February 9, 2021

Q3 financial results for the fiscal year ending March 31, 2021 (FY03/21)—A message from Koji Obuchi, president and CEO of the CROOZ Group

I am Koji Obuchi, president and CEO of the CROOZ Group. Earlier today, on February 9, 2021, we announced our financial results for Q3 FY03/21. Now, I would like to share with you my thoughts and impressions to give you a better understanding of the current situation. (This will be a long message, but please have a read.)

First of all, our Q3 consolidated results were encouraing considering the past one or two fiscal years. Consolidated sales were JPY10,297mn and consolidated operating profit came to JPY750mn. Compared to Q3 FY03/20 consolidated sales of JPY9,298mn and operating profit of JPY37mn, sales rose by 10.7% and operating profit by 1,927.0%, showing growth in both sales and operating profit. In addition, as I have previously mentioned, the consolidated operating profit of the entire group on a quarterly basis has been in the black since Q3 FY03/20, and as I noted in Q1 FY03/21, there is no need to worry about losses going forward. We will also make sure that we can generate sufficient profit even if we reinvest from Q3 FY03/21 onward.

The key driver of the improvement in Q3 consolidated operating profit was substantially higher operating profit in the SHOPLIST Business segment, which I will discuss in more detail below. Other reportable segments also continue to become businesses that steadily produce results within the scope of the 25 companies[*1] we cultivated since FY03/19. Now allow me to explain the results of each segment in detail.

First, I would like to address the SHOPLIST Business. In July 2020, I returned as president of CROOZ SHOPLIST, Inc., and at the same time, we brought on directors from CROOZ headquarters who have grown several businesses, as well as executives who are leading subsidiaries within the Group, to join SHOPLIST and work on over 200 critical projects. In Q3 FY03/21, our sales growth rate exceeded 10% for the first time in about two years, or eight quarters, rising 17.6% YoY to JPY8,033mn while producing operating profit of JPY506mn and an operating profit margin of 6.3%. In Q3 FY03/20, sales amounted to JPY6,831mn, with operating profit of JPY144mn and an operating profit margin of 2.1%, so we managed to boost sales, operating profit, and operating profit margin.

Now, let me talk about sales. As I explained in Q2 FY03/21, in order to get SHOPLIST's sales back on a growth trajectory, we are currently promoting the Critical Project Program under my direct supervision whereby project owners are given the same authority as I have and are responsible for implementing solutions. In FY03/21, the quarterly sales growth rates were even stronger in Q3 compared to 1H, with sales growing 5.3% in Q1, 4.5% in Q2, and 17.6% in Q3. The main reason behind this is that the number of visitors grew 23% YoY in Q3, reflecting the progress of the Critical Project Program launched in July 2020. There is still much to be achieved in terms of our target sales CAGR of 30%, so we will continue to generate results through our critical projects to boost sales.

Next, I will go over operating profit. As I have mentioned previously, we have attached utmost importance to improving operating profit in the SHOPLIST Business segment since FY03/20. In FY03/19, higher shipping charges in the transportation industry and other external factors had an impact on the entire e-commerce industry. In addition, we expanded and relocated our distribution warehouses to secure future growth. As a result of these expenditures, our logistics cost-to-sales ratio rose and we posted an operating loss of JPY544mn in Q4 FY03/19. We have been drafting and implementing a variety of measures since FY03/20, giving top priority to quickly returning our cost structure to its normal level. These efforts led to substantial improvements, with operating profit coming to JPY585mn in Q1, JPY448mn in Q2, and JPY506mn in Q3 FY03/21.

Our curtailment of logistics costs has had a marked impact on results. We have limited open space within our warehouses as much as possible and increased efficiency by collaborating with Group subsidiary CROOZ EC Partners to share warehouse space and implementing a variety of initiatives that include handling logistics operations for external clients. As a result of these efforts, our logistics cost-to-sales ratio declined from 15.4% in Q3 FY03/20 to 13.9% in Q3 FY03/21.

We also reduced our promotional cost-to-sales ratio from 12.8% in Q3 FY03/20 to 9.8% in Q3 FY03/21. The ratio dropped primarily because we conducted thorough investigations regarding promotional costs and measures with the involvement of a director in charge of the CROOZ Group's advertising starting in Q1 FY03/21, and because we accelerated our PDCA cycle and conducted efficient advertising investment. Q3 sales grew 17.6% YoY as we simultaneously curtailed costs and grew sales, which resulted in improving our cost structure.

Having improved our cost structure, it is essential that we expand sales moving forward. To achieve our medium- to long-term target of JPY100bn in annual SHOPLIST sales, we are simply pursuing two key indicators included in our results briefing materials: 1) 5 million annual unique purchasers and 2) an annual spend per user of JPY20,000. There are many measures we should be implementing to achieve these two key indicators, but we are most focused on encouraging users who visit the SHOPLIST website to make purchases before leaving and on increasing the number of repeat users who come back and make a second purchase through the website. We believe that strengthening the lineup of each company brand will be a key driver contributing to the achievement of these key indicators and, accordingly, continue to focus on bolstering this lineup.

As a result of aggressively pursuing our goal of opening 150 shops with high user recognition in FY03/21, we were able to open 88 shops from a total of 62 companies by the end of Q3. In addition, from FY03/21, we plan to expand our product lineup by providing products in categories which we have not previously handled, such as sports and outdoor apparel brands and cosmetics. While expanding product categories and brands, we will thoroughly analyze data to enhance our UI/UX and step up promotional measures so that customers will make multiple visits to the SHOPLIST website and continue to purchase products.

In terms of new businesses, CROOZ Media Partners, a reportable component of the Advertising Agency Businesses segment, generated Q3 sales of JPY397mn (-64.9% YoY) and operating profit of JPY25mn. The first reason for the drop was due to the loss of a contract from one major client in FY03/20. The second reason was that because it was urgent to revamp promotions for SHOPLIST, the representative of CROOZ Media Partners, who also serves as a director of CROOZ SHOPLIST, placed a higher priority on the promotion of SHOPLIST over the operation of CROOZ Media Partners for the time being. However, the Advertising Agency Business is a new business that has only been up and running for about three years, so from a short-term perspective, volatility in performance is unavoidable. Going forward, we aim to recover sales by capturing orders from other companies in the Advertising Agency Business, while focusing on the promotion of SHOPLIST and other measures to improve operations.

In the Media Businesses segment, in Q3 FY03/21 sales grew 87.4% YoY from JPY167mn in Q3 FY03/20 to JPY313mn, and operating profit was JPY108mn. Sales and profit were driven by Rank King, Inc., an e-commerce-related media operator in its second year of business, which we established in September 2019. If we look at it as an early-stage venture company that just started operations, it is growing quickly enough to go for an IPO.

In addition, in the Investment Businesses segment, Q3 sales came to JPY263mn while operating profit reached JPY147mn. Sales growth was driven by a gain on the sale of shares in one of our investees that went public.

As I mentioned above, as in Q1 and Q2, operating profit improved in Q3 FY03/21 as we cut logistics costs associated with SHOPLIST and reduced promotional costs through efficient promotion-related investment. Through substantial cost cutting over a short period, we have established a management structure that allows us to generate profit, but we believe that reinvesting this profit and expanding sales are essential as we move forward, and we plan to implement them as such. Going forward, we will reinvest to expand sales while generating profit to boost both sales and profit.

Previously, I mentioned that we established the Critical Project Program under my direct supervision at SHOPLIST wherein members of all departments hold daily meetings to identify issues, and then they themselves become project owners with the same level of authority as I have to solve issues that could boost sales or substantially reduce costs and workload. Since I took office in July 2020, we have identified 2,000 issues and established over 200 critical projects, and the project owners are digging deeper into the background and reasons for these challenges and implementing solutions based on various data. Every day, the critical issues and proposed solutions for 10 to 15 projects are reported to me.

In Q2 FY03/21, I told you that we would reinvest in ideas that have the potential to create breakthroughs throughout 2H FY03/21. However, we have not been able to achieve vertical sales growth, or our target sales CAGR of 30–40%, and if I were to grade our efforts to reinvest for sales expansion on a 100-point scale, I would say that our current score is about 10. That said, our promotional costs amounted to JPY873mn in Q3 FY03/20 and JPY791mn in Q3 FY03/21, or a decrease of about JPY100mn YoY, while our number of visitors grew 12% YoY in Q2 and 23% YoY in Q3, suggesting that the solutions proposed as part of our critical projects launched in July 2020 are starting to bear fruit. If we can reinvest exactly as we envisioned, I am confident that we can achieve our target sales CAGR of 30–40%. And as of December 31, 2020, we have a total of 27 critical projects with breakthrough potential, up four projects in Q3 from our Q2 total of 23 projects. Starting in Q4, we will reinvest more in projects with breakthrough potential to boost our sales CAGR above 30%. I believe we'll gradually start seeing results from these projects in April and following months. The aforementioned 23% increase in visitors is the result of one critical project, and knowing that we can still achieve great results like this again brings me nothing but high hopes for the future of SHOPLIST.

We announced one of the critical projects with breakthrough potential as part of the SHOPLIST Sustainability Project during our Q3 results announcement. In response to the current global issue of mass production, mass consumption, and mass disposal in the apparel industry, we aim to take part in solving these big challenges. Specifically, we endeavor to contribute to the apparel and e-commerce industries by engaging in sustainable acitivities such as carrying out outlet sales of excess inventory that would otherwise be disposed of.

Last but not least, my personal intention is to reduce warehouse rent, labor costs, and delivery costs by 0.5%, payment processing fees by 0.2%, and office rent by 0.2% as a percentage of sales by the end of December 2021 through critical projects. If we combine these cost reductions to the average operating profit margin of 7.2% for the first three quarters of FY03/21, SHOPLIST will be able to generate an operating profit margin of over 8%.*2 On top of that, we will invest in advertising and promotion to maximize sales for partner companies with stores on SHOPLIST, systems that make it easier to open new stores, and reinvest in projects with breakthrough potential. Through these efforts, we aim to achieve a sales CAGR of 30% and a full-year operating profit margin of at least 5% by September 30, 2021. After September 30, 2021, we will complete other improvements by March 31, 2022, and starting in the April–June 2022 quarter, we will aim for a 30% sales CAGR and an 8% full-year operating profit margin. [*3]

I said at the beginning of this letter that our results looked encouraging, but only because we compared it with the past fiscal year or two. Personally, as a business leader, I feel that the scale and growth of sales and profit, as well as the time it is taking to solve SHOPLIST's problems, are moving slower than I'd like. And as a management team striving for better, we all agree that the results weren't encouraging in its truest sense. Meanwhile, our ongoing critical projects are gradually producing results, and when we are done working through the challenges of all the projects, I believe our achievements will be unthinkable coming from our current level of sales and operating profit. We will work at full speed to achieve results in the shortest amount of time possible.

February 9, 2021

Koji Obuchi

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*1 Number of Group companies as of December 31, 2020. This figure indicates the number of Group companies that are actually involved in the Company's operations and does not include funds or other entities that are considered subsidiaries in consolidated financial reporting.

*2 Q4 FY03/21 results are not taken into account as they are not yet available.

*3 Currently, SHOPLIST's gross profit margin is roughly 20% on a cumulative basis through Q3, taking into account the main variable costs such as purchasing costs (about 60%), logistics costs (14%), and payment processing fees. Roughly speaking, gross profit was JPY4.2bn and operating profit was JPY1.5bn on a cumulative basis through Q3, with fixed costs (incurred regardless of sales figures) coming out to a little over JPY2.5bn, or a little less than 12% of sales. If we simply double our sales, the fixed cost-to-sales ratio will drop by 6%, thus boosting operating profit margin by 6%. In reality, we will be making investments to strengthen our workforce, so it will not be as simple as this calculation, but the business is structured in a way where profit margins rise in line with sales growth. Therefore, even if we reinvest from our current profits, I believe we can still achieve an operating profit margin of over 8% through sales expansion.