

COMPANY RESEARCH AND ANALYSIS REPORT

SOU

9270

TSE Mothers

11-Jul.-2019

FISCO Ltd. Analyst

Kimiteru Miyata



FISCO Ltd.

<http://www.fisco.co.jp>

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Summary

A luxury goods reuse company that is continuing to grow with view to global expansion

SOU Inc. <9270> (hereafter, also “the Company”) buys and sells high-value, luxury reuse items, including brand goods, precious metals, antiques and works of art. It has a business model never seen before in the luxury goods industry, including appealing to customers through digital marketing, its buying offices, sales through auctions, and data-focused management using SOU Brain, its product management system. Against the backdrop of this business model, it has continued to grow rapidly and was listed on the stock market only seven years after its establishment. Moreover, it is also further expanding its business scope, including expanding overseas sales channels, establishing omnichannel for retailing, and developing apps. The Company’s business model, which combines the digital and the real worlds and provides services from a new perspective, can be said to be a highly differentiated model that is extremely unique within the more conventional reuse industry.

The Company utilizes digital marketing to attract many sellers, and it buys a large number of items at its 63 buying offices (as of the end of February 2019, same below) that are located throughout the country, mainly NANBOYA. The bought items are collected at the headquarters in two days on average. After the goods have been inspected and maintained, many of them are sold at the auctions for dealers in the same month or the following month and the transactions have a stably short cash conversion cycle. Some sales are through retailing, and it operates high-class, luxury goods stores with a lineup of mainly vintage items, while the Company also operates e-commerce websites for progressing the establishment of omnichannel. In this way, it has grown by rapidly cycling through its three strengths: seller attraction, buying power, and selling power. While it can be said that its business is centered on these three strengths, the core of the Company’s business model is SOU Brain, the product management system. The Company’s digital literacy, of its use of the Internet and its own system, is also considered to be one of its major features that has not been seen before in the conventional luxury reuse industry.

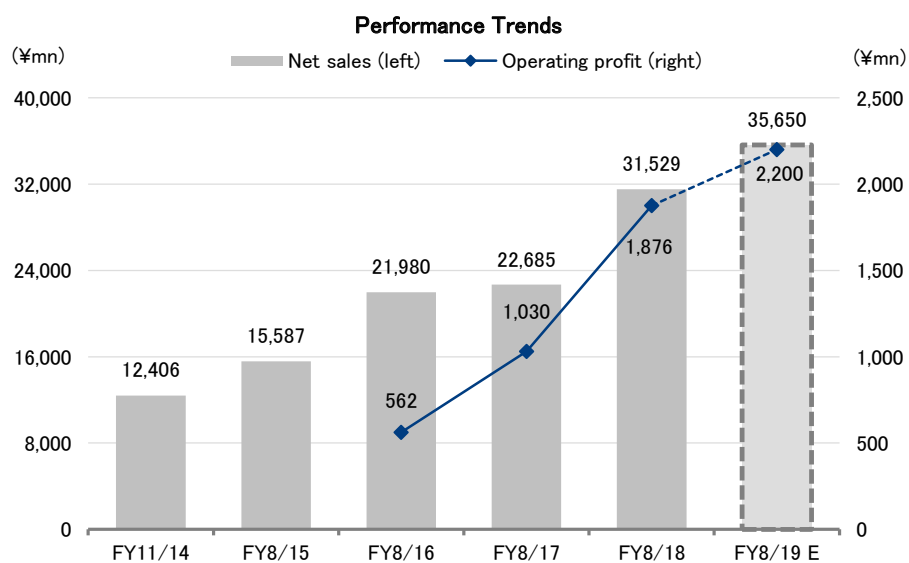
In the FY8/19 Q2 results, net sales were ¥18,956mn (up 23.2% year-on-year (YoY)) and operating profit was ¥1,152mn (down 3.3%). Operating profit decreased, but the profit forecast progress rate was around 52%, which seems to be in line with the Company’s expectations. The decrease in operating profit was due to the sharp rising of yen during December and January. It seems that among the buyers participating in the auctions in Japan, the motivation to buy in buyers for overseas markets declined slightly, although this appears to be recovering at the present time. In the outlook for the FY8/19 results, the Company is forecasting net sales of ¥35,650mn (up 13.1% YoY) and operating profit of ¥2,200mn (up 17.2%). As the rates of progress toward these forecasts have been steady and purchasing has been favorable, the Company considers its FY8/19 results outlook to be “conservative.”

Summary

In order to realize its management mission of “providing global access to pricing and valuing data for smarter lifestyles,” and its management vision of “transition from a luxury reuse company to a luxury market data company,” the Company is working to expand its domestic network of buying offices, strengthen and expand the business to overseas, and improve the usability of miney, its asset management app. First, by expanding domestic buying bases, it intends to stably grow its existing business in Japan. Overseas, the idea is to grow sales mainly through online auctions and also to develop the network of buying offices. For miney, its objective is to promote its use through improving usability and developing it as an asset management tool for individuals. Through these measures, it will be able to not only conduct purchasing and sales, but also to collect a wide range of profound data in Japan and overseas, so the accuracy of SOU Brain is expected to increase more and more. It is considered that the Company’s business model can differentiate it from its competitors overseas also, it is expected to grow in the medium- to long-term.

Key Points

- The Company continues to grow through its three strengths: seller attraction, buying power, and selling power
- SOU Brain, its product management system, is the core of its business model
- The Company is set to take a leap forward both in Japan and overseas as a global luxury market data company



Note: results up to FY8/15 are stand alone
 Source: prepared by FISCO from the Company’s results summary report and securities report

■ Company overview

A highly unique reuse company that specializes in luxury goods

1. Company overview

The Company conducts buying and sales of high-value, luxury items, including luxury brand goods and precious metals. Buying is mainly carried out at its specialized offices, and the majority of the purchased goods are from general consumers. The Company has been a pioneer in utilizing digital marketing to attract customers and does not rely on traditional signboards, through which it has been able to rapidly increase the purchasing volume in a short period of time. It also accumulated a vast amount of buying data. For sales, it conducts wholesales to buyers in Japan and overseas, with its own auctions as the main sales channel. As a large number of transactions at the auctions take place at high speed, it has been able to rapidly accumulate a huge volume of sales information, such as market trends. It realizes highly accurate pricing by integrating the enormous amount of data accumulated in this way into SOU Brain, the product management system developed in-house, and creating a database. In this way, the Company continues to grow rapidly, as it has created a new business model for purchasing goods from individuals then selling them to dealers, and moreover at high speed. Furthermore, it is now expanding its business scope, including overseas business development and establishing omnichannel for retailing. As a luxury goods reuse company for luxury brand goods, antiques, and works of art, the Company's business model, which integrates the real and the digital worlds and provides services from a new perspective, can be said to be extremely distinctive and highly differentiated within the conventional reuse industry.

Discharge notice from a J-League soccer team as the springboard for growth

2. Company history

The Company's President and Representative Director Shinsuke Sakimoto is a former J-League professional soccer player. He played for Gamba Osaka, but in 2003 he received a discharge notice (he was cut from the player roster) and he retired in 2004. After his retirement, he launched MKS Corporation with his two older brothers, taking over the electrical appliance reuse stores operated by his father, and developing pastry stores. As he suddenly received a discharge notice during his time in the J-League, he conducted business with a sense of crisis, a feeling that it was necessary to constantly improve and evolve. In this frame of mind, his attention turned to branded goods, and in 2007 he started a branded goods buying business and opened the first NANBOYA buying office in Namba. The pastry business and the luxury brand reuse business were then separated, and Mr. Sakimoto established SOU Inc., to conduct the luxury brand reuse business. After that, the Company steadily achieved one success after another by expanding the business area, launching auctions, acquiring a company for developing an app, and it was listed on the stock market only seven years after its establishment.

Company overview

Company history

Date	Event
June 2004	Established MKS Corporation
March 2007	Started the branded goods purchasing business and opened the first NANBOYA Main Store in Namba
December 2011	Established SOU Inc. (Capital: ¥5 million, Head office: Naniwa Ward, Osaka City, Osaka Prefecture)
April 2012	Opened the Tokyo office (Aoyama, Minato Ward, Tokyo)
March 2013	Relocated the Tokyo office (Udagawa Town, Shibuya Ward, Tokyo)
April 2013	Started the BtoB auction Tokyo Star Auction (currently STAR BUYERS AUCTION)
March 2014	Relocated the Tokyo office (Dogenzaka, Shibuya Ward, Tokyo)
April 2014	Relocated the Osaka office (Head office) (Kita Ward, Osaka City)
December 2014	Received The First Company 2015 Award. Started the Concierge (appraiser) Hospitality Contest Started the branded goods purchasing store BRAND CONCIER with an advance booking system Opened the BRAND CONCIER Ginza Store, the first store
March 2015	Started Inspection by LINE, a first of its type, in LINE Business Connect
June 2015	Announced the NANBOYA buying office with a new brand logo and concept
September 2015	Made STAR BUYERS LIMITED (Hong Kong) a wholly-owned subsidiary
November 2015	Changed the name of Tokyo Star Auctions to STAR BUYERS AUCTION
December 2015	Relocated the Tokyo office (Konan, Minato Ward, Tokyo)
January 2016	Started retail sales for general consumers Opened the BRAND RESALE SHOW ZIPANG in Izumisano city, Osaka prefecture
February 2016	Announced the new brand concept and logo for SOU Inc. Announced the new brand concept and logo for BRAND CONCIER, a branded goods purchase business
May 2016	Acquired BRAND CONCIER Co., Ltd., through an absorption merger
June 2016	Made Matomedia Inc. (currently Market Insight Inc.) a consolidated subsidiary (liquidated in August 2018)
October 2016	Opened ALLU, a new brand-name vintage select shop in Ginza In conjunction with this, opened the ALLU EC website
February 2017	Made Hakkoudo Inc., a wholly-owned subsidiary
March 2017	Stated STAR BUYERS AUCTION in Hong Kong
October 2017	Launched miney, an asset management app
November 2017	Relocated the headquarters to the Tokyo office
March 2018	Listed on the Mothers Section of the Tokyo Stock Exchange Started full-scale sales on Wandou Gongzhu, a Chinese cross-border EC shopping app
May 2018	Started the donation program BLUE BATON
August 2018	Hakkoudo Inc., started THE EIGHT AUCTION
September 2018	Launched online bidding auctions in Japan
January 2019	Launched the new EC website, usus
February 2019	Concluded an official partnership agreement with Waseda University Association Football Club.
March 2019	Launched HATTRICK, an auctions service

Source: prepared by FISCO from the Company's securities report, etc.

Globally unparalleled player in the reuse market for dealers

3. Position in the luxury goods reuse industry

The distribution of used luxury brand goods can be broadly divided into C-to-C, which involves purchases and sales between individual consumers; C-to-B-to-C*, which involves businesses purchasing from consumers and selling to consumers; B-to-B-to-C, which involves businesses purchasing from businesses and selling to consumers; and C-to-B-to-B, which involves businesses purchasing from consumers and selling to businesses. C-to-C includes flea markets, online auctions such as Yahoo Auctions (Yahoo <4689>), and flea market apps like Mercari <4385>, and while the consumers listing products can set the asking price for bids, they cannot expect to receive the money immediately. In C-to-B-to-C, there are many general reuse stores for specific areas, and while the seller can receive the money immediately, the buying prices tend to be lower. Buying through men's clothing chains, Amazon, and ZOZOTOWN (ZOZO<3092>) can be said to be one form of this type, but because these businesses often provide their own coupons, it is said that such operations are similar to sales promotions for them. In B-to-B-to-C, the purchasing is solely from dealers, and often combined with C-to-B-to-C.

※ C: Consumer, B: Business.

C-to-B-to-B, conducted by the Company, is a form of wholesale in which products are bought from consumers by various methods, and sold mainly via auctions. It is difficult to start a business like the Company's, which uses sophisticated digital marketing and has the ability to collect big data. Therefore, the company holds a dominant, unrivalled position for wholesales including auctions of branded goods to dealers. Currently, the reuse market is said to be growing, but this is against the backdrop of the growth of C-to-C like Mercari, while the growth of C (B) toBtoC is flat. In particular, it is thought that over-the counter-type sales at reuse stores, which is the main method, are declining slightly.

Reuse was originally a concept that was associated with antiques, used clothing, and pawned goods, but it now refers to the reusable value that can be retained from the time that products, such as a car and motorcycles, were new. This reusable value has come to be gradually recognized and widely used, reflecting the progress of deflation and the era of oversupply in the 30-year period following the collapse of the economic bubble. Within this situation, rarity is an important element in reusable value, and therefore it can often exceed new value. The categories in which such rarity appears most strongly are the categories in which the Company deals, of luxury brand goods and jewelry. Other than the Company, there are other companies conducting comparatively large businesses in this area, including Komehyo <2780> and Daikokuya Holdings <6993>.

Incidentally, according to a 2015 survey by the Ministry of the Environment, the market for luxury brand goods excluding clothes and accessories was worth ¥188.7 billion, the reuse market as a whole was worth ¥3.1,425 trillion, the market excluding cars and motorbikes was worth ¥1.1,237 trillion, the book reuse market, which can often be seen in commercial districts, was worth ¥78.7 billion, and the market for software and types of media was worth ¥73.4 billion. Despite the fact that not much time has passed since the Company was established, it already ranks second for sales in the luxury reuse market, which is the second biggest market after the cars and motorbikes market. In terms of buying, as of 2018 it is estimated that the Company ranks in the top class not only in Japan, but in the world also. It can be said to be the biggest player without major rivals in the luxury goods reuse market for CtoBtoB.

Company overview

Position in the industry

Top 10 in Luxury Brand Jewelry Sales			
Rank	Company	Luxury Brand Jewelry Sales (JPY100M)	Ratio to Total Sales
1	Komehyo Co.,Ltd.	335.4	86.0%
2	SOU	271.8	86.2%
3	Daikokuya Holdings Co., Ltd.	201.0	100.0%
4	HappyPrice	126.2	100.0%
5	EcoRing Inc.	125.3	87.5%
6	Okura	106.7	100.0%
7	Brand off Co.,Ltd.	99.2	97.0%
8	RK Enterprise co.,Ltd	98.3	95.0%
9	K-GOLD INTERNATIONAL CORPORATION.	85.0	100.0%
10	GALLERY RARE Ltd.	73.8	94.0%

Source: The Company's results briefing materials

Business overview

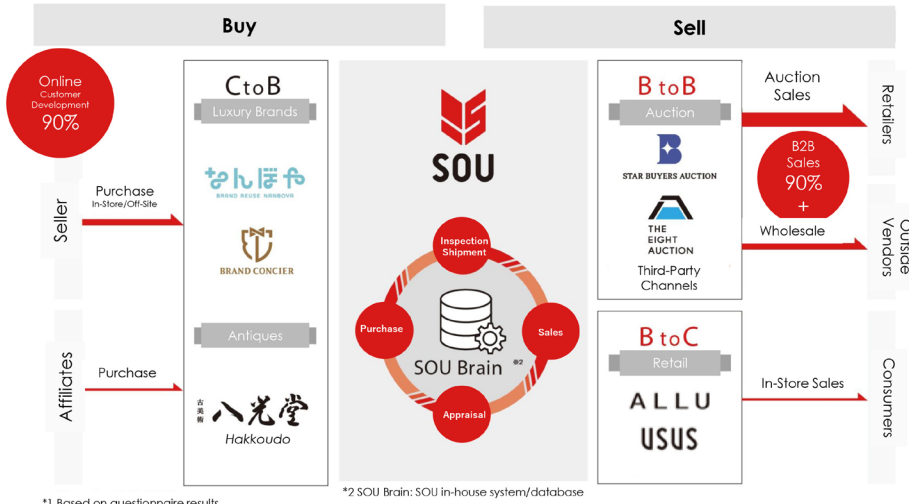
An emerging start-up with high digital literacy in the luxury goods reuse market

1. Business description and business model

The Company can be said to be the most recent entrant into the reuse market. However, the time around 2011, which is when it was established, was 10 years after the IT revolution in 2000. It overlaps with a period in which even late entrants such as Amazon as a comprehensive EC company, ZOZOTOWN as a brand clothing EC mall, and Mercari as a comprehensive reuse company were not restricted by the industry's traditional management resources and rapidly came to the fore utilizing IT in every category. The Company has also been developing digital marketing and a network of buying offices, with SOU Brain, the self-built product management system as the core of its business, and grown by its auctions for dealers which have gained a high market share in the luxury goods reuse industry on a par with companies like Amazon even as a newcomer skilled in digital technologies. Furthermore, it is progressing measures for unrivalled differentiation. Such activities include actively incorporating digital technologies like apps and big data, and evolving its existing business by establishing omnichannel for online auctions and retailers. On the other hand, it is proceeding with businesses overseas while also expanding its business in Japan for acquiring brand goods owned by individuals.

Business overview

Business model



Source: The Company's results briefing materials

Digital marketing and a nationwide network of specialized buying offices

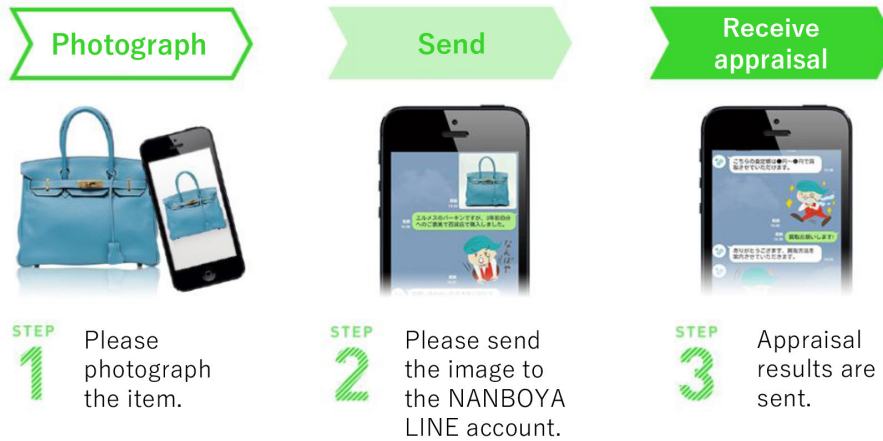
2. Buying operations

(1) Overwhelming power to attract customers supported by its high digital literacy

Ever since the foundation of the Company, while other companies were working to attract customers to their stores conducting both buying and sales mainly through signboards, the company have been utilizing digital marketing. They used the latest advertising methods, of top ranking in searches through SEO and listing advertisements linked to searches, and established a system of O-to-O (Online to Offline: attracting customers to physical locations from the Internet) to draw customers to its buying offices in locations that are easy to visit, such as near to stations and in commercial districts. Therefore, about 90% of the customers in its buying offices are individual customers visiting via the Internet, and 99% of the items purchased are from individual customers. Moreover, it has also built a system called LINE appraisals, in which when a customer is considering selling an item, such as a luxury brand good, they send photos and information on the item they wish to sell to the account of NANBOYA, by which they can confirm the approximate amount they will receive as the buying price. As the results of this appraisal are returned in just a few minutes, the system has an excellent reputation for its convenience and has become a major weapon for attracting customers. In addition, the height of the Company's digital literacy means it can easily synchronize with its major customers, of the economic-bubble generation and the baby-boomer generation who tend to be highly digital literate and like luxury brands, and this is also considered to be one of the reasons why these consumers feel a high sense of affinity with the Company.

Business overview

The LINE appraisal is completed in three steps, requires no appraisal fees, and it takes 30 seconds to apply



Source: The Company's website

Miney, which was released in 2017, is an app that is indicative of the Company's high level of digital literacy. It is an asset management app in which users can check the present value of an item, price trends from the past to the present, and the total amount of registered items. It is a revolutionary marketing tool that enables users to manage their personal belongings as real assets and to easily sell them through indicating the prices of these possessions that change on a daily basis. It is considered effective not only for retaining existing customers, but also for acquiring new customers. Currently, users can manage watches, brand jewelry, bags, and purses and wallets, but it would also seem to be highly extendable in terms of the items it can handle. The Company is also progressing collaborations with other companies for miney. In December 2017, it began a collaboration with Money Forward, an automatic household accounts and asset management service. In October 2018, with ONE, a photo buying app (the collaboration with ONE has now ended). By continuing and expanding such collaborations, the targets for personal asset management may expand to genres that have large synergies with the Company's business, like real estate, antiques, and alcoholic drinks. In other words, miney can be said to be a tool not only to maintain and expand the customer base, but also to increase the sales amount per customer.

(2) Overwhelming buying power from a nationwide network of specialized buying offices

The main products that the Company handles are second-hand items, such as luxury brand goods, precious metals, watches, bullion, precious stones, antiques, and works of art. Among them, it mainly purchases products that are very difficult to appraise and that can secure a high unit price when sold. Due to the effects of digital marketing, the number of items it purchases annually has risen to 500,000 items, while the average purchase price is also high, at ¥50,000. There are three buying methods: over-the-counter buying, mail-order buying, and off-site buying. For over-the-counter buying, the concierge (the appraiser) appraises and evaluates the brand good or other item that the customer wants to sell at the office, and the item is bought then and there. The Company's buying offices are extremely distinctive and are linked online to veteran appraisers at the headquarters, and in particular, the buying prices of high-value items can be double checked simultaneously at the office and at the headquarters. Also, while other companies perform the two tasks of buying and sales at their stores, in contrast the Company's buying offices specialize only in buying, which makes them easier to manage both financially and operationally and has facilitated its development of a network of offices. This is considered to be one of the reasons for the accelerated growth.

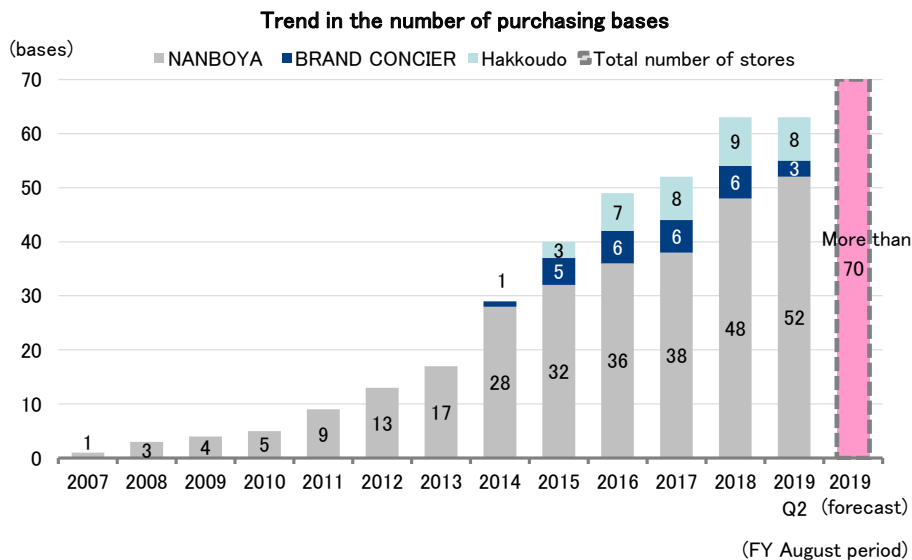
Business overview

Other than buying offices, for delivery purchases, the Company appraises and evaluates items sent to it by customers, such as by courier, notifies them by email or other method of the buying price, and purchases the item (or it returns the item if it decides not to buy it). For visit buying, in the event that it is difficult for the customer to go to an office or send the item, a concierge visits them to conduct the appraisal, evaluation, and buy the item. The Company has developed 52 NANBOYA, buying offices which have interior designs similar to elegant beauty salons with bright, white harmonious color schemes, and 3 BRAND CONCIER buying offices that are full of sense of luxury, including one in department stores in Japan, in which customers can make reservations by telephone or online. Also, the subsidiary Hakkoudo Inc., manages 8 Hakkoudo offices, which handle items including antiques and old and contemporary works of art. On comparing the number of buying locations and business formats to those of other companies in the same industry, we see that the Company buys a wider array of items. Items are delivered to the stock center in two days after buying, and after being inspected and maintained by specialists, most are sent to auctions.

NANBOYA



Source: The Company's results briefing materials



Source: prepared by FISCO from the Company's Briefing Materials on Growth Potential and results briefing materials

We encourage readers to review our complete legal statement on "Disclaimer" page.

Realizing a high-speed turnover by auctions while aiming to stablish omnichannel for retail

3. Sales operations

(1) Overwhelming sales power by auctions in Japan and overseas

The purchased items are mainly sold at STAR BUYERS AUCTION, which are auctions for dealers owned and managed by the Company. They are also sold via wholesales to dealers in Japan and overseas, including via the auctions of other companies domestically and abroad and at overseas exhibitions. Wholesales constitute a large percentage of total sales, of around 96%, and the remainder are retail sales to general consumers through the Company's own retail stores and EC website. The auctions in Japan are held over four days every month at the auction site in the headquarters. Every month around 16,000 products are exhibited and the monthly transaction amount is approximately ¥1.5bn (FY8/19 Q2). In Japan, the Company has also started online bidding auctions (held on the 23rd of each month).

Other than the above, as its own sales channel, the subsidiary Hakkoudo holds THE EIGHT AUCTION for antiques for dealers twice a month, and the number of small-scale auctions is also increasing. Antiques and works of art are highly profitable, because the aspect of information asymmetry due to rarity is strong and they are difficult to handle on the Internet. Moreover, another of the Company's strengths is that it employs 35 antiques appraisers. On adding this to the Company's strength in collecting items, it is able to have an overwhelming presence in the field of antiques and works of art.

Overseas, in March 2017 the Company started auctions in Hong Kong for diamonds and melee diamonds (small diamonds with a carat of 0.1 or less). In August 2018, the number of times the auctions are held was increased to 4 times a year, and the business scale is expanding, such as launching test sales of watches. In FY8/19, watch auctions will become fully fledged and a total of 10 auctions are scheduled to be held for diamonds and watches.

Approximately 64% of sales are from wholesales to dealers via auctions (FY8/19 Q2). Although profitability is low, it is possible to conduct high-turnover transactions for which stable demand can be expected. Also, because a large number of diverse products are sold at the auctions, it is easy to ascertain information on market trends and market prices, which the Company uses to improve SOU Brain's functions and the concierges' appraisal and evaluation skills. This in turn leads to a large number of buying of even more high-quality products and many sales at the auctions. In this way, the Company can be said to have created a virtuous circle for its business.

The auctions (left: an auction in Japan, right: a watch auction in Hong Kong)

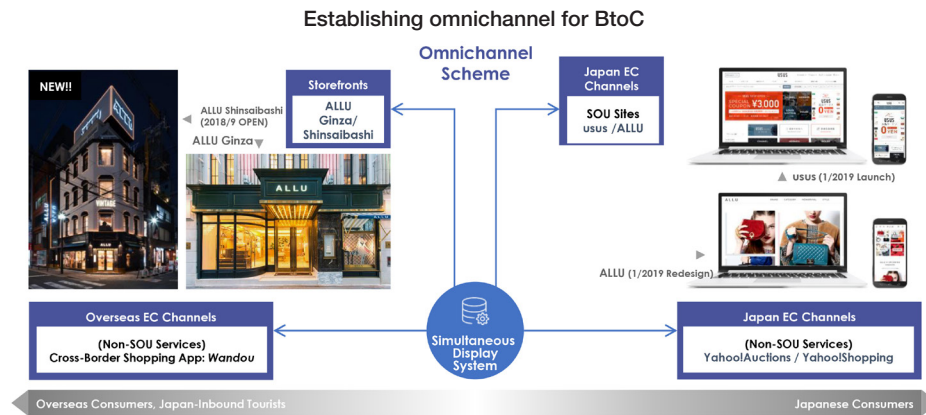


Source: The Company's results briefing materials

Business overview

(2) Retail shifts towards an omnichannel approach

The Company’s retail business has a short history. It began in January 2016, when it held the Brand Resale Show ZIPANG at a multi-function facility near to Kansai International Airport for general inbound tourists and domestic consumers (it closed in January 2019). In October 2016, it opened the retail brand ALLU Ginza Store in Ginza, Tokyo, for wealthy and inbound customers, with a product lineup focused on highly rare vintage items and antiques, and which does not compete with comparable brand shops. The ALLU Shinsaibashi Store was opened in Shinsaibashi, Osaka, in September 2018, and the average sales price for ALLU is said to be about ¥370,000. At the same time as opening the ALLU Ginza Store, the Company launched the ALLU EC website, on which customers can buy the items in the physical store. Next, in March 2018, it fully opened the store for the cross-border e-commerce app Wandou Gongzhu, which has 5 million members in China, and then in January 2019, it opened “usus”, a new e-commerce site that handles a wide range of street brands for general consumers, and in such ways the number of contact points with consumers is gradually increasing. Furthermore, the Company is strongly progressing the establishment of omnichannel for retail, including developing a simultaneous exhibition system that synchronizes the stock held at each contact point (stores and e-commerce).



Source: The Company's results briefing materials

SOU Brain, the core of the business model, and the Company’s three strengths

4. Short business cycle through the Company’s three strengths

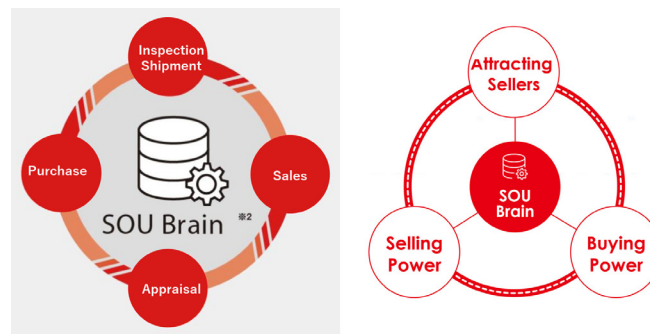
SOU Brain, which is the product management system developed in-house, is a database in which it has accumulated a huge volume of data on buying and selling, covering transaction information from what is bought by what kind of person and for how much, to the latest information on sales trends, such as when items are sold and for how much. By accumulating a huge volume of transaction data collected through transactions in SOU Brain, including from the over-the-counter buying of customer goods and LINE appraisals, and from sales from auctions and retail, the Company is able to indicate the price quickly and accurately when carrying out the appraisal and evaluation. Using SOU Brain gives it the time to conduct appraisals and evaluations at buying offices, and the points of contact with customers can be expanded to enable concierges to listen to them about the background to the sale, which is important for luxury, high-value items, and this helps to build relations of trust with customers. Therefore, not only will customers sell their items even when a comparatively low price is indicated to them, they also become repeaters who continuously visit the offices.

Business overview

In addition, it is also possible to buy items at high prices depending on product trends, because the pricing is firm (the trend risk can be mitigated because of the high turnover of transactions). Moreover, by supporting the concierges, SOU Brain makes it possible to shorten the period of education to acquire “discerning eyes,” which is considered difficult to cultivate. Of course, each office is connected to the headquarters online, and a system is in place in which the experts for each product category support the concierges when necessary. The development and upgrading of the system and of the elements surrounding the system are conducted in-house. It can be said that SOU Brain makes discerning eyes scientific through the size of its database and data-collection capability, serving as the Company’s driving force that overwhelms the competition, and this difference is expanding day by day.

As described above, based on the data accumulated in SOU Brain, the Company attracts sellers through digital marketing and has these customers visit the buying offices that it manages throughout the country, where it buys high-value items. Even among these items, it buys items that are difficult to appraise but highly profitable, and then stably and quickly sells them to business dealers, mainly via auctions, with an average stock turnover of two months. In other words, centered on SOU Brain, which is the growth engine, it can be said that the Company is realizing growth by rapidly cycling through its three strengths: seller attraction, buying power, and sales power. The data collected from this is accumulated in SOU Brain and the next business cycle is rotated. This is its business model, evolving in a spiral.

Image of SOU Brain and the Company’s three strengths



Source: The Company's results briefing materials

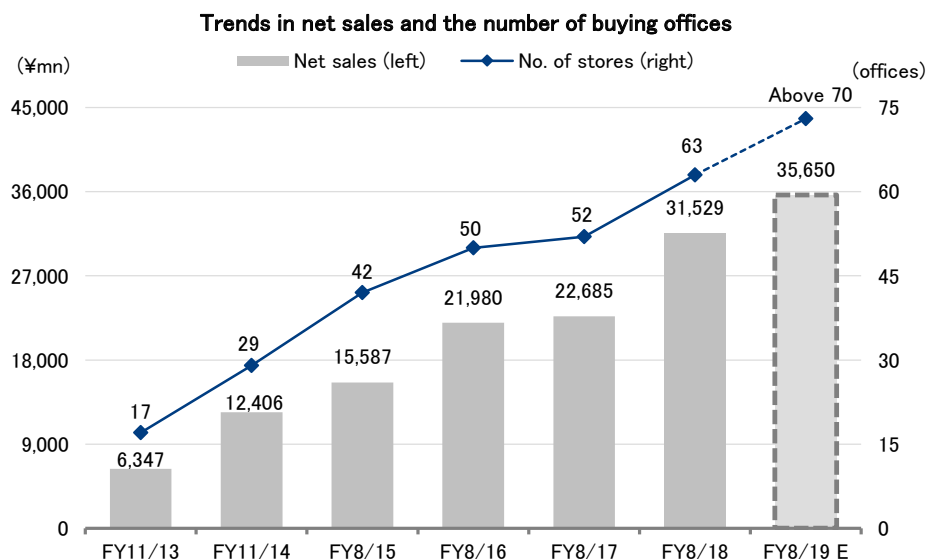
Performance trends

Outperforming competitors through high growth potential and high profitability

1. Earnings structure

Generally, the winner in the reuse industry is the company that dominates in buying activities at the entrance to the value chain. This trend was considered to be even more pronounced when items were purchased only from general consumers in the areas (markets) around the stores. Therefore, every company makes great efforts on buying. In this sort of industry, the Company launched a business focused on buying premised on wholesales through auctions. This is a method different to reuse stores for general consumers, and through overwhelming differentiation from its unique business model, it has been able to dominate the competition not only in buying activities at the entrance to the value chain, but also to as far as the exit, at the auctions. This is considered to have resulted in the Company's fast growth and high profitability.

The Company's gross profit margin is slightly low as it conducts wholesales, but the turnover rate is high against the backdrop of its large number of buying locations and auctions. The ratio of gross profit to inventory investment, which indicates profits, is far higher than those of other companies. Due to the entrance and exit being different, it seems that management costs (SG&A expenses) are low. Therefore, the Company's operating profit margin is comparatively high. While there is a sense that online companies are able to realize a high ratio of gross profit to inventory investment, in many cases they do not have the sales (the sales unit price) to cover management costs. Compared to the Company, which integrates the online with real locations, it seems that such companies are a little overconfident in the Internet.



Note: results are stand-alone up to FY8/15
 Source: prepared by FISCO from the Company's prospectus, etc.

Performance trends

Comparison of listed companies in the luxury goods reuse industry

Code	Company name	Financial period	Inventory Turnover rate (%)	Sales Gross margin (%)	Ratio of gross profit to inventory investment (%)	SG&A expenses ratio (%)	Sales Profit margin (%)	Main sales channels
9270	SOU	FY8/18	7.8	27.2	213.2	21.2	6.0	Auctions
2780	Komehyo	FY3/18	4.4	28.5	124.1	24.9	3.6	Stores
6993	Daikokuya Holdings	FY3/18	5.4	35.5	191.3	32.0	3.4	Stores
3545	Defactostandard (Brandear)	FY9/18	9.1	49.0	444.8	45.3	3.7	EC
4385	Mercari	FY6/18	-	81.0	-	93.3	-12.4	Internet

Note: inventory turnover rate = net sales / inventory average, ratio of gross profit to inventory investment = inventory turnover rate × gross profit margin
 Source: prepared by FISCO from each company's results summary report, etc.

Although profits declined in the 1H, the rate of progress for profit is slightly ahead of schedule at 52%

2. FY8/19 Q2 performance trends

In the FY8/19 Q2 results, net sales were ¥18,956mn (up 23.2% YoY), operating profit was ¥1,152mn (down 3.3%), ordinary profit was ¥1,149mn (down 2.1%), and profit attributable to owners of parent was ¥770mn (down 11.2%). In FY8/19 Q2, the rates of progress toward achieving the forecasts were low compared to in FY8/18 Q2, but this was because the contribution to profits of FY8/18 Q3, which is when the Company was listed, was reduced, which meant that the contributions to profits of FY8/18 Q2 became comparatively large. Therefore, it can be said that the low rates of progress in FY8/19 Q2 are not particularly a cause for concern. However, it seems that for the gross profit margin, the Company wanted to take a little more. That said, while sufficient inventory was secured through the active expansion of the NANBOYA, the strong yen in December and January meant that among the dealers participating in the auctions, the motivation for purchases of the dealers planning sales overseas temporarily declined, which led to a decline in bid prices, and this is thought to be the reason for the fall in the gross profit margin. On analyzing the decline in operating income, it seems that in addition to the decline in the gross profit margin, the main factors were the expenses for M&A preparations and relating to the TOB, and the increase in personnel expenses and rent following the active business expansion. Profit attributable to owners of parent declined by double digits due to tax effects.

FY8/19 Q2 performance trends

(units: ¥mn, %)

	FY8/18 Q2	% of sales	Progress rate	FY8/19 Q2	% of sales	Increase-decrease rate	Progress rate
Net sales	15,390	100.0	48.8	18,956	100.0	23.2	53.2
Gross profit	4,401	28.6	51.4	4,817	25.4	9.4	50.2
SG&A expenses	3,210	20.9	48.0	3,665	19.3	14.2	49.5
Operating profit	1,191	7.7	63.5	1,152	6.1	-3.3	52.4
Ordinary profit	1,174	7.6	65.0	1,149	6.1	-2.1	54.0
Profit attributable to owners of parent	867	5.6	69.8	770	4.1	-11.2	53.1

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

Performance trends

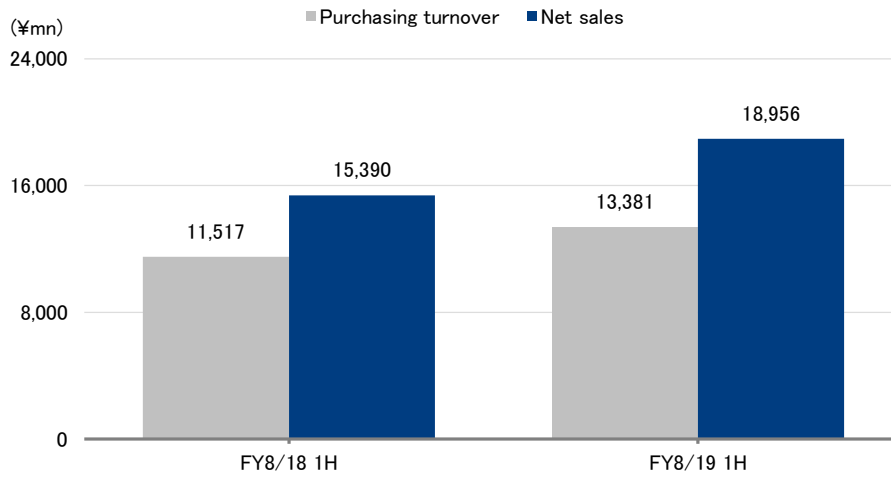
In buying, the Company is working to improve the utilization rates of buying offices and to improve the efficiency of the buying brands, in addition to strengthening buying. It closed 3 BRAND CONCIER and 1 Hakkoudo at the subsidiary, while it opened 4 NANBOYA, for which it has many offices and which play the main role for attracting customers. There were also the effects from the buying office openings in the previous fiscal year, and the Q2 purchasing turnover trended steadily, at ¥13,381mn (up 16.2% YoY). For sales, alongside the rise in the purchasing turnover, sales trended favorably both in Japan and overseas. In particular, overseas sales achieved high growth exceeding sales in Japan, and there is the sense that overseas, the efforts to acquire customers are achieving a response. By sales channel, in the auctions, the ratio of successful bids declined slightly, including in the online auctions. But even so, sales showed high growth of around 33% both in Japan and overseas against the backdrop of the increase in the number of times the Company's own auctions were held. For retail, while the sales scale is still small, a double-digit increase in sales was achieved through enhancing the online channel.

In Japan, STAR BUYERS AUCTION held 24 real auctions, which is the same number as in the previous fiscal year, while it started online bidding auctions in September. In Hong Kong, diamond auctions (September and November 2018, and February 2019) and watch auctions (November 2018 and February 2019) were held. While it mainly uses the sales channels of other companies, Hakkoudo also made a fully-fledged start for its own auctions, holding them twice a month (antiques and tea-making utensils on even-numbered months, paintings and drawings on odd-numbered months). In retail, the second ALLU store, which deals mainly with rare, vintage items, was opened in Shinsaibashi, Osaka, and in addition, the usus e-commerce website, which handles a wide variety of items from luxury brands to second-tier brands, was opened.

Moreover, aiming to strengthen e-commerce sales, the Company worked to coordinate inventory across all of e-commerce sites, including its own sites of ALLU and usus, the ZIPANG store on Yahoo! Auctions and the cross-border e-commerce shopping app Wandou Gongzhu. It promoted efficiency alongside the establishment of the omnichannel scheme through the simultaneous exhibition system that makes it possible to simultaneously exhibit items in multiple sales channels. For miney, which is an asset management app that manages the users' personal belongings as real assets and proposes the management of them, the Company strengthened measures to increase the number of users and the registered asset amount, through collaborations with other companies and the fully-fledged release of the Android version. In addition, it considered an M&A of U.M.E. Co., Ltd., and also acquired its own shares. It did not reach an agreement with U.M.E. on the terms of the acquisition, which was cancelled. With regards to the acquisition of treasury shares, the Company did not cancel them after the acquisition and is holding them as treasury shares, as it is considering utilizing them for its growth strategy, such as for employee incentives and M&A.

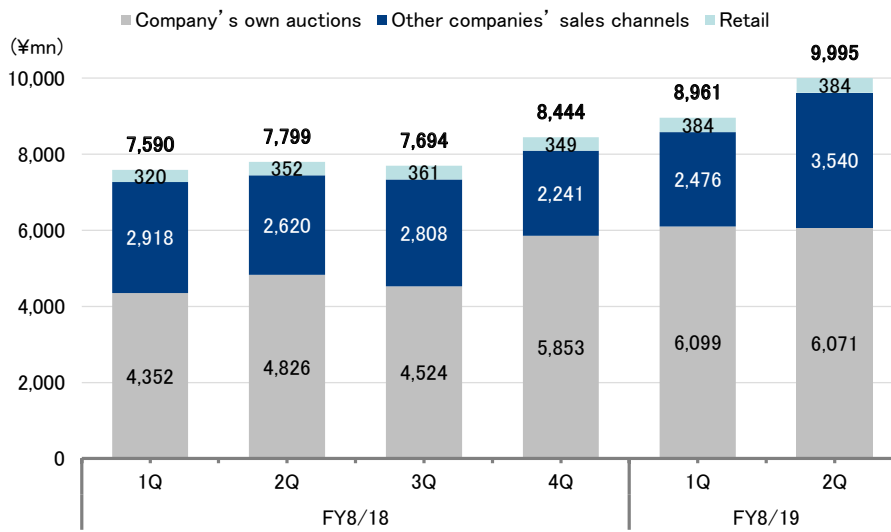
Performance trends

Trends in the purchasing turnover and net sales



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

Sales trends by sales channel



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

FY8/19 results may exceed the forecasts

3. FY8/19 results outlook

For the FY8/19 results outlook, the Company is forecasting net sales of ¥35,650mn (up 13.1% YoY), operating profit of ¥2,200mn (up 17.2%), ordinary profit of ¥2,130mn (up 17.9%), and profit attributable to owners of parent of ¥1,450mn (up 16.7%). The rates or progress in FY8/19 Q2 toward achieving the forecasts were at a level that is not a problem. But on considering the fact that that sales-increase effect was more than expected, and that dealers' motivation to participate in the auctions, which had fallen due to the strong yen, is recovering, it is possible that the results will slightly exceed the Company forecasts, despite the concerns that SG&A expenses may increase as new buying offices will be opened in the 2H. It seems that the Company itself has positioned them to be conservative.

FY8/19 results outlook

	(unit: ¥mn, %)				
	FY8/18	% of sales	FY8/19 E	% of sales	Increase-decrease rate
Net sales	31,529	100.0	35,650	100.0	13.1
Gross profit	8,570	27.2	9,600	26.9	12.0
SG&A expenses	6,693	21.2	7,400	20.8	10.6
Operating profit	1,876	6.0	2,200	6.2	17.2
Ordinary profit	1,806	5.7	2,130	6.0	17.9
Profit attributable to owners of parent	1,242	3.9	1,450	4.1	16.7

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

Competition in the reuse industry is forecast to further intensify, due to the growth of the various companies alongside the market expansion and the increase in the number of new entrants. In this sort of environment, the Company's policy is to continuously open buying offices in order to ensure stable purchasing. In FY8/19 2H, it plans to open around 10 buying offices. Also, in order to improve office efficiency, it intends to relocate some of its existing locations. The same number of auctions are expected to be held as in the 1H both in Japan and overseas. For profits, the impact of the strong yen in the 1H has run its course and the gross profit margin is forecast to improve, but on considering the same uncertain factors and the increase in SG&A expenses, including due to the openings of offices, the Company decided to leave the initial operating profit forecast unchanged. In particular, to deal with these uncertain factors, its policy is to devise techniques in sales so that it can continue to prioritize buying, as before. For example, it has the option of setting a conservative bid price or not selling, but these options can adversely affect the transaction-completion rate, so in the future it plans to have SOU Brain predict the pricing that will maximize profits by having the AI study the uncertain factors. Such pricing is considered to be effective not only for auctions, but also for all pricing, including for retail and buys, the Company intends to actively use digital technology in the future.

Medium-term strategy

Aiming to be a global luxury market data company

1. Vision and policy

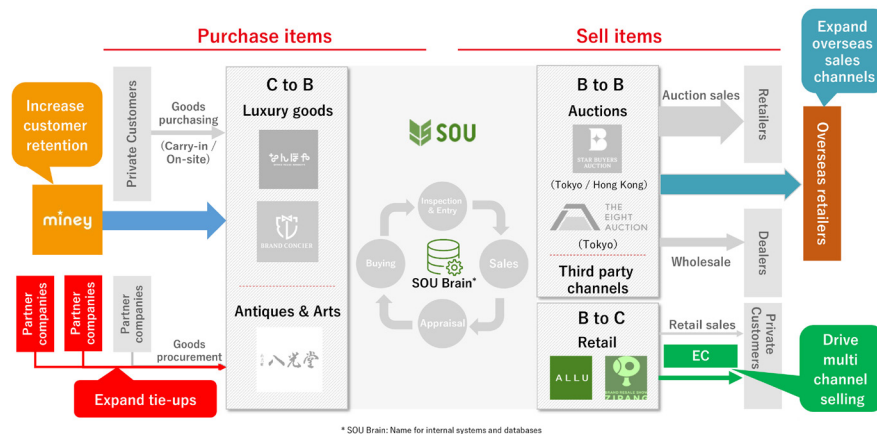
The Company's management mission is to provide global access to pricing and value data for smarter lifestyles, and its management mission is to change from being a luxury reuse company to being a global luxury market data company. In its management mission, the word "global access" can be said to be a keyword in the Company's business model and is an idea not conventionally found in the reuse industry. We can read its strong overseas orientation and self-confidence in SOU Brain from the above. Based on this vision and management mission, the Company has formulated the policies of strengthening luxury goods market data collection and promoting personal wealth management, and moreover toward further growth. It is working to 1) expand and enhance buying bases, 2) strengthen and expand overseas buying and sales, and 3) improve the functions of miney, the asset management app. Through these efforts, it is evolving its business model, which is expected to lead to growth in the medium- to long-term.

The new growth engines are the overseas business and miney

2. Medium-term strategy

In order to expand the existing luxury reuse business in Japan, for the time being the Company's policy is to continuously increase the number of buying offices at a pace of around 10 a year, mainly in major cities and within commercial facilities. To expand the business scope, it is also envisaging M&A focusing on locations, expertise, genres, and customers. Sufficient medium-term profit growth can be expected solely from these efforts, but since the upper limit of the number of buying offices in Japan is considered to be around 200 stores, in the medium- to long-term, it will be necessary to create purchasing sites and sales destinations using a different approach than previously. The trump cards for this will be the overseas strategy and miney. The Company intends to use its overseas strategy to expand its field of business and to use miney to retain and expand customers. In conjunction with this, it will collect data more widely through the overseas strategy, while using miney will enable it to collect data more deeply. This is expected to lead to the strengthening of SOU Brain, which is the core of the Company's business, and also to its dominant position in the global luxury goods reuse industry.

The targeted business model



Source: The Company's results briefing materials

We encourage readers to review our complete legal statement on "Disclaimer" page.

Medium-term strategy

The global market for new luxury items is forecast to expand in scale from ¥24 trillion (2017) to ¥32 trillion (2022). It is generally said that when a market for new items exists, a market for used (reuse) items will also form. The same as the luxury market, the used market, which is said to be worth ¥2.5 trillion, is forecast to grow to ¥4 trillion by 2022. The market shares by area vary, but for the new-items market, North America constitutes 25.8%, Europe 17.6%, and the Asia Pacific region, 52.3%, so the Asia Pacific region, which is realizing remarkable economic growth, constitutes more than half of it. On the other hand, for the used-items market, North America constitutes 23.3%, Europe 32.9%, and the Asia Pacific region 30.1%, from which we understand that the concept of reuse has spread across Europe. But we can also understand from this that despite driving the global new-items market, the used-items market in the Asia-Pacific region is still small. However, given the correlation between new and used items, it can be said that the Asia Pacific used-items market may grow significantly in the future. Of course, even in areas other than the Asia Pacific region, the used-items markets are expected to grow to a certain extent.

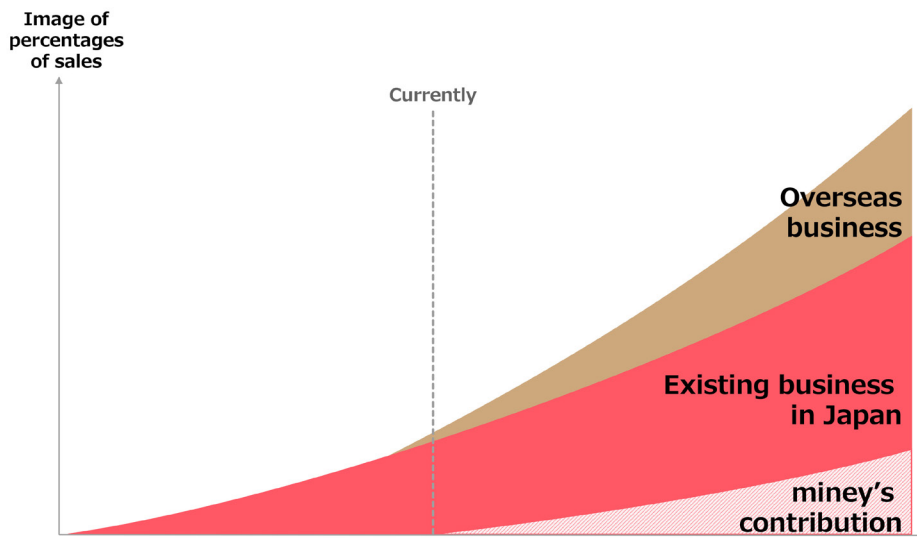
Therefore, the Company has begun to expand and enhance its buying offices and investigate measures to strengthen sales overseas, including in the Asia Pacific region, Europe, and the United States. For the buying offices, it is investigating buying in various countries, starting with Hong Kong where the Company currently holds auctions. It also plans to directly enter markets, but it seems that it can save time by creating a network locally, such as by investing in local companies. For sales also, it intends to strengthen wholesales for the wholesalers in each country. For this, it is considered that the focus will be on efficient online auctions that do not place limitations on where the auction is held. In this way, it seems that the Company plans to develop globally the model that has proven successful in Japan, and at the same time, to progress the globalization of SOU Brain by accumulating luxury goods market data that it obtains in its business on buying, sales and household inventories. There is no other company with a similar business model to that of the Company throughout the world, and the awareness of “Checked in Japan,” which is displayed on items of good quality and shows they have been appraised with accuracy and fairness, is spreading among consumers throughout the world, is considered to be a major advantage. The aim would seem to be to create a global luxury reuse platform. If it conducts fair auctions of good-quality items, then more and more information will be concentrated in the Company, which is likely to even further increase its profitability and growth potential.

On the other hand, the Company has launched fully-fledged measures to strengthen miney so it can widen the customer groups, retain customers, and collect data more deeply. The app was launched in October 2017, and even without any promotions, by February 2019 it had 34,000 members, 37,000 registered products, and ¥5.5bn worth of registered assets. It is calculated that ¥300mn worth of items are newly registered a month. Among them, it seems that already 5% result in actual buyings. In this way, miney can be said to be a marketing tool with extremely large potential, and it is thought that the Company intends to develop it to serve as its growth driver. Toward this, it is currently working to improve miney’s functions, and in December 2018 it released an Android version. It also introduced push notifications as a technique to guide users to actual purchases. During FY8/19, the Company plans to expand its genres to antiques and works of art. Moreover, going forward, it seems that it is considering actively pursuing collaborations with other industries and services and expanding the genres even wider, including to real estate and automotive. Of course, by reflecting the luxury data collected in the global strategy, it is expected to be applicable to the management and operations of all types of individual assets. As indicated by the Company, if a lifestyle spreads, of changing from buying, using and discarding to buying, using and changing to an asset for all goods, then miney can also be expected to evolve from being merely a luxury reuse tool to being the standard personal asset management tool for individuals. At that time, it is highly likely to have become one of the powerful drivers of the Company’s growth.

Medium-term strategy

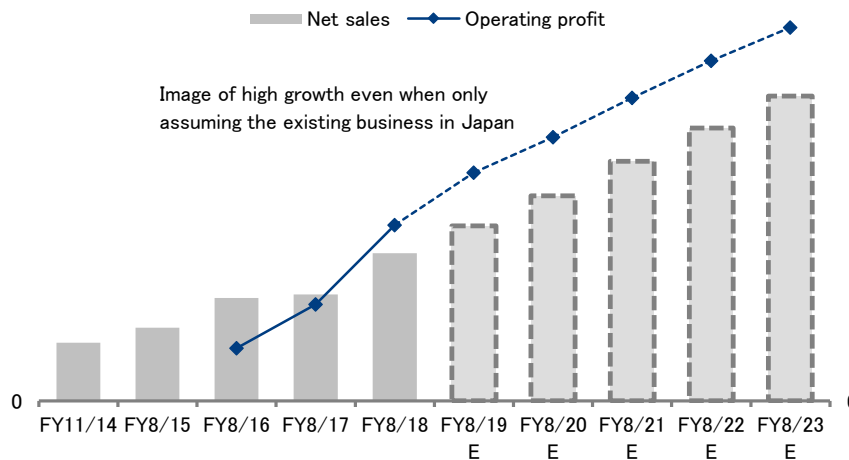
As described above, the Company intends to continue to grow in the medium to long term based on the growth of its existing business in Japan, through expanding its business overseas and using miney to acquire new customers. On the other hand, currently there is the aspect of its business in Japan and Hong Kong being supported by inbound demand, and if there is a risk, then it is considered to be related to the inbound tourism market. However, for Japan, the Tokyo Olympics and Paralympic Games will be held, so the stable growth of the last few years is expected to continue. For overseas, it is thought that business diversification will result in risk diversification. Whatever the case, these cannot be described as significant risks. Rather, if it can suppress the competition at the entrance and exit to the luxury goods market, we can expect the Company, which realizes high-speed turnover for transactions that no other company can match, to grow in the medium to long term.

Medium-term growth image (the Company's image)



Source: reprinted from the Company's Briefing Materials on Growth Potential

Medium-term growth image
 (image of existing business bases in Japan, prepared by FISCO)



Source: prepared by FISCO from the Company's Briefing Materials on Growth Potential

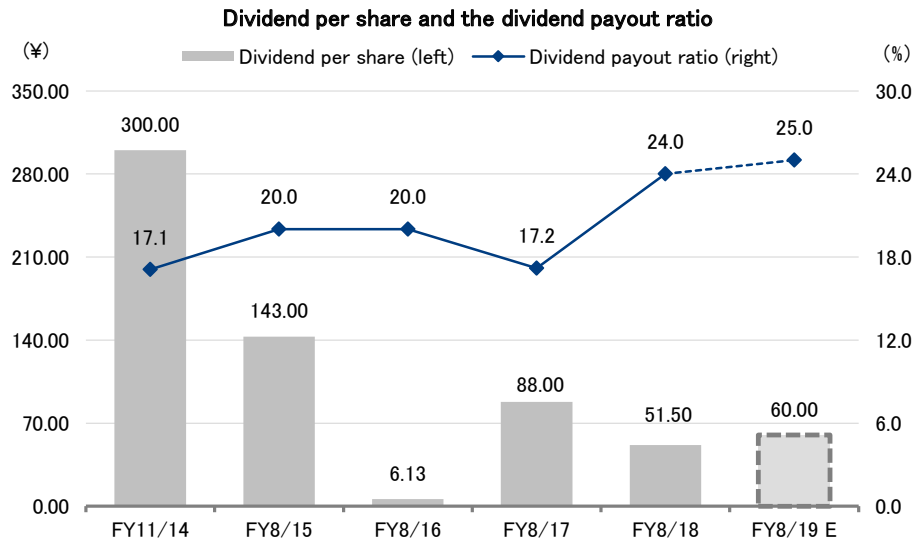
■ Shareholder return policy

Targeting a dividend payout ratio of 25% or above

The Company's basic policy is to stably pay dividends to shareholders alongside its intention to reinvest funds based on its business plan, which is founded on an awareness that continuously improving enterprise value will contribute to the interests of shareholders in the long term. For the dividend from surplus, in principle it targets a consolidated dividend payout ratio of 25% or above, while taking into consideration the consolidated results and also aspects such as the business environment, capital efficiency, and free cash flow. However, in a fiscal year in which net income and the capital structure fluctuate greatly due to special factors, it determines the dividend amount and the dividend payout ratio by taking into consideration the effects of these factors. Also, while the base date for the year-end dividend is August 31 and the base date for the interim dividend is the last day of February, the basic policy is to have a year-end dividend once a year. With regards to the matters prescribed in Article 459 Paragraph 1 of the Companies Act on the Dividends from Surplus, etc., its Articles of Incorporation stipulate that resolutions of the Board of Directors may be made, unless otherwise provided for in the laws and regulations. For the FY8/18 dividend, based on the above-described basic policy of paying a stable dividend, the Company paid a dividend per share of ¥51.50, while also retaining the internal funds to invest in growth. It has not yet decided on the dividend per share for FY8/19, but a dividend payout ratio of 25% or above can be expected.

The Company purchased its own shares in February 2019. In response to the intention of a major shareholder, SF Property Management LLC, to sell ¥1bn worth of the Company's shares, it comprehensively took into account the effects of this sale, such as on the liquidity and price of the Company's shares due to the temporary release of a large volume of them onto the stock market, and decided to purchase these shares as treasury shares. The acquisition of treasury shares does not significantly affect the Company's financial position or its dividend policy, but rather, it is considered that it will ultimately lead to the return of profits to shareholders through improving capital efficiency, including earnings per share and return on equity. With regards to the disposal of these treasury shares, the Company is investigating ways to directly utilize them for profit growth, including an incentive plan for its employees and an external growth strategy through M&A or other methods.

Shareholder return policy



Note: The Company has not yet decided the FY8/19 dividend and the value shown is FISCO's forecast
 Results are stand-alone up to FY8/15
 Source: prepared by FISCO from the Company's securities report, etc.

Information security

Aiming to improve the personal information protection management

In areas such as its buying office operations and sales promotions, the Company handles customer information, including their addresses, names, occupations, ages, and credit card information. The Company registers and manages this personal information in ledgers and other records, or by electromagnetic methods. Therefore, it is establishing a system to take appropriate steps to protect personal information and to acquire the Privacy Mark. In addition, it is working to improve its personal information protection management functions, to comply with the Act on the Protection of Personal Information, and to prevent leakages of personal information, by establishing in-Company regulations and other rules, strengthening the in-Company management structure, thoroughly implementing employee education, and bolstering the security of the information system.



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■ For inquiry, please contact: ■

FISCO Ltd.

5-11-9 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062

Phone: 03-5774-2443 (Financial information Dept.)

Email: support@fisco.co.jp