months
Source: Prepared by FISCO from the Company's financial results

Company profile

Primarily operates popular ISOMARU SUISAN and Toriyoshi Shoten

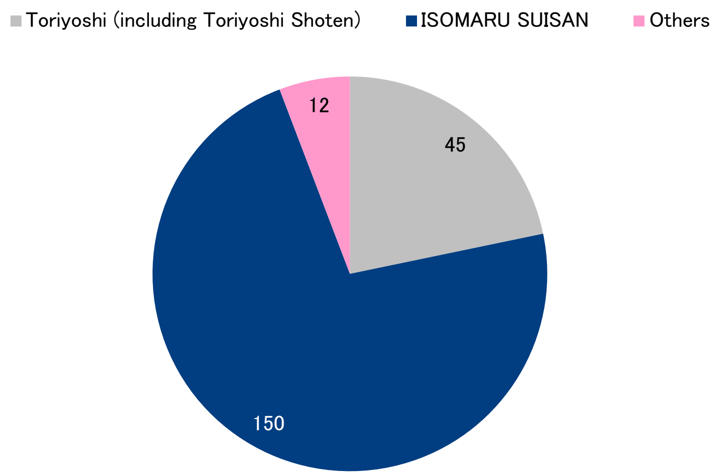
1. Business content

SFP Dining primarily operates seafood izakaya ISOMARU SUISAN, a popular restaurant open 24 hours a day at locations next to train stations and in commercial districts (street-level stores). SFP Dining had 207 stores with 11 formats (also 5 franchise stores) as of end-February 2017. ISOMURA SUISAN is the largest format at 150 stores, and stores are concentrated with 193 stores in metro Tokyo (including 127 stores in the prefecture). The Company aimed to establish brand presence and expand store number with focused openings in metro Tokyo (particularly in the city center and commercial districts).

SFP Dining has been ramping up Toriyoshi Shoten (chicken restaurants), using the same income model as ISOMARU SUISAN, as a second brand and should continue strong growth. It concluded a capital alliance with create restaurant holdings <3387> in April 2013 and listed shares on the Second Section of the Tokyo Stock Exchange as a consolidated subsidiary in December 2014.

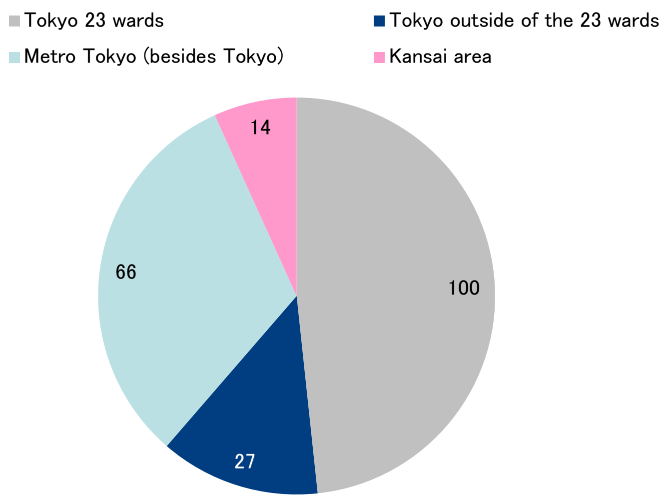
While the Company only has the food and beverages segment, it operates in three areas – the founding Toriyoshi business (including Toriyoshi Shoten), the mainstay ISOMARU SUISAN business, and other business. The ISOMARU SUISAN business generates 72.4% of sales (FY2/17 result).

Store volume by format (end-Feb 2017)



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

Store area situation (end-Feb 2017)



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

Store number and features by brand

Brand	Store number	Features
Toriyoshi	23	Fried chicken wings with a special sauce, chicken specialty restaurant
Omotenashi Toriyoshi	3	New Toriyoshi with refined hospitality
Toriyoshi Shoten	19	Tasty, quick food provision typical of a chicken restaurant
ISOMARU SUISAN	150	Seafood izakaya mainly for a seafood BBQ
Teppan 200°c	3	Enjoy teppan-yaki at a large counter
CASA DEL GUAPO	1	Authentic recreation of a Spanish bar style
Tamacho Honten	1	Nagoya's famous misonikomi udon (udon in a thick miso soup)
Bistro ISOMARU	1	Casual Western-style izakaya
Kizuna Sushi	3	All-year shop that supplies fresh, delicious, and inexpensive sushi
Kisoba Tamagawa	1	Reasonably priced fresh ground, prepared, and boiled noodles
ISOMARU Sushi	1	Seafood and sushi izakaya with an izakaya menu
Backstreet Wine Bar BUENO	1	Relaxing wine bar

Source: Prepared by FISCO from Company materials

SFP Dining transferred some of its food and beverage services and product provision business to a subsidiary and transitioned to a holding company organization from September 2016. This change aims to promote dynamic corporate reorganization and operational reforms inside and outside the Company, encourage creation of new businesses leveraging the current base, and reinforce management functions and corporate governance.

Income model of 24-hour operation at locations next to train stations and in commercial districts (street-level stores) is a key strength

2. Corporate advantages

The Company's advantage lies in its unique income model, in addition to the conventional izakaya income model. Mainstay ISOMARU SUISAN's income model selects locations next to train stations and in commercial districts with high rents for its street-level stores and sustains strong operation rates by maximizing customer draw at these attractive sites with unique and highly visible facades, welcoming and open atmospheres, and 24-hour operations that cover a wide range of demand. It realizes leverage by securing large sales that sufficiently cover expensive rents that would erode profitability at typical izakaya restaurants. This format cannot be easily copied because it relies on a location analysis scheme, street-level store development skills, and know-how in rotating optimal menus for 24-hour operations and specific hours. We think expensive opening costs and the difficulties of 24-hour operations present major hurdles to other firms. SFP Dining's accumulation of know-how ahead of others and build-up of robust brand presence through focused openings in metro Tokyo have driven a beneficial cycle of lowering store opening risk. The Company has only closed 4 of the 154 stores (ISOMARU SUISAN) that it opened thus far (one closure was a change in location). Success with a strategy of opening stores in suburban areas of metro Tokyo* and the Kansai region after establishment of brand presence next to train stations and in commercial districts accelerated growth too. These various aspects enabled the Company to building unique positioning with high profitability and growth potential.

* However, the Company is revising the store-opening policy for suburban small markets because of low inflow of new customers and vulnerability to impacts from economic trends.

SFP Dining can also apply the income model established for ISOMARU SUISAN to other formats and has substantial room for further advances. Toriyoshi Shoten, which has potential to become a second major brand, applied ISOMARU SUISAN's income model to the Company's founding Toriyoshi business and has been steadily gaining momentum. Key points are overlapping openings with ISOMARU SUISAN (at the same time or in the same area as existing stores) and selective openings that meet market features (location and format). The Company has been successful with openings next to ISOMARU SUISAN stores, proving that demand is not cannibalized. This brand is likely to contribute significantly to expansion of store-opening capacity as a new growth driver. SFP Dining is also pursuing development of new businesses and should further enhance opening capacity and certainty if it ramps up new formats.

Founded with the Toriyoshi restaurant that specializes in Nagoya-style fried chicken wings

3. History

The Company started with the opening of Toriyoshi, a fried chicken wing specialty restaurant, in Tokyo's Musashino city (now Toriyoshi Shoten's Kichijoji South Exit store) in April 1984 by founder Ryosaku Samukawa (former Representative Director & Chairman, retired in December 2015). Toriyoshi served Nagoya-style fried chicken wings arranged with a special recipe as its main menu and steadily increased store number. It presented a vision of "becoming a comprehensive food service business that creates a rich menu of foods" in 2001 and expanded operations to 50 stores, including format diversification, in 2008.

Following the economic crisis triggered by the Lehman Brothers bankruptcy and changes in the industry environment, the Company outlined a vision of "becoming a food specialty store group that enriches Japan." With the switch in course to pursuit of "specialty stores," it opened ISOMARU SUISAN based on a unique income model in 2009 and built the foundation for growth.

The Company decided to pursue listing its stock as the quickest path to "building a lasting corporate organization" after smoothly ramping up ISOMARU SUISAN and confirming a growth path. It accepted capital participation by Polaris No.2 Investment Limited Partnership (Polaris Capital Group Co., Ltd.), a private-equity fund, in December 2010 as well as enhanced management and organizational operating precision by adopting objective standards and rational methods. San Francisco Holdings Co., Ltd., which was established as an SPC (special purpose company), served as the nominal surviving company and absorbed Samukawa Food Planning Co., Ltd., which had been the main entity prior to then, in May 2011 (the Company was renamed SFP Dining Co., Ltd. in October 2011).

The Company concluded a capital alliance with create restaurants holdings, which mainly operates restaurants and food courts in suburban shopping centers, in April 2013 and listed on the Second Section of the Tokyo Stock Exchange as a consolidated subsidiary in December 2014.

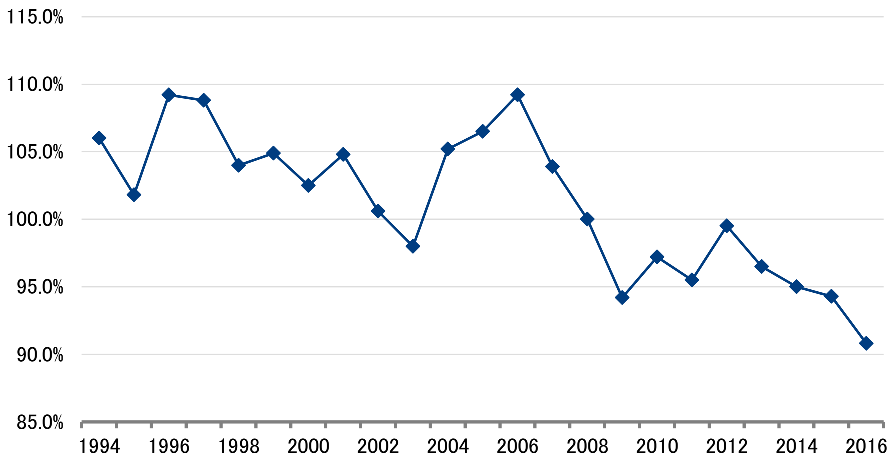
SFP Dining accelerated the pace of store openings for ISOMARU SUISAN, which had solidified a brand presence as a popular store format, after listing on the market and reached 100 stores for ISOMARU SUISAN in May 2015. It also started franchising ISOMARU SUISAN stores in Nagoya (Aichi Prefecture). It began opening Toriyoshi Shoten stores, which are expected to become the second major growth driver, and ramped up this business to 10 stores as of end-March 2016. SFP Dining transitioned to a holding company format to be capable of quickly responding to changes in the business environment in September 2016.

Industry environment

Emergence of restaurants with low average customer spend in a difficult industry environment

The “pub restaurant/izakaya” industry, which is SFP Dining’s segment, has been steadily shrinking, despite signs of economic recovery, because of sluggish personal consumption, growing popularity of drinking at home, and less alcoholic beverage drinking by younger people, according to a survey conducted by the Japan Foodservice Association. This industry’s sales dropped further in 2016 to 90.8% of the previous year.

Pub restaurant/izakaya industry annual sales (YoY change)



Source: Prepared by FISCO from Japan Foodservice Association survey results

This industry is highly volatile because of relatively low hurdles to market entry and heavy impact from consumer sentiment and preference changes. While new formats with cuisine specialties had recently been popular as a replacement of general izakaya that lacked notable characteristics, store formats with lower average customer spend have surfaced. Main firms in this industry include COLOWIDE Co., Ltd. <7616>, Chimney Group Co., Ltd. <3178>, Diamond Dining Co., Ltd. <3073>, AP Company <3175>, and Torikizoku Co., Ltd. <3193>.

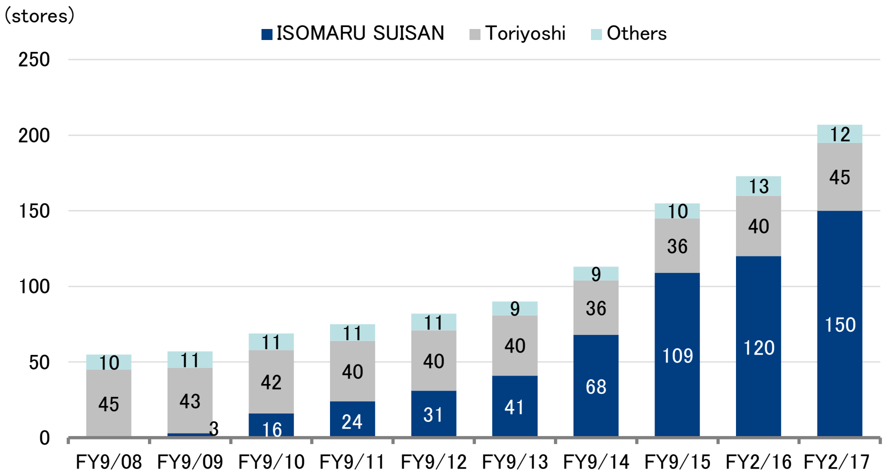
Business results

Sustaining strong growth potential and profit margin by aggressively increasing store number

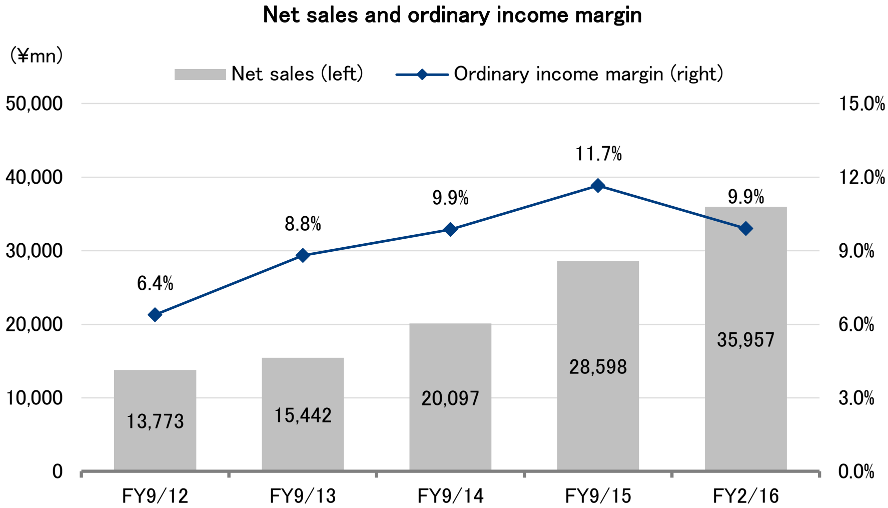
1. Past performance

Increases in store number have driven the Company's growth in past years. Income growth accelerated from FY9/10 when the Company ramped up openings of ISOMARU SUISAN stores based on a unique income model, and ordinary profit margin improved significantly with the rise in sales. Margin moved above the 8% goal in FY9/13 and subsequently increased to 11.7% in FY9/15. It has remained at a strong level near 10% since then.

Store number trends



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



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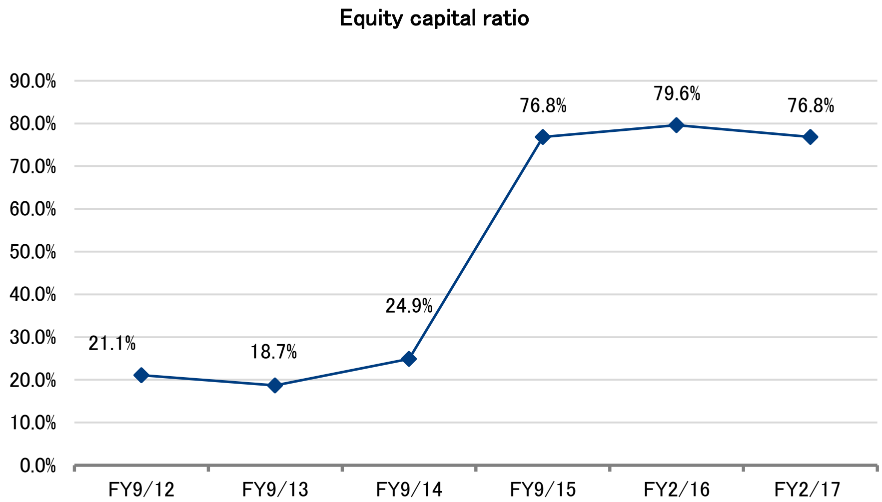


Source: Prepared by FISCO from the Company's financial results

In financial standing, the equity ratio had been about 20% for many years, but strengthened to 76.8% at end-FY9/15 owing to the public-offering capital increase for the TSE-2 listing in December 2014 (about ¥12,758mn). It has stayed above 70% thereafter.

ROE, which indicates capital efficiency, climbed along with improvement in ordinary income margin, and has also been sustaining a high level since FY9/15 after the reinforcement of capital. We think the Company possesses excellent financial standing.

Profit declined on higher sales in FY2/17
Missed period-start targets due to weakness at suburban stores

2. Overview of FY2/17 results

In FY2/17, net sales increased 13.4% to ¥35,957mn* while operating income dropped 7.8% to ¥3,307mn and ordinary income was down 8.8% to ¥3,560mn. Profit was lower despite positive sales growth, and both sales and profits missed guidance.

* SFP Dining changed the fiscal year from FY2/16, and the comparison covers results for the period from March 1, 2015 to February 29, 2016 (unaudited so simply reference values).

Full-year contributions from stores opened in FY2/16 and 40 stores opened in FY2/17 supported higher sales. The upbeat Toriyoshi Shoten business posted substantially higher sales thanks to the addition of seven new stores. Sales shortfall versus guidance, however, occurred because of weak same-store sales at just 92.4% YoY (vs. 96.0% in the period-start view), due to slumps at suburban stores from inclement weather and slower consumption activity. The result also missed lowered guidance (announced on January 13, 2017) because of 1) opportunity losses due to temporary suspensions to deploy tablets at stores (implemented in Jan-Feb) and initial operational disruptions (unfamiliarity), 2) signs of healthier activity in the year-end and New Year's season faded in late January and February, and 3) delays in some new openings scheduled for 4Q. Period-end store number stood at 207 stores following 40 new openings and 6 closures.

In earnings, meanwhile, operating income declined, despite controlling costs to reflect sales, because of higher new store opening costs with an extra four new stores compared to the same period in previous fiscal year and unexpected costs (such as increased depreciation costs related to tablet deployment). Operating income margin weakened to 9.1% (from 11.3% for the same period in the previous year), though was still at a high level. The Company booked extraordinary losses (¥363mn) for costs to close stores and impairment losses for unprofitable stores.

In financial standing, total assets expanded 12.0% YoY to ¥26,257mn due to expansion of store number, and net assets also rose by 8.1% to ¥20,172mn because of additions to internal reserves. The equity ratio hence remained at a strong 76.8% (vs. 79.6% at the end of the previous fiscal year). ROE, an indicator of capital efficiency, was at a double-digit level, despite the impact of income margin decline, including impairment charges.

Overview of FY2/17 results

(¥mn)

	Previous-year period Mar 2015 to Feb 2016 results		FY2/17 results		Change		FY2/17			
							Initial forecast		Revised forecast (January 13)	
		% of total		% of total		Change rate		% of total		% of total
Net sales	31,697		35,957		4,260	13.4%	38,300		36,500	
Toriyoshi	6,234	19.7%	7,514	20.9%	1,280	20.5%	-	-	-	-
ISOMARU SUISAN	23,479	74.1%	26,031	72.4%	2,552	10.9%	-	-	-	-
Others	1,984	6.2%	2,410	6.7%	426	21.5%	-	-	-	-
Cost of sales	8,943	28.2%	10,270	28.6%	1,327	14.8%	10,905	28.5%	10,414	28.6%
Gross profit	22,754	71.8%	25,687	71.4%	2,933	12.8%	27,395	71.5%	26,086	71.4%
SG&A expenses	19,164	60.5%	22,379	62.2%	3,230	16.9%	23,565	61.5%	22,586	61.9%
Operating income	3,589	11.3%	3,307	9.1%	-296	-8.2%	3,830	10.0%	3,500	9.6%
Ordinary income	3,904	12.3%	3,560	9.9%	-344	-8.8%	4,100	10.7%	3,800	10.4%
Profit attributable to owners of parent	-	-	2,081	5.7%	-	-	2,590	6.8%	2,300	6.3%
Depreciation costs	1,042		1,244		897	259.4%				

Note: Previous-year period not audited and should be used as reference values

Total assets	23,434		26,258		2,824	12.1%
Net assets	18,650		20,172		1,522	8.2%
Equity ratio	79.6%		76.8%		-2.8p	

Source: Prepared by FISCO from the Company materials

Results are reviewed by main business fields below.

The Toriyoshi business posted ¥7,514mn in sales (up 20.5% YoY). Sales at upbeat Toriyoshi Shoten grew significantly with seven openings (vs. five stores in the period-start plan) and three conversions. Same-store sales were relatively solid at 96.9% of the previous-year level. This business had a total of 45 stores at period-end (including 19 Toriyoshi Shoten stores) with 7 openings, 3 conversions, and 3 closures.

The ISOMARU SUISAN business recorded ¥26,031mn in sales (up 10.9% YoY). While sales benefited from full-year contributions for stores opened in the previous fiscal year and 32 new stores added in FY2/17, same-store sales were weak at 90.2% of the prior year, due to backlash decline from opening costs, inclement weather, and sluggish consumption, weighing on overall income. Street-level stores are easily affected by rain, and typhoons and other rainfall doubled versus the previous year in the upbeat months of August to October. Furthermore, the number of cases of not seeing recovery in customer traffic (YoY), which normally improves after the backlash decline from strong post-opening activity, increased for suburban stores vulnerable to economic trends. Opportunity losses caused by operating suspensions to deploy tablets at stores and post-installation disruptions (unfamiliarity) had an impact too. However, this is a temporary setback and tablet deployment should switch to having a positive impact over time as seen in the recent rise in average customer spend. As an overall trend, customer average spend appears to be weakening, even with relatively stable customer number in dinner-time hours, because of a change from primary usage to secondary and tertiary use. This business had 150 stores at period-end following 32 openings and 2 closures.

Store openings and closures in FY2/17

(stores)

	Businesses			Total	Region			
	Toriyoshi	ISOMARU SUISAN	Others		Tokyo 23 wards	Tokyo outside the 23 wards	Metro Tokyo (besides Tokyo)	Kansai area – Chubu area
End-February 2016	40	120 (3)	13	173 (3)	89	21	50	13 (3)
Openings (a)	7	32 (2)	1	40 (2)	13	8	17	2 (2)
Format conversions	3	0	2	5	3	0	2	0
Closures (including format conversions)	-5	-2	-4	-11	-5	-2	-3	-1
End-February 2017	45	150 (5)	12	207 (5)	100	27	66	14 (5)
Full-year openings plan (b)	5	35	1	41				
(a)/(b)	140.0%	91.4%	100.0%	97.5%				

Source: Prepared by FISCO from the Company materials

Issues and initiatives

Changing the store-opening policy plus existing store reinforcement and new business development

SFP Dining has identified issues it faces based on current conditions and future growth acceleration and is aiming for improvement with the following initiatives. Existing store reinforcement and new business development are major themes.

(1) Renovations at existing stores (27 stores)

The Company must renovate stores with a faster cycle that of ordinary izakaya because of its 24-hour operations that underpin the unique income model. In FY2/18, it plans to renovate 2 Toriyoshi stores and 25 ISOMARU SUISAN stores and thereby maintain and improve income through reinforcement of existing stores. Specific measures include enhancing customer draw by updating the exterior to a cleaner image plus creation of a more comfortable environment and improvements in operational efficiency by replacing floors, installing cooker-storing tables, revising the interior layout, and revamping interior walls. Tables with cooker-storing tables appear to be helping boost average customer spend by securing more space.

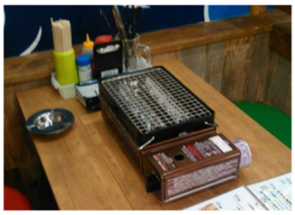
Specific case of an upgraded exterior

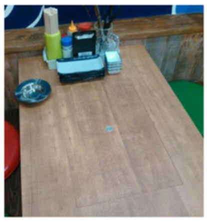
Kabukicho Central Road Store

Hon-Atsugi North Exit Store

Source: Company materials

Cooker-storing tables installation





Source: Company materials

(2) Raising average customer spend

To raise average customer spend, the Company hopes to make effective use of tablet devices* deployed at stores in FY2/17. Tablets significantly reduce order-related efforts by changing the flow from the conventional pattern of “requesting staff,” “placing orders,” “inputting in terminals,” “repeating orders,” “cooking,” and “provision” to just “inputting in terminals,” “cooking,” and “provision.” These revisions can also shorten the amount of time it takes until customers receive ordered items. The Company expects improvements in customer convenience and higher customer average spend (thanks to the easier ordering process and shorter waiting time). Tablets aid in catering to inbound demand too (with support for English, Korean, Cantonese, Chinese, and other languages).

* The Company implemented a concentrated rollout at ISOMARU SUISAN stores in Jan-Feb 2017 and 141 of the 150 stores are utilizing tablets (94.0% deployment rate).

Additionally, decline in average customer spend due to a shift in dinner-hour usage from primary to secondary and tertiary could be attributed to growing familiarity with ISOMARU SUISAN whereby customers utilize the stores for demand at various times. Yet the Company is taking steps to enhance course menus to accommodate banquet demand because of the importance of the dinner hours and this effort is contributing to higher average customer spend as well.

(3) New business initiatives

ISOMARU SUISAN and Toriyoshi Shoten, the Company's main stores, utilize a unique business model that maximizes customer draw from having excellent locations next to train stations and in commercial districts and at street-level stores and also benefit from expanded opening leeway and improved store operating efficiency because the different formats allow for adjacent positioning. SFP Dining aims to develop another 2-3 new store formats in order to leverage advantages of its unique income model. The first new launch was opening the Toragoro gyoza izakaya, which makes and sells gyoza, in Shinjuku on March 27, 2017. This store has extensive gyoza menu offerings (13 types in 4 categories) to keep customers from losing interest. While customer average spend is lower than at ISOMARU SUISAN, the Company expects sales at roughly the same level due to fast turnover (boosting customer number). Additionally, business has started strongly and suggests that this could be a third major brand. The Company aims to develop a new income model as well, besides the traditional izakaya model and the ISOMARU SUISAN model, thereby broadening format options and limiting opportunity losses.

(4) Focused openings in prime areas of Tokyo and Osaka

SFP Dining redirected its store-opening policy to emphasis on commercial districts again in light of risk from vulnerability to economic trend impact in suburban smaller-scale markets. While its ISOMARU SUISAN strategy had involved raising awareness with dominant openings in prime city-center areas followed by expansion to suburban areas, the Company is revising the stance of opening stores in suburban areas and instead will strengthen its development of the Kansai area that has room for opening new stores. For Toriyoshi Shoten, the second major store brand, the Company opened a number of stores adjacent to ISOMARU SUISAN locations up to now and will be seeking to expand the store numbers with openings mainly in prime city-center areas that do not have a store yet.

Results outlook

Guides for strategic flattening in FY2/18 results

The FY2/18 guidance projects higher sales and profits with gains of 2.9% YoY in sales to ¥37,000mn, 1.3% in operating income to ¥3,350mn, 3.9% in ordinary income to ¥3,700mn, and 17.7% in profit attributable to owners of parent to ¥2,450mn. The Company's moderate growth outlook, compared to prior momentum, stems from curtailing new openings and concentrating business resources (particularly human resource) in existing store reinforcement and new business development. SFP Dining plans to pursue stronger growth again from FY2/19.

In guidance, SFP Dining factors in full-year contributions from stores opened in the previous fiscal year and sales from 20 new stores scheduled to begin operating in FY2/18. The sales growth rate is relatively modest because it lowered new openings to 20 stores (versus 40 stores in FY2/17). The plan assumes that same-store sales reach 97.1% of previous-year sales (vs. 92.4% in FY2/17). SFP Dining hopes to improve the growth rate (narrow the decline margin) compared to FY2/17 through measures to strengthen existing stores explained above (benefits from store renovations and tablet deployment). While it currently plans to open 10 stores each for ISOMARU SUISAN and Toriyoshi Shoten formats, the breakdown could vary depending on progress with the new Toragoro format that is having an upbeat start.

SFP Dining targets higher operating income accompanying increased sales and decline in store opening costs, but operating income margin is likely to be flat at 9.1% (also 9.1% in FY2/17) because of added depreciation costs from store renovations. The strong growth rate in profit attributable to owners of parent shareholders stems from the subsidiary's exemption from the consumption tax that creates tax-related profit as extraordinary profit (estimated at about ¥1bn). This needs to be viewed as a one-time special factor. From a conservative standpoint, meanwhile, SFP Dining included a certain amount of impairment charges for unprofitable stores (extraordinary losses) in the budget.

We think the FY2/18 guidance reflects a strategy plateau and do not see tough hurdles for attaining these values. The same-store sales (YoY) target seems to be a reasonable assumption because existing store reinforcement is currently providing positive results. Our main focus is on the extent to which existing store reinforcement, new business development, and other measures generate results for renewed growth from FY2/19.

Medium term management plan

Lowered medium term goals, though still offers longer-term growth potential

SFP Dining steadily implemented its three-year medium term management plan that started in FY2/17 and disclosed a new medium-term plan for the next three years that reflects the impact of revising the store opening policy and flat earnings in FY2/18. The previous medium-term plan assumed an opening pace of about 40 stores per year. While the decision to revise this stance to 20 stores in FY2/18 lowered overall results growth rates, the Company still intends to add about 40 stores a year from FY2/19. Final-year (FY2/20) goals are ¥47,000mn in sales (14.3% three-year average growth rate), ¥4,700mn in ordinary income (14.9%), and ¥2,850mn in profit attributable to owners of parent shareholders (17.0%).

ISOMARU SUISAN and Toriyoshi Shoten are the core store formats slated to drive medium-term growth. We expect heightened certainty of earnings growth from FY2/19 if the new Toragoro store format, which had an upbeat start, grows as a third brand. As mentioned earlier, the Company plans to open stores mainly in the Kansai area for the ISOMARU SUISAN brand and in city-center prime areas not covered yet for the Toriyoshi Shoten brand.

In earnings, ordinary income margin is expected to remain about flat at the current level of about 10%, just as in the previous medium term management plan. Although the Company's income margin is already at a high level in the industry, we find this stance slightly conservative considering future sales increase benefits and the relatively low production cost margin at Toriyoshi Shoten, a format that will be adding more stores. SFP Dining targeted 8% ordinary income margin up to now and plans to retain this policy. Earnings beyond this threshold are likely to be effectively allocated to initiatives that help sustain growth, such as service enhancement, management capabilities, personnel recruitment, format development.

We think SFP Dining is capable of attaining medium term management plan goals, despite revisions to the store opening policy, because it has sufficient room to add more ISOMARU SUISAN and Toriyoshi Shoten stores. The upbeat start with the Toragoro store has positive implications as well. We see successful ramp-up of a new format as a third brand brings further enhancement of store expansion leeway and higher certainty.

While FY2/18 results are headed for a temporary plateau, the stance of promptly revising store-opening policy and giving priority to issue resolution and new business development appears to be a rational decision that works toward sustainable growth. Key points are 1) results from bolstering existing stores, 2) rollout of ISOMARU SUISAN stores in the Kansai area and subseduent results, 3) the pace of Toriyoshi Shoten store openings in city-center prime areas, and 4) new format development and strategies for full-fledged deployment. We think 3) and 4) are important benchmarks to assess the Company's ability to roll out its unique income model.

Medium term management plan

(¥mn)

	FY2/17		FY2/18 plan		FY2/19 plan		FY2/20 plan	Average growth rate
	Previous	Results	Previous	Revised	Previous	Revised		
Sales	38,300	35,957	44,500	37,000	50,000	41,000	47,000	9.3%
(Growth rate)	20.8%	13.4%	16.2%	2.9%	12.4%	10.8%	14.6%	
Ordinary income	4,100	3,560	4,750	3,700	5,350	3,800	4,700	9.7%
(Margin)	10.7%	9.9%	10.7%	10.0%	10.7%	9.3%	10.0%	
Profit attributable to owners of parent shareholders	2,590	2,081	3,020	2,450	3,400	2,200	2,850	11.1%
(Margin)	6.8%	5.7%	6.8%	6.6%	6.8%	5.4%	6.1%	
Number of stores	41	40	40	20	46	40	40	
Store volume at period-end	214	207	254	225	300	265	305	

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

Shareholder returns

Aiming for 30% dividend payout ratio
Possesses significant leeway to raise dividends linked to profit growth over the longer term

SFP Dining aims for a stable dividend with 30% payout ratio as the target. It plans to pay a ¥26 annual dividend (¥13 interim, ¥13 year-end) for FY2/17, in line with initial guidance (putting payout ratio at 36.6%). It is targeting ¥26 (¥13 interim, ¥13 year-end) again in FY2/18 (payout ratio at 31.2%).

We expect flat earnings in FY2/18, but renewed growth from FY2/19 and see sufficient room to increase the dividend as earnings grow over the longer term.

SFP Dining has also adopted a shareholder gift program. It allocates food coupons that can be used as SFP Dining stores twice a year (covering shareholders with 100 or more shares listed in the shareholder registery at end-February and end-August). The gift amount varies depending on the number of shares owned.

Shareholder gift program

Number of shares owned	Shareholder gift coupon (per time)
100-499 shares	¥4,000
500-999 shares	¥10,000
1,000 or more shares	¥20,000

Source: Prepared by FISCO from the Company materials

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