CROOZ

May 13, 2021

Financial results for the fiscal year ended 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 May 13, 2021, we announced our financial results for 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 full-year consolidated results were encouraging considering the past one or two fiscal years. Consolidated sales were up 5.1% YoY to JPY35,714mn, while consolidated operating profit made a dramatic recovery to JPY2,134mn, compared to a consolidated operating loss of JPY97mn in FY03/20.

The main reason for the substantial improvement in consolidated operating profit was the significant improvement in full-year operating profit of our mainstay SHOPLIST Business. This is the first full-year results announcement for the SHOPLIST Business since I returned to the company as president. **Full-year sales for FY03/21 were JPY27,194mn (+10.6% YoY), posting growth of over 10% for the first time in two fiscal years, while full-year operating profit surged to JPY1,942mn (+440.9% YoY), reaching all time highs in terms of sales and operating profit for the SHOPLIST Business**.

Please allow me to explain the results of each segment in detail.

First, I would like to address the SHOPLIST Business. As I have previously mentioned, 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 FY03/21, full-year sales were JPY27,194mn (+10.6% YoY) and full-year operating profit was JPY1,942mn (+440.9% YoY). In Q4 FY03/21, sales, operating profit, and operating profit margin all improved. Q4 sales were JPY5,802mn (+15.5% YoY), with growth continuing to exceed 10% from Q3, while operating profit was JPY401mn (+278.3% YoY) with an operating profit margin of 6.9% (2.1% in Q4 FY03/20). The SHOPLIST Business is usually the least profitable in Q4 due to seasonality, but operating profit did not drop as strongly compared to Q1–Q3 operating profit. Excluding fiscal years with special factors such as losses, as in the past fiscal year or two, Q4 operating profit in the past was between JPY4mn and JPY63mn, and operating profit margin was around 0.1–0.8% (operating profit margin for the full year was 2.5–4.0%). Taking this into consideration, it’s safe to say our Q4 FY03/21 performance was strong. I will explain in more detail later, but this performance was underpinned by a **stronger SHOPLIST Business resulting from business and organizational reforms centered around the Critical Project Program**, which helped offset some of the negative seasonal impact.

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 2H compared to 1H, with sales growing 5.3% in Q1, 4.5% in Q2, 17.6% in Q3, and 15.5% in Q4. The main reason behind this is that the number of visitors grew 23% YoY in Q3 and 20% YoY in Q4, 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 grew and we posted an operating loss of JPY544mn in Q4 FY03/19. To address this, 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 amounting to JPY585mn in Q1, JPY448mn in Q2, JPY506mn in Q3, and JPY401mn in Q4, for a record high total of JPY1,942mn (+440.9% YoY) for the full year.

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 fell from 15.3% in Q4 FY03/20 to 14.4% in Q4 FY03/21. Over the medium to long term, we aim to achieve a logistics cost-to-sales ratio of around 13.7%.

Our promotional cost-to-sales ratio declined substantially from 11.6% in Q4 FY03/20 to 6.4% in Q4 FY03/21 due to one-time factors. While we continue to invest efficiently in advertising, the ratio fell as we have not been able to invest as aggressively as we had initially anticipated. As for why we couldn't invest as anticipated, we frankly had other priorities to deal with and couldn't make the investments in time. Specifically, since we cannot maximize investment advertising effectiveness until we complete UI/UX improvements and merchandising-related measures to strengthen product lineups, such as expanding product brands and categories, we prioritized these measures. However, even under these circumstances, we believe the good news is that our investment efficiency in advertising is improving and our ability to boost sales is growing, as sales rose 15.5% YoY in Q4. Also, I mentioned not being able to make the investments in time, but had we been able to make them in time, of course sales would have expanded, and I believe operating profit would have absorbed the investment costs and grown even further.

Having improved our cost structure, it is essential that we expand sales further moving forward. To achieve our medium- to long-term target of JPY100bn in annual SHOPLIST transaction value, 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 93 shops by the end of Q4. We missed our targets, but this was due to a slight change in our policy from 2H wherein we switched to only opening stores with especially high user recognition and reassigned sales staff for new openings to merchandising in order to focus on merchandising-related measures. In addition, moving forward, 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 Q4 sales of JPY345mn (+11.3% YoY) and operating profit of JPY19mn (versus an operating loss of JPY4mn in Q4 FY03/20). However, on a full-year basis, sales fell substantially to JPY2,229mn (-43.2% YoY). 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 expanding advertising sales through our own media as well as through other companies' media, while focusing on the promotion of SHOPLIST and other measures to improve operations.

<u>The Media Business segment saw very strong growth, with full-year sales of JPY1,249mn (+59.7% YoY) and full-year operating profit of JPY379mn (versus an operating loss of JPY169mn in FY03/20). Looking at Q4 FY03/21, sales were JPY338mn (+14.6% YoY) and operating profit was JPY131mn (+718.8% YoY)</u>, a substantial boost compared to Q4 FY03/20. In addition to Rank King, which we have previously mentioned, other new media also performed well, leading to strong results for the Media Business as a whole. We anticipate substantial growth in this business going forward. As the Media Business is new and in its early stages, I will not go into details at this time, but will talk about it in more detail when the business grows. I believe we can expect profit growth more so than top-line growth in the Media Business.

In addition, in the Investment Businesses segment, full-year sales were JPY394mn (+6.2% YoY) while full-year operating loss was JPY196mn (versus an operating profit of JPY48mn in FY03/20). Q4 sales were JPY17mn (-93.7% YoY) and operating loss was JPY283mn (versus operating profit of JPY171mn in Q4 FY03/20), with the operating loss mainly reflecting the recording of impairment losses on some investments in Q4 FY03/21. The business model of the Investment Business is to invest in start-up companies and earn capital gains from the sale of these companies several years later through M&A deals or IPO, and it usually takes five to seven years for the investment results to be realized. Considering the probability of success of a business or startup, not all investees will do well, and for such investees, we may record impairment losses. However, if we look at the overall investment portfolio, only a small portion of the investments will lead to significant success, but the returns from these investments will greatly exceed the overall investment amount.

Due to the nature of this business, we may incur upfront costs, including impairment charges and management costs, but the Investment Business is still in the early stages, just two years and ten months since inception, and there are no particular issues with its progress. Several of the investees are preparing to list on the stock market, and we hope that this will generate substantial profit within a few years.

In the Internet Content Business segment, full-year sales reached JPY2,248mn (+4.9% YoY) and full-year operating profit came to JPY149mn (-18.1% YoY). Q3 operating profit was JPY4mn (-91.3% YoY) and Q4 operating loss was JPY21mn (versus operating profit of JPY36mn in Q4

FY03/20), showing a sharp decrease in profit in 2H. However, this was due to an increase in development costs for new games, and exclusive of these development costs, operating profit came in at JPY91mn in Q3 and JPY89mn in Q4. This indicates that the profit structure of the business has not deteriorated, and there are no notable issues with the progress of the business.

As I explained above, consolidated results for Q4 FY03/21 were strong for the SHOPLIST Business segment following the healthy performance in Q1, Q2, and Q3, but **operating losses in the Investment Businesses and Internet Content Business segments dragged down consolidated operating profit. Nevertheless, as mentioned earlier, these were attributable to one-time factors and there are no notable issues with either business. Excluding the operating losses from the two segments (impairment losses in the Investment Business and higher new game development costs in the Internet Content Business), Q4 consolidated operating profit would have exceeded JPY500mn, which means that the overall consolidated profit structure has improved.**

In addition, the SHOPLIST Business established a management structure that allows us to generate stable 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.

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 about 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 came to JPY791mn in Q3 (versus JPY873mn in Q3 FY03/20) and JPY373mn in Q4 (versus JPY584mn in Q4 FY03/20), or a decrease of about JPY300mn YoY in 2H, while our number of visitors grew 23% YoY in Q3 and 20% YoY in Q4, suggesting that the solutions proposed as part of our critical projects launched in July 2020 are starting to bear fruit. And as of March 31, 2021, we have a total of 33 critical projects with breakthrough potential, up six projects in Q4 from our Q3 total of 27 projects. Over the next year or so, we will invest 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 YoY increase of over 20% in visitors from Q3 FY03/21 onward that I mentioned earlier is the result of one critical project. I haven't talked about this before, but aside from that, we carried out a project to maximize sales of children's apparel, which contributed to a 37% YoY increase in sales of children's apparel in Q4. We also executed a project to minimize the number of days it takes to open a new brand store and increase first-day sales tenfold, which yielded first-day sales that almost doubled the highest first-day sales recorded prior to launching the project (yielded 2.5x the previous sales record for first-month sales). Another one we carried out was a project to maximize sales of Korean apparel brands, wherein we nearly doubled monthly sales in April compared to January prior to project launch. As you can see, the critical projects are starting to produce substantial results.** In addition, we continue to see results from our critical projects focused on cost reductions, such as the project to reduce the labor cost-to-sales ratio by 0.5% and the project to reduce the delivery cost-to-sales ratio by 1.1%. **Furthermore, with regard to strengthening sales of outlet products under the Sustainability Project that I announced in Q3, we will be carrying out full-fledged promotions from mid-June to early July.** I have nothing but high hopes for the future of SHOPLIST, as I believe that we will continue to see great results from our critical projects. If we can reinvest exactly as we envisioned, including for promotions on social networking sites, which we have underinvested in, I am confident that we can achieve our target sales CAGR of 30–40%.

SHOPLIST's average operating profit margin for FY03/21 was 7.2%. Even if fixed costs rise slightly in FY03/22 from an increase in headcount and other factors, if we can maintain the same level of sales growth from FY03/21, SHOPLIST will be able to generate an operating profit margin of over 8%. In reality, fixed costs may increase as we 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 to boost SHOPLIST sales. **My intention is to boost both sales and operating profit, and to achieve a sales CAGR of 30% and an operating profit margin of at least 8% for SHOPLIST on a stand-alone basis over the next year or so.[1]**

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.

All listed companies that use Japanese accounting standards will be required to adopt the Accounting Standard for Revenue Recognition from fiscal years beginning on or after April 1, 2021. As a result, SHOPLIST and some other businesses will be required to disclose sales net of purchase costs from April 2021 onward (i.e., from Q1 FY03/22 results announcement). Therefore, sales in FY03/22 will appear lower, but this is only a change in reporting and will not have any impact on profit. In the past, I did not specifically mention transaction value because we referred to it as sales, but starting in FY03/22, we will start referring to sales, sales growth rate, and operating profit margin as transaction value, transaction value growth rate, and operating profit-to-transaction value ratio in our disclosures. It is safe to assume that transaction values disclosed from FY03/22 onward is equivalent to what we disclosed as sales until FY03/21.

May 13, 2021

Koji Obuchi

Currently, SHOPLIST's marginal profit ratio (the ratio of profit to sales calculated by subtracting variable costs from sales, or in other words, the ratio of incremental profit to sales) is about 20%, taking into account the main variable costs such as purchasing costs (about 60%), logistics costs (14%), and payment processing fees. Roughly speaking, FY03/21 sales were JPY27.1bn, marginal profit was 20% of that, or about JPY5.4bn, and operating profit was JPY1.9bn, with the difference being our fixed costs at about JPY3.5bn. If increased by 30%, sales would be about JPY35.2bn, and marginal profit would come out to roughly JPY7bn, so if fixed costs remained the same, operating profit would be about JPY3.5bn, bringing the operating profit margin to around 10%. 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.