# ARATA CORPORATION / 2733

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**How to read a Shared Research report:** This report begins with the trends and outlook section, which discusses the company's most recent earnings. First-time readers should start at the business section later in the report.

# Executive summary

## Business overview

- ARATA CORPORATION mainly wholesales everyday items and cosmetics, which it buys from manufacturers. The goods are delivered to the company's logistics centers, where they are sorted and dispatched to retailers to whom they are sold. It is one of just two major Japanese wholesalers specializing in everyday items, the other being PALTAC (TSE1: 8283). These two companies have a combined market share of nearly 50%. ARATA handles around 120,000 items such as cosmetics (Health & Beauty product category), detergents, and paper products bought from some 1,600 Japanese and overseas manufacturers. The company wholesales these products to Japanese retailers (around 55,000 stores operated by 5,000 companies, including almost all domestic drugstores, supermarkets, and DIY centers according to its 2018 Integrated Report). We estimate that sales exceed JPY700.0bn, which would be more than JPY900.0bn on a retail basis (converted to instore retail prices), and the volume of items it handles is equivalent to that of top-10-ranking retailers in Japan. Upon receiving an order from a retailer, the company's role is to deliver the right quantity of the right products to the right location at the right time.
- Over the past five years, the company's GPM trended slightly over 10%. Shared Research thinks the company has four major sources of added value: First, it has the logistics capabilities to respond accurately to small-lot orders. Second, because the company handles such a wide range of items, it can serve as a one-stop wholesaler. Third, the company can offer proposals that connect manufacturer promotions with instore retail methods. Fourth, the company has a vast store of transaction data, which it sometimes sells to retailers and manufacturers.
- ARATA was formed in 2002 as a result of the business combination of three wholesalers. The company thinks of the first 15 years since its formation as its first stage, and positions FY03/18 to FY03/20, the period of its current medium-term management plan, as the time for stepping up to the second stage of growth. During this stage, it intends to pursue new possibilities in the wholesaling industry. To this end, it plans to 1) boost GPM by expanding sales in highly profitable merchandise, 2) strengthen business targeting overseas markets, 3) expand e-commerce, 4) improve logistics efficiency, and 5) make better use of information.

## Trends and outlook

- In FY03/19, sales were JPY754.4bn (+2.9% YoY), operating profit was JPY8.9bn (+0.4% YoY), and net income was JP6.9bn (+8.5% YoY). Sales to drugstores (48.6% share) were up 4.9% YoY, sales to supermarkets (12.3% share) were up 0.8% YoY, and sales to discount stores (7.3% share) were up 4.5% YoY. In contrast, sales to GMS (5.4% share) were down 4.1% YoY and sales to DIY centers (16.4% share) grew only 0.2% YoY. GPM fell slightly from 10.43% in FY03/18 to 10.36% in FY03/19, but gross profit was up 2.3% YoY. Operating profit increased slightly, because SG&A expenses were up 2.5% YoY, mainly due to a rise in transportation costs.
- FY03/20 company forecasts are sales of JPY771.0bn (+2.2% YoY), operating profit of JPY9.3bn (+4.6% YoY), net income of JPY6.5bn (-5.8% YoY), and EPS of JPY374.5.
- FY03/20 is the final year of the company's medium-term management plan, which started in FY03/18. In May 2018, ARATA raised its final year targets to sales of JPY780.0bn (from JPY760.0bn), recurring profit of JPY10.5bn (from 10.0bn), and net income of JPY6.8bn (from JPY6.5bn), but now does not expect to attain these values. The company commented that it plans to continue strengthening the functions it has built so far and developing new businesses so that it can transition effectively to the next medium-term plan starting in FY03/21.

## Strengths and weaknesses

Shared Research thinks the company's strengths are: 1) the logistics capabilities to deliver the right quantity of the right products to the right location at the right time, 2) the ability to advise retailers about how to create highly effective retail spaces, and 3) the information it accumulated leveraging handling volume that would rank the company as a top-10 retailer on an instore retail price conversion basis (based on Shared Research estimates). We believe ARATA's weakness are its 1) relatively high logistics

costs owing to its history of business combinations, 2) weak development capabilities overseas, where the company sees upstream and downstream growth opportunities, and 3) limited ability to respond to changing commercial channels amid the spread of e-commerce (see “Strengths and weaknesses” section for more details).

# Key financial data

| Income statement (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. | FY03/20 Est. |
|---|---|---|---|---|---|---|---|---|---|---|
| **Sales** | **601,949** | **606,705** | **616,327** | **651,954** | **638,792** | **676,743** | **704,610** | **732,914** | **754,447** | **771,000** |
| YoY | 2.0% | 0.8% | 1.6% | 5.8% | -2.0% | 5.9% | 4.1% | 4.0% | 2.9% | 2.2% |
| **Gross profit** | **76,327** | **69,033** | **64,286** | **66,730** | **64,613** | **70,731** | **73,068** | **76,475** | **78,197** | |
| YoY | 0.0% | -9.6% | -6.9% | 3.8% | -3.2% | 9.5% | 3.3% | 4.7% | 2.3% | |
| GPM | 12.7% | 11.4% | 10.4% | 10.2% | 10.1% | 10.5% | 10.4% | 10.4% | 10.4% | |
| **SG&A expenses** | **76,041** | **64,859** | **60,560** | **62,258** | **62,152** | **65,032** | **65,684** | **67,618** | **69,305** | |
| YoY | -0.3% | -14.7% | -6.6% | 2.8% | -0.2% | 4.6% | 1.0% | 2.9% | 2.5% | |
| SG&A ratio | 12.6% | 10.7% | 9.8% | 9.5% | 9.7% | 9.6% | 9.3% | 9.2% | 9.2% | |
| **Operating profit** | **286** | **4,174** | **3,726** | **4,472** | **2,461** | **5,699** | **7,384** | **8,857** | **8,892** | **9,300** |
| YoY | 302.8% | - | -10.7% | 20.0% | -45.0% | 131.6% | 29.6% | 19.9% | 0.4% | 4.6% |
| OPM | 0.0% | 0.7% | 0.6% | 0.7% | 0.4% | 0.8% | 1.0% | 1.2% | 1.2% | 1.2% |
| **Recurring profit** | **4,257** | **3,915** | **3,605** | **4,388** | **2,469** | **5,811** | **7,842** | **9,439** | **9,429** | **10,000** |
| YoY | 9.5% | -8.0% | -7.9% | 21.7% | -43.7% | 135.4% | 35.0% | 20.4% | -0.1% | 6.1% |
| RPM | 0.7% | 0.6% | 0.6% | 0.7% | 0.4% | 0.9% | 1.1% | 1.3% | 1.2% | 1.3% |
| **Net income** | **1,015** | **1,628** | **1,768** | **2,435** | **1,124** | **3,244** | **4,863** | **6,361** | **6,903** | **6,500** |
| YoY | -21.6% | 60.4% | 8.6% | 37.7% | -53.8% | 188.6% | 49.9% | 30.8% | 8.5% | -5.8% |
| Net margin | 0.2% | 0.3% | 0.3% | 0.4% | 0.2% | 0.5% | 0.7% | 0.9% | 0.9% | 0.8% |
| **Per share data (split-adjusted; JPY)** | | | | | | | | | | |
| Shares outstanding (ex. treasury shares; mn) | 15.4 | 15.4 | 15.4 | 15.4 | 15.4 | 15.4 | 14.7 | 16.7 | 17.7 | - |
| EPS | 67.6 | 105.6 | 114.7 | 158.0 | 73.0 | 210.4 | 331.0 | 399.1 | 397.7 | 374.5 |
| EPS (fully diluted) | - | - | - | - | - | - | 294.9 | 377.8 | 381.2 | - |
| Dividend per share | 35.0 | 40.0 | 40.0 | 50.0 | 50.0 | 55.0 | 65.0 | 75.0 | 80.0 | 85.0 |
| Book value per share | 2,960 | 3,068 | 3,180 | 3,309 | 3,496 | 3,628 | 4,055 | 4,285 | 4,547 | - |
| **Balance sheet (JPYmn)** | | | | | | | | | | |
| Cash and cash equivalent | 9,640 | 9,985 | 8,108 | 10,965 | 11,800 | 14,119 | 13,693 | 17,826 | 19,798 | |
| **Total current assets** | **132,911** | **143,020** | **145,806** | **158,015** | **143,906** | **151,873** | **153,455** | **172,149** | **175,156** | |
| Tangible fixed assets | 44,034 | 44,897 | 45,980 | 48,772 | 51,896 | 50,841 | 50,248 | 51,041 | 49,022 | |
| Investments and other assets | 10,083 | 10,332 | 10,804 | 10,124 | 11,890 | 13,194 | 15,695 | 17,696 | 15,776 | |
| Intangible fixed assets | 4,511 | 4,255 | 4,108 | 4,289 | 4,147 | 3,781 | 3,576 | 3,495 | 3,659 | |
| **Total assets** | **191,541** | **202,506** | **206,699** | **221,202** | **211,840** | **219,689** | **222,974** | **244,381** | **243,614** | |
| Short-term debt | 41,315 | 42,934 | 35,380 | 37,069 | 35,271 | 38,017 | 28,147 | 32,653 | 17,945 | |
| **Total current liabilities** | **111,230** | **115,798** | **116,515** | **122,910** | **122,414** | **129,756** | **124,003** | **145,831** | **129,829** | |
| Long-term debt | 24,331 | 29,042 | 30,904 | 38,048 | 27,157 | 24,215 | 27,930 | 14,648 | 21,861 | |
| **Total fixed liabilities** | **34,646** | **39,384** | **41,140** | **47,251** | **35,515** | **33,992** | **39,358** | **27,078** | **33,269** | |
| **Total liabilities** | **145,876** | **155,182** | **157,655** | **170,161** | **157,929** | **163,748** | **163,361** | **172,909** | **163,099** | |
| Shareholders' equity (adjusted) | 45,646 | 47,306 | 49,023 | 51,017 | 53,897 | 55,923 | 59,605 | 71,462 | 80,499 | |
| **Total net assets** | **45,665** | **47,324** | **49,044** | **51,041** | **53,911** | **55,941** | **59,613** | **71,472** | **80,515** | |
| Total interest-bearing debt | 62,384 | 68,707 | 62,566 | 70,872 | 58,637 | 58,982 | 52,569 | 43,640 | 36,524 | |
| **Statement of cash flows (JPYmn)** | | | | | | | | | | |
| Cash flows from operating activities | 1,919 | -720 | 9,959 | 1,481 | 21,955 | 7,594 | 12,637 | 11,649 | 9,513 | |
| Cash flows from investing activities | -3,227 | -4,575 | -4,054 | -5,878 | -6,775 | -3,360 | -3,155 | -2,924 | -880 | |
| Cash flows from financing activities | 2,697 | 5,257 | -7,699 | 7,246 | -13,990 | -1,791 | -9,948 | -4,501 | -6,678 | |
| **Finantial ratios** | | | | | | | | | | |
| ROA (RP-based) | 2.3% | 2.0% | 1.8% | 2.1% | 1.1% | 2.7% | 3.5% | 4.0% | 3.9% | |
| ROE | 2.2% | 3.5% | 3.7% | 4.9% | 2.1% | 5.9% | 8.4% | 9.7% | 9.1% | |
| Equity ratio | 23.8% | 23.4% | 23.7% | 23.1% | 25.4% | 25.5% | 26.7% | 29.2% | 33.0% | |
| Total asset turnover | 321.2% | 307.9% | 301.2% | 304.7% | 295.0% | 313.6% | 318.4% | 313.6% | 309.2% | |
| Net margin | 0.2% | 0.3% | 0.3% | 0.4% | 0.2% | 0.5% | 0.7% | 0.9% | 0.9% | |
| Equity ratio | 23.8% | 23.4% | 23.7% | 23.1% | 25.4% | 25.5% | 26.7% | 29.2% | 33.0% | |

Source: Shared Research based on company data; per-share information has been adjusted for a stock split

# Recent updates

## Highlights

On **June 26, 2019**, Shared Research initiated coverage of ARATA CORPORATION.

**For previous releases and developments, please refer to the "News and topics" section.**

# Trends and outlook

## Quarterly trends and results

| Cumulative (JPYmn) | FY03/17 Q1 | Q2 | Q3 | Q4 | FY03/18 Q1 | Q2 | Q3 | Q4 | FY03/19 Q1 | Q2 | Q3 | Q4 | FY03/20 FY Est. |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | 177,504 | 355,644 | 539,598 | 704,610 | 183,701 | 369,766 | 559,985 | 732,914 | 191,872 | 381,081 | 578,125 | 754,447 | 771,000 |
| YoY | 5.0% | 4.7% | 4.3% | 4.1% | 3.5% | 4.0% | 3.8% | 4.0% | 4.4% | 3.1% | 3.2% | 2.9% | 2.2% |
| Gross profit | 18,232 | 36,577 | 55,541 | 73,068 | 19,228 | 38,266 | 57,923 | 76,475 | 19,865 | 39,204 | 59,427 | 78,198 | |
| YoY | 3.6% | 3.5% | 3.3% | 3.3% | 5.5% | 4.6% | 4.3% | 4.7% | 3.3% | 2.5% | 2.6% | 2.3% | |
| GPM | 10.3% | 10.3% | 10.3% | 10.4% | 10.5% | 10.3% | 10.3% | 10.4% | 10.4% | 10.3% | 10.3% | 10.4% | |
| SG&A expenses | 16,190 | 32,874 | 49,525 | 65,684 | 16,771 | 33,793 | 50,996 | 67,618 | 17,379 | 34,726 | 52,499 | 69,306 | |
| YoY | 0.7% | 0.6% | 1.0% | 1.0% | 3.6% | 2.8% | 3.0% | 2.9% | 3.6% | 2.8% | 2.9% | 2.5% | |
| SG&A ratio | 9.1% | 9.2% | 9.2% | 9.3% | 9.1% | 9.1% | 9.1% | 9.2% | 9.1% | 9.1% | 9.1% | 9.2% | |
| Operating profit | 2,042 | 3,703 | 6,016 | 7,384 | 2,457 | 4,473 | 6,927 | 8,857 | 2,486 | 4,478 | 6,928 | 8,892 | 9,300 |
| YoY | 33.7% | 38.9% | 28.1% | 29.6% | 20.3% | 20.8% | 15.1% | 19.9% | 1.2% | 0.1% | 0.0% | 0.4% | 4.6% |
| OPM | 1.2% | 1.0% | 1.1% | 1.0% | 1.3% | 1.2% | 1.2% | 1.2% | 1.3% | 1.2% | 1.2% | 1.2% | 1.2% |
| Recurring profit | 2,193 | 3,910 | 6,393 | 7,842 | 2,701 | 4,844 | 7,424 | 9,439 | 2,551 | 4,673 | 7,285 | 9,429 | 10,000 |
| YoY | 38.6% | 43.7% | 34.0% | 35.0% | 23.2% | 23.9% | 16.1% | 20.4% | -5.6% | -3.5% | -1.9% | -0.1% | 6.1% |
| RPM | 1.2% | 1.1% | 1.2% | 1.1% | 1.5% | 1.3% | 1.3% | 1.3% | 1.3% | 1.2% | 1.3% | 1.2% | 1.3% |
| Net income | 1,315 | 2,433 | 3,881 | 4,863 | 1,795 | 3,231 | 5,205 | 6,361 | 1,760 | 3,332 | 5,208 | 6,903 | 6,500 |
| YoY | 42.9% | 55.4% | 38.0% | 49.9% | 36.5% | 32.8% | 34.1% | 30.8% | -1.9% | 3.1% | 0.1% | 8.5% | -5.8% |
| Net margin | 0.7% | 0.7% | 0.7% | 0.7% | 1.0% | 0.9% | 0.9% | 0.9% | 0.9% | 0.9% | 0.9% | 0.9% | 0.8% |

| Quarterly (JPYmn) | FY03/17 Q1 | Q2 | Q3 | Q4 | FY03/18 Q1 | Q2 | Q3 | Q4 | FY03/19 Q1 | Q2 | Q3 | Q4 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | 177,504 | 178,140 | 183,954 | 165,012 | 183,701 | 186,065 | 190,219 | 172,929 | 191,872 | 189,209 | 197,044 | 176,322 |
| YoY | 5.0% | 4.3% | 3.6% | 3.5% | 3.5% | 4.4% | 3.4% | 4.8% | 4.4% | 1.7% | 3.6% | 2.0% |
| Gross profit | 18,232 | 18,345 | 18,964 | 17,527 | 19,228 | 19,038 | 19,657 | 18,552 | 19,865 | 19,339 | 20,223 | 18,771 |
| YoY | 3.6% | 3.4% | 3.0% | 3.2% | 5.5% | 3.8% | 3.7% | 5.8% | 3.3% | 1.6% | 2.9% | 1.2% |
| GPM | 10.3% | 10.3% | 10.3% | 10.6% | 10.5% | 10.2% | 10.3% | 10.7% | 10.4% | 10.2% | 10.3% | 10.6% |
| SG&A expenses | 16,190 | 16,684 | 16,651 | 16,159 | 16,771 | 17,022 | 17,203 | 16,622 | 17,379 | 17,347 | 17,773 | 16,807 |
| YoY | 0.7% | 0.5% | 1.6% | 1.1% | 3.6% | 2.0% | 3.3% | 2.9% | 3.6% | 1.9% | 3.3% | 1.1% |
| SG&A ratio | 9.1% | 9.4% | 9.1% | 9.8% | 9.1% | 9.1% | 9.0% | 9.6% | 9.1% | 9.2% | 9.0% | 9.5% |
| Operating profit | 2,042 | 1,661 | 2,313 | 1,368 | 2,457 | 2,016 | 2,454 | 1,930 | 2,486 | 1,992 | 2,450 | 1,964 |
| YoY | 33.7% | 46.0% | 13.8% | 36.7% | 20.3% | 21.4% | 6.1% | 41.1% | 1.2% | -1.2% | -0.2% | 1.8% |
| OPM | 1.2% | 0.9% | 1.3% | 0.8% | 1.3% | 1.1% | 1.3% | 1.1% | 1.3% | 1.1% | 1.2% | 1.1% |
| Recurring profit | 2,193 | 1,717 | 2,483 | 1,449 | 2,701 | 2,143 | 2,580 | 2,015 | 2,551 | 2,122 | 2,612 | 2,144 |
| YoY | 38.6% | 50.7% | 21.1% | 39.3% | 23.2% | 24.8% | 3.9% | 39.1% | -5.6% | -1.0% | 1.2% | 6.4% |
| RPM | 1.2% | 1.0% | 1.3% | 0.9% | 1.5% | 1.2% | 1.4% | 1.2% | 1.3% | 1.1% | 1.3% | 1.2% |
| Net income | 1,315 | 1,118 | 1,448 | 982 | 1,795 | 1,436 | 1,974 | 1,156 | 1,760 | 1,572 | 1,876 | 1,695 |
| YoY | 42.9% | 73.1% | 16.1% | 127.8% | 36.5% | 28.4% | 36.3% | 17.7% | -1.9% | 9.5% | -5.0% | 46.6% |
| Net margin | 0.7% | 0.6% | 0.8% | 0.6% | 1.0% | 0.8% | 1.0% | 0.7% | 0.9% | 0.8% | 1.0% | 1.0% |

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

## FY03/19 results

### Summary

- FY03/19 results: Sales were JPY754.4bn (+2.9% YoY), operating profit was JPY8.9bn (+0.4% YoY), recurring profit was JPY9.4bn (-0.1% YoY), and net income attributable to owners of parent was JP6.9bn (+8.5% YoY).
  - Sales by segment: Sales to drugstores (48.6% share) were up 4.9% YoY, sales to supermarkets (12.3% share) were up 0.8% YoY, and sales to discount stores (7.3% share) were up 4.5% YoY. In contrast, sales to GMS (5.4% share) were down 4.1% YoY and sales to DIY centers (16.4% share) grew only 0.2% YoY.
  - Operating profit slightly up: GPM fell slightly from 10.43% in FY03/18 to 10.36% in FY03/19, but gross profit was up 2.3% YoY. Operating profit increased slightly. SG&A expenses were up 2.5% YoY, mainly due to a rise in distribution expenses. OPM fell slightly from 1.21% in FY03/18 to 1.18% in FY03/19. Extraordinary profit was JPY1.2bn (including a JPY1.1bn gain on the sale of shareholdings in business partners), and extraordinary loss was JPY516mn.
  - Q4 results: In January–March 2019 (Q4 FY03/19), sales were JPY176.3bn (+2.0% YoY), gross profit was JPY18.8bn (+1.2% YoY), SG&A expenses were JPY16.8bn (+1.1% YoY), and operating profit was JPY2.0bn (+1.8% YoY).
- FY03/20 company forecasts are sales of JPY771.0bn (+2.2% YoY), operating profit of JPY9.3bn (+4.6% YoY), net income of JPY6.5bn (-5.8% YoY), and EPS of JPY374.5.
  - Sales up 2.2% YoY: The company is focusing on growing sales in the Health & Beauty category (handles mainstay cosmetics products), primarily targeting drugstores. It aims to improve GPM by mainly fostering sales of competitive products and targets OP growth by absorbing rises in SG&A expenses, such as freight.
- Dividends: The company forecasts annual DPS of JPY85 (+JPY5.0 YoY) and a dividend payout ratio of 22.7%.

Seasonality: Sales and operating profit tend to be higher in Q3 (October–December) than in the other quarters, because product volume increases due to the year-end holiday shopping season and other factors.

### Sales by customer type

| Sales by customer type Cumulative (JPYmn) | FY03/17 Q1 | FY03/17 Q2 | FY03/17 Q3 | FY03/17 Q4 | FY03/18 Q1 | FY03/18 Q2 | FY03/18 Q3 | FY03/18 Q4 | FY03/19 Q1 | FY03/19 Q2 | FY03/19 Q3 | FY03/19 Q4 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total sales | 177,504 | 355,644 | 539,598 | 704,610 | 183,701 | 369,766 | 559,985 | 732,914 | 191,872 | 381,081 | 578,125 | 754,447 |
| YoY | 5.0% | 4.7% | 4.3% | 4.1% | 3.5% | 4.0% | 3.8% | 4.0% | 4.4% | 3.1% | 3.2% | 2.9% |
| Drugstores | 83,293 | 167,184 | 252,275 | 331,310 | 88,212 | 176,603 | 265,509 | 349,940 | 93,147 | 184,853 | 279,663 | 367,008 |
| YoY | 6.9% | 7.1% | 6.5% | 6.2% | 5.9% | 5.6% | 5.2% | 5.6% | 5.6% | 4.7% | 5.3% | 4.9% |
| % of total sales | 46.9% | 47.0% | 46.8% | 47.0% | 48.0% | 47.8% | 47.4% | 47.7% | 48.5% | 48.5% | 48.4% | 48.6% |
| DIY centers | 30,454 | 60,610 | 92,447 | 117,565 | 31,197 | 62,783 | 96,246 | 123,558 | 32,555 | 64,090 | 97,030 | 123,829 |
| YoY | 1.8% | 1.2% | 1.4% | 1.1% | 2.4% | 3.6% | 4.1% | 5.1% | 4.4% | 2.1% | 0.8% | 0.2% |
| % of total sales | 17.2% | 17.0% | 17.1% | 16.7% | 17.0% | 17.0% | 17.2% | 16.9% | 17.0% | 16.8% | 16.8% | 16.4% |
| Supermarkets | 21,886 | 44,316 | 67,802 | 88,414 | 23,123 | 46,609 | 70,777 | 92,264 | 23,202 | 46,469 | 71,166 | 93,043 |
| YoY | 4.3% | 3.6% | 2.6% | 2.3% | 5.7% | 5.2% | 4.4% | 4.4% | 0.3% | -0.3% | 0.5% | 0.8% |
| % of total sales | 12.3% | 12.5% | 12.6% | 12.5% | 12.6% | 12.6% | 12.6% | 12.6% | 12.1% | 12.2% | 12.3% | 12.3% |
| Discount stores | 12,661 | 25,526 | 38,920 | 50,678 | 13,364 | 26,860 | 40,980 | 53,054 | 13,539 | 27,641 | 42,374 | 55,448 |
| YoY | 5.7% | 6.6% | 5.7% | 4.8% | 5.6% | 5.2% | 5.3% | 4.7% | 1.3% | 2.9% | 3.4% | 4.5% |
| % of total sales | 7.1% | 7.2% | 7.2% | 7.2% | 7.3% | 7.3% | 7.3% | 7.2% | 7.1% | 7.3% | 7.3% | 7.3% |
| General merchandising stores (GMS) | 11,329 | 22,614 | 35,087 | 47,061 | 11,000 | 21,848 | 32,793 | 42,557 | 10,417 | 20,577 | 31,321 | 40,818 |
| YoY | -4.2% | -2.8% | -0.8% | 2.8% | -2.9% | -3.4% | -6.5% | -9.6% | -5.3% | -5.8% | -4.5% | -4.1% |
| % of total sales | 6.4% | 6.4% | 6.5% | 6.7% | 6.0% | 5.9% | 5.9% | 5.8% | 5.4% | 5.4% | 5.4% | 5.4% |
| Convenience stores | 1,641 | 3,153 | 4,775 | 5,763 | | | | | | | | |
| YoY | -23.9% | -30.5% | -27.9% | -32.0% | | | | | | | | |
| % of total sales | 0.9% | 0.9% | 0.9% | 0.8% | | | | | | | | |
| Other | 16,240 | 32,241 | 48,292 | 63,819 | 16,805 | 35,063 | 53,680 | 71,541 | 19,012 | 37,451 | 56,571 | 74,301 |
| YoY | 13.6% | 10.3% | 8.8% | 7.2% | 3.5% | 8.8% | 11.2% | 12.1% | 13.1% | 6.8% | 5.4% | 3.9% |
| % of total sales | 9.1% | 9.1% | 8.9% | 9.1% | 9.1% | 9.5% | 9.6% | 9.8% | 9.9% | 9.8% | 9.8% | 9.8% |

| Sales by customer type Quarterly (JPYmn) | FY03/17 Q1 | FY03/17 Q2 | FY03/17 Q3 | FY03/17 Q4 | FY03/18 Q1 | FY03/18 Q2 | FY03/18 Q3 | FY03/18 Q4 | FY03/19 Q1 | FY03/19 Q2 | FY03/19 Q3 | FY03/19 Q4 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total sales | 177,504 | 178,140 | 183,954 | 165,012 | 183,701 | 186,065 | 190,219 | 172,929 | 191,872 | 189,209 | 197,044 | 176,322 |
| YoY | 5.0% | 4.3% | 3.6% | 3.5% | 3.5% | 4.4% | 3.4% | 4.8% | 4.4% | 1.7% | 3.6% | 2.0% |
| Drugstores | 83,293 | 83,891 | 85,091 | 79,035 | 88,212 | 88,391 | 88,906 | 84,431 | 93,147 | 91,706 | 94,810 | 87,345 |
| YoY | 6.9% | 7.2% | 5.4% | 5.3% | 5.9% | 5.4% | 4.5% | 6.8% | 5.6% | 3.8% | 6.6% | 3.5% |
| % of total sales | 46.9% | 47.1% | 46.3% | 47.9% | 48.0% | 47.5% | 46.7% | 48.8% | 48.5% | 48.5% | 48.1% | 49.5% |
| DIY centers | 30,454 | 30,156 | 31,837 | 25,118 | 31,197 | 31,586 | 33,463 | 27,312 | 32,555 | 31,535 | 32,940 | 26,799 |
| YoY | 1.8% | 0.6% | 1.7% | 0.1% | 2.4% | 4.7% | 5.1% | 8.7% | 4.4% | -0.2% | -1.6% | -1.9% |
| % of total sales | 17.2% | 16.9% | 17.3% | 15.2% | 17.0% | 17.0% | 17.6% | 15.8% | 17.0% | 16.7% | 16.7% | 15.2% |
| Supermarkets | 21,886 | 22,430 | 23,486 | 20,612 | 23,123 | 23,486 | 24,168 | 21,487 | 23,202 | 23,267 | 24,697 | 21,877 |
| YoY | 4.3% | 2.9% | 0.8% | 1.5% | 5.7% | 4.7% | 2.9% | 4.2% | 0.3% | -0.9% | 2.2% | 1.8% |
| % of total sales | 12.3% | 12.6% | 12.8% | 12.5% | 12.6% | 12.6% | 12.7% | 12.4% | 12.1% | 12.3% | 12.5% | 12.4% |
| Discount stores | 12,661 | 12,865 | 13,394 | 11,758 | 13,364 | 13,496 | 14,120 | 12,074 | 13,539 | 14,102 | 14,733 | 13,074 |
| YoY | 5.7% | 7.5% | 3.9% | 2.1% | 5.6% | 4.9% | 5.4% | 2.7% | 1.3% | 4.5% | 4.3% | 8.3% |
| % of total sales | 7.1% | 7.2% | 7.3% | 7.1% | 7.3% | 7.3% | 7.4% | 7.0% | 7.1% | 7.5% | 7.5% | 7.4% |
| General merchandising stores (GMS) | 11,329 | 11,285 | 12,473 | 11,974 | 11,000 | 10,848 | 10,945 | 9,764 | 10,417 | 10,160 | 10,744 | 9,497 |
| YoY | -4.2% | -1.3% | 3.1% | 14.8% | -2.9% | -3.9% | -12.3% | -18.5% | -5.3% | -6.3% | -1.8% | -2.7% |
| % of total sales | 6.4% | 6.3% | 6.8% | 7.3% | 6.0% | 5.8% | 5.8% | 5.6% | 5.4% | 5.4% | 5.5% | 5.4% |
| Convenience stores | 1,641 | 1,512 | 1,622 | 988 | | | | | | | | |
| YoY | -23.9% | -36.4% | -22.2% | -46.9% | | | | | | | | |
| % of total sales | 0.9% | 0.8% | 0.9% | 0.6% | | | | | | | | |
| Other | 16,240 | 16,001 | 16,051 | 15,527 | 16,805 | 18,258 | 18,617 | 17,861 | 19,012 | 18,439 | 19,120 | 17,730 |
| YoY | 13.6% | 7.1% | 6.0% | 2.5% | -6.0% | 4.3% | 5.3% | 8.2% | 13.1% | 1.0% | 2.7% | -0.7% |
| % of total sales | 9.1% | 9.0% | 8.7% | 9.4% | 9.1% | 9.8% | 9.8% | 10.3% | 9.9% | 9.7% | 9.7% | 10.1% |

Source: Shared Research based on company data
Note: The company revised its breakdown of sales by customer type in FY03/19. Figures may differ from company materials due to differences in rounding methods.

Sales grew 2.9% YoY to JPY754.4bn in FY03/19. By customer type, sales to drugstores, which make up a large sales share, were up 4.9% YoY while sales to discount stores grew 4.5% YoY. Sales are also trending up in the overseas business, E-commerce, and cross-border E-commerce businesses in the Other category, although their sales shares are relatively small. Sales to DIY centers and supermarkets were flat, increasing 0.2% YoY and 0.8% YoY, respectively, while sales to GMS were weak, declining 4.1% YoY.

In Q4 FY03/19, sales to drugstores rose 3.5% YoY, and sales to discount stores grew 8.3% YoY, driving the company's growth. Sales to DIY centers declined for the third consecutive quarter starting in Q2 FY03/19.

By product category, sales increased 4.7% YoY in Health & Beauty, 4.6% YoY in Household, and 4.7% YoY in Home Goods, which were the main sales drivers.

### Sales by product category

| Sales by category (cumulative) | FY03/17 | | | | FY03/18 | | | | FY03/19 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| (JPYmn) | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Total sales | 177,504 | 355,644 | 539,598 | 704,610 | 183,701 | 369,766 | 559,985 | 732,914 | 191,872 | 381,081 | 578,125 | 754,447 |
| YoY | 5.0% | 4.7% | 4.3% | 4.1% | 3.5% | 4.0% | 3.8% | 4.0% | 4.4% | 3.1% | 3.2% | 2.9% |
| Health & Beauty | | | | | 53,528 | 110,212 | 168,938 | 223,800 | 58,529 | 117,319 | 178,343 | 234,426 |
| YoY | | | | | - | - | - | - | 9.3% | 6.4% | 5.6% | 4.7% |
| % of total sales | | | | | 29.1% | 29.8% | 30.2% | 30.5% | 30.5% | 30.8% | 30.8% | 31.1% |
| Household | | | | | 25,442 | 51,259 | 78,550 | 100,899 | 26,469 | 52,979 | 82,199 | 105,506 |
| YoY | | | | | - | - | - | - | 4.0% | 3.4% | 4.6% | 4.6% |
| % of total sales | | | | | 13.8% | 13.9% | 14.0% | 13.8% | 13.8% | 13.9% | 14.2% | 14.0% |
| Home Care | | | | | 21,985 | 41,119 | 54,374 | 70,553 | 22,093 | 40,131 | 53,338 | 69,179 |
| YoY | | | | | - | - | - | - | 0.5% | -2.4% | -1.9% | -1.9% |
| % of total sales | | | | | 12.0% | 11.1% | 9.7% | 9.6% | 11.5% | 10.5% | 9.2% | 9.2% |
| Paper Products | | | | | 36,842 | 72,923 | 111,230 | 147,167 | 36,420 | 71,910 | 111,010 | 147,203 |
| YoY | | | | | - | - | - | - | -1.1% | -1.4% | -0.2% | 0.0% |
| % of total sales | | | | | 20.1% | 19.7% | 19.9% | 20.1% | 19.0% | 18.9% | 19.2% | 19.5% |
| Home Goods | | | | | 12,334 | 25,979 | 41,567 | 54,082 | 13,050 | 27,625 | 43,974 | 56,631 |
| YoY | | | | | - | - | - | - | 5.8% | 6.3% | 5.8% | 4.7% |
| % of total sales | | | | | 6.7% | 7.0% | 7.4% | 7.4% | 6.8% | 7.2% | 7.6% | 7.5% |
| Pet Goods, other | | | | | 33,569 | 68,272 | 105,323 | 136,413 | 35,311 | 71,117 | 109,261 | 141,499 |
| YoY | | | | | - | - | - | - | 5.2% | 4.2% | 3.7% | 3.7% |
| % of total sales | | | | | 18.3% | 18.5% | 18.8% | 18.6% | 18.4% | 18.7% | 18.9% | 18.8% |
| **Sales by category** | **FY03/17** | | | | **FY03/18** | | | | **FY03/19** | | | |
| **Quarterly (JPYmn)** | **Q1** | **Q2** | **Q3** | **Q4** | **Q1** | **Q2** | **Q3** | **Q4** | **Q1** | **Q2** | **Q3** | **Q4** |
| Total sales | 177,504 | 178,140 | 183,954 | 165,012 | 183,701 | 186,065 | 190,219 | 172,929 | 191,872 | 189,209 | 197,044 | 176,322 |
| YoY | 5.0% | 4.3% | 3.6% | 3.5% | 3.5% | 4.4% | 3.4% | 4.8% | 4.4% | 1.7% | 3.6% | 2.0% |
| Health & Beauty | | | | | 53,528 | 56,684 | 58,726 | 54,862 | 58,529 | 58,790 | 61,024 | 56,083 |
| YoY | | | | | - | - | - | - | 9.3% | 3.7% | 3.9% | 2.2% |
| % of total sales | | | | | 29.1% | 30.5% | 30.9% | 31.7% | 30.5% | 31.1% | 31.0% | 31.8% |
| Household | | | | | 25,442 | 25,817 | 27,291 | 22,349 | 26,469 | 26,510 | 29,220 | 23,307 |
| YoY | | | | | - | - | - | - | 4.0% | 2.7% | 7.1% | 4.3% |
| % of total sales | | | | | 13.8% | 13.9% | 14.3% | 12.9% | 13.8% | 14.0% | 14.8% | 13.2% |
| Home Care | | | | | 21,985 | 19,134 | 13,255 | 16,179 | 22,093 | 18,038 | 13,207 | 15,841 |
| YoY | | | | | - | - | - | - | 0.5% | -5.7% | -0.4% | -2.1% |
| % of total sales | | | | | 12.0% | 10.3% | 7.0% | 9.4% | 11.5% | 9.5% | 6.7% | 9.0% |
| Paper Products | | | | | 36,842 | 36,081 | 38,307 | 35,937 | 36,420 | 35,490 | 39,100 | 36,193 |
| YoY | | | | | - | - | - | - | -1.1% | -1.6% | 2.1% | 0.7% |
| % of total sales | | | | | 20.1% | 19.4% | 20.1% | 20.8% | 19.0% | 18.8% | 19.8% | 20.5% |
| Home Goods | | | | | 12,334 | 13,645 | 15,588 | 12,515 | 13,050 | 14,575 | 16,349 | 12,657 |
| YoY | | | | | - | - | - | - | 5.8% | 6.8% | 4.9% | 1.1% |
| % of total sales | | | | | 6.7% | 7.3% | 8.2% | 7.2% | 6.8% | 7.7% | 8.3% | 7.2% |
| Pet Goods, other | | | | | 33,569 | 34,703 | 37,051 | 31,090 | 35,311 | 35,806 | 38,144 | 32,238 |
| YoY | | | | | - | - | - | - | 5.2% | 3.2% | 2.9% | 3.7% |
| % of total sales | | | | | 18.3% | 18.7% | 19.5% | 18.0% | 18.4% | 18.9% | 19.4% | 18.3% |

Source: Shared Research based on company data
Note: The company revised its sales breakdown by customer type in FY03/19. Figures may differ from company materials due to differences in rounding methods.

Gross profit grew 2.3% YoY to JPY79.2bn. Profit growth was slightly slower than sales growth, and GPM was down slightly from 10.43% in FY03/18 to 10.36% in FY03/19. External factors had a negative impact. Weather-related factors (summer heat wave and warm winter) affected sales of seasonal items, and consumer sentiment dipped in 2H FY03/19. From a long-term point of view, the company also invested upfront to increase its transaction share. Meanwhile, focusing on profitable items such as cosmetics underpinned earnings.

SG&A expenses were up 2.5% YoY to JPY69.3bn. Packaging and transportation expenses were JPY20.3bn; the company kept the rate of increase down to 7.5% YoY, despite the effect of higher logistics costs, through efficiency gains such as improvements in the loading ratio and warehouse operations. Personnel expenses were down 0.5% YoY to JPY29.7bn thanks to improved efficiency despite a period of sales growth.

Operating profit was JPY8.9bn (+0.4% YoY) and recurring profit was JPY9.4bn (-0.1% YoY). Extraordinary profit was JPY1.2bn, including a JPY1.1bn gain on the sale of shareholdings in business partners, and extraordinary loss was JPY516mn, including a JPY264mn loss associated with a fire. Net income grew 8.5% YoY to JPY6.9bn. The company expects to partially recover the fire-related loss from insurers, but booked the full amount as a loss, because the payout had not been finalized as of the end of FY03/19.

**For details on previous quarterly and annual results, please refer to the "Historical financial statements" section.**

## Full-year company forecasts

| (JPYmn) | FY03/18 1H | FY03/18 2H | FY03/18 FY | FY03/19 1H | FY03/19 2H | FY03/19 FY | FY03/20 1H Est. | FY03/20 2H Est. | FY03/20 FY Est. |
|---|---|---|---|---|---|---|---|---|---|
| **Sales** | **369,766** | **363,148** | **732,914** | **381,081** | **373,366** | **754,447** | **394,000** | **377,000** | **771,000** |
| YoY | 4.0% | 4.1% | 4.0% | 3.1% | 2.8% | 2.9% | 3.4% | 1.0% | 2.2% |
| Cost of sales | 331,500 | 324,939 | 656,439 | 341,877 | 334,372 | 676,249 | | | |
| **Gross profit** | **38,266** | **38,209** | **76,475** | **39,204** | **38,994** | **78,198** | | | |
| YoY | 4.6% | 4.7% | 4.7% | 2.5% | 2.1% | 2.3% | | | |
| GPM | 10.3% | 10.5% | 10.4% | 10.3% | 10.4% | 10.4% | | | |
| SG&A expenses | 33,793 | 33,825 | 67,618 | 34,726 | 34,580 | 69,306 | | | |
| YoY | 2.8% | 3.1% | 2.9% | 2.8% | 2.2% | 2.5% | | | |
| SG&A ratio | 9.1% | 9.3% | 9.2% | 9.1% | 9.3% | 9.2% | | | |
| **Operating profit** | **4,473** | **4,384** | **8,857** | **4,478** | **4,414** | **8,892** | **4,900** | **4,400** | **9,300** |
| YoY | 20.8% | 19.1% | 19.9% | 0.1% | 0.7% | 0.4% | 9.4% | -0.3% | 4.6% |
| OPM | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% |
| **Recurring profit** | **4,844** | **4,595** | **9,439** | **4,673** | **4,756** | **9,429** | **5,200** | **4,800** | **10,000** |
| YoY | 23.9% | 16.9% | 20.4% | -3.5% | 3.5% | -0.1% | 11.3% | 0.9% | 6.1% |
| RPM | 1.3% | 1.3% | 1.3% | 1.2% | 1.3% | 1.2% | 1.3% | 1.3% | 1.3% |
| **Net income** | **3,231** | **3,130** | **6,361** | **3,332** | **3,571** | **6,903** | **3,400** | **3,100** | **6,500** |
| YoY | 32.8% | 28.8% | 30.8% | 3.1% | 14.1% | 8.5% | 2.0% | -13.2% | -5.8% |
| Net margin | 0.9% | 0.9% | 0.9% | 0.9% | 1.0% | 0.9% | 0.9% | 0.8% | 0.8% |

Source: Shared Research based on company data

FY03/20 company forecasts are sales of JPY771.0bn (+2.2% YoY), operating profit of JPY9.3bn (+4.6% YoY), and net income of JPY6.5bn (-5.8% YoY). FY03/20 earnings forecasts are difficult, because a consumption tax hike Japan is set to occur during the fiscal year, which will likely result in a last-minute demand surge followed by a reactionary slump or purchase cutbacks. The company forecasts sales growth of 3.4% YoY in 1H and 1.0% YoY in 2H.

The company intends to continue focusing on high value-added, profitable merchandise such as cosmetics, pet goods, and home goods in FY03/20, targeting over 5% YoY sales growth in Health & Beauty, especially cosmetics, which account for a 30% share of the category. The company aims to increase sales by collaborating with cosmetics companies to plan and propose instore promotions to retailers. Following the absorption of wholly owned subsidiary Fashion ARATA on April 1, 2019, the company set up a cosmetics business unit that reports directly to the president. The establishment of this business unit suggests that, in terms of organization, the company is working strategically to increase cosmetics sales.

In the Pet Goods category, the company aims to consolidate its No. 1 position in the business through wholly owned subsidiary Japell Co., Ltd., targeting over 5% YoY sales growth. The company seeks to bring more distributors into the fold by improving business efficiency. It aims to achieve this feat by transferring a portion of business from the parent and harnessing its strengths, including a diverse product range and an ability to design retail spaces. In Home Goods, the merchandise have relatively slow turnover rates in stores, but the company has a lineup of merchandise needed by drugstores and supermarkets. The company aims to increase market share by harnessing its ability to make proposals to retailers based on data analysis (a relatively new trend in this product category) to win bulk orders from retailers for greater efficiency.

The company aims to lift OPM and raise GPM by around 0.1pp by increasing sales of relatively profitable products to absorb higher SG&A expenses (such as increased distribution expenses).

## Initial company forecast and results

| Results vs. Initial Est. (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| Sales (Initial Est.) | 600,000 | 609,000 | 628,000 | 622,000 | 640,000 | 643,000 | 679,000 | 719,000 | 760,000 |
| Sales (Results) | 601,949 | 606,705 | 616,327 | 651,954 | 638,792 | 676,743 | 704,610 | 732,914 | 754,447 |
| **Results vs. Initial Est.** | **0.3%** | **-0.4%** | **-1.9%** | **4.8%** | **-0.2%** | **5.2%** | **3.8%** | **1.9%** | **-0.7%** |
| Operating profit (Initial Est.) | 1,200 | 400 | - | 4,700 | 4,550 | 4,250 | 6,600 | 8,100 | 9,700 |
| Operating profit (Results) | 286 | 4,174 | 3,726 | 4,472 | 2,461 | 5,699 | 7,384 | 8,857 | 8,892 |
| **Results vs. Initial Est.** | **-76.2%** | **943.5%** | **-** | **-4.9%** | **-45.9%** | **34.1%** | **11.9%** | **9.3%** | **-8.3%** |
| Recurring profit (Initial Est.) | 4,700 | 4,300 | 4,800 | 4,400 | 4,400 | 4,300 | 6,700 | 8,300 | 10,000 |
| Recurring profit (Results) | 4,257 | 3,915 | 3,605 | 4,388 | 2,469 | 5,811 | 7,842 | 9,439 | 9,429 |
| **Results vs. Initial Est.** | **-9.4%** | **-9.0%** | **-24.9%** | **-0.3%** | **-43.9%** | **35.1%** | **17.0%** | **13.7%** | **-5.7%** |
| Net income (Initial Est.) | 1,500 | 1,440 | 2,000 | 1,900 | 1,900 | 1,900 | 3,600 | 5,200 | 6,500 |
| Net income (Results) | 1,015 | 1,628 | 1,768 | 2,435 | 1,124 | 3,244 | 4,863 | 6,361 | 6,903 |
| **Results vs. Initial Est.** | **-32.3%** | **13.1%** | **-11.6%** | **28.2%** | **-40.8%** | **70.7%** | **35.1%** | **22.3%** | **6.2%** |

Source: Shared Research based on company data

## Medium-term outlook

### Overview

The company announced its current medium-term management plan (FY03/18 to FY03/20) in May 2017. The plan targets sales of JPY760.0bn (CAGR of 2.6%, based on FY03/17 figures), recurring profit of JPY10.0bn (8.4%), net income of JPY6.0bn (7.3%), and ROE of around 9% (8.4% in FY03/17). Performance was above target in FY03/18, and the company expects to hit the plan's recurring profit target of JPY10.0bn in FY03/19. Given these results, in May 2018, the company upped the plan's targets to sales of JPY780.0bn, recurring profit of JPY10.5bn, and net income of JPY6.8bn. The company made small adjustments to its FY03/20 forecasts (sales: JPY771.0bn, recurring profit: JPY10.0bn, and net income: JPY6.5bn), but no major change in management strategy.

ARATA was formed in 2002 as a result of the business combination of three wholesalers. The medium-term management plans formulated since then had focused on "strengthening the foundation," along with themes such as increasing profits, improving operations, and integrating and unifying the company. Having been through several such plans, the company believes it now has a relatively solid foundation in place and is using "first stage" as a catch-all phrase for initiatives to date. It is positioning the current plan as the start of the "second stage," a period for "pursuing new possibilities in the wholesale business while looking a decade ahead." The three key points of this stage are to 1) "continue to draw a growth strategy," 2) "lay the groundwork for the future," and 3) "further strengthen the business foundation."

### 1) "Continue to draw a growth strategy"

This strategy indicates how the company plans to grow its core business of wholesaling in Japan. The company plans to concentrate on expanding business in three product categories: health and beauty (including cosmetics, hair care, and body care products), home goods, and pet goods.

#### Health & Beauty

In this category, the company plans to focus specifically on cosmetics. The company says it is particularly competitive in wholesaling cosmetics and has earned a high degree of trust from cosmetics manufacturers and drugstores that sell cosmetics, which have a relatively high GPM. With the percentage of women working outside the home on the rise in Japan, the company aims to step up sales efforts to "meet the needs of the time-crunched working woman." To this end, it strengthened collaboration with Fashion Arata (a subsidiary the company absorbed in April 2019) and plans to bolster sales through sales activities that harness specialist knowledge. The company already handles over-the-counter drugs, but believes that ample room for growth still exists. The company plans to enlarge this business in tandem with market growth, which it believes will expand as the Japanese population ages and emphasis on self-medication increases.

#### Home Goods

In this category, the company has a market share of more than 10%, which it plans to increase further. Numerous wholesalers handle home goods, and some are specialized wholesalers focusing on specific types of home goods. However, few general wholesalers offer a wide range of home goods, and few companies cover a broad range of fields on a nationwide scale. ARATA thus believes it can leverage its strengths as a general wholesaler with nationwide coverage. Supermarkets and other retailers benefit from being able to place consolidated orders for all the non-food items they need.

#### Pet Goods

The company is strengthening its presence in items for pets via Japell, a subsidiary. Operations had overlapped, as Japell was a leading wholesaler of pet goods, which ARATA (parent) also handled. The company has concentrated the handling of all pet-related items at Japell. ARATA is also working with its subsidiary on strengthening the ability to make integrated proposals regarding pets and pet-related goods to retailers. It aims to provide end-to-end support for the creation of retail spaces dedicated to pets, adopting a captive selling strategy.

**Strengthening operations in Kyushu, Tokyo, Nagoya, and Osaka**

The company is working to strengthen operations in the regions of Kyushu, Tokyo, Nagoya, and Osaka. The company has bases across most of Japan. It considers the ability to respond to the needs of regional customers to be one of its strengths. However, to date the company has covered the entire Kyushu region in the south of Japan through the Kyushu Kita (north) center in Fukuoka. From the standpoint of business continuity planning, the company recognizes the need to diversify risks. To do so, the company built the Kyushu Minami (south) center, which commenced operations in June 2018. This logistics center, which involved total investment of JPY3.1bn, has an AI-equipped depalletizing robot and was designed to be highly efficient and reduce labor requirements. With Japan's population increasingly concentrated in the three main urban areas (Tokyo, Osaka, and Nagoya), ARATA recognizes a growing need to have logistics networks in place in the area. The need is particularly pronounced in the Tokyo area. The company estimates that if distribution continues to expand at its recent pace, in a few years, demand will outstrip its capacity. For that reason, the company is selecting a logistics base, where it intends to begin operations around 2021–2022.

**Aiming to make itself essential by providing information to retailers and offering retail space proposals**

To meet changing consumer needs, the company intends to provide information to retailers and enhance its retail space proposals. The company explains that commercial zones are shrinking as Japan's population ages and becomes increasingly concentrated in urban areas. At the same time, the products consumers want differ by customer type and commercial area. The company's sales exceed JPY700.0bn (converted to instore retail prices, Shared Research estimates retail value of more than JPY900.0bn), and it possesses associated sales and inventory data. The company is providing retailers with its analyses of big data and commercial zones and moving forward with proposals on how to respond to shrinking commercial zones. Its aim is to boost retailers' sales (and thus the volume of products they procure from ARATA).

## 2) "Lay the groundwork for the future"

The company aims to lay the steppingstones for medium- to long-term expansion by growing beyond its current core business of wholesaling daily necessities and cosmetics. Specifically, it aims to develop business overseas, respond to online needs, and strengthen in-house product development (functioning partly like a manufacturer).

**Overseas development**

The company established a subsidiary in Shanghai in 2011 and one in Thailand in 2013. Despite such overseas developments, overseas sales account for less than 1% of the total. In China, demand for Japanese cosmetics and other products is growing, setting the stage for online shopping from overseas. Large manufacturers can export products to China, but small and medium-sized manufacturers find this more difficult, as they do not have sales networks in place in the country. Sales companies in China that sell Japanese products find dealing with multiple Japanese companies problematic. If they were to work through ARATA, although procurement costs would rise to some extent, they would be able to source products from numerous manufacturers at once; the company intends to capture the demand of such companies. In Thailand, in addition to Japanese companies based in the country, ARATA plans to expand the number of local retailers it works with.

**Online**

The company currently handles some online sales, mainly for everyday items and cosmetics, but the scale is less than 1% of total sales. ARATA plans to gradually expand information systems and distribution functions. By doing so, it thinks it can better leverage the advantages that come from handling 120,000 items (based on 2018 Integrated Report) by meeting demand for products that are well suited for online sales because they are heavy, bulky, or handled by few stores. The company plans to look into ways it can utilize the data on brick-and-mortar stores it has accumulated through the wholesale business and turn it into useful marketing information for online business operations.

**Products developed in-house (private brands)**

The company also plans to continue pursuing in-house product development. So far, the company has developed around 350 such products. ARATA maintains a lineup of widely used products to meet retail store demand for products that are economical and profitable but for which small to mid-size retailers find it difficult to build their own private brands. According to the company, such products are also attractive for outsourced manufacturers because they help keep manufacturing equipment in

constant operation. These products therefore foster win–win–win relationships for retailers, manufacturers, and ARATA. The company plans to also develop high-value-added products that can boost retailers' unit selling prices.

**Main products developed independently and in collaboration**


Source: Company materials

## 3) "Further strengthen the business foundation"

The company's efforts to further strengthen its business foundation involve reinforcing its logistics functions. The company has 11 large logistics centers around Japan, each capable of handling products worth a total shipment value of more than JPY15.0bn per year. Including these bases, the company operates 32 logistics centers (four in Hokkaido, three in Tohoku, nine in the Tokyo metro area, four in Chubu, three in Kansai, seven in Shikoku/Chugoku, and two in Kyushu), many of which are small. In general, large-scale logistics centers tend to be more efficient. ARATA's recurring profit margin compares unfavorably to that of rival PALTAC (TSE1: 8283). Since the two companies book expenses differently, it is difficult to decipher the difference based on annual securities reports and other disclosed data. However, Shared Research considers ARATA's logistics system (operating multiple small logistics centers) to be a likely factor contributing to the difference in profitability. (See "Competitors" in the "Market and value chain" section.) The company opened large-scale logistics centers in Saitama and Chiba in 2008, Ishikari in 2011, Konan in 2013, and Kitakami in 2015, but this number appears insufficient. By continuing to invest in existing logistics centers, the company aims to increase levels of automation and labor savings, boosting efficiency. It is also considering a new large-scale logistics center in the Tokyo metro area in response to rising sales there. Strengthening its logistics functions has social significance as well, notes the company, as it would help ensure a stable supply of everyday items in the event of a large earthquake or other natural disaster.

**Logistics network**


Source: Company materials

## Historical medium-term plans

| Medium-term management plans | Targets and results (JPYbn) | | | | Key initiatives |
|---|---|---|---|---|---|
| FY03/06–FY03/08 (out Feb. 2005) | | FY03/05 Est. | FY03/08 Init. Target | **Act.** | Strengthen wholesale capabilities, and improve financial structure<br>- Enhance expertise in the five major categories<br>- Offer standardized services throughout the nation<br>- Raise market share further in the Kanto and Kansai regions |
| | Sales | 420.5 | 520.0 | **551.8** | |
| | RP | 8.0 | 9.0 | **1.9** | |
| FY03/08–FY03/10 (out Mar. 2007) | | FY03/07 Est. | FY03/10 Init. Target | **Act.** | Grow into a locally-rooted nationwide wholesaler<br>- Enhance organizational integration and build a low-cost management structure<br>- Further reduce assets to build an efficient business structure<br>- Improve profitability by enhancing wholesale capabilities |
| | Sales | 511.6 | 557.0 | **589.9** | |
| | RP | 1.4 | 4.9 | **3.9** | |
| FY03/10–FY03/12 (out May 2009) | | FY03/09 Act. | FY03/12 Init. Target | **Act.** | Strengthen ARATA brand<br>- Enhance sales and store-based marketing capabilities<br>- Bolster category management capability through group management<br>- Build a nationwide optimized logistics network<br>- Establish corporate governance structure and enhance management base |
| | Sales | 569.7 | 600.0 | **606.7** | |
| | RP | 2.3 | 5.8 | **4.3** | |
| FY03/12–FY03/14 (out May 2011) | | FY03/11 Act. | FY03/14 Init. Target | **Act.** | Grow into a next-generation wholesaler<br>- Enhance value-added offerings suitable to a next-generation wholesaler<br>(Improve sales support capabilities collaborating with other industries; expand services for sales and logistics)<br>- Expand and develop markets (promote group synergies; develop overseas businesses)<br>- Renovate cost structure (integrate and optimize internal operations; rebuild group logistics networks) |
| | Sales | 601.9 | 650.0 | **652.0** | |
| | RP | 4.3 | 8.0 | **4.4** | |
| FY03/15–FY03/17 (out May 2014) | | FY03/14 Act. | FY03/17 Init. Target | **Act.** | Build a new structure for a next-generation wholesaler<br>- Adopt profit management by company to enhance profitability<br>- Bolster product development leveraging ARATA's group-wide sales capabilities and network<br>- Strengthen profitability by enhancing expertise of sales, sales promotion, and store managing groups<br>- Gain earnings through investing management resources in overseas businesses and tighten profit management<br>- Propose products for e-commerce; improve logistics structure<br>- Integrate internal operations to office work center and procurement center to promote reduction of overhead |
| | Sales | 652.0 | 670.0 | **704.6** | |
| | RP | 4.4 | 6.7 | **7.8** | |
| FY03/18–FY03/20 (out May 2017) | | FY03/17 Act. | FY03/20 Init. Target | **Act.** | ARATA Second Stage: Looking a decade ahead, pursue new possibilities in the wholesale business<br>- Continue formulating growth strategies<br>- Lay the foundation for the future<br>- Further strengthen the management base |
| | Sales | 704.6 | 760.0 | | |
| | RP | 7.8 | 10.0 | | |
| | Net income | 4.9 | 6.0 | | |

Source: Shared Research based on company data

# Business

## Business model

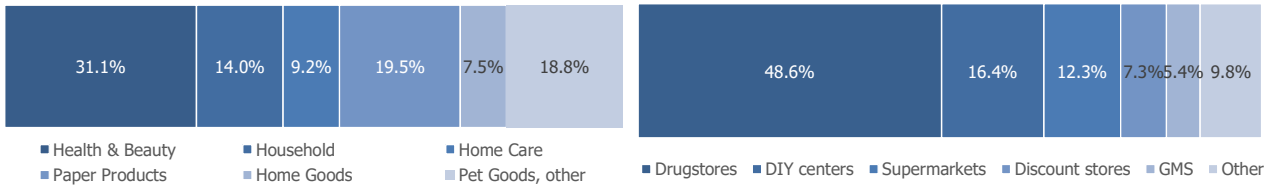
ARATA mainly wholesales everyday items and cosmetics, which it buys from manufacturers. The goods are delivered to the company's logistics centers, where they are sorted and dispatched to retailers to whom they are sold. Based on the company's 2018 Integrated Report, it handles around 120,000 items (such as cosmetics and other Health & Beauty products, detergents, paper products), which it buys from some 1,600 Japanese and overseas manufacturers. The company wholesales these products to almost all Japanese retailers (around 55,000 stores operated by 5,000 companies, including drugstores, supermarkets, and DIY centers). Upon receiving an order from a retailer, the company's role is to deliver the right quantity of the right products to the right location at the right time. The company has systems in place to handle detailed customer orders, including orders as small as a single toothbrush.

Sales exceed JPY700.0bn, which we estimate would be more than JPY900.0bn on a retail basis (converted to instore retail prices). The volume of items it handles is equivalent to that of top-10-ranking retailers in Japan.

The company breaks down the products it handles into six categories: 1) Health & Beauty (31% of sales in FY3/19): cosmetics, cosmetic accessories, bathwater additives, body cleansers, hair-care products, oral-care products, and health foods; 2) Paper Products (20%): baby products, baby diapers, nursing care items, adult diapers, sanitary goods, tissue paper, and toilet paper; 3) Household (14%): laundry detergent, kitchen cleansers and dish soap, and household cleansers; 4) Home Care (9%): fragrances and deodorizers, insect repellants, insecticides, incenses and candles for home altars, dry cell batteries and products that use them, recording media, lighting, electrical products, OA products, and photo-related products; 5) Home Goods (8%): kitchen consumables, products used on sinks, cleaning supplies, storage supplies, seasonal products, storage products, cooking items, tabletop items, and picnic supplies; 6) Pet Goods/Other (19%): pet supplies, stationery, toys, and auto products. The company's wide range of products excludes foods, apparel, consumer electronics, PCs, and mobile devices, which all vary in distribution channels.

The company sells its products to drugstores (49% of sales in FY3/19), DIY centers (16%), supermarkets (12%), discount stores (7%), GMSs (5%), and others (10%). Previously, convenience stores were among its important customers, but this sales channel has shrunk since Circle K Sunkus and FamilyMart merged and changed their procurement policies. The company does little business with online retailers, which are in the "Other" category. The company is not highly dependent on any individual business partner. Tsuruha Holdings (TSE1: 3391) accounted for 12.0% of sales in FY03/18, and is the only company to account for more than 10%.

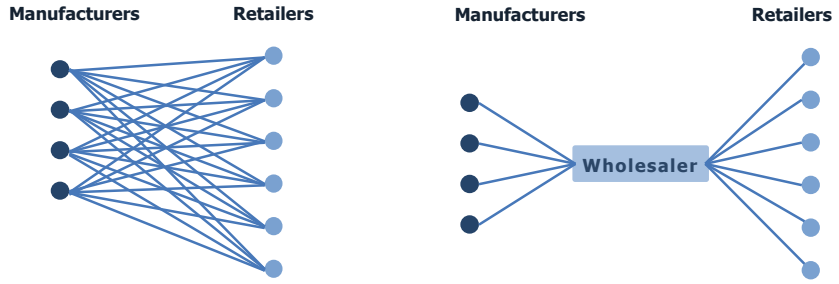
**Sales mix by product category (left) and sales mix by customer type (right) (FY3/19)**




Source: Shared Research based on company data

The company's GPM is generally between 10% and 11%. The average over the past five years was 10.3%, with 10.5% being the highest (in FY03/16) and 10.1% the lowest (in FY03/15). Shared Research thinks the company has four major sources of added value: First, it has the logistics capabilities to respond accurately to small-lot orders. Second, because the company handles such a wide range of items, it can serve as a one-stop wholesaler. Third, the company has the ability to make proposals that connect manufacturer promotions with instore retail methods. Fourth, the company has a vast store of transaction data (available for free or for a fee to retailers and manufacturers) that it can use to identify what is being sold and where, at any particular time.

The function of wholesaling: Simplifying connections between numerous suppliers and numerous sellers




Source: Shared Research

### Accurate deliveries from logistics centers a source of added value

The company believes the logistics capabilities that enable it to respond accurately even to small orders are a source of added value. A wholesaler's role is to efficiently distribute products from multiple manufacturers to multiple retailers. ARATA works to ensure accurate and inexpensive product distribution, mainly through the operation of 11 large logistics centers across Japan, each capable of handling product volumes worth more than JPY15.0bn per year.

Products are typically delivered from manufacturers to logistics centers, where they are inspected, manually sorted, and then transported to large automated warehouses or areas for handling in smaller lots. In the past, after products arrived at a logistics center and were inspected, stickers were affixed at a designated location, and then first-round sorting was necessary. However, ARATA's state-of-the-art logistics centers now employ systems that streamline the receipt of goods. Developed in cooperation with manufacturers, these systems allow employees on the distribution end to simply wave a handheld terminal over the goods, automating the first-round sorting process. Even a medium-sized logistics center handles 40–50 trucks per day. Making forwarding operations more efficient helps to reduce operational mistakes, decreases truck congestion at logistics centers, and reduces the number of trucks waiting to be unloaded. (Shortening the long hours required for loading/unloading trucks helps lower transport costs.)

For small-lot deliveries, the company relies on human capabilities and mechanical checks to ensure that operations are efficient and mistakes are kept to a minimum. ARATA has introduced AiMAS, picking carts equipped with scales, at its logistics centers. Employees follow the instructions on a cart's screen, taking products off shelves and placing them on the cart. A bar code confirms that the correct products are taken, and the cart senses the weight of the cart before and after the product(s) have been added to confirm that the quantity is correct. The company uses such systems to make deliveries, in quantities as small as a single toothbrush, to 55,000 stores operated by some 5,000 companies, with a misdelivery rate of less than 1/100,000 (source: 2018 Integrated Report).

The Kyushu Minami center, the company's newest facility, has an AI-equipped depalletizing robot. Due to the sheer number of items the company handles, the task of locating the right container of goods from the vast number of containers stacked on pallets, and placing it on the conveyers for shipping yielded a number of permutations so large that robot programming was impracticable. For that reason, until recently, the company relied on humans for this task. However, the company has eliminated the need to program the robot by using a system comprising 2D/3D cameras and deep learning functionality, improving operational speed. As a result, work that previously required six employees can now be handled by one. The company makes capital investments of around JPY5.0bn per year; by using state-of-the-art distribution systems, it aims to handle more quantity without increasing the total number of employees, while ensuring accurate and efficient deliveries.

**AiMAS picking cart (left) and AI-equipped depalletizing robot (right)**

Source: Shared Research based on company materials

### Information system that facilitates one-stop service

The company has an information system to ensure the accuracy of orders it places and receives for the 120,000 items it handles. It uses an electronic data interchange (EDI) backbone provided by Planet (TSE JASDAQ Standard: 2391). Investors in Planet include manufacturers of everyday items such as Lion (TSE1: 4912) and Unicharm (TSE1: 8113), as well as Intec (now TIS [TSE1: 3626]). Planet was established to create systems for communicating data between wholesalers and manufacturers of everyday items, sundries, and cosmetics. ARATA has been working with Planet on EDI backbone development since that company's establishment, helping it create a framework for accurately handling information regarding the placement and receipt of orders between manufacturers and distributors. Planet also provides a supplementary service for small and medium-sized manufacturers without the wherewithal to install the EDI backbone. The service helps ensure the accuracy of information ARATA exchanges with these manufacturers, as well.

Different retailers use different systems for placing orders, but most are compliant with the distribution Business Message Standard (BMS). The distribution BMS arose as the result of an April 2007 project ran by the Ministry of Economy, Trade and Industry that aimed to standardize distribution systems so that EDIs could use specifications common among members of the distribution sector (manufacturers, wholesalers, and retailers). Distribution BMS compliance accelerates and reduces the cost of communicating data on order placement, shipping, receipt, inspections, and invoicing among these members. In the past, transferring data on order receipt and placement could be time-consuming, owing to limitations on telecommunication speed. Currently, such data can be transmitted and received rapidly and accurately. ARATA outsources management of the EDI system it uses for order receipt and placement with retailers (its customers).

Since 2011, the company has used InfoFrame DWH Appliance, an ultrahigh-speed data analysis platform provided by NEC (TSE1: 6701), and in March 2019, the company transitioned to NEC's next-generation product, the Data Platform for Analytics (DP4A). Each day, the company receives data on orders received from retailers and has thereby amassed a huge volume of data over time. The company uses this information in sales activities, to improve distribution efficiency, and to provide feedback to manufacturers. Before introducing NEC's platform in 2011, the company used its own dbQuest search system for extracting data. At busy times, particularly at the beginning and end of each month, search requests could take anywhere from dozens of minutes to several hours, limiting the number of searches possible.

The NEC system increased search speed by approximately 100 times, making it possible to use the data for a variety of purposes. Currently, the company uses it to manage profitability by customer and product group. In the future, it intends to utilize the DP4A's machine learning function to increase the amount of data it sells. In such ways, the company says it uses third-parties effectively to build information systems at little cost.

### Advice on creating successful retail spaces

Shared Research understands that the company stands out in the industry for its ability to make proposals that connect manufacturer promotions with instore retail methods. Facilitating such proposals is Dentsu Retail Marketing (DRM), an equity-method affiliate the company established in November 2006 along with Dentsu Tec Inc., a subsidiary of Dentsu (TSE1: 4324), NEC (TSE1: 6701), and Dai Nippon Printing (TSE1: 7912). Dentsu is a leading advertising agency with the top domestic market share and handles the creation of TV and online ads for many companies including manufacturers. ARATA has a 36% stake

in DRM (previously 20%). DRM's services include consulting on the analysis and use of customer purchasing data, planning and creating sales promotional tools tailored to store- or region-specific demand, managing instore product displays, and putting sales promotion tools in place in stores. Through DRM, the company works to maximize the combined effectiveness of different types of advertising and instore retail spaces. Recently, the company has been stepping up its efforts to create spaces in tie-ups with regional TV stations and newspaper advertisements. In addition to advertising products nationwide, the company creates plans to capitalize on regional events and proposes to retailers plans that link the three: special events, ads, and products.

In April 2007, the company established ISM Corporation as a subsidiary. As requested by manufacturers, employees of this subsidiary visit individual stores, particularly chain stores, at a specified time on a certain day to monitor store conditions, help design retail spaces, and provide feedback to the manufacturer. The service is designed to promote the effective nationwide rollout of products while helping create retail spaces that are on-trend. The company provides added value by offering advice on how to design "spaces that sell."

The company's SG&A ratio (SG&A expenses to sales) is generally between 9% and 10%. Over the past five years, the ratio has averaged 9.4%, with a high of 9.7% in FY03/15 and a low of 9.2% in FY03/19. Of this figure, salaries and allowances have been the largest component, averaging 2.8% of sales during the period, followed by packaging and transportation expenses, at 2.6%. Sales grew 18.1% from JPY638.8bn in FY03/15 to JPY754.4bn in FY03/19. The number of employees (consolidated basis) increased a modest 2.4% from 2,946 at end-FY03/15 to 3,016 at end-FY03/18, and salaries and allowances were up slightly. Packaging and transportation expenses, meanwhile, rose due to higher freight volumes and trended upward as a percentage of sales due to higher freight rates.

OPM was 0.4% in FY03/15, 0.8% in FY03/16, 1.0% in FY03/17, 1.2% in FY03/18, and 1.2% in FY03/19. Through FY03/18, gross profit rose in tandem with sales, with the GPM rising because sales grew faster than SG&A expenses. Packaging and transportation expenses rose, but the company raised the overall profit margin by controlling the rise in salaries and allowances and other personnel costs. OPM fell slightly YoY in FY03/19, but operating profit increased, because gross profit rose faster than SG&A expenses.

## Business breakdown

| Sales by category (JPYmn) | FY03/11 Act. | FY03/12 Act. | FY03/13 Act. | FY03/14 Act. | FY03/15 Act. | FY03/16 Act. | FY03/17 Act. | FY03/18 Act. | FY03/19 Act. |
|---|---|---|---|---|---|---|---|---|---|
| **Total sales (new categories)** | | | | | | | | **732,914** | **754,447** |
| YoY | | | | | | | | - | 2.9% |
| Health & Beauty | | | | | | | | 223,800 | 234,426 |
| YoY | | | | | | | | - | 4.7% |
| % of total sales | | | | | | | | 30.5% | 31.1% |
| Household | | | | | | | | 100,899 | 105,506 |
| YoY | | | | | | | | - | 4.6% |
| % of total sales | | | | | | | | 13.8% | 14.0% |
| Home Care | | | | | | | | 70,553 | 69,179 |
| YoY | | | | | | | | - | -1.9% |
| % of total sales | | | | | | | | 9.6% | 9.2% |
| Paper Products | | | | | | | | 70,553 | 69,179 |
| YoY | | | | | | | | - | -1.9% |
| % of total sales | | | | | | | | 9.6% | 9.2% |
| Home Goods | | | | | | | | 54,082 | 56,631 |
| YoY | | | | | | | | - | 4.7% |
| % of total sales | | | | | | | | 7.4% | 7.5% |
| Pet Goods, other | | | | | | | | 136,410 | 141,499 |
| YoY | | | | | | | | - | 3.7% |
| % of total sales | | | | | | | | 18.6% | 18.8% |
| **Total sales (old categories)** | **601,949** | **606,705** | **616,327** | **651,954** | **638,792** | **676,743** | **704,610** | **732,914** | **754,447** |
| YoY | 2.0% | 0.8% | 1.6% | 5.8% | -2.0% | 5.9% | 4.1% | 4.0% | 2.9% |
| Health & Beauty | 174,270 | 181,028 | 180,304 | 186,283 | 181,492 | 196,853 | 212,207 | 225,283 | |
| YoY | 2.3% | 3.9% | -0.4% | 3.3% | -2.6% | 8.5% | 7.8% | 6.2% | |
| % of total sales | 29.0% | 29.8% | 29.3% | 28.6% | 28.4% | 29.1% | 30.1% | 30.7% | |
| Toiletary | 155,835 | 159,510 | 160,467 | 169,839 | 163,503 | 162,333 | 169,312 | 175,291 | |
| YoY | - | 2.4% | 0.6% | 5.8% | -3.7% | -0.7% | 4.3% | 3.5% | |
| % of total sales | 25.9% | 26.3% | 26.0% | 26.1% | 25.6% | 24.0% | 24.0% | 23.9% | |
| Paper Products | 135,329 | 127,376 | 128,777 | 138,652 | 135,584 | 145,872 | 146,026 | 147,245 | |
| YoY | -1.3% | -5.9% | 1.1% | 7.7% | -2.2% | 7.6% | 0.1% | 0.8% | |
| % of total sales | 22.5% | 21.0% | 20.9% | 21.3% | 21.2% | 21.6% | 20.7% | 20.1% | |
| Home Goods | 42,591 | 43,004 | 45,498 | 48,833 | 47,440 | 50,021 | 51,912 | 54,285 | |
| YoY | - | 1.0% | 5.8% | 7.3% | -2.9% | 5.4% | 3.8% | 4.6% | |
| % of total sales | 7.1% | 7.1% | 7.4% | 7.5% | 7.4% | 7.4% | 7.4% | 7.4% | |
| Pet Goods, other | 93,924 | 95,787 | 101,281 | 108,347 | 110,773 | 121,664 | 125,153 | 130,810 | |
| YoY | -66.7% | 2.0% | 5.7% | 7.0% | 2.2% | 9.8% | 2.9% | 4.5% | |
| % of total sales | 15.6% | 15.8% | 16.4% | 16.6% | 17.3% | 18.0% | 17.8% | 17.8% | |

Source: Shared Research based on company data

Breaking sales down by product category, Health & Beauty, Home Goods, and Pet Goods/Other are the categories driving growth. According to the company, GPM is higher for Health & Beauty than other categories, although it varies between product items. We believe the company is competitive in this category and increasing its market share.

# Market and value chain

## Sales rising slightly more than drugstore sales

Drugstores are the company's largest customers, by percentage of sales. The top-selling product categories reflect this: Health & Beauty (mainly cosmetics and oral-care products) and Paper Products (mainly baby diapers, sanitary goods, and toilet paper) are sold in drugstores. Total drugstore sales across Japan have grown by a CAGR of 2.9% between FY2012 and FY2017 (from JPY5.9tn to JPY6.9tn). The company's sales have risen faster, climbing by a CAGR of 3.5%, from JPY616.3bn in FY03/13 to JPY732.9bn in FY03/18.

Looking at trends in the drugstore industry, large drugstores have been seeking to increase sales by aggressively opening new stores and through acquisitions. Meanwhile, small and medium-sized drugstores have been closing, accounting for a shrinking market share. ARATA delivers products to all the big drugstores in Japan. These drugstores make up a growing share of the market, driving up the company's sales. By customer type, ARATA's sales to drugstores have been rising at an annual rate of 5.1%, outpacing the growth rate of the drugstore industry itself. Major drugstores have established many tax-free stores to capture increasing demand from inbound tourists. ARATA thinks its ability to abundantly supply these stores with items popular among inbound tourists has contributed to its increase in sales.

However, the company has not benefited completely from sales growth in the large-drugstore subset. Sales at the six largest drugstores in Japan grew at a CAGR of 7.6% between FY2012 (JPY2.2tn) and FY2017 (JPY3.0tn), rising faster than ARATA's sales. The reason is that large drugstores have accelerated growth by stocking food items, which make up only a tiny proportion of the company's products.

Sales data for six large drugstores is from Matsumotokiyoshi Holdings (TSE1: 3088), cocokara fine (TSE1: 3098), Cosmos Pharmaceutical (TSE1: 3349), Tsuruha Holdings (TSE1: 3391), Sugi Holdings (TSE1: 7649), and Sundrug (TSE1: 9989). Data for Welcia Holdings (TSE1: 3141) has been omitted, as FY02/15 was an irregular period due to a change in the fiscal year-end.

Among drugstores, the company's sales to Tsuruha Holdings make up more than 10% of total sales, requiring a separate breakdown in its annual securities report. (In FY03/18, sales to Tsuruha were JPY87.6bn, or 12.0% of FY03/18 sales).

**Sales growth ratios**

| (JPYtn) | FY2012 | FY2013 | FY2014 | FY2015 | FY2016 | FY2017 | CAGR FY2012–2017 |
|---|---|---|---|---|---|---|---|
| Sales: Total drugstores | 5.94 | 6.01 | 6.07 | 6.13 | 6.49 | 6.85 | 2.9% |
| YoY | | 1.2% | 1.0% | 1.1% | 5.9% | 5.5% | |
| Sales: Six major drugstores | 2.22 | 2.42 | 2.51 | 2.80 | 2.95 | 3.20 | 7.6% |
| YoY | | 9.1% | 3.9% | 11.5% | 5.3% | 8.5% | |
| PALTAC (8283) (JPYbn) | 785.8 | 831.9 | 794.2 | 860.4 | 922.1 | 966.7 | 4.2% |
| YoY | | 5.9% | -4.5% | 8.3% | 7.2% | 4.8% | |
| ARATA (JPYbn) | 616.3 | 652.0 | 638.8 | 676.7 | 704.6 | 732.9 | 3.5% |
| YoY | | 5.8% | -2.0% | 5.9% | 4.1% | 4.0% | |
| Drugstore sales | 272.9 | 292.9 | 293.0 | 311.9 | 331.3 | 349.9 | 5.1% |
| YoY | | 7.3% | 0.1% | 6.4% | 6.2% | 5.6% | |
| Other sales | 343.4 | 359.1 | 345.8 | 364.9 | 373.3 | 383.0 | 2.2% |
| YoY | | 4.6% | -3.7% | 5.5% | 2.3% | 2.6% | |

Source: Shared Research based on information from the Japan Association of Chain Drug Stores and individual companies

The company also sells product to other customer types, so sales growth is affected by their performance, as well. Over the past five years, ARATA's sales to discount stores have risen by a CAGR of 5.8%. Among key customers, store numbers have grown, and discount stores have also benefited from increased demand from inbound tourists. On the other hand, sales to DIY centers have risen 1.4%, to supermarkets 0.7%, and to general merchandise stores (GMSs) 0.3%. Sales to convenience stores are no longer on a meaningful scale, falling as convenience stores have restructured and changed their procurement policies.

### Sales by customer type

| Sales by customer type (JPYmn) | FY03/11 Act. | FY03/12 Act. | FY03/13 Act. | FY03/14 Act. | FY03/15 Act. | FY03/16 Act. | FY03/17 Act. | FY03/18 Act. | FY03/19 Act. |
|---|---|---|---|---|---|---|---|---|---|
| **Total sales** | **601,949** | **606,705** | **616,327** | **651,954** | **638,792** | **676,743** | **704,610** | **732,914** | **754,447** |
| YoY | 2.0% | 0.8% | 1.6% | 5.8% | -2.0% | 5.9% | 4.1% | 4.0% | 2.9% |
| Drugstores | | | 272,929 | 292,880 | 293,028 | 311,892 | 331,310 | 349,940 | 367,008 |
| YoY | | | - | 7.3% | 0.1% | 6.4% | 6.2% | 5.6% | 4.9% |
| % of total sales | | | 44.3% | 44.9% | 45.9% | 46.1% | 47.0% | 47.7% | 48.6% |
| DIY centers | | | 115,295 | 120,156 | 112,415 | 116,301 | 117,565 | 123,558 | 123,829 |
| YoY | | | - | 4.2% | -6.4% | 3.5% | 1.1% | 5.1% | 0.2% |
| % of total sales | | | 18.7% | 18.4% | 17.6% | 17.2% | 16.7% | 16.9% | 16.4% |
| Supermarkets | | | 84,050 | 86,825 | 85,880 | 86,393 | 88,414 | 92,264 | 93,043 |
| YoY | | | - | 3.3% | -1.1% | 0.6% | 2.3% | 4.4% | 0.8% |
| % of total sales | | | 13.6% | 13.3% | 13.4% | 12.8% | 12.5% | 12.6% | 12.3% |
| Discount stores | | | 39,970 | 42,766 | 42,961 | 48,354 | 50,678 | 53,054 | 55,448 |
| YoY | | | - | 7.0% | 0.5% | 12.6% | 4.8% | 4.7% | 4.5% |
| % of total sales | | | 6.5% | 6.6% | 6.7% | 7.1% | 7.2% | 7.2% | 7.3% |
| General merchandising stores (GMS) | | | 47,211 | 49,242 | 45,540 | 45,791 | 47,061 | 42,557 | 40,818 |
| YoY | | | - | 4.3% | -7.5% | 0.6% | 2.8% | -9.6% | -4.1% |
| % of total sales | | | 7.7% | 7.6% | 7.1% | 6.8% | 6.7% | 5.8% | 5.4% |
| Convenience stores | | | 11,331 | 9,904 | 9,554 | 8,481 | 5,763 | | |
| YoY | | | - | -12.6% | -3.5% | -11.2% | -32.0% | | |
| % of total sales | | | 1.8% | 1.5% | 1.5% | 1.3% | 0.8% | | |
| Other | | | 45,541 | 50,181 | 49,414 | 59,531 | 63,819 | 71,539 | 74,298 |
| YoY | | | - | 10.2% | -1.5% | 20.5% | 7.2% | 2.8% | 3.9% |
| % of total sales | | | 7.4% | 7.7% | 7.7% | 8.8% | 9.1% | 9.8% | 9.8% |

Source: Shared Research based on company data

## Competitors

ARATA's main competitor is PALTAC (TSE1: 8283). Both companies are large wholesalers that handle cosmetics and everyday items and focus mainly on drugstores. The third-largest company in the industry, Chuo Bussan Corporation, is the main company operated by CB Group Management (TSE1: 9852), and has sales of JPY145.8bn (FY03/19). ARATA and PALTAC together account for the lion's share of everyday-item wholesale in Japan, with a combined market share of nearly 50%. The companies are similar in that overseas sales account for less than 10% of the total, and that OPM levels are lower than either upstream manufacturers or downstream drugstores.

### Sales by customer type

| | ARATA (2733) | | | |
|---|---|---|---|---|
| | FY03/18 | | FY03/19 | |
| | (JPYmn) | % of sales | (JPYmn) | % of sales |
| **Sales** | **732,914** | **100.0%** | **754,447** | **100.0%** |
| Drugstores | 349,940 | 47.7% | 367,008 | 48.6% |
| DIY centers | 123,558 | 16.9% | 123,829 | 16.4% |
| Discount stores | 53,054 | 7.2% | 55,448 | 7.3% |
| Supermarkets (SMs), GMS | 134,821 | 18.4% | 133,861 | 17.7% |
| Convenience stores | - | - | - | - |
| Other | 71,541 | 9.8% | 74,301 | 9.8% |
| **Gross profit** | **76,475** | **10.4%** | **78,197** | **10.4%** |
| SG&A expenses | 67,618 | 9.2% | 69,305 | 9.2% |
| Packing and transportation expenses | 18,834 | 2.6% | 20,255 | 2.7% |
| Salaries and allowances | 19,760 | 2.7% | - | - |
| Provision for bonuses | 1,590 | 0.2% | - | - |
| Retirement benefit expenses | 950 | 0.1% | - | - |
| Other | 26,484 | 3.6% | - | - |
| **Operating profit** | **8,857** | **1.2%** | **8,892** | **1.2%** |
| Depreciation | 4,353 | 0.6% | 4,455 | 0.6% |
| **EBITDA** | **13,210** | **1.8%** | **13,347** | **1.8%** |

| | PALTAC (8283) | | | |
|---|---|---|---|---|
| | FY03/18 | | FY03/19 | |
| | (JPYmn) | % of sales | (JPYmn) | % of sales |
| **Sales** | **966,684** | **100.0%** | **1,015,253** | **100.0%** |
| Drugstores | 607,722 | 62.9% | 638,883 | 62.9% |
| DIY centers | 93,156 | 9.6% | 93,409 | 9.2% |
| Discount stores, other | 59,037 | 6.1% | 69,908 | 6.9% |
| SMs, SSMs, GMS | 93,155 | 9.6% | 92,020 | 9.1% |
| Convenience stores | 71,880 | 7.4% | 75,064 | 7.4% |
| Export, other | 41,734 | 4.3% | 45,969 | 4.5% |
| **Gross profit** | **76,051** | **7.9%** | **79,645** | **7.8%** |
| SG&A expenses | 53,045 | 5.5% | 54,246 | 5.3% |
| Distribution expenses | 10,210 | 1.1% | 11,062 | 1.1% |
| Salaries and allowances | 17,019 | 1.8% | 17,051 | 1.7% |
| Provision for bonuses | 2,035 | 0.2% | 1,713 | 0.2% |
| Retirement benefit expenses | 1,452 | 0.2% | 1,253 | 0.1% |
| Other | 22,329 | 2.3% | 23,167 | 2.3% |
| **Operating profit** | **23,006** | **2.4%** | **25,399** | **2.5%** |
| Depreciation | 4,830 | 0.5% | 4,493 | 0.4% |
| **EBITDA** | **27,836** | **2.9%** | **29,892** | **2.9%** |

Source: Shared Research based on company data. SSM refers to "super supermarkets."

### Different customer bases

In FY03/18, PALTAC had sales of JPY1.2tn, compared with JPY754.4bn for ARATA. Drugstores account for a high percentage of products delivered by both companies, but this ratio is higher for PALTAC than for ARATA (more than 60% vs. under 50%). Matsumoto Kiyoshi is PALTAC's major drugstore client, accounting for around 10% of total sales.

PALTAC's sales to convenience stores account for around 7% of total sales, while ARATA's are minimal. In the past, the Circle K Sunkus chain of convenience stores was a major client, but ARATA's sales to convenience stores essentially disappeared after the chain effectively merged with FamilyMart and changed its procurement policies. Conversely, ARATA has higher sales to DIY centers and supermarkets/GMSs than PALTAC. PALTAC outpaces ARATA in sales to discount stores, but the difference is relatively small.

Although the companies have different strengths, their market shares are stable. As the table at the start of this section shows, CAGR for sales over the past five years has been 4.1% at PALTAC versus 3.0% for ARATA, with favorable drugstore sales contributing relatively more to PALTAC.

### Different cost structures

In FY03/18, ARATA had a GPM of 10.4%, versus 7.9% at PALTAC. Although the companies use different methods for booking sales and expenses, based on the data released in the annual securities reports, we have drawn the conclusion that customers view ARATA to be providing greater added value.

ARATA has an SG&A ratio of 9.2%, versus 7.9% for PALTAC. ARATA explains this difference as being the cost necessary to create and maintain added value. According to their annual securities reports, distribution-related costs (called "packaging and transportation expenses" at ARATA, "distribution expenses" at PALTAC) were 2.6% of sales at ARATA, versus 1.1% for PALTAC. ARATA, which was formed through mergers, has many small logistics centers, whereas PALTAC has more large-scale logistics centers, which are more efficient. HR-related costs (the sum of salaries or salaries and allowances, provision for bonuses, and retirement benefit costs) was 3.0% for ARATA, vs. 2.1% for PALTAC. Shared Research believes ARATA has room to improve its distribution and HR efficiency.

### Holdings of business partners' shares

ARATA holds significant amounts of equity in business partners as policy shareholdings, as does PALTAC. According to their annual securities reports, in FY03/18 ARATA held JPY11.2bn worth of shares in 108 companies; PALTAC held JPY24.9bn in shares of 68 companies. Most of these shares are in the companies' suppliers (manufacturers) or customers (drugstores and other retailers).

# Strengths and weaknesses

## Strengths

- **Logistics capabilities:** After the company receives an order from a retailer, it works to efficiently deliver the right quantity of the right products to the right location at the right time. ARATA handles around 120,000 items (such as cosmetics and other Health & Beauty products, detergents, and paper products), most of which it buys from around 1,600 Japanese and overseas suppliers (source: 2018 Integrated Report). The company wholesales these products to around 55,000 stores operated by 5,000 companies, including drugstores, supermarkets, and DIY centers, covering almost all retail subsectors in Japan. We understand that this variety of items is attractive for retailers, as it allows them to order everything they need from one supplier. Despite repeated attempts by retailers to have manufacturers deliver to them directly, successes with this approach have been few. This situation creates an effective barrier to entry.
- **Ability to propose solutions:** For retailers, creating effective retail spaces is vital. ARATA can assist in this, as it knows what products peer retailers are selling in large volumes and how. The company uses this knowledge to propose new ideas to retail stores about how to create on-trend retail spaces. When a retailer introduces a new cosmetic product, for example, the company might suggest the retailer collaborate with the manufacturer to create an instore space with a TV commercial tie-in. (This approach enables the manufacturer to deliver sales promotion materials along with the product.) The company works with Dentsu Retail Marketing, a 36%-owned equity-method affiliate, to create regional sales promotion campaigns linked with regional TV commercials. This capability sets ARATA apart from peers. Dentsu, a business partner in these services, is a leading advertising agency with top domestic market share and handles the creation of TV and online ads for many companies including manufacturers.
- **Accumulated information:** We estimate that the sheer volume of the products ARATA handles would place it among Japan's top-10-ranking retailers (on an instore retail price basis). The company has thus accumulated a large amount of up-to-date data on retail orders (what is selling well, and where and what changes are occurring). Accurate information on what products are selling well (and which are not) at other companies is valuable for retailers. For the manufacturers as well, ARATA has information on peer products being sold at the retailers (what is selling, under what sort of a promotion plan and retail space design). Such information could at times be more valuable to manufacturers than the results of their own field research and can also be useful for their product development.

## Weaknesses

- **Logistics costs:** The company has numerous small-scale logistics centers, partly due to its corporate history of business combinations among wholesalers with close regional ties. Although the company is gradually building more efficient large-scale logistics centers, the rising quantity of products it handles has hampered a scrap-and-build approach. Logistics costs are relatively high as a result, which holds down profitability. A comparison with PALTAC based on disclosure materials points to the disadvantage of ARATA's logistic costs. Although the company is not losing out in the face of severe price competition, the current situation limits profits.
- **Overseas development capabilities:** Many large manufacturers and retailers are shifting their operations to China, ASEAN countries, and other markets that offer more room for growth than Japan. ARATA's overseas sales account for less than 1% of the total, and the company does not have a framework in place to sufficiently support customers that are developing operations overseas. Shared Research thinks this weakness may stem from the fact that wholesaling has grown more slowly than upstream and downstream parts of the supply chain.
- **Ability to respond to changing commercial channels:** The trend toward increasing online sales represents an existential threat to brick-and-mortar retailers (i.e., risk of market share erosion). Although ARATA has online retailer customers, they account for less than 1% of sales. Its competitiveness stems from the ability to connect manufacturers and retailers, but the company is not fully equipped to respond to the shift to e-commerce. Shared Research is awaiting for the company to disclose strategies concerning functions and value added it plans to offer in order to grow sales to online retailers.

# Historical results and financial statements

## Income statement

| Income statement (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| **Sales** | **601,949** | **606,705** | **616,327** | **651,954** | **638,792** | **676,743** | **704,610** | **732,914** | **754,447** |
| YoY | 2.0% | 0.8% | 1.6% | 5.8% | -2.0% | 5.9% | 4.1% | 4.0% | 2.9% |
| Cost of sales | 525,622 | 537,672 | 552,041 | 585,224 | 574,179 | 606,012 | 631,542 | 656,439 | 676,249 |
| **Gross profit** | **76,327** | **69,033** | **64,286** | **66,730** | **64,613** | **70,731** | **73,068** | **76,475** | **78,197** |
| GPM | 12.7% | 11.4% | 10.4% | 10.2% | 10.1% | 10.5% | 10.4% | 10.4% | 10.4% |
| SG&A expenses | 76,041 | 64,859 | 60,560 | 62,258 | 62,152 | 65,032 | 65,684 | 67,618 | 69,305 |
| SG&A ratio | 12.6% | 10.7% | 9.8% | 9.5% | 9.7% | 9.6% | 9.3% | 9.2% | 9.2% |
| **Operating profit** | **286** | **4,174** | **3,726** | **4,472** | **2,461** | **5,699** | **7,384** | **8,857** | **8,892** |
| YoY | 302.8% | - | -10.7% | 20.0% | -45.0% | 131.6% | 29.6% | 19.9% | 0.4% |
| OPM | 0.0% | 0.7% | 0.6% | 0.7% | 0.4% | 0.8% | 1.0% | 1.2% | 1.2% |
| Non-operating income | 5,195 | 949 | 942 | 927 | 944 | 977 | 1,158 | 1,195 | 1,189 |
| Non-operating expenses | -1,224 | -1,208 | -1,063 | -1,011 | -936 | -865 | -700 | -613 | -652 |
| Interest income | 9 | 8 | 6 | 7 | 6 | 6 | 7 | 7 | 6 |
| Dividend income | 91 | 98 | 111 | 113 | 120 | 128 | 148 | 161 | 172 |
| Interest expenses | -866 | -824 | -774 | -712 | -661 | -554 | -436 | -325 | -217 |
| Equity in earnings of affiliates | 6 | 12 | 14 | 9 | 27 | 17 | 26 | 14 | 8 |
| Forex gains (losses) | - | - | - | - | - | - | - | - | - |
| **Recurring profit** | **4,257** | **3,915** | **3,605** | **4,388** | **2,469** | **5,811** | **7,842** | **9,439** | **9,429** |
| YoY | 9.5% | -8.0% | -7.9% | 21.7% | -43.7% | 135.4% | 35.0% | 20.4% | -0.1% |
| RPM | 0.7% | 0.6% | 0.6% | 0.7% | 0.4% | 0.9% | 1.1% | 1.3% | 1.2% |
| Extraordinary gains | 188 | 3 | 22 | 611 | 148 | 69 | 51 | 411 | 1,239 |
| Gain on sale of fixed assets | - | - | 1 | 74 | - | 3 | 50 | 361 | 160 |
| Other | 188 | 3 | 21 | 537 | 148 | 66 | 1 | 50 | 1,079 |
| Extraordinary losses | 1,280 | 208 | 84 | 268 | 124 | 188 | 416 | 168 | 516 |
| Loss on disposal of fixed assets | 35 | 101 | 12 | 29 | 114 | 96 | 305 | 4 | 157 |
| Loss on retirement of fixed assets | 75 | 30 | 11 | 42 | 10 | 64 | 27 | 16 | 6 |
| Impairment losses | - | - | - | 57 | - | 26 | 7 | 103 | - |
| Loss on valuation of securities | 149 | 28 | 27 | 138 | - | 1 | - | 43 | 2 |
| Other | 1,170 | 77 | 61 | 140 | - | 2 | 77 | 45 | 353 |
| Income taxes | 2,149 | 2,081 | 1,772 | 2,294 | 1,376 | 2,458 | 2,624 | 3,319 | 3,244 |
| Implied tax rate | 67.9% | 56.1% | 50.0% | 48.5% | 55.2% | 43.2% | 35.1% | 34.3% | 32.0% |
| Net income attributable to non-controlling interests | - | - | 2 | - | -8 | -10 | -9 | 2 | 4 |
| **Net income attributable to owners of the parent** | **1,015** | **1,628** | **1,768** | **2,435** | **1,124** | **3,244** | **4,863** | **6,361** | **6,903** |
| YoY | -21.6% | 60.4% | 8.6% | 37.7% | -53.8% | 188.6% | 49.9% | 30.8% | 8.5% |
| Net margin | 0.2% | 0.3% | 0.3% | 0.4% | 0.2% | 0.5% | 0.7% | 0.9% | 0.9% |

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Over the past five years, sales have grown by a CAGR of 3.5%, although sales declined in FY03/15, affected by a consumption tax hike in Japan. Other than that, the company has grown each year. By customer type, sales to drugstores and discount stores have continued to drive overall growth, while growth in sales to DIY centers, supermarkets, and GMSs have been relatively low.

The company's GPM is generally between 10% and 11%. The average over the past five years was 10.3%, with 10.5% being the highest (in FY03/16) and 10.1% the lowest (in FY03/15). The SG&A ratio is generally between 9% and 10%. Over the past five years, the ratio has averaged 9.4%, with a high of 9.7% in FY03/15 and a low of 9.2% in FY03/19. Of this figure, salaries and allowances have been the largest component, averaging 2.8% of sales during the period, followed by packaging and transportation expenses, at 2.7%. Although sales have continued to grow, sales and allowances have fallen slightly as a percentage of sales. Packaging and transportation expenses have been up due to higher freight volumes and trended upward as a percentage of sales due to higher freight rates.

OPM was 0.4% in FY03/15, 0.8% in FY03/16, 1.0% in FY03/17, 1.2% in FY03/18, and 1.2% in FY03/19. In FY03/17, non-operating income and expenditures was a net positive JPY458mn, rising to JPY582mn in FY03/18 and remaining positive at JPY269mn in FY03/19. This increase was due mainly to a decline in interest payments, as interest-bearing debt decreased. The recurring profit margin was 1.1% in FY03/17, exceeding 1% for the first time since FY03/04.

In the past, the company recorded purchase discounts as non-operating income (amounting to JPY3.0–4.5bn per year). Since FY03/13, the company has recorded purchase discounts in cost of sales, as a deduction from purchases. (For this report, we have retroactively adjusted figures for FY03/12 to reflect this change.)

## Balance sheet

| Balance sheet (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and deposits | 9,640 | 9,985 | 8,108 | 10,965 | 11,800 | 14,119 | 13,693 | 17,826 | 19,798 |
| Notes and accounts receivable | 70,942 | 78,328 | 82,592 | 89,542 | 82,649 | 86,133 | 82,212 | 97,321 | 98,763 |
| Inventories | 30,203 | 30,907 | 31,009 | 30,981 | 28,072 | 27,971 | 29,556 | 29,997 | 30,804 |
| Accounts receivable–other | 16,952 | 18,719 | 17,953 | 20,222 | 17,650 | 19,877 | 23,939 | 22,827 | 22,825 |
| Other | 5,174 | 5,081 | 6,144 | 6,305 | 3,735 | 3,773 | 4,055 | 4,178 | 2,966 |
| **Total current assets** | **132,911** | **143,020** | **145,806** | **158,015** | **143,906** | **151,873** | **153,455** | **172,149** | **175,156** |
| Buildings and structures | 16,949 | 18,972 | 18,201 | 19,828 | 22,730 | 21,415 | 21,829 | 22,983 | 21,906 |
| Land | 20,076 | 19,996 | 19,997 | 19,853 | 20,540 | 21,330 | 21,004 | 20,461 | 19,936 |
| Other | 7,009 | 5,929 | 7,782 | 9,091 | 8,626 | 8,096 | 7,415 | 7,597 | 7,180 |
| **Total tangible fixed assets** | **44,034** | **44,897** | **45,980** | **48,772** | **51,896** | **50,841** | **50,248** | **51,041** | **49,022** |
| Goodwill | 2,294 | 1,874 | 1,524 | 1,093 | 661 | 230 | 7 | - | 14 |
| Other | 2,217 | 2,381 | 2,584 | 3,196 | 3,486 | 3,551 | 3,569 | 3,495 | 3,645 |
| **Total intangible assets** | **4,511** | **4,255** | **4,108** | **4,289** | **4,147** | **3,781** | **3,576** | **3,495** | **3,659** |
| Investment securities | 4,513 | 5,301 | 5,314 | 6,631 | 8,426 | 9,732 | 11,713 | 13,539 | 11,153 |
| Deferred tax assets | 2,480 | 2,171 | 1,266 | 541 | 308 | 347 | 327 | 270 | 572 |
| Other | 3,090 | 2,860 | 4,224 | 2,952 | 3,156 | 3,115 | 3,655 | 3,887 | 4,051 |
| **Investments and other assets** | **10,083** | **10,332** | **10,804** | **10,124** | **11,890** | **13,194** | **15,695** | **17,696** | **15,776** |
| **Total fixed assets** | **58,630** | **59,486** | **60,893** | **63,187** | **67,934** | **67,816** | **69,519** | **72,232** | **68,458** |
| **Total assets** | **191,541** | **202,506** | **206,699** | **221,202** | **211,840** | **219,689** | **222,974** | **244,381** | **243,614** |
| **Liabilities** | | | | | | | | | |
| Accounts and notes payable | 56,843 | 58,081 | 65,031 | 69,039 | 68,989 | 72,135 | 76,579 | 89,112 | 90,031 |
| Short-term debt | 41,315 | 42,934 | 35,380 | 37,069 | 35,271 | 38,017 | 28,147 | 32,653 | 17,945 |
| Accounts payable–other | 6,651 | 7,962 | 8,682 | 10,037 | 9,681 | 10,200 | 10,884 | 12,783 | 12,883 |
| Other | 6,421 | 6,821 | 7,422 | 6,765 | 8,473 | 9,404 | 8,393 | 11,283 | 8,970 |
| **Total current liabilities** | **111,230** | **115,798** | **116,515** | **122,910** | **122,414** | **129,756** | **124,003** | **145,831** | **129,829** |
| Long-term debt | 24,331 | 29,042 | 30,904 | 38,048 | 27,157 | 24,215 | 27,930 | 14,648 | 21,861 |
| Deferred tax liabilities for land revaluation | 1,063 | 860 | - | - | 648 | 517 | 1,052 | 1,626 | 442 |
| Retirement benefit liabilities | 7,366 | 7,479 | 7,977 | 6,589 | 4,898 | 6,478 | 7,276 | 7,535 | 7,724 |
| Other | 1,886 | 2,003 | 2,259 | 2,614 | 2,812 | 2,782 | 3,100 | 3,269 | 3,242 |
| **Total fixed liabilities** | **34,646** | **39,384** | **41,140** | **47,251** | **35,515** | **33,992** | **39,358** | **27,078** | **33,269** |
| **Total liabilities** | **145,876** | **155,182** | **157,655** | **170,161** | **157,929** | **163,748** | **163,361** | **172,909** | **163,099** |
| **Net assets** | 45,665 | 47,324 | 49,044 | 51,041 | 53,911 | 55,941 | 59,613 | 71,472 | 80,515 |
| Shareholders' equity | 45,747 | 46,930 | 48,078 | 49,894 | 51,108 | 53,181 | 55,474 | 65,861 | 76,259 |
| Accumulated other comprehensive income | -101 | 376 | 945 | 1,123 | 2,789 | 2,742 | 4,131 | 5,601 | 4,240 |
| Subscription rights to shares | - | - | - | - | - | - | - | - | - |
| Non-controlling interests | 19 | 18 | 21 | 24 | 14 | 18 | 8 | 10 | 16 |
| **Total net assets** | **45,665** | **47,324** | **49,044** | **51,041** | **53,911** | **55,941** | **59,613** | **71,472** | **80,515** |
| Working capital | 44,302 | 51,154 | 48,570 | 51,484 | 41,732 | 41,969 | 35,189 | 38,206 | 39,536 |
| Total interest-bearing debt | 62,384 | 68,707 | 62,566 | 70,872 | 58,637 | 58,982 | 52,569 | 43,640 | 36,524 |
| Net debt (net cash) | 52,744 | 58,722 | 54,458 | 59,907 | 46,837 | 44,863 | 38,876 | 25,814 | 16,726 |

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Although the scale of sales is large, at fiscal year-end the company maintains cash and deposits worth only about 0.3 months' sales, as its business model requires little cash on hand. Trade receivables (notes and accounts receivable) exceed trade payables (notes and accounts payable), but by a small margin. Inventory turnover is around 0.5 months. As of end-FY03/19, the company had JPY39.5bn in working capital.

Most tangible fixed assets are related to logistics centers (buildings, structures, and land). Intangible fixed assets are primarily software used by the company. Investments and other assets are mainly investments in securities (cross-shareholdings). The company says it plans to reduce its amount of cross-shareholdings.

Interest-bearing debt has fallen between end-FY03/12 and end-FY03/19 (from JPY68.7bn to JPY36.5bn). Shared Research understands the company includes convertible bond-type bonds with share acquisition rights within interest-bearing debt.

## Cash flow statement

| Cash flow statement (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| Cash flows from operating activities (1) | 1,919 | -720 | 9,959 | 1,481 | 21,955 | 7,594 | 12,637 | 11,649 | 9,513 |
| Pre-tax profit | 3,165 | 3,709 | 3,543 | 4,731 | 2,493 | 5,691 | 7,477 | 9,682 | 10,152 |
| Depreciation | 2,983 | 3,348 | 3,631 | 3,975 | 4,317 | 4,526 | 4,452 | 4,353 | 4,455 |
| Impairment losses | - | 27 | - | 57 | - | 26 | 7 | 103 | - |
| Amortization of goodwill | 624 | 419 | 423 | 431 | 431 | 431 | 223 | 7 | 7 |
| Gain on negative goodwill | - | - | - | - | - | - | - | -26 | - |
| Change in working capital | -1,888 | -7,067 | 1,533 | -3,094 | 12,316 | -202 | 6,500 | -2,956 | -977 |
| Income taxes | -2,202 | -1,939 | -1,851 | -2,039 | -1,386 | -1,806 | -3,097 | -2,539 | -3,685 |
| Cash flows from investing activities (2) | -3,227 | -4,575 | -4,054 | -5,878 | -6,775 | -3,360 | -3,155 | -2,924 | -880 |
| Purchase of tangible/intangible fixed assets | -3,158 | -4,034 | -3,843 | -6,338 | -7,289 | -3,392 | -3,093 | -5,086 | -3,198 |
| Proceeds from sale of tangible/intangible fixed assets | 160 | 14 | 103 | 380 | 94 | 74 | 212 | 2,031 | 703 |
| Free cash flow (1+2) | -1,308 | -5,295 | 5,905 | -4,397 | 15,180 | 4,234 | 9,482 | 8,725 | 8,633 |
| Cash flows from financing activities | 2,697 | 5,257 | -7,699 | 7,246 | -13,990 | -1,791 | -9,948 | -4,501 | -6,678 |
| Net increase in short-term borrowings | -1,300 | -600 | -8,400 | 500 | -3,400 | 4,400 | -5,340 | 1,913 | -10,600 |
| Net increase in long-term borrowings | 4,400 | 6,923 | 1,989 | 6,306 | -10,334 | -3,555 | -6,124 | -3,858 | -2,413 |
| Proceeds from issuance of, and redemption of, bonds | -30 | - | - | 1,978 | 1,475 | -500 | 5,480 | -500 | 3,979 |
| Issuance of bonds | - | - | - | 2,478 | 1,975 | - | 5,980 | - | 5,979 |
| Redemption of bonds | -30 | - | - | -500 | -500 | -500 | -500 | -500 | -2,000 |
| Proceeds from issuance of shares | - | - | - | - | - | - | - | - | 3,061 |
| Acquisition of treasury shares | -1 | - | -3 | -2 | -370 | -2 | -2,123 | -9 | -5 |
| Disposal of treasury shares | 402 | - | - | - | 368 | - | - | - | 1,517 |
| Dividends paid | -377 | -538 | -616 | -617 | -771 | -1,171 | -910 | -1,101 | -1,389 |

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

### Cash flows from operating activities

Working capital varies depending on year-end sales trends, but the company's main cash flows from operating activities are income before income taxes, depreciation and amortization, and income taxes.

### Cash flows from investing activities

Investments in tangible and intangible fixed assets vary between JPY3.0bn and more than JPY7.0bn, when payments rise to account for major expenditures as logistics centers. The company is thinking of establishing the tentatively named Tokyo Metropolitan Area Logistics Center, which would become operational between 2021 and 2022. The company expects cash flows from investing activities to rise as it purchases land, buildings/structures, and machinery and equipment for that center.

### Cash flows from financing activities

The company uses free cash flow mainly to repay borrowings. At the end of FY03/14, demand for working capital increased to fund the purchase of products amid a demand surge ahead of a hike in Japan's consumption tax rate. In FY03/15, however, cash flow was used to repay loans. In FY03/19, new share issuance, the selling of treasury stock, and the issuance of convertible bond-type bonds with share acquisition rights all had a positive effect on cash flow, but these factors were offset by repayment of borrowings, and cash flow used in financing activities finished at JPY6.7bn.

The company has not indicated a specific target for its dividend payout ratio. This ratio was 26.1% in FY03/16, 19.6% in FY03/17, 18.8% in FY03/18, and 20.1% in FY03/19.

## Profitability and safety analysis

| Profit margins (JPYmn) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| Gross profit | 76,327 | 69,033 | 64,286 | 66,730 | 64,613 | 70,731 | 73,068 | 76,475 | 78,197 |
| GPM | 12.7% | 11.4% | 10.4% | 10.2% | 10.1% | 10.5% | 10.4% | 10.4% | 10.4% |
| Operating profit | 286 | 4,174 | 3,726 | 4,472 | 2,461 | 5,699 | 7,384 | 8,857 | 8,892 |
| OPM | 0.0% | 0.7% | 0.6% | 0.7% | 0.4% | 0.8% | 1.0% | 1.2% | 1.2% |
| EBITDA | 3,269 | 7,522 | 7,357 | 8,447 | 6,778 | 10,225 | 11,836 | 13,210 | 13,347 |
| EBITDA margin | 0.5% | 1.2% | 1.2% | 1.3% | 1.1% | 1.5% | 1.7% | 1.8% | 1.8% |
| Net margin | 0.2% | 0.3% | 0.3% | 0.4% | 0.2% | 0.5% | 0.7% | 0.9% | 0.9% |
| **Financial ratios** | | | | | | | | | |
| ROA (RP-based) | 2.3% | 2.0% | 1.8% | 2.1% | 1.1% | 2.7% | 3.5% | 4.0% | 3.9% |
| ROE | 2.2% | 3.5% | 3.7% | 4.9% | 2.1% | 5.9% | 8.4% | 9.7% | 9.1% |
| Total asset turnover | 328.0% | 323.8% | 312.8% | 318.6% | 298.6% | 312.6% | 326.6% | 331.1% | 322.9% |
| Working capital | 44,302 | 51,154 | 48,570 | 51,484 | 41,732 | 41,969 | 35,189 | 38,206 | 39,536 |
| Current ratio | 119.5% | 123.5% | 125.1% | 128.6% | 117.6% | 117.0% | 123.8% | 118.0% | 134.9% |
| Quick ratio | 87.7% | 92.4% | 93.3% | 98.2% | 91.6% | 92.6% | 96.6% | 94.6% | 108.9% |
| OCF / Current liabilities | 1.7% | -0.6% | 8.6% | 1.2% | 17.9% | 6.0% | 10.0% | 8.6% | 6.9% |
| Net debt / Equity | 115.5% | 124.1% | 111.0% | 117.4% | 86.9% | 80.2% | 65.2% | 36.1% | 20.8% |
| OCF / Total liabilities | 1.3% | -0.5% | 6.3% | 0.9% | 13.9% | 4.6% | 7.7% | 6.7% | 5.8% |
| Cash conversion cycle (days) | 3.83 | 5.89 | 6.95 | 6.38 | 5.32 | 3.02 | 0.63 | -1.36 | -0.91 |
| Change in working capital | 2,688 | 6,852 | -2,584 | 2,914 | -9,752 | 237 | -6,780 | 3,017 | 1,330 |

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

# Historical performance

## Q3 FY03/19 results

### Summary

- **Q3 results:** Sales for the nine months ended December 31, 2018 were JPY578.1bn (+3.2% YoY), operating profit was JPY6.9bn (flat YoY), and net income was JPY5.2bn (+0.1% YoY). During the October–December quarter, sales were JPY197.0bn (+3.6% YoY), operating profit was JPY2.5bn (-0.2% YoY), and net income was JPY1.9bn (-5.0% YoY).
- **Downward revision to full-year forecast:** The company revised downward its forecast for FY03/19 to sales of JPY755.0bn (+3.0% YoY, previous forecast called for JPY760.0bn), operating profit of JPY8.6bn (-2.9% YoY, JPY9.7bn), net income of JPY6.4bn (+0.6% YoY, JPY6.5bn), and EPS of JPY371.1 (JPY389.8). The company maintained its dividend forecast of JPY80/share.
- **Sales by customer type:** During the October–December quarter, sales were up 3.6% YoY, recovering from an increase of just 1.7% YoY in the July–September quarter. By customer type, sales to drugstores were up 6.6% YoY, and sales to discount stores were up 4.3%, driving overall growth. Sales to supermarkets were up 2.2%, sales to DIY centers were down 1.6%, and sales to GMSs were down 1.8%.
- **Gross profit and SG&A expenses:** In the October–December quarter, gross profit was JPY20.2bn, up 2.9% YoY, but SG&A expenses rose 3.3% YoY, to JPY17.8bn. OPM was 1.2%, down from 1.3% a year earlier.

#### Performance in October–December 2018

In the October–December 2018 quarter, sales rose 3.6% YoY, to JPY197.0bn; operating profit fell 0.2% YoY, to JPY2.5bn; and net income decreased 5.0% YoY, to JPY1.9bn. The 3.6% YoY sales rise represented a recovery from a 1.7% YoY increase in the July–September quarter. Even so, operating profit continued to decline, following a 1.2% YoY fall in the July–September quarter.

By customer type, sales to drugstores were up 6.6% YoY, and sales to discount stores were up 4.3%, driving overall growth. Sales to supermarkets were up 2.2%, sales to DIY centers were down 1.6%, and sales to GMSs were down 1.8%.

Gross profit rose 2.9% YoY, to JPY20.2bn. The company worked to boost GPM through increased sales of highly profitable products, but says these efforts have not come to fruition as of yet. SG&A expenses were up 3.3% YoY, to JPY17.8bn. Until FY03/18, the company was able to raise profitability by constraining the rate of growth in SG&A expenses. In the October–December quarter, however, packaging and transportation expenses grew 9.2% YoY, to JPY5.4bn, making it difficult to hold down SG&A expenses.

#### Downward revisions to FY03/19 forecast

Along with cumulative Q3 earnings, the company announced downward revisions to its full-year forecast for FY03/19. The company revised downward its forecast to sales of JPY755.0bn (+3.0% YoY, previous forecast called for JPY760.0bn), operating profit of JPY8.6bn (-2.9% YoY, JPY9.7bn), net income of JPY6.4bn (+0.6% YoY, JPY6.5bn), and EPS of JPY371.1 (JPY389.8). Sales grew only 1.7% in the July–September quarter due to unseasonable weather and natural disasters. The company revised its forecast because it was unable to compensate for this slower growth even with the higher 3.6% YoY growth in the October–December quarter. Furthermore, higher freight rates made it difficult to curtail SG&A expenses, leading the company to forecast a decline in operating profit.

## 1H FY03/19 results

### Summary

- **1H results:** Sales were JPY381.1bn (+3.1% YoY), operating profit was JPY4.5bn (+0.1% YoY), and net income was JPY3.3bn (+3.1% YoY). The rate of progress toward targets was 50.1% for sales, 46.1% for operating profit, and 51.2% for net income. The company maintained its full-year forecasts.

- **July–September results:** Sales were JPY189.2bn in the three-month period (+1.7% YoY), operating profit was JPY2.0bn (-1.2% YoY), and net income was JPY1.6bn (+9.5% YoY).
- **Deceleration in sales:** In the July–September quarter, unseasonable weather resulted in lower sales of insecticide and other seasonal products, and repeated natural disasters resulted in a lower YoY sales growth compared to Q1 (April–June), when sales were up 4.4% YoY. By customer type, sales to drugstores were up 3.8% YoY, and sales to discount stores were up 4.5% YoY, driving overall growth, but sales to DIY centers were down 0.2% YoY, sales to supermarkets were down 0.9% YoY, and sales to GMSs were down 6.3% YoY.
- **Gross profit and SG&A expenses:** Gross profit was up 1.6% YoY, while SG&A expenses rose 1.9%. As a result, operating profit fell slightly in the July–September quarter.

#### July–September 2018 results

Sales were JPY189.2bn in the three-month period (+1.7% YoY), operating profit was JPY2.0bn (-1.2% YoY), and net income was JPY1.6bn (+9.5% YoY). In the July–September quarter, unusually hot weather led to slower sales of insecticide. Unseasonable weather caused sales of these and other seasonal products to decrease. Also, repeated natural disasters resulted in a lower YoY sales growth compared to Q1 (April–June), when sales were up 4.4% YoY. Partly because of these seasonal factors, gross profit was up 1.6%, rising less than sales. Consequently, GPM worsened slightly YoY, at 10.2%. However, in the July–September quarter SG&A expenses rose 1.9% YoY, so the SG&A ratio worsened slightly, to 9.2%. Operating profit fell 1.2% YoY.

By customer type, sales to drugstores were up 3.8% YoY, and sales to discount stores were up 4.5% YoY, driving overall growth, but sales to DIY centers were down 0.2% YoY, sales to supermarkets were down 0.9% YoY, and sales to GMSs were down 6.3% YoY.

The company left its forecast unchanged. The forecast called for FY03/19 sales of JPY760.0bn (+3.7% YoY), operating profit of JPY9.7bn (+9.5% YoY), net income of JPY6.5bn (+2.2% YoY), and EPS of JPY389.8.

## Q1 FY03/19 results

### Summary

- **Q1 results:** Sales were JPY191.9bn (+4.4% YoY), operating profit was JPY2.5bn (+1.2% YoY), and net income was JPY1.8bn (-2.0% YoY).
- **Sales by customer type:** Sales to drugstores (the company's core customers) grew 5.6% YoY, driving overall sales. Sales to DIY centers rose 4.4% YoY. Other sales growth was relatively sluggish. Sales to discount stores were up 1.3% YoY, sales to supermarkets were up 0.3% YoY, and sales to GMSs were down 5.3% YoY.
- **GPM down slightly:** Gross profit was up 3.3% YoY, and the GPM worsened slightly to 10.4% from 10.5% in Q1 FY03/18. SG&A expenses were up just 3.6% YoY, enabling the company to keep OPM essentially flat, at 1.3%.
- **Maintain full-year forecast:** The company left its initial forecast for FY03/19 unchanged. The forecast called for FY03/19 sales of JPY760.0bn (+3.7% YoY), operating profit of JPY9.7bn (+9.5% YoY), net income of JPY6.5bn (+2.2% YoY), and EPS of JPY389.8.
- **Equity financing:** Ahead of the earnings announcement, on July 4, the company announced the issuance of new shares, the sale of treasury stock, the secondary offering of shares, and the issuance of convertible bond-type bonds with share acquisition rights.

#### Q1 FY03/19 results

On August 2, 2018, the company announced results for Q1 of FY03/19. Sales were JPY191.9bn (+4.4% YoY), operating profit was JPY2.5bn (+1.2% YoY), and net income was JPY1.8bn (-2.0% YoY). The rate of progress toward full-year forecasts was 25.2% for sales, 25.6% for operating profit, and 22.4% for net income. Driving overall sales growth were robust sales to drugstores (+5.6% YoY). Sales to DIY centers were also brisk (+4.4% YoY). Other sales growth was relatively sluggish with sales to discount stores

and supermarkets rising by just 1.3% YoY and 0.3% YoY, respectively. Sales to GMSs were down 5.3% YoY. The company worked to increase its share of transactions with existing customers to expand business in line with its medium-term management plan.

GPM worsened slightly, from 10.5% in Q1 FY03/18 to 10.4%. The decrease was due to the fact that investments preceded the acquisition of a higher share of transactions. The company held the rise in SG&A expenses to 3.6% YoY, and OPM was essentially flat YoY, at 1.3%.

#### Equity financing

On July 4, the company announced the issuance of new shares, the sale of treasury stock, the secondary offering of shares, and the issuance of convertible bond-type bonds with share acquisition rights (CBs). Through these efforts, the company raised a total of JPY10.6bn (JPY4.6bn in new share issuance and the sale of treasury stock and JPY6.0bn through the CBs). The company plans to use these funds for capital investment to introduce IT and robotics to facilitate operations at the Tokyo Metropolitan Area Logistics Center (tentative name), to repay borrowings taken out to build the Kyushu Minami center, to repay other borrowings to improve the company's financial standing, and as working capital to expand the business. As a result, the number of issued shares (excluding treasury stock) increased by 917,000 shares (+5.5%) from 16.7mn shares at end-FY03/18. The number of dilutive shares from the issuance of CBs was 919,000 (conversion price of JPY6,528).

## FY03/18 results

### Summary

- **Results:** In FY03/18, sales rose 4.0% YoY, to JPY732.9bn; operating profit increased 19.9% YoY, to JPY8.9bn; and net income grew 30.8% YoY, to JPY6.4bn. Results were slightly higher than the company forecast (for sales of JPY724.0bn, operating profit of JPY8.7bn, and net income of JPY5.8bn).
- **Sales by customer type:** Driving overall sales growth was a 5.6% YoY rise in sales to drugstores, which accounts for a large percentage of total sales. Sales to DIY centers were up 5.1% YoY, and sales to discount stores rose 4.7% YoY.
- **Curtailing SG&A expenses:** Gross profit increased 4.7%, outpacing the rise in sales, so GPM rose to 10.4%. The rise in SG&A expenses was small, at 2.9%, so OPM grew to 1.2% (1.0% in FY03/17).
- **Forecast for FY03/19:** The forecast called for FY03/19 sales of JPY760.0bn (+3.7% YoY), operating profit of JPY9.7bn (+9.5% YoY), recurring profit of JPY10.0bn (+5.9% YoY), net income of JPY6.5bn (+2.2% YoY), and EPS of JPY389.8. The dividend forecast was JPY80/share.
- **Upward revision to medium-term plan:** The company revised upward its targets for the medium-term management plan ending in FY03/20. The new targets were for sales of JPY780.0bn (previously JPY760.0bn), recurring profit of JPY10.5bn (JPY10.0bn), and net income of JPY6.8bn (JPY6.0bn). The company left its ROE target unchanged, at 9%.

#### FY03/18 results

In FY03/18, sales rose 4.0% YoY, to JPY732.9bn; operating profit increased 19.9% YoY, to JPY8.9bn; and net income grew 30.8% YoY, to JPY6.4bn. Results were slightly higher than company forecasts (for sales of JPY724.0bn, operating profit of JPY8.7bn, and net income of JPY5.8bn). Driving overall sales growth was a 5.6% YoY rise in sales to drugstores, which accounts for 47.7% of total sales. Sales to DIY centers (16.9% of total sales) were up 5.1% YoY, and sales to discount stores (7.2%) rose 4.7% YoY. Sales to GMSs (6.5%) rose a slight 1.6% YoY. Sales to supermarkets (11.9%) were down 1.6%. Sales to convenience stores were JPY5.8bn in FY03/17. In FY03/18, these sales were not disclosed separately, as the figure had become immaterial.

Gross profit rose 4.7% YoY, to JPY76.5bn, increasing faster than sales, and GPM was 10.4%. The company employs thorough profitability management based on activity-based costing. By promoting high-value-added products, it has succeeded in boosting the unit price of products. The rise in SG&A expenses was smaller, at +2.9% YoY. The company continued to increase transaction volume, but managed to constrain rises in packaging and transportation expenses by curtailing the cost of product returns. Also, personnel costs rose less than sales, causing the SG&A ratio to fall from 9.3% in FY03/17 to 9.2%. OPM was 1.2%, up from 1.0% in the previous year.

Non-operating income and expenditures came to a net positive of JPY582mn, a slight improvement from the previous year's JPY458mn. Lower interest payments were part of the reason. In FY03/18, the company recorded JPY411mn in extraordinary gain on the sale or disposal of fixed assets, as well as an extraordinary loss of JPY168mn on impairment losses.

Dividends for the year were JPY75 per share (JPY35 at end-1H, JPY40 at year-end). The dividend payout ratio was 18.8%.

In FY03/18, cash flows provided by operating activities amounted to JPY11.6bn, and cash flows used in investing activities were JPY2.9bn, resulting in free cash flows of JPY8.7bn. Although interest-bearing debt fell and dividends increased, cash and cash equivalents at year-end were JPY17.1bn (from JPY12.9bn at end-FY03/17).

**Company forecast**

The forecast called for FY03/19 sales of JPY760.0bn (+3.7% YoY), operating profit of JPY9.7bn (+9.5% YoY), net income of JPY6.5bn (+2.2% YoY), and EPS of JPY389.8. The dividend forecast was JPY80/share (dividend payout ratio of 20.5%). Its medium-term management plan called for ARATA to achieve these numerical targets as part of its growth strategy for stepping up to the second stage.

Along with its results announcement, the company adjusted upward the targets of its medium-term management plan (for FY03/18 to FY03/20) to sales of JPY780.0bn (previous target was JPY760.0bn), recurring profit of JPY10.5bn (JPY10.0bn), and net income of JPY6.8bn (JPY6.0bn). The company gave two reasons for the upward adjustment: 1) the Japanese economy remained in a phase of modest growth, and 2) in FY03/18, recurring profit exceeded initial targets; the company expected to achieve recurring profit of JPY10.0bn in FY03/19. The company left the ROE target unchanged, at 9%. (Actual ROE for FY03/18 was 9.7%.)

# Other information

## History

| Date | | Event |
|---|---|---|
| April | 2002 | Established the holding company ARATA CORPORATION together with Daika Kabushiki Kaisha, Ito-I Co., Ltd. and Sunvic Co., Ltd. and listed on the JASDAQ |
| September | | Made Tokukura Co., Ltd. a subsidiary through a stock-for-stock merger |
| April | 2004 | Transitioned from a holding company to an operating company |
| August | | Made Kisosei Co., Ltd. a subsidiary through a stock-for-stock merger |
| April | 2005 | Merged with subsidiary Kisosei Co., Ltd., and its subsidiaries Kisosei Service Co., Ltd. and Dorf Co., Ltd. |
| December | | Made Japell Co., Ltd. a subsidiary through a stock-for-stock merger |
| October | 2006 | Merged with SISCO Co., Ltd. |
| November | | Established DENTSU RETAIL MARKETING INC. together with DENTSU TEC INC., a wholly owned subsidiary of DENTSU INC., NEC Corporation, and Dai Nippon Printing Co., Ltd. |
| April | 2007 | Established ISM Corporation as a subsidiary |
| December | | Acted to acquire treasury stock with the aims of improving capital efficiency and returning profits to shareholders, acquiring 4,066,750 shares (5.13%) through a tender offer |
| September | 2008 | Started service of sending planograms (information for shelving) together with CS YAKUHIN CO., LTD., CYBERLINKS CO., LTD., and NIPPON SOGO SYSTEMS, INC. |
| March | 2010 | Concluded a business cooperation agreement with NIPPON ACCESS, INC. and Alfresa Holdings Corporation |
| March | 2011 | Listed stock on the Second Section of the Tokyo Stock Exchange |
| February | 2012 | Established ARATA (Shanghai) Trade Co., Ltd. |
| March | | Listed on the First Section of the Tokyo Stock Exchange |
| August | | Acquired share of Ichino Co., Ltd. (currently Living Arata Co., Ltd.) and made the company a subsidiary |
| October | 2013 | Established ARATA (THAILAND) CO., LTD. in Bangkok, Thailand as a subsidiary |
| March | 2015 | Established joint venture SIAM ARATA CO., LTD. with Saha Group Co., Ltd. in Bangkok Thailand |
| June | 2016 | Issued 1st unsecured convertible bond-type bonds with share acquisition rights and 120% call option attached |
| July | 2018 | Issued new shares, disposed of treasury share, and issued 2nd unsecured convertible bond-type bonds with share acquisition rights and 120% call option attached |
| April | 2019 | Merged with subsidiary Fashion ARATA |

Source: Shared Research based on company materials

In April 2002, Daika K.K., Ito-I Co., Ltd., and Sunvic Co., Ltd. jointly established ARATA Corporation as a holding company and became fully owned subsidiaries. In the early 2000s, Japan was experiencing an increasingly pronounced deflationary trend. All manner of items was experiencing downward price pressure, affecting the everyday items and cosmetics industries and making it difficult to remain profitable in the wholesaling business. In the downstream retail segment, 2000 was marked by the opening in Japan of the Costco Makuhari warehouse and a Carrefour store, also in Makuhari. The emergence in Japan of such foreign retailers with global procurement capabilities prompted the nationwide expansion (increase in area) of some of Japan's largest retailers and proactive emergence as chains.

The wholesale sector was also called on to expand operations nationwide, offer services that were consistent throughout Japan, and reduce costs. This was the backdrop for the merger between Daika (base of operations in eastern Japan, from Hokkaido to Kanto), Ito-I (Chubu region), and Sunvic (Kyushu/Chugoku region). Later in 2002, Tokukura Co., Ltd., became a subsidiary. Kisosei Co., Ltd., became a subsidiary in 2004. In 2006, the company merged with Kansai-based SISCO Co., Ltd., transitioning to "ARATA," a wholesaler of everyday items offering services throughout Japan and with a strong regional focus.

In 2005, Japell Co., Ltd., a company specializing in pet foods, became a subsidiary. To this day, pet goods help differentiate ARATA from its competitors.

In November 2006, ARATA established Dentsu Retail Marketing in collaboration with three other companies: Dentsu Tec, a subsidiary of Dentsu (TSE1: 4324), NEC (TSE1: 6701), and Dai Nippon Printing (TSE1: 7912). (Initially, ARATA held 20% of this company, an equity-method affiliate. Its equity stake is now 36%.) In April 2007, ARATA established ISM Corporation as a subsidiary. Its goal in setting up these companies was to help ARATA evolve from an entity connecting manufacturers and retailers into a company that could make useful proposals to retailers on creating effective retail spaces, adding value to the wholesale business.

In February 2012, the company established a subsidiary in Shanghai, followed by a subsidiary in Bangkok in 2013. These subsidiaries are part of ARATA's efforts to increase its overseas sales.

## News and topics

### February 2019

**On February 5, 2019,** the company announced downward revisions to its forecast for FY03/19. The revised plan called for sales of JPY755.0bn (+3.0% YoY, initial forecast was for JPY760.0bn), operating profit of JPY8.6bn (-2.9% YoY, JPY9.7bn), recurring profit of JPY9.2bn (-2.5% YoY, JPY10.0bn), and net income attributable to owners of parent of JPY9.2bn (+0.6% YoY, JPY10.0bn). As reasons for the downward revision in sales, the company explained that sales in the July–September quarter had grown only 1.7% YoY due to unseasonable weather and natural disasters, and that sales growth of 3.6% YoY in the October–December quarter was insufficient to compensate for the slower growth in July–September. Also, the company said it was having difficulty constraining SG&A expenses due to a rise in freight rates, so it revised the forecast for operating profit downward.

**On February 1, 2019,** the company announced the decision to conduct an absorption-type merger of fully owned subsidiary Fashion Arata Corporation. It announced April 1, 2019 as the effective date of the merger.

### December 2018

Effective **December 21, 2018,** the company announced the establishment of a Nominating Committee and a Compensation Committee. ARATA explained that its aim in establishing these committees was to ensure that outside directors and auditors had sufficient opportunity to participate and provide advice in decision-making related to the nomination and compensation of directors. By enhancing objectivity and accountability, with this move the company aimed to strengthen its corporate governance framework. The two new committees were thus established as voluntary bodies to advise the company's Board of Directors. The committees are made up of three or more members, the majority of whom are independent executives (independent outside directors or independent outside auditors).

### November 2018

**On November 2, 2018,** the company announced the start of considerations on an absorption-type merger of Fashion Arata Corporation, a wholly owned subsidiary. The company was working to strengthen the Health & Beauty business as one of the strategies under its medium-term management plan ending in FY03/20. Fashion Arata is a wholesaler of cosmetics, cosmetics accessories, and light clothing; expanding its product line-up and area coverage, it has grown to conduct business with retailers throughout Japan in recent years. The company explained that by consolidating management resources, it aimed to accelerate efforts to strengthen the Health & Beauty business through more efficient sales and operational activities.

### July 2018

**On July 4, 2018,** the company announced the issuance of new shares, the sale of treasury stock, and the issuance of convertible bond-type bonds with share acquisition rights (CBs). Payment was concluded on July 24. Under this initiative, 617,000 new shares were issued (including over-allotments), the company sold 300,000 shares of treasury stock, and CBs were issued in the amount of JPY6.0bn (conversion price of JPY6,528), with 919,000 dilutive shares. As of end-FY03/18, the number of shares issued and outstanding was 16,675,000 (excluding treasury stock). The total amount raised through equity financing was JPY10.6bn (JPY4.6bn from new share issuance and the sale of treasury stock, JPY6.0bn from CBs). The company plans to use these funds for capital investment to introduce IT and robotics to facilitate operations at the Tokyo Logistics Center (tentative name), to repay borrowings taken out to build the Kyushu Minami center, to repay other borrowings to improve the company's financial standing, and as working capital to expand the business.

### Funding details

| | No. of shares | Paid-in amount | Offer price | Use of funds |
|---|---|---|---|---|
| | ('000 shares) | (JPYmn) | (JPY) | |
| New share issuance (incl. overallotment) | 617 | 3,121 | 5,276 | JPY4,615mn for financing new investments including capex for introducing IT system and robotics to warehouse operations at Tokyo Logistics Center (tentative name) under the Greater Tokyo Logistics Concept |
| Disposal of treasury stock | 300 | 1,518 | 5,276 | |

| | Potential shares | Offer price | Conversion price | Use of funds |
|---|---|---|---|---|
| Convertible bonds | 919 | 6,000 | 6,528 | 1) JPY3.0bn to repay loans on construction of Kyushu-Minami Center in the Kyushu Logistics Concept<br>2) JPY1,532mn to repay loans from financial institutions with the aim of improving financial structure<br>3) JPY1,455mn for working capital required for business expansion |
| Total | 1,836 | 10,639 | | |
| (Ref.) Shares outstanding (excluding treasury shares) at end FY03/18 | 16,675 | | | |

Source: Shared Research based on company data

## May 2018

**On May 9, 2018,** the company announced an upward revision to the targets of its medium-term management plan. Along with earnings results for FY03/18, the company announced revisions to its targets for the medium-term management plan (from FY03/18 to FY03/20). The revised targets for FY03/20 were sales of JPY780.0bn (previously JPY760.0bn, up 2.6% compared with the previous targets), recurring profit of JPY10.5bn (JPY10.0bn, +5.0%), net income attributable to owners of parent of JPY6.8bn (JPY6.0bn, +13.3%), and ROE of around 9% (around 9%). As reasons for the revisions, the company explained that the wholesaling of everyday items and cosmetics was benefiting from a gradual recovery in the Japanese economy, supported by favorable stock prices and corporate earnings. The company also pointed to resurgent personal consumption and strong ongoing demand from inbound tourism, which continued to drive strong growth. The company explained that due to efforts to improve profitability and productivity, it now expected to hit the medium-term management plan's JPY10.0bn target for recurring profit in FY09/19, so it had revised this figure upward for the final year of the plan, in FY03/20.

# Corporate governance and top management

## Corporate governance

| Form of organization and capital structure | |
|---|---|
| Form of organization | Company with Audit & Supervisory Board |
| Controlling shareholder and parent company | None |
| **Directors and Audit & Supervisory Board members** | |
| Number of directors under Articles of Incorporation | 15 |
| Number of directors | 9 |
| Directors' terms under Articles of Incorporation | 1 year |
| Chairman of the Board of Directors | Chairman |
| Number of outside directors | 2 |
| Number of independent outside directors | 2 |
| Number of members of Audit & Supervisor Board under Articles of Incorporation | 5 |
| Number of members of Audit & Supervisor Board | 4 |
| Number of outside members of Audit & Supervisory Board | 2 |
| Number of independent outside members of Audit & Supervisory Board | 2 |
| **Other** | |
| Participation in electronic voting platform | Y |
| Providing convocation notice in English | Y |
| Implementation of measures regarding director incentives | Performance-linked compensations |
| Eligible for stock option | - |
| Disclosure of individual director's compensation | None |
| Policy on determining amount of compensation and calculation methodology | In place |
| Corporate takeover defenses | None |

Source: Shared Research based on company materials

## Top management

**Nobuyuki Hatanaka, representative director, chairman, and CEO (born August 1, 1949)**

Joined Tomen Corporation in 1972. In June 1974, entered Shukosha K.K., becoming a director in November, being appointed managing director in 1983, vice president in 1988, and president in 1998. In 2002, appointed representative director and

chairman of Itoyasu Co., Ltd.; appointed representative director and chairman of SISCO Co., Ltd., in 2004; appointed representative director, vice president and executive officer of ARATA in 2006; and appointed representative director, president, and executive officer in 2007. In 2008, appointed representative director and chairman of Fashion Arata Corporation. Appointed representative director, chairman, and CEO of ARATA in 2017.

**Hiroaki Suzaki, representative director, president, and COO (born October 25, 1955)**

Joined Daika K.K. in 1978. In 2002, appointed branch manager of the Chiba branch. Became manager of the Tokorozawa branch of ARATA in 2004, and the general manager in charge of products in the sales division in 2007. Also made executive officer in 2008. In 2012, appointed executive officer, general manager in charge of products and general manager in charge of development strategy in the sales division. In 2014, appointed director, managing executive officer, and general manager of the Chubu branch. In January 2017, appointed director, vice president, operating officer, standing general manager of sales headquarters. In April, became representative director, president, and COO.

## Dividend policy

| Per share data (split-adjusted; JPY) | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| **Shares outstanding (ex. treasury shares, mn)** | 15.4 | 15.4 | 15.4 | 15.4 | 15.4 | 15.4 | 14.7 | 16.7 | 17.7 |
| EPS | 67.6 | 105.6 | 114.7 | 158.0 | 73.0 | 210.4 | 331.0 | 399.1 | 397.7 |
| EPS (fully diluted) | - | - | - | - | - | - | 294.9 | 377.8 | 381.2 |
| Dividend per share | 35.0 | 40.0 | 40.0 | 50.0 | 50.0 | 55.0 | 65.0 | 75.0 | 80.0 |
| Payout ratio | 51.8% | 37.9% | 34.9% | 31.6% | 68.5% | 26.1% | 19.6% | 18.8% | 20.1% |
| Book value per share | 2,960 | 3,068 | 3,180 | 3,309 | 3,496 | 3,628 | 4,055 | 4,285 | 4,547 |

Source: Shared Research based on company materials

The company has a basic policy of maintaining stable dividends, deciding the figure after taking into overall consideration performance during each fiscal year, as well as financial condition, and future development plans. The company has not set a specific target for the dividend payout ratio. This ratio was 26.1% in FY03/16, 19.6% in FY03/17, 18.8% in FY03/18, and 20.1% in FY03/19. Based on its initial forecasts for FY03/20 of JPY85/share, the payout ratio would be 22.7%.

## Major shareholders

| Top shareholders | Shares held ('000) | Shareholding ratio |
|---|---|---|
| Otowasyokusan Co., Ltd. | 1,081 | 6.06% |
| ARATA Employee Shareholding Association | 945 | 5.30% |
| The Master Trust Bank of Japan, Ltd. | 825 | 4.63% |
| Lion Corporation | 721 | 4.04% |
| Japan Trustee Services Bank, Ltd. | 707 | 3.97% |
| NORTHERN TRUST CO. (AVFC) SUB A/C USL NON TREATY | 509 | 2.85% |
| Nobuyuki Hatanaka | 461 | 2.59% |
| Northern Trust Co. (AVFC) Re IEDU Clients Now Leading 15 Pct Treaty Account (Standing proxy: The Hongkong and Shanghai Banking Corporation Limited, Custody Department) | 435 | 2.44% |
| Government of Norway (Standing proxy: Citibank N.A. Tokyo Branch) | 430 | 2.41% |
| Gomei Kaisha Kisosei Shoten | 344 | 1.93% |
| SUM | 6,458 | 36.22% |

Source: Shared Research based on company materials (as of March 31, 2019)

## Employees

| Number of employees | FY03/11 Cons. | FY03/12 Cons. | FY03/13 Cons. | FY03/14 Cons. | FY03/15 Cons. | FY03/16 Cons. | FY03/17 Cons. | FY03/18 Cons. | FY03/19 Cons. |
|---|---|---|---|---|---|---|---|---|---|
| Consolidated | 3,010 | 2,977 | 2,960 | 2,924 | 2,917 | 2,914 | 2,926 | 3,023 | 3,016 |
| Temporary staff (average) | 4,138 | 4,648 | 4,935 | 5,287 | 5,174 | 5,091 | 5,052 | 5,255 | 5,219 |
| Parent | 2,250 | 2,209 | 2,174 | 2,102 | 2,083 | 2,056 | 2,047 | 2,096 | 2,061 |
| Temporary staff (average) | 3,579 | 4,052 | 4,290 | 4,647 | 4,505 | 4,446 | 4,339 | 4,444 | 4,408 |

Source: Shared Research based on company materials

Sales are growing at an annual rate of 3–4%, but the overall number of employees (parent-only basis, including temporary employees) remains generally flat. Per-capita productivity is therefore growing.

## Key group companies

| Name | Location | Voting rights | Category | Business |
|---|---|---|---|---|
| Japell Co., Ltd. | Kasugai | 100% | Subsidiary | Wholesaling of pet-related products |
| Japell Partnership Service Co., Ltd. | Kasugai | 100% | Subsidiary | Retail sales of pet-related products, grooming services, recruitment of franchise stores |
| Pet Library Ltd. | Komaki | 100% | Subsidiary | Sales of pets, pet food and pet goods, pet grooming, boarding, pet insurance services |
| Mobby Co., Ltd. | Hiratsuka | 100% | Subsidiary | Export and import of pet-related products |
| ISM Corporation | Tokyo | 80% | Subsidiary | Store management company |
| Living Arata Co., Ltd. | Higashi Osaka | 100% | Subsidiary | Wholesaling of home goods |
| ARATA (Shanghai) Trade Co., Ltd. | Shanghai | 100% | Subsidiary | Wholesaling and import/export sales of daily goods, cosmetics, pet goods, and home goods, as well as other related services |
| Japell (Hong Kong) Co., Limited | Hong Kong | 100% | Subsidiary | Retailing, wholesaling, and import/export sales of pet-related products, as well as other related services |
| Arata (Thailand) Co., LTD. | Bangkok | 49% | Subsidiary | Wholesale business in Thailand |
| SIAM ARATA CO., LTD. | Bangkok | 75% | Subsidiary | Wholesale business in Thailand |
| DENTSU RETAIL MARKETING INC. | Tokyo | 36% | Equity-method affiliate | Field support services |
| Asahi Keshohin Hanbai Co., Ltd. | Urasoe, Okinawa | 49% | Equity-method affiliate | Wholesale of cosmetics, perfumed soap, tooth paste, food and beverages, textile products, and miscellaneous goods |

Source: Shared Research based on company materials

## Profile

| Company Name | Head Office |
|---|---|
| ARATA CORPORATION | East 21 Tower<br>6-3-2, Toyo, Koto-ku, Tokyo |
| **Phone** | **Exchange Listing** |
| +81-3-5635-2800 | Tokyo Stock Exchange, First Section |
| **Established** | **Listed On** |
| April 1, 2002 | March 19, 2012 |
| **Website** | **Fiscal Year-End** |
| http://www.arata-gr.jp/company/en/data.html | March 31 |
| **IR Contact** | **IR Web** |
| - | http://www.arata-gr.jp/ir/ |

We offer corporate clients comprehensive report coverage, a service that allows them to better inform investors and other stakeholders by presenting a continuously updated third-party view of business fundamentals, independent of investment biases. Shared Research can be found on the web at http://www.sharedresearch.jp.

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DIC Corporation
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Digital Garage Inc.
Dream Incubator Inc.
Earth Corporation
Elecom Co., Ltd.
en-Japan Inc.
euglena Co., Ltd.
Evolable Asia Corp.
FaithNetwork Co., Ltd.
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Hakuto Co., Ltd.
Happinet Corporation
Harmonic Drive Systems Inc.
HOUSEDO Co., Ltd.
IDOM Inc.
IGNIS LTD.
i-mobile Co.,Ltd.
Inabata & Co., Ltd.
Infocom Corporation
Infomart Corporation
Intelligent Wave, Inc.
ipet Insurance CO., Ltd.
istyle Inc.
Itochu Enex Co., Ltd.
JSB Co., Ltd.
JTEC Corporation
J Trust Co., Ltd
Japan Best Rescue System Co., Ltd.
JINS Inc.
JP-HOLDINGS, INC.
KAMEDA SEIKA CO., LTD.
Kenedix, Inc.
KFC Holdings Japan, Ltd.
KI-Star Real Estate Co., Ltd.
Kondotec Inc.
Kumiai Chemical Industry Co., Ltd.
Lasertec Corporation
LUCKLAND CO., LTD.
MATSUI SECURITIES CO., LTD.
Medical System Network Co., Ltd.
MEDINET Co., Ltd.
MedPeer,Inc.
Mercuria Investment Co., Ltd.
Micronics Japan Co., Ltd.
Milbon Co., Ltd.
MIRAIT Holdings Corporation
Monex Goup Inc.
MORINAGA MILK INDUSTRY CO., LTD.
NAGASE & CO., LTD
NAIGAI TRANS LINE LTD.
NanoCarrier Co., Ltd.
Net One Systems Co.,Ltd.
Nichi-Iko Pharmaceutical Co., Ltd.
Nihon Denkei Co., Ltd.
Nippon Koei Co., Ltd.
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ROUND ONE Corporation
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Take and Give Needs Co., Ltd.
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Tenpo Innovation Inc.
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TOYOBO CO., LTD.
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