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【Speech Summary for FY2022 Third Quarter Financial Results Briefing】

Director & Managing Executive Officer
Hideki Moriya
Director & Executive Officer, CFO
Keita Shimizu

1. Overview of FY2022 Third Quarter Financial Results

Director & Executive Officer, CFO, Keita Shimizu

▪Report of Financial Results for Q3 (presentation p.4)

In Q3 of FY2022, cumulative figures were 452.8 billion yen in net sales, 19.4 billion yen in operating profit, and 15.8 billion yen in net income. We achieved positive increases year-on-year across all items, an increase in both sales and profits, and the highest performance ever was reported for Q3. Looking at the cumulative figures, we can see that both net sales and net income have increased from the previous period.

▪Executive Summary for Q3 (presentation p.5)

In Q3 of FY2022, we were able to achieve an increase in both sales and profits despite restrictions on human flow and other pre-emergency measures put in place to prevent the spread of COVID-19 in Japan. Even without taking into account the new consolidation of Gelson's, we achieved record-high sales and profits in Q3.

Particularly in the aspect of operating profit, steady effects have been produced by strategic initiatives set forth at the beginning of the fiscal year, such as the strengthening of PB with originality, improving pricing accuracy, and improving inventory turnover ratio to enhance the "Something New" concept as announced in Q2. We successfully improved profitability while enhancing store appeal and differentiation from our competitors.

One of the particularly noteworthy achievements is the year-on-year increase in operating profit for existing stores in the GMS business of 600 million yen.

Therefore, there are no changes in the full-year earnings forecast. We will continue to focus on strategic measures in the fourth quarter and beyond with a view to achieving further growth.

▪Domestic Discount Store Business (presentation p.6)

The Discount Store (DS) business achieved an increase in both sales and profits, with various strategic measures continuing to produce steady results from Q2.

Existing stores contributed to growth at 100.9% year-on-year growth. As the graph shows, the gross profit margin of existing stores has improved every month year-on-year as a result of the promotion of the strategic measures mentioned earlier, achieving greater year-on-year increases than in Q2.

Regarding SG&A expenses, we have also continued to control them successfully and kept them within the budget, despite the rise in utility costs and other factors.

▪Discount Store Business: Efforts to differentiate stores and improve their attractiveness (presentation p.7)

▪Strengthening of PB/OEM

As for the private brand (PB) and OEM, PB was rebranded in February last year and was promoted to simultaneously strengthen differentiation from national brands (NB) and other retailers while improving profit margin. As a result, PB sales in the DS business attained significant growth, increasing by 19.9 billion yen year-on-year. In particular, gross profit grew to 8.1 billion yen, becoming the greatest driver of gross profit growth for the entire group.

Measures such as the development of hit products with originality, improvement of affordability, and enhancement of brand recognition through marketing measures inside and outside stores have been successful. Since this is still the first year for focusing on strengthening PB/OEM, we will continue to further expand sales in the next fiscal year and beyond. The specific targets and measures will be announced during the announcement of the mid-term corporate plan, scheduled for August.

▪Improve inventory turnover

With regard to inventory turnover ratio, we controlled inventory growth by closely monitoring each product in both the sales (= exit) and purchasing (= entry) aspects, with a view to creating attractive shop floors that constantly offer “Something new.” As a result, we successfully reduced the inventory at existing stores by 10.2 billion yen by the end of Q3 of FY2022.

Going forward, we will continue to put effort into controlling inventory growth with the aim of reducing inventory valuation loss at the end of the period.

▪Discount Store Business: Strengthening customer contact points with majica app as a starting point (presentation p.8)

With regard to the digital measures that we have been focusing our efforts on starting from the current period, we worked on increasing the number of majica members with a view to improving understanding of our customers and improving points of contact with them. As a result of the measures, the number of members increased rapidly to 9.16 million by the end of March, as shown in the graph.

By the end of August, we plan to strengthen the app's functions. More specifically, we will update it to enhance the existing payment and information provision functions, as well as add new review and product search functions. Through the completely overhauled app, we aim to attract and acquire even more members with the goal of reaching 10 million members soon.

As we have also touched on at the Q2 Financial Results Briefing, we have been analyzing the purchasing behavior of app members, which has enabled us to launch trial measures to promote purchasing. With the full-scale implementation of CRM measures from the next fiscal year, we plan to improve the level of sales contribution. The details of this will also be communicated during the announcement of mid-term corporate plan in August.

▪GMS Business (presentation p.9)

The GMS business had faced a difficult struggle until Q2 of FY2022 due to the harsh external environment, but successful measures to improve gross profit margin in Q3 have resulted in positive increases year-on-year in both sales and operating profit for existing stores.

As we have been explaining from before, we established a new business model in the GMS business with a major shift in direction, such as individual store management, product lineups that correspond to the trade area, and a small head office. For FY2024, we aim to achieve operating profit growth of 20 billion yen in combination with UDR compared to the time of acquisition in 2019.

Q3 can be described as a stage in our progress toward achieving that goal. In this quarter, existing store sales achieved 100.3% growth, and the success of measures to improve gross profit margin in particular have led to a year-on-year increase in operating profit for existing stores for the first time in the current period. As we have explained during Q2, for renovations, we aim to work on expanding profits while making the shift to a small-scale renovations that is highly effective from now on.

▪GMS Business: Profit Improvement Initiatives for strengthen individual stores (presentation p.10)

Concerning initiatives to improve gross profit margin for the GMS business, in light that gross profit margin declined significantly in the first half of the period due to internal and external factors, we focused on three initiatives in Q3 of FY2022.

At the Q2 Financial Results Briefing, Mr. Sekiguchi, President of UNY, spoke about an overly strong focus on low prices. With that in mind, we worked on optimizing pricing for each individual store, sales schedule management for each individual store, and strengthening the sales of high value-added products based on the Meister system.

As a result, we successfully achieved significant improvement in gross profit margin. Although we revised the gross profit margin target upward by 0.2% from Q3 of FY2022, most of the stores achieved the target.

From Q4 till the next fiscal year, we aim to further expand earnings by firmly putting each measure on track, enhancing the efficiency of headquarter functions, and fundamentally reviewing product measures and product mix.

These details will also be announced with the end-of-year financial results.

▪Overseas Business (presentation p.11)

The Asia business saw the opening of four new stores in Q3, and the business has continued to expand smoothly, including plans for three new stores in Q4. PPIC's contribution, among other factors, has helped to maintain operating profit margin of existing stores at a level over 10%, and we are continuing to develop business formats to capture greater earnings opportunities.

Although there have been no major changes in the trends for the North America business, improvements in gross profit margin, as in Asia, have contributed to a year-on-year increase in operating profit. Gelson's has also continued to make a significant contribution.

PPIC's activities to expand the value chain of the overseas business in order to strengthen differentiation and improve profitability have been progressing and expanding steadily. These include the signing of a partnership agreement with the fifth prefecture, that is, Okinawa Prefecture, and the trial shipments of products from Sendai Port.

▪Overseas Business: Initiatives to improve profitability and expand profit-earning opportunities (presentation p.12)

Putting the spotlight on the gross profit margin of the overseas business, we can see a steady year-on-year improvement for existing stores in both Asia and North America.

Backed by the strengthening of PPIC's activities, improvements in product procurement capability and logistical efficiency amidst the significant expansion of business scale, as well as the strengthening of PB/OEM products overseas, we aim to further improve profits from the next fiscal year and beyond.

As for the development of business formats to capture greater earnings opportunities, sushi and rice milling/onigiri (rice balls) is one specific example of such development. By expressing our "Japan Brand Specialty Store" initiative in various formats and encouraging customers to use these offerings, we aim to expand the company's profit-earning opportunities.

Though it has just launched, we aim to put further effort into it from the next fiscal year and beyond, using it as a means to directly expand the overseas business or expand its potential.

▪Financial business: Progress after Q1 announcement (presentation p.13)

For the financial business, steady preparations are ongoing to proactively integrating payment functions into the value chain with the aim of achieving cost reductions and capturing revenue.

The progress is shown on the right side of the presentation materials. We have officially obtained the international brand license and will launch the merchant management business from June.

This will immediately facilitate the reduction of settlement fees borne by the company. The contributions are significant, with confirmed cost reductions amounting to approximately 100 million yen for the month of June in the current period and approximately 1.3 billion yen for the full year in FY2023.

Preparations are also underway toward the strengthening of member businesses accompanying the start of external use of majica from the second half of the next fiscal year, as well as toward the launch of financial services such as insurance and investments.

Numerical targets will be updated during the announcement of the mid-term corporate plan in August.

▪Shareholder Returns (presentation p.16)

With regard to the shareholder returns announced in January this year, we have decided to award the benefits by utilizing the gift code function that will be installed in conjunction with the majica app update announced earlier.

In the same way as services offered by other companies, the majica balance will increase when the gift code is registered on “My Page.” In the initial round, a gift code worth 2,000 points will be enclosed with the dividend-related documents sent out around the end of September to all shareholders recorded in the register as at the end of June.

2. Initiatives for FY 2022 4Q and Onwards

Director & Managing Executive Officer, Hideki Moriya

▪DS/GMS Business Overview in April (Flash Report) (presentation p.17)

With regard to the monthly overview for April, the four main domestic retail companies recorded sales at 101.6% year-on-year for existing stores.

Looking at each business, the DS business achieved sales of 102.4% year-on-year while the GMS business recorded sales of 99.6% year-on-year. On the other hand, gross profit for existing stores surpassed the results for the previous year for both the DS and GMS businesses.

In April, the relaxation of COVID-19 restrictions led to reduced demand for alternatives to dining out, and sales of food products were sluggish particularly for stores that handle fresh produce. However, the DS business recorded a year-on-year increase in sales in all areas because sales in the nighttime, after 9 p.m., have begun to recover due to more people started going out for leisure such as cherry-blossom viewing parties and for events such as travelling during long holiday weekends. Moreover, the sale of trendy items has also boosted sales.

On the other hand, the GMS business has registered sales on par with the previous year. In addition to the recovery of the number of visits from senior customers, which had declined drastically while they remained at home due to the COVID-19 pandemic, sales figures mainly in areas such as apparel have also risen through various sales promotion and strengthening measures. In comparison with sales in April 2019, sales for the GMS business landed at 100.8%, exceeding pre-COVID-19 levels.

With regard to the current situation in May, although a major long holiday has just ended, sales for both the DS and GMS businesses exceeded previous year sales, while gross profit margin registered a similar trend.

▪Initiatives for Q4 and Onwards

Q4 is positioned as a preparatory period for strategies that we will advance in the next fiscal year, while we continue to implement the priority measures that we announced during the Q2 Financial Results Briefing. I shall explain the three primary measures that we will be putting particular focus on in Q4.

1) Strengthening profitability with a focus on expanding and rolling out PB/OEM

With regard to PB/OEM products, both sales and gross profits have grown significantly, and we have already achieved the gross profit margin contribution target of +0.4% that we set out at the beginning of the fiscal year. In order to further increase the contribution to gross profit in Q4, we aim to strengthen the sale of value-added “single items” with originality and special functions, which were launched in December last year and have been a great hit.

In addition, our strategy for spot products is to immediately sell products that are trending on social media (with a focus on items such as confectionery and cosmetics), thereby creating a great sensation among customers and contributing to popularity, sales, and profits. We will work on increasing the number of such sensational and trending products by using our company’s great strength, which is our information gathering and product procurement systems for these spot products.

2) Building a cycle for maintaining new products, with a focus on the “interest expiration date measures”

With the expansion of our lineup of PB/OEM products, inventory management is becoming even more important than before. To build sales floors that maintain the new products that customers will remain interested in all the time, we have started to implement inventory management measures based on the concept of “interest expiration date.” This involves setting a unique expiration date for non-food products that do not originally have any expiration date. These measures are beginning to produce results.

Specifically, this process includes:

▪Narrowing down SKU through “careful purchasing” at the product purchasing stage

▪Adjusting the number of items ordered and controlling inventory based on their “interest expiration dates”

▪Reducing product valuation loss reserves beforehand, and through encashment, controlling the reserves for product valuation loss in the accounting books

▪Securing spaces and opportunities for introducing new PB products and spot products

Through this cycle, we will put effort into managing inventory and gross profit, and improving the inventory turnover ratio.

3) Controlling SG&A expenses

With the recent rapid hike in energy and resource prices, utility costs and expenses for consumables and office supplies, among other costs, are increasing.

In Q4, we aim to control cost increases by strengthening cross-functional follow-up checks as well as the lateral dissemination of the effective management and operation of measures that have been implemented since the beginning of the fiscal year, such as the daily management of power consumption and methods of managing rental costs and maintenance costs.

Furthermore, the introduction of labor distribution ratio as an indicator from Q3 has helped to improve awareness of reducing man-hours for store processes and contributed to the thorough use of the shift control system. We will also control labor costs through appropriate staffing.

Utility costs and other costs are expected to reach high levels going forward, and labor costs per worker are also certain to increase from the next fiscal year. Therefore, SG&A expenses will continue to increase with many such contributory factors. Going forward, we aim to control SG&A expenses by further streamlining head office and headquarter functions across the corporate group, enhancing the efficiency of store processes, and improving profitability and productivity per worker.