

Kita no Tatsujin Corporation KK

2930

Tokyo Stock Exchange First Section/Sapporo Securities Exchange

21-Jun.-2019

FISCO Ltd. Analyst

Ikuo Shibata



FISCO Ltd.

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

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Summary

Sales and profits increased significantly in the previous fiscal year, as the active investment in advertising was successful In FY2/20 also, sales are expected to surpass ¥10bn as growth will be maintained

Kita no Tatsujin Corporation KK <2930> (hereafter, also “the Company”) conducts an e-commerce (EC) business for online sales of health foods and cosmetics to general consumers. On the J North Farm website, which is its original brand, it focuses on the development and sales of products that specialize in supporting bodily problems, such as constipation, atopy, and acne. In particular, KAITEKI OLIGO, which uses oligosaccharide as a raw material, has been driving the Company’s growth. Recently, new products are growing significantly, including HYALO DEEP PATCH and EYE KIRARA, which have become new pillars of earnings, and along with the business expansion, the sales mix has improved. Due in particular to the strengthening of the customer acquisition system and the growth in new products, the percentage of sales from skin care products (cosmetics) is increasing compared to in the past, when sales were centered on health foods, and expanded the breadth of membership, including to middle-aged and elderly men.

In the FY2/19 results, sales and profits grew significantly, with net sales increasing 57.1% year-on-year (YoY) to ¥8,312mn and operating profit rising 32.6% to ¥1,861mn, and both net sales and operating profit were new record highs. But compared to the initial forecasts, while net sales greatly exceeded the forecast, profits were below forecast. In net sales, HYALO DEEP PATCH, which is called an “injecting cosmetic” because it directly injects hyaluronic acid and other beauty ingredients that have been solidified into a needle shape into the skin, was an explosive hit, and this contributed greatly to sales. According to the Company, in total around 10 million of this product has been sold since it was launched, and currently it seems that it is so popular that production cannot keep up with demand. Other than this, sales of the products launched in the last one and two years have been growing significantly. The Company succeeded in acquiring new customers (and accumulating regular-purchase members) through actively conducting advertising, mainly for the top-ranking products, and strengthening the customer acquisition system, which is driving the results growth. At the end of February 2019, the number of members had increased to nearly 250,000 (compared to around 170,000 members at the end of the previous fiscal year). Conversely, in profits, sales, general and administrative (SG&A) expenses rose greatly due to the active investment in advertising, but this was absorbed by the higher sales, so profits grew. While profits were below forecast, the reasons for this included that the Company strategically invested in advertising more than was initially planned in order to avoid opportunity losses and to increase the acquisition of new customers.

For the FY2/20 results, the Company is forecasting that sales and profits will increase significantly, with net sales rising 31.6% to ¥10,939mn and operating profit growing 45.2% to ¥2,702mn, so the outlook is for net sales to exceed ¥10bn. The same as in the previous fiscal year, it is anticipated that the results growth will be driven by the acquisition of new customers (and the accumulation of regular-purchase members) from the active investment in advertising, focused on the top-ranking products. In addition, the Company intends to improve the efficiency and accuracy of its advertising investment by strengthening the customer acquisition system, including the operations of its in-house advertising system and other aspects, and at the same time by working to improve the performances of products that have not performed well up to the present time. It is planning to release around 5 new products. For profits, it is expected that the active investment in advertising will continue, that personnel expenses will increase, and that there will be expenses related to the relocation of the Head Office and the opening of the Tokyo Branch Office. But even so, the outlook is for profits to increase due to the higher sales and for the operating margin to improve to 24.7% (22.4% in the previous fiscal year).

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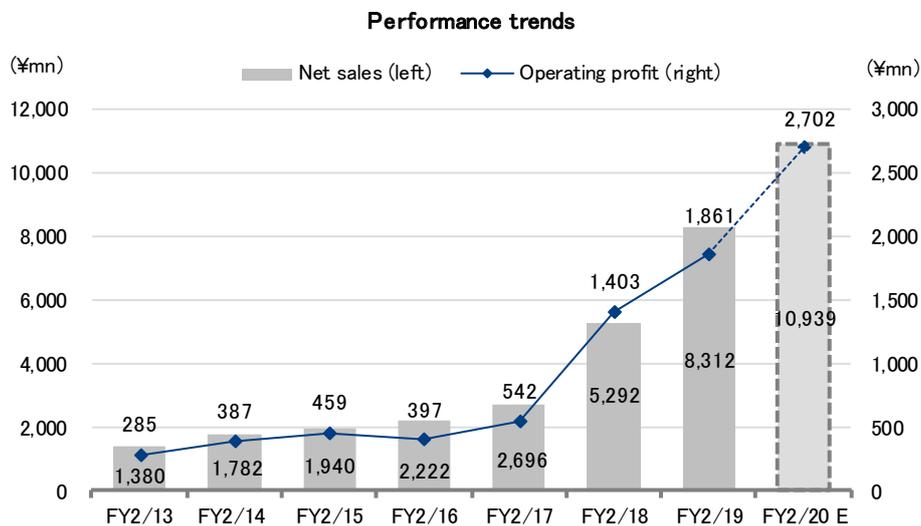
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Summary

The Company's growth strategy is the same as up to the present time; namely, to realize stable growth by aiming to have the top products in niche markets through utilizing its overwhelming product appeal in product fields in which it is easy for customers to feel their effects for their health, beauty, and other concerns, and therefore for which it is easy to obtain repeat sales. The Company is accelerating the growth through actively investing in advertising, and in the near future it has in sight achieving its targets of net sales of ¥10bn. Going forward, as the next growth stage it has set targets of net sales of ¥30bn, and it seems that is aiming to achieve them by 5 years' time. At FISCO, we consider that, in addition to the sustainable growth, the key to achieving further growth will be developing a large number of products that are top in their niche market with a sales scale of ¥300mn to ¥1bn. Going forward, we will be focusing on the following 5 points; 1) the state of the development of new products and their contributions to earnings, 2) the strengthening of the customer acquisition system and its effects, 3) the progress made in reducing costs, including in overseas production, 4) the fully fledged business development in Asia, and 5) the investment strategy that utilizes its solid financial base (particularly M&A).

Key Points

- In FY2/19, sales and profits were driven by the performance of HYALO DEEP PATCH and increased significantly, including due to the active investment in advertising and the strengthening of the customer acquisition system.
- The percentage of total sales provided by skin care products (cosmetics) is increasing compared to healthcare products, which have been the main products, due to the growth of new products. The range of member attributes is also expanding, including to middle-aged and elderly men.
- Sales and profits are set to increase in FY2/20 and the outlook is for net sales to exceed the present target of ¥10bn.
- Has entered a new stage toward achieving the next target (of net sales of ¥30bn within 5 years)



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

■ Company profile

Conducts an e-commerce business through Kitano-Kaitekikobo, its original brand

1. Business description

The Company conducts online sales of health foods and cosmetics to general consumers. On the Kitano-Kaitekikobo website, which is its original brand, it focuses on the development and sales of products that specialize in supporting bodily problems, such as constipation, atopy, and acne. In particular, KAITEKI OLIGO, which uses oligosaccharide as a raw material, has been driving the Company's growth. At the end of February 2019, it is estimated that it had more than 250,000 members. Based on the major increase in members from the previous fiscal year (FY2/18) alongside the dramatic growth in results, it appears that the upward trend in member numbers is continuing. In addition to KAITEKI OLIGO, which has been its main product since its establishment, sales of the Company's new products are growing significantly, including HYALO DEEP PATCH and EYE KIRARA, which have become new earnings pillars.

KAITEKI OLIGO is a highly pure, high quality food with functional claims (the details are given below, it is effective for constipation) created by compounding several types of oligosaccharide, including sugar beet produced in Hokkaido, as the main ingredients. In addition, the Company handles nearly 30 other products (as of the end of February 2019), including HYALO DEEP PATCH, which concentrates and replenishes moisture by using micro-sized needles of hyaluronic acid to reach the deep parts of fine wrinkles around the eyes; EYE KIRARA, which is a cream to improve bags under the eyes; and CLEAR NAIL SHOT α , which is a penetrating, specialized nail care product that contributes to beautiful and healthy nails.

Company profile

Product overview (in order of launch)

Item	Description
KAITEKI OLIGO	Japan's first "food with functional claims" with 5 ingredients to improve bowel movements is a high-purity, high-quality oligosaccharide food effective for improving constipation
KOJUKAN	The Company's first food with functional claims, with low-molecular weight lychee polyphenol as the main ingredient, to which is added ingredients including hyaluronic acid, vitamin C and L-citrulline
MINNANO HADAJUNTO ~ ATO CARE TYPE ~	A moisturizing-care product that is 100% derived from plants, with the main ingredient being sugars made from sugar beet produced in Hokkaido
KAITEKI DOKA SLIM CHA	A health food formulated using a unique blend of natural herbs developed by thoroughly studying the peristaltic motion of the intestines
20NEN HOIPPU	A facial cleanser to improve facial skin dullness that uses a proprietary manufacturing method called direct flame pot kneading and that adds whey to the ingredients as the moisturizing compound
MINNANO HADAJUNTO ~ CLEAR TYPE ~	An acne-prevention skin care product coated with plant oils, including lavender and peppermint, and which uses sugars made from sugar beet produced in Hokkaido as the main ingredient
EZOSHIKI SU-SU-CHA	A health food independently developed by the Company which blends three types of tea leaves in a perfect balance—bamboo grass that has been used as a herbal remedy in Hokkaido since the olden days, red perilla, and tencha (tea leaves) of the rose family. The product suppresses allergy symptoms, including sneezing, runny nose, and nasal congestion
KITANO DAICHINO YUMESHIZUKU	A new concept of a resting support drink, whose main ingredients are extracts that include rest-inducing compounds extracted using proprietary technologies from asparagus produced in Hokkaido
ZUKI SHIRAZUNO MI	A health food formulated from feverfew, giant knotweed, and bittern (magnesium chloride)
MINNANO HADAJUN LOTION	A lotion formulated from humidity-retention components, such as lipidurea, squalene, and ceramide, and whose main ingredient is sugars made from sugar beet produced in Hokkaido
MINNANO HADAJUNBURO	A moisture-sealing, moisture-care bath additive formulated from sugars made from sugar beet produced in Hokkaido, and also other ingredients including extracts from natural deposits at hot springs and sea buckthorn.
EYE KIRARA	A cream that improves bags under the eyes. It is formulated from ingredients including MGA, which is one type of vitamin C-derivative that supports collagen, and plant oils rich in natural vitamin K that help to make the blood flow smoothly
CLEAR FOOT VEIL	A barrier-type foot care product for use specifically by people with constantly itchy feet
NO ! NO ! SMELL !	A medicated deodorant foot cream that addresses existing issues with foot odor while also treating skin conditions to make it difficult for odor to reappear.
KUROUMEBIYORI	A health food that leads to a life without concerns through normalizing the body and protecting it from the inside
CLEAR NAIL SHOT α	A penetrating, specialized nail care product that deeply penetrates the nail to the source of problems, which leads to beautiful and healthy nails
CARE NANO PACK	A sleeping pack that leads to tightened pores that do not stand out
HYALO DEEP PATCH	A premium, night-care product, in which micro-sized needles of hyaluronic acid reach the deep parts of the fine wrinkles around the eyes, concentrating and replenishing moisture
MAYME WHITE 60	A fast-acting skin whitening cream that leads to ideal whitening in 60 seconds with rapid-action whitening and a deep-layer approach
LUMINAPEEL	A hand peeling gel developed to solve problems with aging hands that are susceptible to UV-related damage
WRINKLY FLAT	A fast-acting, anti-wrinkle beauty gel that stretches wrinkles and leads to younger looking skin in just one minute after it is applied
LID KIRARA	A beauty gel exclusively for the upper eyelids that returns skin to its original condition by thoroughly tightening the upper-eyelid skin. It has a fast-acting effect with the skin tightening immediately after application, and a continuity effect, with the foundation being raised by its continuous use
BUILD MAKE 24	A hybrid protein formulated from 1,750 mg of HMB per single serving that focuses on making body conditioning extremely efficient
RIMO SAVON	A laundry detergent that coats clothing fibers in the Company's proprietary coating compound with each wash, which makes it difficult for pet hairs to stick to clothes, and if they do stick, enables them to be easily removed. The Company's first product to be classified in miscellaneous goods
HANDPURENA	A care cream for aging hands, with a concentrated approach to hand skin that makes the skin feel soft when it is used
NECK ESTHE MIST	An aging-care mist for the neck, which uses a mist to bring tightness and firmness to signs of aging on the neck
Men's EYE KIRARA	Eye-shot cream for under the eyes made to suit men's skin texture
OKOSAMA ORIGO	A powdered oligosaccharide food blended with oligosaccharides made to suit the balance of bifidobacteria in children's intestines

Source: Prepared by FISCO from securities reports and press releases

The Company itself does not have production bases for its products and it mainly consigns production to its OEM partners. On the other hand, at the end of August 2015 it established a Taiwan branch office as a base for strengthening online sales in local markets in Asia.

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Company profile

2. History

The Company was established in May 2002 as Hokkaido dot See Oh dot Jay Pee KK by current President and Managing Director Katsuhisa Kinoshita (in March 2009, the Company name was changed to the current name of Kita no Tatsujin Corporation KK). However, the history of its establishment goes back to May 2000, when Mr. Kinoshita, who had worked at Recruit Holdings <6098>, aimed to expand the e-commerce market and launched the EC website “Hokkaidou.co.jp.,” which marked the start of online sales of specially produced Hokkaido foods.

The first turning point was in July 2007 when, with the aim of differentiating itself in a situation of an increasing number of competing EC websites, the Company established the Kaiteki Friend Club site (currently, Kitano-Kaitekikobo) as a site for comprehensive sales of health and beauty products. In addition, in September of the same year, it established Hokkaido Wakeari Ichiba as a website specializing in outlet (non-standard product) food sales. In particular, Hokkaido Wakeari Ichiba, which was rare among websites at that time, was featured on many mass media outlets, garnering a lot of attention. However, as this business was comparatively easy to imitate, the more that it attracted attention, the more that competition intensified.

The second turning point was when the Company decided to compete by using overwhelming superior product quality and functions that other companies could not easily imitate. It transferred management of the Hokkaidou.co.jp. and Hokkaido Wakeari Ichiba businesses, and at the same time, pivoted to the development and sales of health and beauty products through the Company’s own brand, Kitano-Kaitekikobo. During this period, KAITEKI OLIGO became a hit product, and it has been driving growth at the same time as the Company has worked to steadily expand the base of regular-purchase members. In May 2012, it was listed on the Sapporo Securities Exchange (SSE) Ambitious market, and then in March 2013, its listing was upgraded to the SSE’s main market. Moreover, in November 2014, it was additionally listed on the Tokyo Stock Exchange (TSE) Second Section, and then on November 24, 2015, its listing was upgraded to the TSE First Section. So it achieved an upgrade to a new listing market for four consecutive years.

In FY2/16, the Company began creating and maintaining a business foundation toward accelerating growth, including establishing the Taiwan branch office (the end of August 2015) and strengthening various measures, such as for its products-development structure.

Meanwhile, in terms of external evaluations of the Company, in September 2015 in EY Entrepreneurs of the Year Japan*1, which is a part of an international scheme to recognize entrepreneurship, Mr. Kinoshita was elected as the representative of the Hokkaido block. In February 2017, Mr. Kinoshita was awarded the Special E-Commerce Promotion Award at the Japan Venture Awards 2017*2 hosted by the Organization for Small & Medium Enterprises and Regional Innovation, JAPAN (sponsors: The Small and Medium Enterprises Agency, METI, etc.)

*1 An international awards system that honors the efforts and achievements of entrepreneurs who take on challenges in new business areas. In Japan, it started in 2001 as EY Entrepreneurs of the Year Japan, and each year it honors entrepreneurs selected from all over the country.

*2 A system that honors managers in high-minded venture companies that conduct businesses that are innovative, that have high growth potential, and that contribute to the revitalization of regions.

More recently, aspects such as the Company’s profitability and growth potential have been positively evaluated in the media on a number of occasions. For example, in the Asia version of Forbes, the U.S. economic magazine (the July/August 2018 issue), it was selected among “Asia’s 200 Best Under a Billion,” which are its selection of 200 excellent companies with sales of less than U.S.\$1 billion in the Asian Pacific region (second selection since the August 2014 issue). In addition, In the national edition of the Nippon Keizai Shimbun newspaper dated January 8, 2019, the Company ranked third in the “companies that have increased value in 2018,” and in such ways, it is being highly evaluated for various aspects.

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Company profile

On August 7, 2018, it was selected as a constituent stock of the JPX-Nikkei Mid and Small Cap Index* (applied on August 31, 2018).

* A stock index jointly calculated by Tokyo Stock Exchange Inc. and Nikkei Inc. JPX Nikkei Index 400 introduces the concept of selecting companies that have high investment appeal to investors as its constituent stocks. The JPX-Nikkei Mid and Small Cap Index applies the same concept to select mid and small cap stocks of companies that efficiently utilize capital and conduct management with investors in mind. In addition, the index aims to spread and promote the awareness of investment appeal to a wide range of companies (from the TSE website).

Company features

Strengths include regularly purchased products with high customer satisfaction and effective marketing

1. Overwhelmingly strong product appeal

The reason for the Company's growth so far is because it has used the overwhelming appeal of its products to expand its base of highly loyal customers. It has launched a series of hit products by specializing in providing consumers with support for the body-related problems that they find most concerning, and at the same time, by maximizing customer satisfaction through a product-development concept that prioritizes quality above all and that provides thorough follow-up services. Although they do not stand out in comparison to the major growth of the results of the top-ranking products, including KAITEKI OLIGO, each of the products are supported by long-term demand and positioned as the top product in their respective niche market. These products have also won numerous awards*, mainly in the food field, such as by Monde Selection, an international rating organization that reviews the quality of products. These awards which can be said to indicate the strength of the Company's product capabilities.

* In Monde Selection 2019, all of the Company's products that were evaluated won awards. In particular, KAITEKI OLIGO won the Grand Gold Award for the eighth consecutive year, Minna no Hadajuntou ~ After care type~ won it for the seventh consecutive year, and Minna no Hadajuntou ~ Clear type~ for the fifth consecutive year. Also, 20NEN HOIPPU won the Gold Award for the seventh consecutive year, EYE KIRARA for the fourth consecutive year, HYALO DEEP PATCH for the third consecutive year, and CLEAR NAIL SHOT for the third consecutive year. In addition, HANDPURENA, Men's EYE KIRARA, and KAITEKI OLIGO for Children were each awarded the Gold Award for the first time.

The key to creating hit products that are supported by consumers is highly accurate test marketing. From among the many candidates, it selects those whose effects are easily experienced and that are likely to be purchased repeatedly. In addition, its consistent policy has been to only launch a product that is highly likely to sell well based on the results of a monitor survey of a prototype product.

2. Stability from regular purchases

The same as other EC businesses, the Company has a growth model in which the expansion of the membership base drives results. But in the case of the Company, in addition to the fact that the products are premised on their continuous use, its customer base is composed of highly loyal members who suffer from pressing problems. Therefore, a feature of its business is that the rate of regular purchases is high, which gives it management stability. In the future also, it intends to continue with a strategy of aiming for multiple products that are top of their niche market, not to pursue an explosive growth in results (a boom) that tends to be temporary, and rather to steadily capture long-term demand in each of these respective markets at the same time as aiming to achieve stable results growth by diversifying risk.

Company features

3. Effective marketing methods

Another feature of the Company is a marketing method using detailed data analysis. After conducting multiple types of sales tests at each stage, such as for markets, products, advertisements, and webpages, and comparing and analyzing the results, it finds the definite “winning pattern” and only then starts fully fledged sales. Particularly with regards to advertising investment, an important policy for an EC business is that it directly links it to sales, but the Company judges this only after measuring the advertisement-investment effects for each media up to the level of customers’ lifetime value. Therefore, even if member numbers and net sales are expected to temporarily increase due to investments in advertising, that investment may be foregone depending on assumptions for retention rate after the fact. Amidst this background is the Company’s approach of thoroughly prioritizing profits, and it also reflects its high profit margin. Recently, it has been working on further improvements in efficiency and accuracy through its in-house advertising system starting operations, the introduction of B1*¹ tools and combinations with RPA*².

*1 A system that collects, analyzes, and processes the information accumulated in the various information systems in the Company, and converts it into useful information to assist in the investigation of business strategies and quick decision making.

*2 Abbreviation of Robotic Process Automation. It refers to the use of robots (cognitive technologies, such as artificial intelligence) to automate operations.

Financial highlights

Aiming to accelerate growth through actively investing in advertising expenses

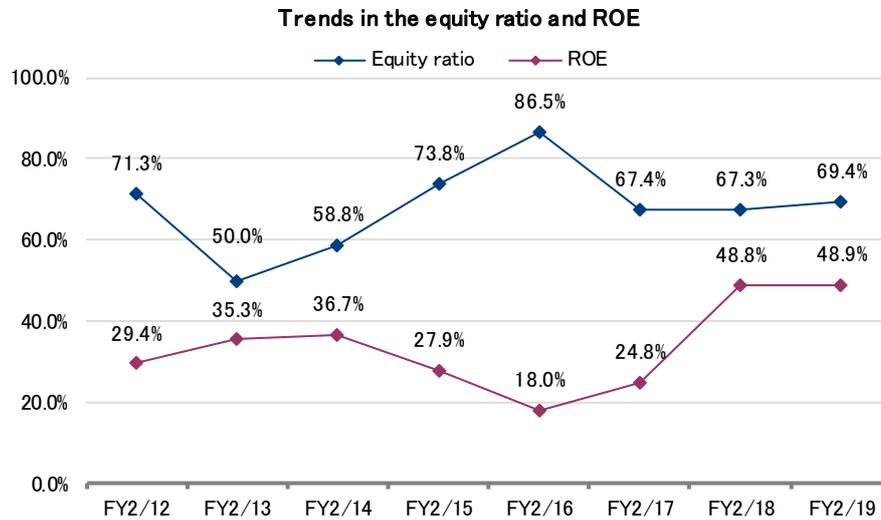
1. Trends in past results

Looking back on the Company’s past results, they have grown alongside the increase in the number of regular-purchase members, while the growth since FY2/13 has been particularly large. This was because up to that time the results’ dependence on KAITEKI OLIGO had been high, but from then on, starting with HYALO DEEP PATCH, the Minna no Hadajuntou series and 20NEN HOIPPU became established as new main products. Also, from FY2/17, the contributions of the new products, such as EYE KIRARA, were added to the results. Therefore, it can be said that in the last few years, the Company’s results have expanded significantly from the growth of the new earnings pillars while reducing the extent of its reliance on KAITEKI OLIGO.

In profits also, alongside the growth in sales from the effective investment in advertising expenses, the operating margin had risen to the high level of above 25%. However, in FY2/19, the operating margin declined slightly because the Company strategically invested in advertising more than it had initially planned in order to avoid opportunity losses and to increase the acquisition of new members. But even so, it was maintained at a level of 22.4%.

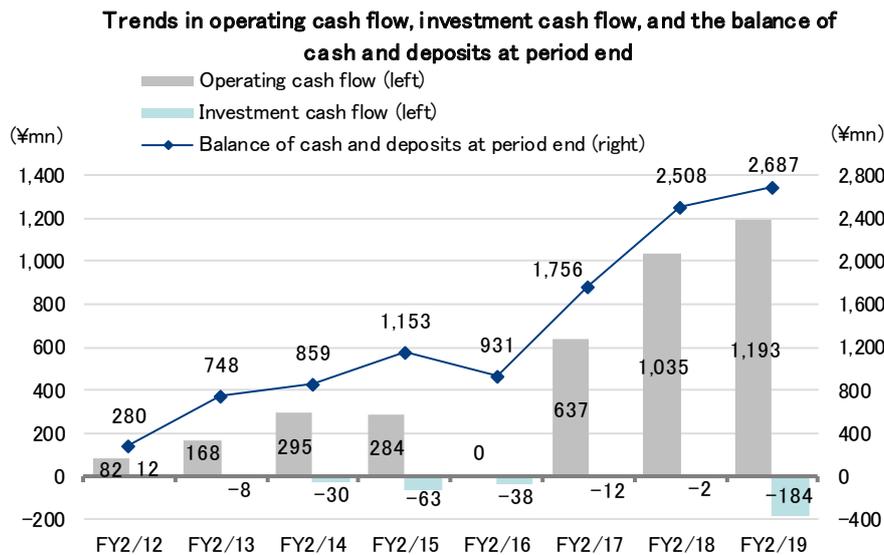
Meanwhile, the equity ratio, which is an indicator of financial stability, reached the high level of 86.5% in FY2/16 through a capital increase from a public offering and the accumulation of retained earnings. It fell once again in FY2/17 to 67.4% in order to secure liquidity from cash on hand through long-term borrowing, but there are no concerns about the stability of the Company’s financial base. In addition, ROE (return on equity), which is an indicator of capital efficiency, has trended around the 50% level recently, supported by the Company’s high profitability, and its financial condition can be evaluated as being extremely good.

Financial highlights



Source: Prepared by FISCO from Company materials

For the cash flow situation also, a feature of the Company’s business is that a large amount of capital investment is not required and investment cash flow falls within the range of its abundant operating cash flow, so the balance of cash and cash equivalents at the end of the fiscal period has accumulated significantly. In FY2/16, operating cash flow temporarily declined, but this was due to inventory investment alongside the growth in net sales, in addition to investment in advertising and publicity expenses and upfront investment with an eye to the future. Since FY2/17, it has one again trended significantly positively. Therefore, going forward it seems that an issue will be how the Company will use its solid financial base and abundant operating cash flow to realize further growth.



Source: Prepared by FISCO from Company materials

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Financial highlights

2. FY2/19 financial highlights

In the FY2/19 results, sales and profits increased significantly, with net sales rising 57.1% YoY to ¥8,312mn, operating profit growing 32.6% to ¥1,861mn, ordinary profit climbing 32.6% to ¥1,861mn, and net profit increasing 36.4% to ¥1,293mn. Moreover, net sales and operating profit were both new record highs. However, while net sales were above the initial forecast, profits were below forecast.

In net sales, the standard hit product KAITEKI OLIGO performed strongly, and in addition, sales of products launched in the last one or two years grew greatly. Among them, in FY2/19 sales of HYALO DEEP PATCH increased remarkably. According to the Company, it is growing to be a highly popular product, and in total it has sold around 10 million of it since it was launched and production cannot keep up with demand, with more than 30,000 people on the waiting list for it as of May. The remaining products are also being supported by the ongoing demand and are performed steadily, despite the constraints in terms of the fixed advertising budget and the number of sales personnel, and it can be said that the depth of the Company's earnings structure has increased. In particular, sales of skin care products are growing and the product structure is changing greatly to focus on them from the previous focus on healthcare products. Moreover, the range of member attributes is widening, including to middle-aged and elderly men.

The reasons why net sales exceeded their initial forecast is that the Company succeeded in acquiring new customers (and accumulating regular-purchase members) through actively investing in advertising, mainly for top-ranking products, and strengthening the customer acquisition system. At the end of February 2019, the number of members had increased to nearly 250,000 (compared to about 170,000 members at the end of the previous fiscal year). In particular, on entering Q4, the number of newly acquired customers per month and monthly product sales grew significantly, which has further accelerated the speed of growth*.

* In January 2019, the number of newly acquired customers exceeded 51,000 for a new record high. Monthly product sales also exceeded ¥800mn for 2 consecutive months in January and February 2019 and are growing greatly compared to the initial level (¥610mn in March 2018).

On the other hand, for profits, the costs ratio rose slightly due to the effects of some products, while SG&A expenses increased considerably due to the active investment in advertising. But these increases were absorbed by the higher sales, so profits rose. The main reason why profits were below the initial forecasts was that the Company strategically invested in advertising more than initially planned. In particular, based on the steady growth for the acquisition of new customers, it decided to increase upfront investment in advertising in Q4, which kept down profits*. Also, it seems that the other factors behind profits not achieving their forecasts were the increase in costs per newly acquired customer due to the expansion in the scope of the customer groups, and that there occurred a temporary decline in acquisition efficiency due to operating errors on the launch of an in-house system. However, operations of this in-house system were temporarily suspended and the problem was resolved, and its operations are being resumed in stages while further improvements are made.

* Normally, four months is expected as the period for the investment in advertising to be recovered through the acquisition of new customers and their subsequent contribution to profits. Therefore, the increase in advertising investment in Q4 will be a positive factor for profits in the next fiscal period.

For the Company's financial condition, total assets were up 21.8% on the end of the previous fiscal year to ¥4,240mn, mainly due to the increase in cash and deposits, accounts receivable and products. The equity ratio slightly rose to 69.4 % (compared to 67.3% at the end of the previous fiscal year), because shareholders' equity increased 25.5% YoY to ¥2,942mn due to the accumulation of retained earnings.

Financial highlights

FY2/19 financial highlights

	FY2/18		FY2/19		Change		(¥mn)		
	Results	% of total	Results	% of total	Amount	% change	FY2/19 Initial forecast	% of total	Achievement rate
Net sales	5,292	-	8,312	-	3,020	57.1%	7,589	-	109.5%
Cost of sales	1,058	20.0%	1,852	22.3%	794	75.0%	-	-	
SG&A expenses	2,823	53.3%	4,590	55.2%	1,767	62.6%	-	-	
Operating profit	1,403	26.5%	1,861	22.4%	457	32.6%	2,430	32.0%	76.6%
Ordinary profit	1,403	26.5%	1,861	22.4%	457	32.6%	2,430	32.0%	76.6%
Net profit	948	17.9%	1,293	15.6%	344	36.4%	1,643	21.6%	78.7%

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

■ Topics

Released 5 new products and also worked to strengthen the customer acquisition system

1. Track record in releasing new products

The Company released 5 products in FY2/19. Specifically, it released 1) RIMO SAVON (on April 11, 2018), which is a laundry detergent that coats the clothing fibers in the Company's proprietary coating compound with each wash, which makes it difficult for pet hairs to stick to clothes, and if they do stick, enables them to be easily removed; 2) HANDPURENA (on June 14, 2018), which is a care cream for aging hands, with a concentrated approach to hand skin that makes the skin feel soft when it is used; 3) NECK ESTHE MIST (on January 23, 2019), which is an aging-care mist for the neck which uses a mist to bring tightness and firmness to signs of aging on the neck; "Men's EYE KIRARA" (January 31, 2019), which is an eye-shot cream for under the eyes made to suit men's skin texture; and 5) KAITEKI OLIGO for Children (on February 26, 2019), which is a product in the KAITEKI OLIGO series specifically designed for children. It seems that all five products have made steady starts. 1) is the Company's first product to be classified in "miscellaneous goods." For the 20NEN HOIPPU and the skin HADAJUNTO series also, which had been mainstay products in the past, the Company is conducting renewal sales through releasing upgraded versions and aiming to re-strengthen them. In particular, because the cost ratio for HADAJUNTO is relatively high, it has had to keep down advertising investment in it in the last few years, so its sales have been declining. However, it has realized a significant cost reduction with the current version upgrade, which has made it possible to increase advertising investment.

Topics

2. Strengthening the customer acquisition system

Continuing on from the previous fiscal period, the Company increased the number of employees in the customer acquisition department (doubled to 40 employees) and worked to strengthen the customer acquisition system. In particular, the introduction of BI tools made it possible to get an overview and confirm the status of all placed advertisements. Moreover, it was able to prevent the occurrence of opportunities losses through newly appointing a product manager to supervise the promotion strategies by product. It can be said that these measures spurred on the increase in the number of newly acquired customers in Q4. Also, with regards to the in-house advertising system, as previously stated there was an increase in some advertising expenses that did not generate profits due to operational errors on the system's launch, and therefore its operations were temporarily suspended. But after further improving its functions, the Company is re-starting its operations in stages and building a system in which even employees with only a few years of experience can generate profits at an early stage. Furthermore, through combining it with RPA, it is constructing an efficient operating system in which all of the data of the in-house advertising system and the BI tools are automatically updated. Going forward, the Company will effectively acquire new customers through these measures, which had been limited to only some products until now, and it is expected that they will be expanded to all products.

3. Foods with functional claims

For the Company's measures to utilize the Foods with Functional Claims System that came into effect in April 2015, most recently in May 2019, the Consumer Affairs Agency accepted its application for KAITEKI OLIGO, which contains five ingredients for improving bowel movements, into the system as a "food with functional claims." The scientific basis for its functionality has been demonstrated in clinical trials, and from September 2019, it will have the functional claim that "This product contains raffinose, lactulose, fructo-oligosaccharides, isomalto-oligosaccharides, and alpha-cyclodextrin, so it has the function to improve the bowel movements of people prone to constipation (increase stool volume and frequency)." It will be the first "food with functional claims" in Japan that contains multiple oligosaccharides as the functional ingredients.

In addition, on November 16, 2018, its application was accepted for the tablet-type KITANO DAICHINO YUMESHIZUKU, which contains ingredients derived from the rafuma plant*.

* In total, it has 3 "foods with functional claims" products, including KOJUKAN (a supplement with low molecular weight lychee polyphenols), which was accepted in May 2017.

4. Establishment of the South Korea Liaison Office

In January 2019, the Company established the South Korea Liaison Office in the South Korean capital of Seoul. South Korea is a major country for beauty with world-class cosmetics technologies, and through this office it intends to investigate the possibility of collaborations, such as whether to outsource manufacturing to within South Korea.

5. Establishment of the Tokyo Branch Office

In April 2019, the Company established the Tokyo Branch Office (Nihonbashi, Chuo Ward). In response to its business expansion, through this establishment it is aiming to secure human resources with high-level skills and an abundance of knowledge and experience, mainly for the sales, product development, and administrative departments, and also to strengthen aspects such as the information collection and dissemination functions.

In addition, in March the Company relocated its Head Office to a prime location in Chuo Ward, Sapporo City.

■ Outlook

In FY2/20 also, the outlook is for net sales to exceed ¥10bn due to the major increases in sales and profits

The Company has left unchanged its initial forecasts for FY2/20, which are for major increases in sales and profits, with net sales to increase 31.6% YoY to ¥10.939mn, operating profit to rise 45.2% to ¥2,702mn, ordinary profit to grow 45.2% to ¥2,703mn, and net profit to climb 46.2% to ¥1,890mn. The Company expects continued higher increases in both sales and profit and net sales to exceed its near-time goal ¥10bn.

The same as in FY2/18, the growth is expected to be driven by active investment in acquiring new customers through advertising (as well as the accumulation of regular-purchase members), particularly for the top-ranking products. Also, the Company intends to increase the accuracy of advertising investment through further strengthening its customer acquisition system, including from the operations of the in-house advertising system and also by working to improve the performance of existing products that have not performed sufficiently well up to the present time. It also plans to release five new products.

For profits, it is expected that the active investment in advertising will continue, that personnel expenses will increase, and that there will be expenses related to the relocation of the Head Office and the opening of the Tokyo Branch Office. But the outlook is still for profits to increase due to the higher sales and for the operating margin to improve to 24.7% (22.4% in the previous fiscal year).

At FISCO, we judge that it fully possible that the Company will achieve its net sales forecast. This is because the customers newly acquired in the previous fiscal period will contribute to improving results as regular-purchase members, that the number of newly acquired customers will trend upward from the effects of the active investment in advertising in the previous Q4, and also as the budget for the active investment in advertising in this fiscal period has been incorporated into the forecasts. On the other hand, the same as in the previous fiscal year, it cannot be denied that profits will be affected by policy decisions, such as whether to prioritize profits at the current time or to prioritize advertising investment towards further growth in the future (realizing net sales of ¥30bn, which is the next target). But at the very least, assuming that the Company will invest in advertising toward realizing growth on a line extending from the current growth, then we think that the profit forecasts are at reasonable levels. Also, the points to focus on will include the effects of the strengthening of the customer acquisition system, including the operations of the in-house advertising system (in particular, improving the performances of existing products), and also the specific developments for overseas business deployment toward reducing cost prices (securing production outsourcing).

FY2/20 forecasts

	FY2/19		FY2/20		Change	
	Results	% of total	Forecast	% of total	Amount	% change
Net sales	8,312	-	10,939	-	2,626	31.6%
Operating profit	1,861	22.4%	2,702	24.7%	840	45.2%
Ordinary profit	1,861	22.4%	2,703	24.7%	841	45.2%
Net profit	1,293	15.6%	1,890	17.3%	596	46.2%

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

■ Growth strategy

Entered a new growth stage targeting net sales of ¥30bn

The Company does not publish specific medium-term management targets, but based on its policy of prioritizing profits above sales, basically it is pursuing a strategy of constantly releasing products every period following sufficient test marketing with the aim of them becoming the top in their niche market, and at the same time, steadily capturing demand through effectively investing in advertising and publicity expenses. The Company is succeeding in linking phased marketing to the acquisition of profits in the future through actively investing in advertising to acquire new members (and to accumulate regular-purchase members), which is accelerating the pace of growth. In the near future it has in sight achieving the targets of net sales of ¥10bn. Going forward, as the next growth stage it has set targets of net sales of ¥30bn, and it seems that is aiming to achieve them by 5 years' time.

At FISCO, we think that it is fully possible that the Company can achieve net sales of ¥30bn within 5 years, as this will be on a line extending from its current growth (based on an annual sale-increase rate of 30%). For profits also, judging from the height of the Company's inherent profitability, realizing operating profit of ¥10bn (an operating margin of 33%) is not considered to be that high of a hurdle to clear. In addition to the continuing growth of the mainstay products, the key to achieving these targets is likely to be realizing sustainable growth from constantly releasing around 5 new products a year, and from among them, growing many of them to be products that are top of their respective niches with sales of around ¥300mn to ¥1bn.

Going forward, we will be focusing on the following 5 points; 1) the state of developing new products and their contributions to results, 2) the strengthening of the customer acquisition system and its effects, 3) the progress made in reducing costs, including in overseas production, 4) the fully fledged business development in Asia, and 5) the M&A strategy. Particularly for 1) and 2), in addition to being the twin drivers of growth in the future, it is highly possible that they will further evolve. Conversely, 4) to 5) can be positioned as factors that will add to results. Especially with regards to 4), since the Company is prioritizing responding to the strong domestic demand, we cannot see any major progress for it at the present time. But if going forward, the Taiwan branch gets on track through the strengthening of its organizational aspects (such as personnel and advertising budget), and if the plan is also to enter the Chinese mainland and Southeast Asia, then it has enormous potential for the future. With regards to 5), it would target a company with a customer base through the EC online sales companies it is close to, but it currently seems to be at the stage of conducting a careful investigation, including for the management structure after M&A. Therefore, depending on the extent of the progress made in 4) to 5), it would seem possible that in 5 years' time, results will actually exceed the targets of net sales of ¥30bn and operating profit of ¥10bn (or they will be achieved ahead of schedule).

Shareholder returns

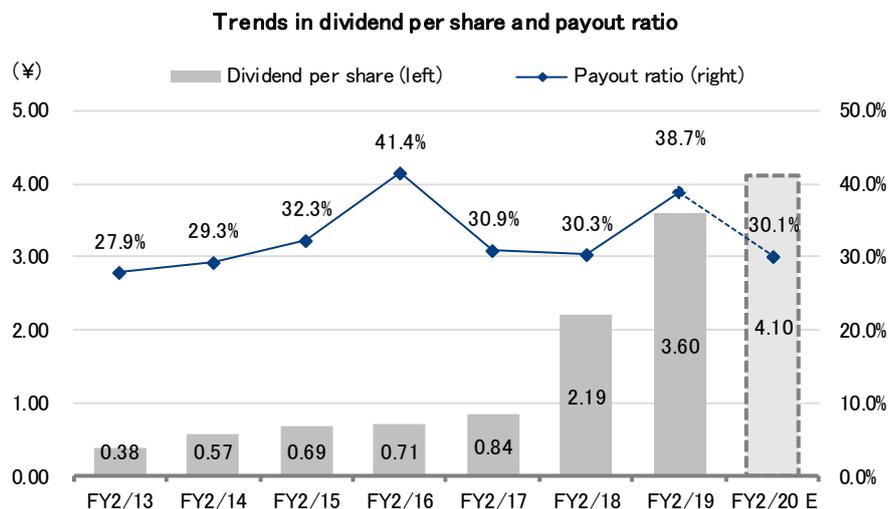
Targets a dividend payout ratio of 30%, and the dividend is expected to continue to increase alongside the profit growth

The Company's basic policy is to return profits to shareholders in accordance with its results, while also aiming to supplement retained earnings to strengthen its financial base. In FY2/19, after adjusting for the share splits*, it greatly increased the annual dividend per share to ¥3.60 (up ¥1.41 after adjusting for the share splits) from an interim dividend of ¥1.60 (¥2.00 after adjusting for the share splits), and a period-end dividend of ¥2.00 (dividend payout ratio, 38.7%).

* In order to improve the liquidity of its shares; a two-for-one share split on April 1, 2017, a two-for-one share split on November 6, 2017, and a three-for-one share split on February 15, 2018. For the dividend amounts after adjusting for the share splits, fractions of less than one yen have been rounded up.

For FY2/20, the Company plans to increase the dividend per share by ¥0.50 to ¥4.10 (interim dividend ¥2.00, period-end dividend ¥2.10, dividend payout ratio 30.1%). It aims to stably pay dividends targeting a dividend payout ratio of 30% as the standard, but there remains plenty of room to increase the dividend in the future alongside the growth in profits.

In addition, based on a resolution in the Board of Directors meeting held on August 6, 2018, the Company has acquired treasury stock. From August 13, 2018, to September 3, 2018, it acquired a total of 700,000 shares (acquisition price, ¥384,432,000).



Note: the dividend per share is after being adjusted for the following four share splits (fractions of less than 1 yen have been rounded-up)

February 9, 2013(1:4); January 3, 2014(1:2); June 1, 2015(1:2);

April 1, 2017(1:2); November 6, 2017(1:2); and February 15, 2018(1:3)

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

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Shareholder returns

In addition, the Company has changed its shareholder benefits program. Previously, shareholders holding 1 or more unit of shares (100 shares) all received KAITEKI OLIGO (150g, about a one-month supply). But from the current fiscal period, shareholders will once a year receive a gift of a Company product with a label price of at least ¥3,564 (including tax) depending on the number of shares they hold (the gift is reviewed each period and may be changed in the future).



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