Arealink Co., Ltd.

Leader in self-storage with nationwide brand; seeks top position in land rights management: growth driven by self-storage business

TICKER: 8914 | TSE Mothers | **HP:** http://www.arealink.co.jp/eng/ | **PUBLISHED on** 2019.10.07

Business

Tokyo-based self-storage company with nationwide brand; also operates growing land rights management business

Arealink has established its position as the largest domestic self-storage company by concentrating on self-storage and rolling out a nationwide brand, Hello Storage. The company's self-storage management and brokerage businesses drive growth and account for over 80% of sales (FY12/18).

The company has two core segments, Property Management and Property Revitalization & Liquidation. Property Management comprises self-storage management (39.1% of FY12/18 sales), self-storage brokerage (41.2%), and other property management (6.9%).

In the self-storage management business, the company sells indoor and outdoor self-storage units as well as storage with land to investors, and then enters sublease agreements with these investors to manage the units. The self-storage brokerage business involves selling indoor storage facilities to investors, and the company books revenue at the time these facilities are sold to investors. Arealink changed its exit strategy for storage with land operations, which are rapidly growing, from selling to holding and custom building for sale, with a focus on self-storage management.

In the second core segment, Property Revitalization & Liquidation (12.8% of sales), Arealink aims to focus on the land rights management business (purchase and sale of land rights). It sees this as a solid business where it can sell land rights of properties that are still under the old Land Lease Law (explained later).

Performance trends

FY12/19: Profit decline in core business offset by one-time gains

1H FY12/19 results: Sales of JPY20.1bn (+44.5% YoY), operating profit of JPY2.6bn (+76.3% YoY), recurring profit of JPY2.5bn (+83.9% YoY), and net income of JPY1.7bn (+85.1% YoY).

FY12/19 full-year company forecasts: Sales of JPY29.0bn (+0.6% YoY), operating profit of JPY2.8bn (+0.6% YoY; includes a JPY1.1bn one-time gain comprising a JPY600mn gain on the sale of real estate and a JPY500mn gain on the sale of storage with land to a fund), recurring profit of JPY2.7bn (+6.4% YoY), and net income of JPY1.5bn (-17.1% YoY).

Medium-term strategy

Strengthening earnings structure: Structural shift from one-time revenue to recurring revenue business

Arealink expects earnings to weaken, albeit temporarily, in FY12/19 and FY12/20 due to the strategy shift. It aims to lower its earnings dependence on the self-storage brokerage business and instead focus on the self-storage management business. However, it expects it will take one to two years to raise occupancy rates at the self-storage management business and secure related profit contributions.

From FY12/21 onward, the company expects 20% or higher growth in operating profit in the self-storage management and brokerage businesses and the land rights management business. It also aims to add profit from niche property businesses.

Strengths and weaknesses

Strengths

Rapid growth from nationwide branding as the leader of the niche market of self-storage: Established a position as the largest company in the domestic storage market by concentrating on the self-storage business and a strategy of rolling out a nationwide brand, Hello Storage.

Stable recurring revenue platform: Increasing unit numbers while maintaining relatively stable occupancy rates and average prices.

Management skills of founder and CEO and flexible chain of command: Established a workplace structure where managers including the CEO can help bring out results from lower-ranked employees.

Weaknesses

Property owners can cancel lease contracts: It is possible to unilaterally break a contract by paying a penalty fee.

Strengthened regulations and poor reputation of outdoor storage: Increasing criticism of containers not compliant with building standards.

Low barriers to entry making it likely that more players will enter the market: Simple business model make it easy for other companies to enter the self-storage market.

Profit growth drivers

To date: self-storage brokerage

Medium-term: self-storage management, land rights (including commercial land rights)

Indices	
Market capitalization	JPY15.2 bn
Stock price (Aug. 27, 2019)	JPY1,172
No. of shares issued (incl. treasury shares)	12,941
Foreign stockholding ratio (Dec. 31, 2018)	19.29 %
BPS (FY12/18)	JPY1,484.4
PBR (FY12/18)	0.79 x
PER (FY12/19 Est.)	9.9 x
Dividend (FY12/19 Est.)	JPY40.0
Dividend yield (FY12/19 Est.)	JPY3.4 %
ROE (FY12/19)	8.0 %
Net debt / Equity ratio (FY12/18)	25.8 %

Earnings results and forecasts		Sales (JPYmn)	YoY	Operating profit (JPYmn)	YoY	Recurring profit (JPYmn)	YoY	Net income (JPYmn)	YoY	EPS (JPY)	BPS (JPY)	ROA (RP-based)	ROE
FY12/10	Cons.	11,143	-8.5%	1,007	-10.2%	775	-6.3%	673	20.8%	54.80	750.6	3.4%	7.6%
FY12/11	Cons.	10,604	-4.8%	1,045	3.8%	954	23.1%	773	14.7%	62.90	813.5	4.3%	8.0%
FY12/12	Cons.	10,124	-4.5%	1,165	11.6%	1,075	12.8%	948	22.7%	77.20	890.8	5.3%	9.1%
FY12/13	Cons.	12,256	21.1%	1,505	29.2%	1,434	33.3%	1,347	42.0%	109.70	1000.5	6.5%	11.6%
FY12/14	Cons.	18,120	47.8%	2,235	48.5%	2,087	45.6%	1,541	14.4%	125.50	1100.9	7.2%	11.9%
FY12/15	Cons.	17,174	-5.2%	2,658	18.9%	2,442	17.0%	1,551	0.6%	126.30	1191.4	8.0%	11.0%
FY12/16	Cons.	16,908	-1.5%	1,936	-27.2%	1,969	-19.4%	1,142	-26.3%	93.06	1245.1	5.3%	7.6%
FY12/17	Cons.	21,489	27.1%	2,380	22.9%	2,441	24.0%	1,547	35.4%	126.08	1332.9	5.8%	9.8%
FY12/18	Cons.	28,828	34.2%	2,782	16.9%	2,537	3.9%	1,810	17.0%	145.47	1484.4	5.3%	10.3%
FY12/19 Est.	Cons.	29,000	0.6%	2,800	0.6%	2,700	6.4%	1,500	-17.1%	118.76	-	-	-

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

Business

Tokyo-based self-storage company with nationwide brand; also operates growing land rights management business

Company overview

Arealink has established a position as the largest company in the domestic storage market by concentrating on the self-storage business (indoor and outdoor storage) and a strategy of rolling out a nationwide brand, Hello Storage. It has two reporting segments: the Property Management segment and the Property Revitalization & Liquidation segment.

Property Management segment

This segment comprises three sub-segments: self-storage management, self-storage brokerage, and other property management services. The company's decision to narrow its focus to storage entails a structural shift from a business model based on one-time property sales to one based on long-term recurring revenue.

Self-storage management

Arealink negotiates with owners of idle land and buildings to lease these properties under a master lease agreement. Once it reaches an agreement with the owners, it installs storage containers on the land or storage units inside the buildings. The company sells to investors the storage units along with the lease contracts for the land and buildings. At the same time, the company enters into a long-term subleasing agreement with investors, under which it manages storage operations. Arealink recruits and collects rent from end-users. It then pays rent to investors after deducting management fees.

In the US, self-storage operators usually own the land themselves, but in Japan, operators generally lease the land. From FY12/16 to FY12/18, Arealink has aimed at achieving higher value-added and tapping into new markets (in particular, women and the elderly: less than 30% of customers are women). To this end, the company focused on temporarily purchasing land in city centers or suburbs, constructing indoor storage facilities on the land, and then selling the storage facilities with the land to investors (it also enters sublease agreements with these investors to manage the facilities).

Starting in FY12/19, the company has been developing its own indoor storage facilities. With these facilities, the company's sales are based on the rent collected from end-users, the same as when the company manages storage on behalf of investors, but expenses are different in that they comprise depreciation, advertising expenses, and other various expenses.

Self-storage brokerage

This entails installing outdoor storage containers and taking orders for storage units inside a building and storage with land, and their subsequent sale. The company books revenue in this sub-segment upon a sale to investors (management outsourcing fees under subleases are recorded in the self-storage management sub-segment).

Starting in FY12/19, when brokering storage facilities, rather than maintaining inventory to be sold to investors as it previously did, Arealink is changing over to a format in which it takes orders for and sells indoor storage facilities suited to customer requests. Hence, it no longer has an inventory of facilities and in this way, seeks to avoid the risk associated with fluctuations in the real estate market.

Other property management

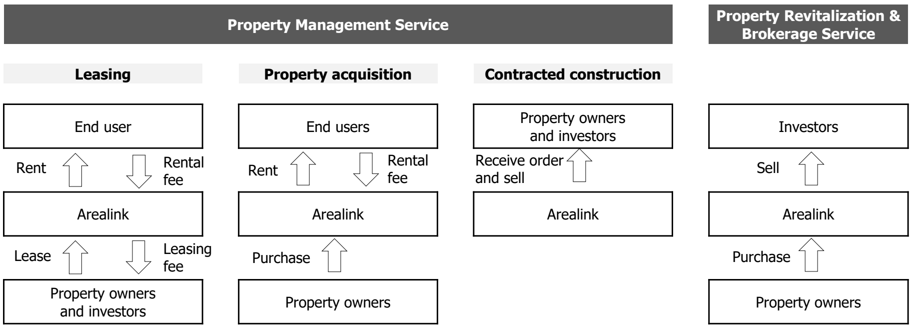
Property other than storage. Includes the asset business (such as office buildings, shopping centers, condominiums, and hotels), SOHO (Hello Office and Hello Rental Meeting Room), and the parking lot (metered parking) business. The company purchases or enters subleases for these properties. It may lease these properties directly to end-users or change the format and operate them under the Hello brand to generate rental revenue.

Property Revitalization & Liquidation segment

In this segment the company purchases real estate (such as office buildings, shopping centers, condominiums, and hotels) and adds value (through increased occupancy rates or major renovations) before selling off the real estate to investors. This is a typical one-time revenue business using bank loans to repeatedly buy and sell real estate. As of February 2019, Arealink has disposed of almost all of its real estate for sale and currently just has income-generating properties held for the long term on its books.

Since FY12/16, Arealink has been purchasing land rights for its land rights management business. The company obtains land rights based on the former Land Lease Law (such as when an estate is settled) and sells these to lessees at an appropriate time after negotiating rights usage. The company thinks this business has solid prospects. It also plans to actively obtain commercial land rights from commercial facilities.

Overview of business



Source: Shared Research based on company data
Note: The reason that investors are included in the leasing categories along with property owners is that Arealink first spends on installing outdoor containers or indoor storage units, then temporarily sells these storage units to investors and simultaneously enters subleasing agreements with them to manage them. Usually, investors contract directly with property owners to lease land/buildings and pay rent (in these cases, Arealink gains prior agreement from property owners to enter master leases for idle land and buildings).

Business model: Property Management segment

Definition of “self-storage business”

Subleasing nonresidential real estate is attracting attention as a stable source of income that minimizes the impact of property price fluctuation risks amid a shrinking population in Japan. In addition to storage (indoor and outdoor storage), Arealink has also been involved in a wide range of real estate including metered parking lots, SOHO (rental meeting rooms and Hello Office), and other income-generating real estate (office buildings, shopping centers, condominiums, and hotels). Still, after the 2008 global financial crisis, the company narrowed its focus to self-storage (indoor and outdoor facilities). The company renovates containers to be used as outdoor storage facilities. Vehicle storage containers are not included in this category, but motorcycle storage containers are.

Indoor storage units are also known in Japan as "unmanned trunk rooms." These are different from the warehouse-type trunk rooms operated by warehousing businesses certified by the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) under the Warehousing Business Act.

For outdoor storage units, the MLIT has issued notifications to the building departments of local governments stating that applications for building verification were necessary based on the Building Standards Act (December 26, 2014 "regarding the thorough application of measures for buildings that use noncompliant containers.") The company said that since 2016, it has applied for verification for newly installed containers.

Definition of warehouse-type trunk room (Warehousing Business Act, Article 2, Paragraph 3)
Trunk room services refer to using all or part of a warehouse for the safekeeping of goods of individuals (except when used as a business or for items deposited under contract for business purposes). As such, contracts for storing goods in warehouse-type trunk rooms operated by warehouse operators differ from the contracts for leasing storage spaces operated by real estate businesses.

Outdoor storage containers required to comply with building regulations; MLIT notification "Regarding thorough application of measures for buildings that use noncompliant containers" (December 26, 2014)
1. Regarding already existing buildings made from containers or those expected to be built using containers, if they do not comply with the Building Standards Act, they will be treated as noncompliant buildings, and guidance for corrective measures shall be issued. In particular, when several containers are stacked on top of each other, those responsible should be aware that the containers may fall in the case of an earthquake and damage the surroundings.
2. Because construction of buildings made from storage containers can be completed quickly, building patrols shall be undertaken so that buildings that use containers can be discovered at an early stage.
3. Buildings made with containers as warehouses and continue such use shall be deemed to be buildings as stipulated under Article 2, Item 1 of the Building Standards Act due to their format and usage. The fact that new installations of containers for these purposes require applications for building verification under the Building Standards Act shall be made widely known by means such as website posts.
Source: MLIT

Rapid growth of outdoor storage

The number of the company's self-storage units has grown steadily, almost tripling (2.8x) from 32,715 at end 2007 to 91,545 at end 2018. Arealink's market share has also risen steadily, from 11.7% in 2010 to 16.1% in 2018 (top share in Japan). In particular, growth in outdoor storage, from 19,418 units (end 2007) to 69,120 (end 2018), has outstripped that of indoor storage, which increased from 13,297 to 22,425 over the same time period. Installing containers for outdoor storage starts with a focus on finding appropriate potential locations nationwide where there is unused land, and then negotiating with the owners.

Outdoor storage is attracting the attention of landowners and investors as they offer the following benefits versus rental apartments, which have a high vacancy risk.

- Less vulnerability to Japan's population decline
- No restrictions in terms of conditions seen in rental apartments, such as topographical features, distance from train stations, or the amount of daylight it receives
- Low installation cost
- Ease of moving or removing a unit
- Usefulness in times of emergency such as the Great East Japan Earthquake in 2011

Furthermore, the comparatively stable occupancy rates compared to parking lots are attractive. Arealink is using a differentiation strategy to raise its nationwide profile by boosting awareness of its Hello Storage brand in collaboration with Hello Kitty. It is also placing signs in target areas and approaching landowners more frequently.

Focusing on indoor storage

In general, indoor storage entails leasing several floors or an entire building and installing storage units, which are rented out to individuals or companies to store their (noncommercial) belongings. In indoor storage, Quraz, Ltd. (owned by a US-based real estate partnership) is the market leader and Arealink is third. Quraz owns relatively large buildings in city centers, and is building up a customer base using increased convenience as a selling point.

From FY12/16 to FY12/18, as a new business, Arealink focused on acquiring land in the suburbs, on which it built storage facilities using the 2x4 construction method and three-story steel-frame indoor storage facilities, and sold the storage facilities with the land to investors.

Nationwide rollout

The share of storage units in the Tokyo metropolitan region (Saitama, Chiba, Tokyo, and Kanagawa) has declined from 81.0% at end 2011 to 69.1% at end 2018 under the company's nationwide rollout strategy, but there is still a heavy concentration in Tokyo. The strategy has accelerated more for outdoor storage, with the share of units in the metropolitan region declining from 75.4% at end 2011 to 63.3% at end 2018. However, the share of indoor storage units in the Tokyo metropolitan region has remained high, dipping only from 89.3% to 87.1% over the same timeframe. Shared Research believes that while there is relatively strong demand for outdoor storage units in regional cities, indoor storage units command higher average rents in the Tokyo metropolitan region, resulting in higher return on investment.

Adoption of marketing based on detailed data analysis

With the help of research companies, Arealink has divided the country into small areas to analyze potential markets and competitors and examine opening criteria, ranking the attractiveness of locations as A, B, or C. Marketing based on precise data analysis has enabled cloud-based marketing activities and standardization (through Salesforce and G Suite), the optimization of product type and pricing, the clarification of opening standards, and the optimization of customer recruitment via revenue management. This enables the company to quickly discover if facilities are in the wrong location and rectify the situation.

Business model: Property Revitalization & Liquidation segment

Land rights management business

From FY12/16, Arealink resumed land purchases to focus on the land rights management business. The company obtains land rights for real estate still under the former Land Lease Law (when an estate is settled, for example) and sells these rights to lessees at an appropriate time after negotiating rights usage. The company thinks this business has solid prospects. Usually, the combination of such land and leasehold rights is priced at a significant discount compared to vacant land rights. Both land rights (held by the landowner) and leasehold rights (held by the lessee) have low liquidity or collateral value on their own, and the situation is economically disadvantageous for both parties. Accordingly, a landowner can get a higher price by selling to the lessee rather than a third party (and vice versa).

In reality, there are often several lessees for one land plot, and upon the transfer of rights, rights relationships become complicated. Arealink aims to solve this issue and create a beneficial situation for the land rights owner, lessee, and itself. According to the company, there are still many plots of land in Japan subject to the former Land Lease Law, and it plans to develop the land rights management business using its nationwide network. There are few companies with a dominant presence in the land rights management market, and Arealink therefore aims to leverage its strengths to become the market leader. In its land rights management business, the company targets returns of 3% per annum from rental income and a 20% gain on sale after one or two years. The company intends to venture into new fields by expanding its operations from Tokyo to Kansai, on the one hand, and from residential land rights to commercial land rights, on the other. Commercial land rights operations have vast potential by virtue of higher rental revenues and project sizes. The company intends to actively obtain commercial land rights from commercial facilities (such as convenience stores, small supermarkets, and family restaurants).

In FY12/18, the company saw sales in the Property Revitalization & Liquidation segment jump to JPY3.7bn (+97.8% YoY) as it solidified its presence as the number two player in the land rights management business. Sansei Landic Co., Ltd. (TSE1: 3277), the top player in the land rights management industry, had land rights sales of JPY7.1bn in FY12/17 (+40.3% YoY), and performance remains robust. Sansei Landic's sales of old underutilized properties were JPY5.5bn (-3.1% YoY), putting the old underutilized properties business on the same level as the land rights management business as an earnings pillar. In commercial land rights operations, Arealink faces competition from Nippon Commercial Development Co., Ltd. (TSE1: 3252).

Land rights (*sokochi* in Japanese) refer to ownership rights over residential land that includes leasehold rights. Leasehold rights refer to surface rights or land lease rights for owning property, but not necessarily the land underneath. The two are basically inseparable. Surface rights (i.e., the property) may be transferred freely, but land lease rights are receivables, so when transferred or subleased, the approval of the landowner or court is necessary and often entails financial compensation. In 1992, the Act on Land and Building Leases came into effect, incorporating fixed-term land lease rights. The former Land Lease Law leaned in the favor of protecting lessees more than lessors (landowners), as leasehold rights under the former law were semi-permanent; unless the lessee requested to cancel the contract, the landowner basically had no chance to fully recover ownership rights. Meanwhile, the lessees would lose their land lease rights if they failed to pay rent. As such, there were often disputes at the time of inheritance or lease renewal, leading to a tense relationship between lessors and lessees.

Number of storage units (outdoor/indoor [includes storage with land]) by region

No. of storage units by region (year-end)	2011	2012	2013	2014	2015	2016	2017	2018	% of total
Hokkaido	1,478	1,478	1,414	1,446	1,446	1,466	1,420	1,489	1.6%
Miyagi	101	143	392	536	920	1,695	1,695	1,682	1.8%
Fukushima	0	0	0	0	0	0	0	56	0.1%
Ibaraki	0	0	208	292	284	571	783	786	0.9%
Tochigi	0	0	62	83	81	81	155	207	0.2%
Gunma	0	0	0	86	109	165	334	337	0.4%
Saitama	3,308	4,392	5,196	5,641	6,872	7,957	9,021	10,443	11.4%
Chiba	5,146	5,322	5,989	7,132	8,359	9,248	10,331	11,128	12.2%
Tokyo	18,987	19,312	20,537	22,169	23,082	24,261	26,378	29,625	32.4%
Kanagawa	4,000	4,393	4,505	5,453	7,018	8,150	10,274	12,073	13.2%
Niigata	0	0	0	0	0	0	69	92	0.1%
Toyama	0	0	0	0	0	0	143	143	0.2%
Ishikawa	0	0	0	0	0	0	204	204	0.2%
Fukui	0	0	0	0	0	0	90	90	0.1%
Yamanashi	0	0	0	0	0	45	89	118	0.1%
Nagano	0	0	0	0	0	0	175	237	0.3%
Gifu	0	0	86	169	483	521	582	621	0.7%
Shizuoka	0	0	81	357	356	822	1,205	1,275	1.4%
Aichi	842	925	1,128	1,526	2,476	3,664	4,502	5,903	6.4%
Mie	50	50	82	204	204	198	340	428	0.5%
Shiga	0	0	0	0	0	66	154	154	0.2%
Kyoto	66	84	460	962	1,126	1,211	1,170	1,298	1.4%
Osaka	2,251	2,583	2,892	3,329	4,006	4,102	4,658	4,882	5.3%
Hyogo	1,609	1,878	2,187	2,379	3,420	3,546	3,533	3,689	4.0%
Nara	0	268	337	469	499	560	567	567	0.6%
Wakayama	0	0	0	0	27	27	27	27	0.0%
Tottori	0	0	0	0	0	0	32	32	0.0%
Shimane	0	0	0	0	0	0	0	0	0.0%
Okayama	0	0	0	0	0	64	218	218	0.2%
Hiroshima	0	0	0	0	0	0	316	312	0.3%
Tokuhsima	0	0	0	0	0	0	27	27	0.0%
Kagawa	0	0	0	45	45	86	181	181	0.2%
Ehime	0	0	0	0	0	0	84	84	0.1%
Kouchi	0	0	0	0	0	0	34	34	0.0%
Fukuoka	251	251	511	706	932	1,551	1,691	1,827	2.0%
Saga	0	0	0	0	0	0	79	79	0.1%
Nagasaki	0	0	0	0	0	0	118	118	0.1%
Kumamoto	48	48	48	48	48	92	177	402	0.4%
Oita	26	26	26	26	26	26	106	106	0.1%
Miyazaki	0	0	0	0	0	0	109	100	0.1%
Kagoshima	502	372	372	372	372	372	380	367	0.4%
Okinawa	173	173	173	134	134	104	104	104	0.1%
Total	38,838	41,698	46,686	53,564	62,325	70,651	81,555	91,545	100.0%
Tokyo metropolitan region	31,441	33,419	36,227	40,395	45,331	49,616	56,004	63,269	
Tokyo metropolitan region as % of total	81.0%	80.1%	77.6%	75.4%	72.7%	70.2%	68.7%	69.1%	

Outdoor storage (year-end)	2011	2012	2013	2014	2015	2016	2017	2018	% of total
Hokkaido	1,052	1,052	988	1,024	1,024	1,044	998	999	1.4%
Miyagi	101	143	392	536	920	1,695	1,695	1,682	2.4%
Fukushima	0	0	0	0	0	0	0	56	0.1%
Ibaraki	0	0	208	292	284	571	783	786	1.1%
Tochigi	0	0	62	83	81	81	155	207	0.3%
Gunma	0	0	0	86	109	165	334	337	0.5%
Saitama	2,735	3,720	4,524	4,978	6,061	7,043	7,711	8,449	12.2%
Chiba	4,864	5,049	5,720	6,803	7,909	8,718	9,524	9,831	14.2%
Tokyo	8,364	8,940	10,044	11,239	11,989	13,430	15,485	17,114	24.8%
Kanagawa	1,559	1,757	2,157	2,912	4,208	5,550	7,537	8,336	12.1%
Niigata	0	0	0	0	0	0	69	92	0.1%
Toyama	0	0	0	0	0	0	143	143	0.2%
Ishikawa	0	0	0	0	0	0	204	204	0.3%
Fukui	0	0	0	0	0	0	90	90	0.1%
Yamanashi	0	0	0	0	0	45	89	118	0.2%
Nagano	0	0	0	0	0	0	175	237	0.3%
Gifu	0	0	86	169	483	521	582	621	0.9%
Shizuoka	0	0	81	357	356	822	1,205	1,275	1.8%
Aichi	589	672	884	1,267	2,107	3,297	3,986	4,858	7.0%
Mie	0	0	32	154	154	148	290	378	0.5%
Shiga	0	0	0	0	0	66	154	154	0.2%
Kyoto	0	0	306	808	972	1,059	1,018	1,146	1.7%
Osaka	1,426	1,759	2,082	2,367	3,002	3,159	3,667	3,839	5.6%
Hyogo	1,562	1,831	2,140	2,332	3,311	3,440	3,427	3,583	5.2%
Nara	0	268	337	469	499	560	567	567	0.8%
Wakayama	0	0	0	0	27	27	27	27	0.0%
Tottori	0	0	0	0	0	0	32	32	0.0%
Okayama	0	0	0	0	0	64	218	218	0.3%
Hiroshima	0	0	0	0	0	0	316	312	0.5%
Tokushima							27	27	0.0%
Kagawa	0	0	0	45	45	86	181	181	0.3%
Ehime	0	0	0	0	0	0	84	84	0.1%
Kouchi	0	0	0	0	0	0	34	34	0.0%
Fukuoka	251	251	511	706	932	1,551	1,691	1,827	2.6%
Saga	0	0	0	0	0	0	79	79	0.1%
Nagasaki	0	0	0	0	0	0	118	118	0.2%
Kumamoto	48	48	48	48	48	92	177	402	0.6%
Oita	26	26	26	26	26	26	106	106	0.2%
Miyazaki	0	0	0	0	0	0	109	100	0.1%
Kagoshima	502	372	372	372	372	372	380	367	0.5%
Okinawa	173	173	173	134	134	104	104	104	0.2%
Total	23,252	26,061	31,173	37,207	45,053	53,736	63,571	69,120	100.0%
Tokyo metropolitan region	17,522	19,466	22,445	25,932	30,167	34,741	40,257	43,730	
Tokyo metropolitan region as % of total	75.4%	74.7%	72.0%	69.7%	67.0%	64.7%	63.3%	63.3%	

Indoor storage (year-end)	2011	2012	2013	2014	2015	2016	2017	2018	% of total
Hokkaido	426	426	426	422	422	422	422	490	2.2%
Saitama	573	672	672	663	811	914	1,310	1,994	8.9%
Chiba	282	273	269	329	450	530	807	1,297	5.8%
Tokyo	10,623	10,372	10,493	10,930	11,093	10,831	10,893	12,511	55.8%
Kanagawa	2,441	2,636	2,348	2,541	2,810	2,600	2,737	3,737	16.7%
Aichi	253	253	244	259	369	367	516	1,045	4.7%
Mie	50	50	50	50	50	50	50	50	0.2%
Kyoto	66	84	154	154	154	152	152	152	0.7%
Osaka	825	824	810	962	1,004	943	991	1,043	4.7%
Hyogo	47	47	47	47	109	106	106	106	0.5%
Total	15,586	15,637	15,513	16,357	17,272	16,915	17,984	22,425	100.0%
Tokyo metropolitan region	13,919	13,953	13,782	14,463	15,164	14,875	15,747	19,539	
Tokyo metropolitan region as % of total	89.3%	89.2%	88.8%	88.4%	87.8%	87.9%	87.6%	87.1%	

Source: Shared Research based on company data

Business strategy and KPIs

Launching and strengthening Arealink's consulting business

Arealink negotiates with landowners about master leasing arrangements and markets business proposals for storage unit installation and management to investors. Investors then enter land leasing agreements with landowners. At the same time, investors enter comprehensive agreements with Arealink to sublease the properties and outsource storage operations management (usually for 10 years). In the case of outdoor storage units, the company often builds long-term relationships (that may include estate planning strategies) with the investors and landowners. The company has already established an "owners' group" of high net worth individuals with land, and also plans to strengthen its consulting business in light of the aging society. The company hires experienced staff over 60 years old (near in age to the landowners) as concierges who can act as consultants in its contracted storage operations. The company also thinks its permanent employees can eventually become consultants when they reach the age of 40.

Benefits for real estate investors

The self-storage business is attracting interest as a way to effectively utilize idle real estate (land, buildings, warehouses, and so on). Benefits for real estate investors compared to rental apartments are as follows.

Prospects for rapid growth in the self-storage market despite shrinking Japanese population

The domestic self-storage business is growing at 4–8% per annum. The self-storage supply per household in the US is more than 20x that in Japan. There is one unit for every six households in the US, but only one per 125 households in Japan. There is plenty of scope for rapid growth if awareness of the convenience of self-storage facilities increases in Japan, where storage space is limited, and the underlying demand can be tapped.

Various types of land can be effectively used for storage

There are many potential obstacles to managing apartments and condominiums, such as the property's distance from a train station, topography, size, daylight, and view. Land may be unsuitable for parking lots as it would inconvenience the neighbors. But in many cases a self-storage business can be operated without problems.

Small initial investment

Unlike for condominiums or apartment buildings, for outdoor storage, there is no need to construct a building, since it is enough to simply install a container. The units are not for residential use and do not need water supply or water heating equipment, which keeps a lid on construction costs. As a rule, there is no need for restoration costs or major repairs once a tenant has vacated the unit. It is also easy to move and remove the unit.

Stable long-term yields under 10-year sublease agreements

Typically, under self-storage sublease agreements, investors incur higher monthly management fees than rental apartments. Still, for self-storage, rental revenue remains stable regardless of occupancy rates, and there are no rent shortfalls due to vacancies or nonpayment. Arealink handles all operations management including tenant recruitment, contracts, rent collection, facility cleaning, and maintenance, so almost all property owners sign sublease agreements. Self-storage is a simple business of providing storage space, so it results in very few complaints and has a track record of comparatively stable occupancy rates.

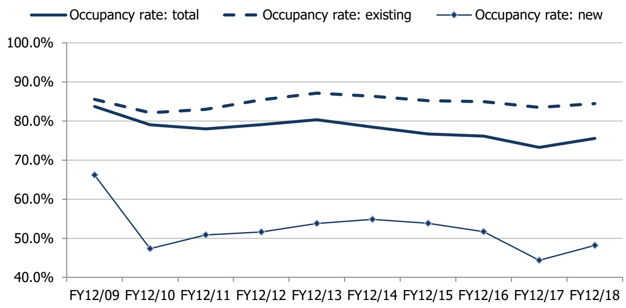
In general, self-storage rent per sqm is double the rent per sqm for offices, and storage space is used more efficiently. There is a gradual uptrend in long-term customers, and a location with a certain occupancy rate offers long-term stability. Furthermore, as there are many small contracts, cancellations are spread out, making it easier to deal with vacancy risk. This is a business with long-term stable management as occupancy rates have no strong correlation with macro factors such as the economic cycle, and risk is low compared to rent guarantees of apartment subleases.

Average occupancy rates

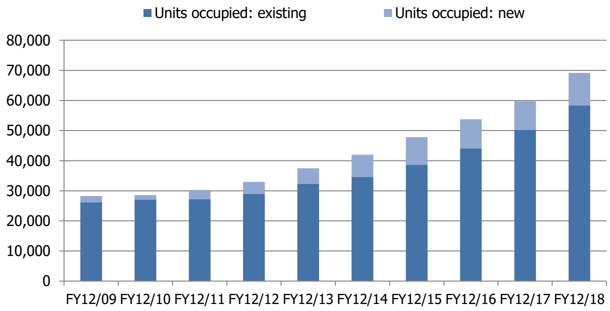
In contrast with rental apartments, it takes one to three years for occupancy at a self-storage facility to surpass the breakeven point. After exceeding a certain occupancy level, self-storage generates relatively stable operational revenue. For Arealink, occupancy rates at existing facilities (storage facilities open for two years or longer) are around 85%, while rates at new facilities (open for less than two years) are in the 45–55% range. These levels have been stable in recent years. As a result of more customers at new facilities, it appears that the average occupancy rate declined from 83.7% in 2009 to 75.6% in 2018. Still, given the occupancy rates for existing facilities, average occupancy rates are expected to have declined due to the increase in new customers accompanying market growth, so occupancy rates are likely to converge to previous levels as the new units become existing units.

From data that Arealink discloses regarding total number of units, units occupied, average occupancy rate, existing facility occupancy rates, and new facility occupancy rates, it is possible to calculate the total number of existing units, the number of occupied existing units, the number of new units, and the number of occupied new units. Shared Research estimates that as of end 2018, there were 58,335 occupied existing units versus 10,834 occupied new units. Compared to end 2009, there was growth of 123% in occupied existing units and 5.2x in occupied new units.

Average occupancy rates (existing, new)



Occupied units (existing, new)

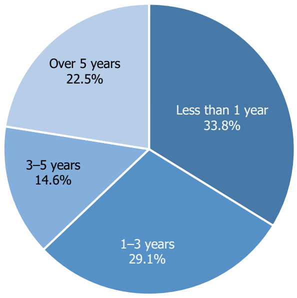


Source: Shared Research based on company data
Note: "Existing" refers to units that started operating two or more years ago; "new" refers to units that started operating less than two years ago.

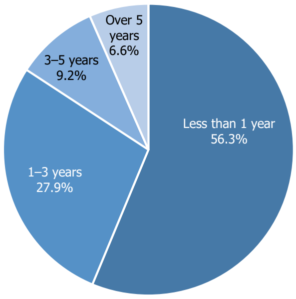
The average occupancy period increased from 36 months in 2014 to 39 months in 2018. The average occupancy period for those canceling contracts has shrunk from 22 months in 2013 to 19 months in 2018. Some 77.5% of customers rent units for 1–5 years. Of contract cancellations, 56.3% were within one year of occupancy. Short-term customers such as those who are moving make up a certain percentage of the canceled contracts, so this is not necessarily a negative thing. Shared Research thinks that tapping into underlying short-term customer demand could boost turnover rates.

Length of occupancy

Customers with ongoing contracts (as of December 2018)



Customers who ended contracts (as of December 2018)



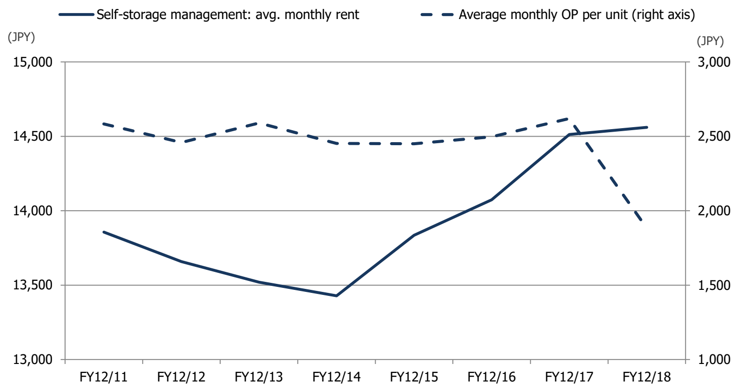
Source: Shared Research based on company data

Average monthly rents

Average monthly rents as of December 2018 were JPY13,890 for outdoor storage units and JPY15,289 for indoor storage units, up from JPY12,165 and JPY13,707 respectively in 2016. According to the company, this was partly due to price rises reflecting higher material costs and increased expenses for building verification applications. We think other factors were also at work, such as the popularity of larger indoor storage units and one-story outdoor units, which are more convenient but also higher-priced. Arealink always holds temporary free rent and other discount campaigns, and offers high value-added products such as storage units with land near city centers as it works to meet diverse needs with an extensive product lineup.

Dividing sales for the self-storage management business by the number of units occupied gives a monthly average rent per unit of about JPY14,000 (trending up in recent years). The average operating profit per unit (calculated on the same basis) has hovered around JPY2,500, but dipped below JPY2,000 in FY12/18.

Average monthly rent and operating profit per self-storage unit



Source: Shared Research based on company data

Recurring revenue business growing due to stable occupancy and rents

A recurring business model features fixed prices and margins, which provide steady, stable earnings as the number of units in operation rises. To maintain prices and margins, it is essential for a company to develop differentiated products not affected by the macro environment or competition, and to avoid increases in fixed and other costs. The self-storage industry faces the structural headwind of a population decline, but it has increased its unit count while maintaining relatively stable occupancy rates and average pricing, making it a classic example of a recurring revenue business.

Key data of the core self-storage management and brokerage businesses (KPIs)

Market (JPYmn)	FY12/10	FY12/11	FY12/12	FY12/13	FY12/14	FY12/15	FY12/16	FY12/17	FY12/18
Storage market in Japan	40,630	42,230	45,570	48,610	52,380	58,630	61,490	65,700	69,890
Indoor storage market	19,280	20,040	20,610	21,430	22,550	23,880	25,360	27,000	28,289
Outdoor storage market	21,350	22,190	24,960	27,180	29,830	32,750	36,130	38,700	41,601
Arealink market share	11.7%	11.6%	11.4%	11.8%	12.2%	12.7%	14.0%	15.0%	16.1%
Indicators									
Total units	36,131	38,838	41,698	46,686	53,564	62,325	70,651	81,555	91,545
Indoor storage	14,573	15,586	15,637	15,513	16,357	17,272	16,915	17,984	22,425
Outdoor storage	21,558	23,252	26,061	31,173	37,207	45,053	53,736	63,571	69,120
Net increase	2,328	2,707	2,860	4,988	6,878	8,761	8,326	10,904	9,990
Units occupied	28,562	30,290	32,968	37,499	42,009	47,796	53,786	59,748	69,169
Occupancy rate	79.05%	77.99%	79.06%	80.32%	78.43%	76.69%	76.13%	73.26%	75.56%
Total existing units (open for 2 years or more)	32,951	32,787	33,869	37,136	40,080	45,423	51,883	60,251	69,069
Units occupied: existing	27,056	27,213	28,927	32,364	34,613	38,696	44,085	50,298	58,335
Occupancy rate: existing	82.11%	83.00%	85.41%	87.15%	86.36%	85.19%	84.97%	83.48%	84.46%
Total new units (open for less than 2 years)	3,180	6,051	7,829	9,550	13,484	16,902	18,768	21,304	22,476
Units occupied: new	1,506	3,077	4,041	5,135	7,396	9,100	9,701	9,450	10,834
Occupancy rate: new	47.36%	50.85%	51.61%	53.77%	54.85%	53.84%	51.69%	44.36%	48.20%
Earnings (JPYmn)									
Self-storage (management and brokerage) sales	5,380	5,773	6,269	7,813	9,124	10,980	13,903	17,575	23,129
Self-storage (management and brokerage) OP	815	997	1,093	1,421	1,600	1,829	2,250	2,572	2,835
Self-storage OPM	15.1%	17.3%	17.4%	18.2%	17.5%	16.7%	16.2%	14.6%	12.3%
Self-storage management sales	4,770	4,893	5,184	5,716	6,406	7,455	8,578	9,886	11,262
Average monthly rent (JPY)	13,992	13,857	13,658	13,519	13,428	13,836	14,074	14,513	14,560
Self-storage management OP	713	912	933	1,095	1,170	1,320	1,522	1,784	1,456
Avg. monthly OP per unit (JPY)	2,091	2,583	2,458	2,590	2,453	2,450	2,497	2,619	1,882

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

Arealink vs. competitors: Market shares

Outdoor storage

In the domestic outdoor storage market, the top two players (leader Arealink and number two Kase Group) have an overwhelming lead in terms of locations and units. However, the 20 companies outside the top 10 players account for 40% of the market, showing the strength of local operators scattered across the country (source: company materials based on Yano Research Institute materials [as of December 2018]). There are many companies operating in the area of outdoor storage. Small local operators (the majority of the company's peers) are likely to outsource operations and management to majors such as Arealink in the future. In the US, outsourcing has already grown rapidly and consolidation is starting to occur. The major participants in the market are storage specialists, warehousing and logistics companies, companies that sell containers, local real estate agents, shed manufacturers, portable building manufacturers, railroad companies, and individual investors.

Indoor storage

Each of the top four indoor self-storage companies (in order of market share: Quraz, Reise, Arealink, and Kase) has at least 10,000 units, far outstripping the other participants. Quraz (US) focuses on large facilities, by buying an entire building and operating self-storage units on most of the floors. Its average facility has 582 units (versus less than 100 for Arealink). The main players in this sector are railroad companies, warehousing and logistics companies, architects, materials companies, property developers and managers, franchises, and other industries. Companies outside the top 10 account for 42% of the market.

Market share of outdoor (left) and indoor (right) storage

	Outdoor storage	Units	Share	Locations	Share	Units per location
1	Arealink	65,612	20.6%	1,458	18.3%	45.0
2	Kase Warehouse	44,215	13.9%	967	12.1%	45.7
3	Sankyo Frontier	18,370	5.8%	361	4.5%	50.9
4	Company A	14,018	4.4%	331	4.1%	42.4
5	Company B	11,355	3.6%	320	4.0%	35.5
6	Company C	8,425	2.6%	269	3.4%	31.3
7	Company D	8,239	2.6%	207	2.6%	39.8
8	Company E	7,298	2.3%	195	2.4%	37.4
9	Company F	7,036	2.2%	229	2.9%	30.7
10	Company G	6,579	2.1%	153	1.9%	43.0
	Others	128,093	40.1%	3,490	43.7%	36.7
	Total	319,240	100.0%	7,980	100.0%	40.0

	Indoor storage	Units	Share	Locations	Share	Units per location
1	Quraz	35,554	17.2%	61	1.9%	582.9
2	Reise	25,853	12.5%	495	15.3%	52.2
3	Arealink	22,472	10.9%	280	8.7%	80.3
4	Company A	16,068	7.8%	352	10.9%	45.6
5	Company B	5,962	2.9%	172	5.3%	34.7
6	Company C	5,146	2.5%	64	2.0%	80.4
7	Company D	4,005	1.9%	23	0.7%	174.1
8	Company E	3,034	1.5%	27	0.8%	112.4
9	Company F	2,799	1.4%	91	2.8%	30.8
10	Company G	2,749	1.3%	51	1.6%	53.9
	Others	82,528	40.0%	1,618	50.0%	51.0
	Total	206,170	100.0%	3,234	100.0%	63.8

Source: Shared Research based on company data (from Yano Research Institute as of December 2018)
Note: Company names represented by the same letters in different columns are not necessarily the same companies.

Earnings

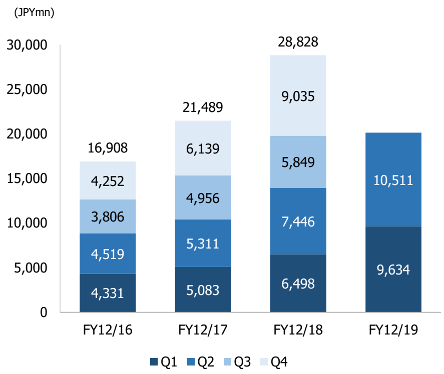
Quarterly results

Cumulative earnings	FY12/17				FY12/18				FY12/19		FY12/19		
Parent (JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	% of 1H Est.	2H Est.	FY Est.
Sales	5,083	10,394	15,350	21,489	6,498	13,944	19,793	28,828	9,634	20,145	69.5%	8,855	29,000
YoY	17.4%	17.4%	21.3%	27.1%	27.8%	34.2%	28.9%	34.2%	48.3%	44.5%			
Cost of sales	3,625	7,510	11,221	15,806	4,979	10,604	15,031	22,173	7,396	15,414			
YoY	19.1%	19.8%	24.0%	30.2%	37.3%	41.2%	34.0%	40.3%	48.5%	45.4%			
Cost ratio	71.3%	72.3%	73.1%	73.6%	76.6%	76.0%	75.9%	76.9%	76.8%	76.5%			
Gross profit	1,458	2,884	4,129	5,683	1,520	3,340	4,762	6,655	2,239	4,732			
YoY	13.2%	11.6%	14.6%	19.1%	4.2%	15.8%	15.3%	17.1%	47.3%	41.7%			
GPM	28.7%	27.7%	26.9%	26.4%	23.4%	24.0%	24.1%	23.1%	23.2%	23.5%			
SG&A expenses	787	1,609	2,439	3,304	890	1,846	2,763	3,873	960	2,097			
YoY	20.4%	18.4%	18.6%	16.5%	13.0%	14.7%	13.3%	17.2%	7.9%	13.6%			
SG&A ratio	15.5%	15.5%	15.9%	15.4%	13.7%	13.2%	14.0%	13.4%	10.0%	10.4%			
Operating profit	670	1,275	1,690	2,380	630	1,494	1,999	2,782	1,279	2,634	94.1%	166	2,800
YoY	-	4.2%	9.3%	22.9%	-	17.2%	18.3%	16.9%	-	76.3%			
OPM	13.2%	12.3%	11.0%	11.1%	9.7%	10.7%	10.1%	9.7%	13.3%	13.1%			
Recurring profit	659	1,301	1,751	2,441	624	1,345	1,763	2,537	1,178	2,473	91.6%	227	2,700
YoY	-	4.5%	11.6%	24.0%	-	3.4%	0.7%	3.9%	-	83.9%			
RPM	13.0%	12.5%	11.4%	11.4%	9.6%	9.6%	8.9%	8.8%	12.2%	12.3%			
Net income	430	858	1,163	1,547	424	911	1,157	1,810	802	1,687	112.4%	-187	1,500
YoY	-	8.7%	17.8%	35.4%	-	6.2%	-0.5%	17.0%	-	85.1%			
Net margin	8.5%	8.3%	7.6%	7.2%	6.5%	6.5%	5.8%	6.3%	8.3%	8.4%			

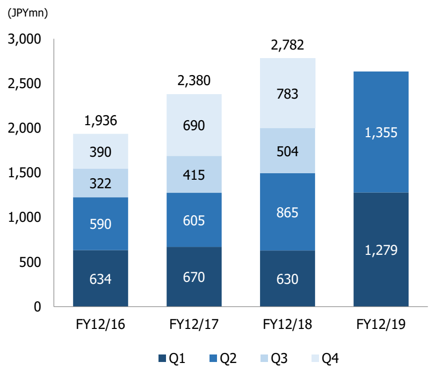
Quarterly earnings	FY12/17				FY12/18				FY12/19	
Parent (JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Sales	5,083	5,311	4,956	6,139	6,498	7,446	5,849	9,035	9,634	10,511
YoY	17.4%	17.5%	30.2%	44.4%	27.8%	40.2%	18.0%	47.2%	48.3%	41.2%
Cost of sales	3,625	3,885	3,711	4,585	4,979	5,625	4,427	7,142	7,396	8,018
YoY	19.1%	20.5%	33.2%	48.6%	37.3%	44.8%	19.3%	55.8%	48.5%	42.5%
Cost ratio	71.3%	73.2%	74.9%	74.7%	76.6%	75.5%	75.7%	79.0%	76.8%	76.3%
Gross profit	1,458	1,426	1,245	1,554	1,520	1,821	1,422	1,893	2,239	2,493
YoY	13.2%	10.1%	22.0%	33.1%	4.2%	27.7%	14.2%	21.8%	47.3%	36.9%
GPM	28.7%	26.8%	25.1%	25.3%	23.4%	24.5%	24.3%	21.0%	23.2%	23.7%
SG&A expenses	787	822	830	864	890	956	918	1,110	960	1,138
YoY	20.4%	16.5%	18.9%	11.1%	13.0%	16.4%	10.5%	28.4%	7.9%	19.0%
SG&A ratio	15.5%	15.5%	16.8%	14.1%	13.7%	12.8%	15.7%	12.3%	10.0%	10.8%
Operating profit	670	605	415	690	630	865	504	783	1,279	1,355
YoY	-	2.5%	28.8%	77.1%	-	43.0%	21.5%	13.5%	-	56.8%
OPM	13.2%	11.4%	8.4%	11.2%	9.7%	11.6%	8.6%	8.7%	13.3%	12.9%
Recurring profit	659	642	450	690	624	721	419	774	1,178	1,295
YoY	-	10.3%	38.8%	72.8%	-	12.4%	-7.1%	12.1%	-	79.6%
RPM	13.0%	12.1%	9.1%	11.2%	9.6%	9.7%	7.2%	8.6%	12.2%	12.3%
Net income	430	428	305	384	424	487	246	654	802	885
YoY	-	15.9%	53.9%	147.6%	-	13.7%	-19.4%	70.1%	-	81.8%
Net margin	8.5%	8.1%	6.2%	6.3%	6.5%	6.5%	4.2%	7.2%	8.3%	8.4%

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

Quarterly sales



Quarterly operating profit



Source: Shared Research based on company data

Quarterly results by segment

Cumulative (JPYmn)	FY12/17 Q1	FY12/17 Q2	FY12/17 Q3	FY12/17 Q4	FY12/18 Q1	FY12/18 Q2	FY12/18 Q3	FY12/18 Q4	FY12/19 Q1	FY12/19 Q2	FY12/19 % of 1H Est.	FY12/19 2H Est.	FY12/19 FY Est.
Sales	**5,083**	**10,394**	**15,350**	**21,489**	**6,498**	**13,944**	**19,793**	**28,828**	**9,634**	**20,145**	**69.5%**	**8,855**	**29,000**
YoY	17.4%	17.4%	21.3%	27.1%	27.8%	34.2%	28.9%	34.2%	48.3%	44.5%			35.0%
Property Management										15,582	64.9%	8,418	24,000
YoY	13.3%	13.6%	18.2%	24.0%	28.4%	34.6%	25.8%	28.1%	24.9%	26.1%			22.3%
% of total	89.2%	88.3%	90.4%	91.3%	89.6%	88.6%	88.2%	87.2%	75.5%	77.4%			
Property Revitalization & Liquidation										4,563	91.3%	437	5,000
YoY	65.9%	57.8%	61.6%	72.0%	23.6%	30.9%	58.4%	97.8%	248.2%	187.4%			167.5%
% of total	10.8%	11.7%	9.6%	8.7%	10.4%	11.4%	11.8%	12.8%	24.5%	22.6%			
Operating profit	**670**	**1,275**	**1,690**	**2,380**	**630**	**1,494**	**1,999**	**2,782**	**1,279**	**2,634**	**94.1%**	**166**	**2,800**
YoY	5.7%	4.2%	9.3%	22.9%	-6.0%	17.2%	18.3%	16.9%	103.1%	76.3%			
Property Management										2,063	73.7%	734	2,797
YoY	3.5%	0.8%	8.4%	14.7%	9.8%	22.5%	14.5%	9.9%	-3.1%	11.2%			
% of total	80.7%	81.4%	85.3%	87.1%	89.3%	86.1%	85.7%	84.1%	51.5%	63.1%			
OPM	17.1%	16.5%	16.1%	16.0%	14.6%	15.0%	14.6%	13.7%	11.4%	13.2%			
Property Revitalization & Liquidation										1,204	100.1%	-1	1,203
Y(YoY	77.9%	72.5%	67.1%	88.7%	-44.9%	-13.6%	11.4%	40.2%	662.9%	303.1%			
0 % of total	19.2%	18.6%	14.7%	12.9%	10.7%	13.9%	14.3%	15.9%	48.5%	36.9%			
Adjustments	-291	-586	-920	-1,218	-324	-660	-977	-1,314	-324	-632	52.7%	-568	-1200

Quarterly (JPYmn)	FY12/17 Q1	FY12/17 Q2	FY12/17 Q3	FY12/17 Q4	FY12/18 Q1	FY12/18 Q2	FY12/18 Q3	FY12/18 Q4	FY12/19 Q1	FY12/19 Q2
Sales	**5,083**	**5,311**	**4,956**	**6,139**	**6,498**	**7,446**	**5,849**	**9,035**	**9,634**	**10,511**
YoY	17.4%	17.5%	30.2%	44.4%	27.8%	40.2%	18.0%	47.2%	48.3%	41.2%
Property Management										
YoY	13.3%	13.9%	28.3%	40.9%	28.4%	40.6%	8.6%	33.6%	24.9%	27.2%
% of total	89.2%	87.5%	94.7%	93.6%	89.6%	87.8%	87.1%	85.0%	75.5%	79.1%
Property Revitalization & Liquidation										
YoY	65.9%	51.9%	80.9%	128.2%	23.6%	36.9%	184.6%	246.3%	248.2%	141.9%
% of total	10.8%	12.5%	5.3%	6.4%	10.4%	12.2%	12.9%	15.0%	24.5%	20.9%
Operating profit	**670**	**605**	**415**	**690**	**630**	**865**	**504**	**783**	**1,279**	**1,355**
YoY	5.7%	2.5%	28.8%	77.1%	-6.0%	43.0%	21.5%	13.5%	103.1%	56.8%
Property Management										
YoY	3.5%	-1.8%	29.1%	33.7%	9.8%	35.8%	-2.7%	-1.2%	-3.1%	23.3%
% of total	80.7%	82.1%	95.3%	91.8%	89.3%	83.6%	84.5%	79.9%	51.5%	74.3%
OPM	17.1%	15.9%	15.2%	15.8%	14.6%	15.3%	13.6%	11.7%	11.4%	14.9%
Property Revitalization & Liquidation										
YoY	77.9%	69.3%	31.5%	409.5%	-44.9%	22.3%	246.7%	175.5%	662.9%	116.9%
% of total	19.2%	17.9%	4.9%	8.2%	10.7%	16.4%	15.5%	20.1%	48.5%	25.7%
Adjustments	-291	-295	-334	-298	-324	-335	-318	-337	-324	-308

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

1H FY12/19 results

Overview

In 1H FY12/19, sales came to JPY20.1bn (+44.5% YoY), operating profit JPY2.6bn (+76.3% YoY), recurring profit JPY2.5bn (+83.9% YoY), and net income JPY1.7bn (+85.1% YoY). Overall results were driven by sales and profit growth in the Property Management and the Property Revitalization & Liquidation segments. Versus full-year FY12/19 company forecasts, 1H sales reached 69.5%, operating profit 94.1%, recurring profit 91.6%, and net income 112.4%. The company revised its full-year FY12/19 forecasts twice (in April and July, respectively), and the 1H results were in line with the revised forecasts.

Performance by segment

Property Management segment

Sales were JPY7.3bn (+24.9% YoY) and segment profit JPY826mn (-3.1% YoY).
In the core self-storage business, storage brokerage contributed to earnings growth. This was due to the sale of storage with land (in April 2019, Arealink established the private equity fund “Trunk House 24 LLC” [not factored into forecasts as of April] and sold eight storage facilities with land). Openings of custom-built outdoor storage units declined as the company adopted stricter opening standards, but still progressed in line with plan.

The breakdown of the segment is as follows:

- ▷ The self-storage management business had sales of JPY6.3bn (+16.4% YoY), gross profit of JPY1.2bn (-1.2% YoY), and operating profit of JPY822mn (+6.7% YoY). The company had a total of 93,885 self-storage units at end June 2019 (+8,888 from end June 2018), and the occupancy rate was 74.63% (versus 75.80% at end June 2018). Sales and profit grew and reached the respective targets. However, GPM was weighed down by the booking of a JPY200mn allowance for subleasing losses, which the company started recording from end FY12/18 amid favorable earnings performance. Excluding this factor, GPM rose as Arealink held down discount rates during sales campaigns.
- ▷ The self-storage brokerage business had sales of JPY8.3bn (+39.7% YoY), gross profit of JPY1.4bn (+16.2% YoY), and operating profit of JPY909mn (+17.5% YoY). GPM fell in Q1 on the early bulk sale of some storage facilities with land, but improved in Q2 on the sale of facilities to the company’s third fund (sales of JPY3.3bn and operating profit of JPY500mn).

Property Revitalization & Liquidation segment

Sales came to JPY4.6bn (+187.4% YoY) and segment profit JPY1.2bn (+303.1% YoY).

- ▷ Settlements for large projects in Q2 contributed to earnings. Sales and profit both increased significantly even after factoring out one-time gains from the sale of real estate.
- ▷ Both sales and profit in the land rights management business rose, with sales roughly doubling YoY and profit reaching JPY560mn (+87.7% YoY). In addition to residential land rights, the company started obtaining commercial land rights. For residential land rights, the company expanded beyond the Tokyo metropolitan area and started obtaining rights in the Kansai area with the aim of further strengthening the land rights management business.
- ▷ The sale of the company’s real estate asset (Kanda Kyodo Building), which it had transferred to real estate for sale, was completed (sold for approximately JPY1.4bn, profit of approximately JPY600mn), contributing significantly to the increase in earnings.

FY12/19 full-year company forecasts

Overview

For full-year FY12/19, Arealink forecasts sales of JPY29.0bn (+0.6% YoY), operating profit of JPY2.8bn (+0.6% YoY; includes a JPY1.1bn one-time gain comprising a JPY600mn gain on the sale of real estate and a JPY500mn gain on the sale of storage with land to a fund), recurring profit of JPY2.7bn (+6.4% YoY), and net income of JPY1.5bn (-17.1% YoY).

The company raised its sales and operating profit forecasts for the Property Management segment by JPY1.8bn and JPY369mn, respectively (versus forecasts announced in April). At the same time, it lowered its sales and operating profit forecasts for the Property Revitalization & Liquidation segment by JPY705mn and JPY229mn, respectively to reflect ongoing efforts related to the acquisition of commercial land rights and expansion into

Kansai heading into next year. On a companywide basis, these changes amounted to upward revisions of JPY1.1bn for sales and JPY106mn for operating profit.

Medium-term strategy (FY12/18 to FY12/20)

Strategy shift

According to its medium-term plan (FY12/18–FY12/20) announced in FY12/18, Arealink aimed to grow its earnings primarily in the self-storage brokerage business. However, recognizing during FY12/18 the possibility of a deteriorating business environment, an economic slump, and restrained lending by financial institutions, the company shifted its strategy in FY12/19, aiming to achieve a profit structure not susceptible to economic cycles.

Earnings outlook

Arealink expects earnings to weaken, albeit temporarily, in FY12/19 and FY12/20 due to the strategy shift. The company aims to lower its profit and sales weightings for the self-storage brokerage business and instead focus on the self-storage management business. However, it expects it will take one to two years to raise occupancy rates at the self-storage management business and secure related profit contributions. From FY12/21 onward, the company expects 20% or higher growth in operating profit in the self-storage management and brokerage businesses and the land rights management business. It also aims to add profit from niche property businesses.

Basic approach

In light of its recognition of the possibility of a deteriorating business environment, an economic slump, and restrained lending by financial institutions, Arealink will focus on achieving a profit structure not overly susceptible to economic cycles (enhancing its recurring-revenue businesses) and securing adequate cash to avoid lost opportunities.

- Shift to profit structure not susceptible to economic cycles (1): Shift exit strategy for storage facilities with land from selling to holding and custom building for sale, with a focus on self-storage management
- Shift to profit structure not susceptible to economic cycles (2): Strengthen the land rights management business
- Secure adequate cash to prepare for changes in business environment: Maintain cash and deposits of about JPY10.0bn, which will allow the company to acquire properties at bargain prices when the real estate market slumps
- Creation of new businesses: Develop and enhance niche businesses that will permit stable growth (for example, business storage with workspace, hobby-related storage, and unit holding of a building)

Shift to profit structure not susceptible to economic cycles (1)

In FY12/18, in its core self-storage management and brokerage businesses, Arealink worked to transition in earnest from its conventional outdoor container-type storage to a new type of storage facility with land. From FY12/19 onward, it will shift its exit strategy for storage facilities with land from selling to holding and custom building for sale, with a focus on self-storage management. However, there will be no change of exit strategy for outdoor and indoor storage (unmanned trunk rooms).

Starting in FY12/19, the company has been developing its own indoor storage facilities. With these facilities, the company's sales are based on the rent collected from end-users, the same as when the company manages storage on behalf of investors, but expenses are different in that they comprise depreciation and sundry expenses including advertising costs.

Arealink says expenses related to holding its own properties are lower than the subleasing expenses, allowing it to move into the black faster. With the conventional method of selling facilities to investors and then managing the facilities under a sublease agreement, the occupancy rate to reach the breakeven point was about 70%, and it took about 18 months from the time the company began managing a facility to move into the black. By contrast, in the event the company holds its own properties, the occupancy rate to reach the breakeven point is about 40%, and it takes only about 12 months to move into the black.

Shift to profit structure not susceptible to economic cycles (2): Strengthen land rights management business

In the land rights management business, Arealink obtains land rights based on the former Land Lease Law (such as when an estate is settled) and sells these to lessees at an appropriate time after negotiating rights usage. The company thinks this business has solid prospects.

Strengths and Weaknesses

Strengths

- **Rapid growth from nationwide branding as the leading specialist in the niche market of self-storage:** Arealink has become a major player in the domestic self-storage market by concentrating on storage and rolling out a nationwide brand (Hello Storage). The company's two-pronged sales strategy leverages marketing based on data analysis and sign-based marketing, and gives the company a competitive edge. If the company is able to win contracted storage orders from its nationwide rollout and further grow market share, it should be able to reap the benefits of economies of scale.
- **Stable recurring revenue platform:** In the self-storage business Arealink is increasing unit numbers while maintaining relatively stable occupancy rates and average prices. This is a classic example of a recurring revenue business. As such, the company has improved its balance sheet by reducing interest-bearing debt and building up cash and cash equivalents, and is operating effectively debt-free. The company now has a stable earnings platform resilient to market fluctuations.
- **Management skills of founder and CEO and flexible chain of command:** The company's track record relies extensively on the management skills of founding CEO Hayashi. In order to introduce flexibility to the chain of command, the company has established a workplace structure where managers including the CEO can help bring out results from lower-ranked employees. CEO Hayashi is testing and evaluating structures that will ensure that the company functions in his absence. The aim is to build a structure where all employees from top management down can take leadership.

Weaknesses

- **Property owners can cancel lease contracts:** In the Property Management segment, the company enters long-term leasing contracts (usually 10 years) as the lessee with individual property owners. However, it is possible to unilaterally break a contract by paying a penalty fee, which may hinder stable management in the long term. In fact, since Arealink launched this business through end 2016, property owners canceled contracts before expiry in 64 cases.
- **Strengthened regulations and poor reputation of outdoor storage:** For outdoor storage units, the MLIT has notified the construction divisions of local governments of the need for building verification applications under the Construction Standards Law. Since the notification was issued the company has been applying for verification when newly installing outdoor storage units, but if these

regulations are extended to containers that it has already installed, this may result in unforeseen costs. Many Japanese consumers have a poor image regarding the safety and quality of outdoor storage containers, and there is increasing criticism of containers not being compliant with building standards.

- **Low barriers to entry making it likely that more players will enter the market:** The real estate industry is struggling to cope with Japan's population decline and dramatic shifts in the external environment such as evolving customer needs and fluctuating market conditions. The self-storage industry already has a plethora of participants and barriers to entry are low. Arealink has not created barriers to entry such as patents that would legally prevent other companies from running similar businesses, and its business model is simple, meaning other companies may follow Arealink into the self-storage market. However, the company is working to differentiate itself by adopting favorable points from management strategies learned in other industries such as IT and distribution, so it could be said, in a sense, that it is building its own distinctive barriers to entry. In fact, this approach is proving successful, helping it to increase its market share each year.

Income statement

Income statement (JPYmn)	FY12/10 Parent	FY12/11 Parent	FY12/12 Parent	FY12/13 Parent	FY12/14 Parent	FY12/15 Parent	FY12/16 Parent	FY12/17 Parent	FY12/18 Parent	FY12/19 Par. Est.
Sales	11,143	10,604	10,124	12,256	18,120	17,174	16,908	21,489	28,828	29,000
YoY	-8.5%	-4.8%	-4.5%	21.1%	47.8%	-5.2%	-1.5%	27.1%	34.2%	0.6%
Cost of sales	8,967	8,238	7,494	8,950	13,759	12,100	12,136	15,806	22,173	
YoY	-9.1%	-8.1%	-9.0%	19.4%	53.7%	-12.1%	0.3%	30.2%	40.3%	-
Cost ratio	80.5%	77.7%	74.0%	73.0%	75.9%	70.5%	71.8%	73.6%	76.9%	-
Gross profit	2,176	2,365	2,630	3,306	4,361	5,073	4,771	5,683	6,655	
YoY	-6.1%	8.7%	11.2%	25.7%	31.9%	16.3%	-6.0%	19.1%	17.1%	-
GPM	19.5%	22.3%	26.0%	27.0%	24.1%	29.5%	28.2%	26.4%	23.1%	-
SG&A expenses	1,169	1,321	1,464	1,801	2,125	2,416	2,836	3,304	3,873	-
YoY	-2.3%	13.0%	10.9%	23.0%	18.0%	13.7%	17.4%	16.5%	17.2%	-
SG&A ratio	10.5%	12.5%	14.5%	14.7%	11.7%	14.1%	16.8%	15.4%	13.4%	-
Operating profit	1,007	1,045	1,165	1,505	2,235	2,658	1,936	2,380	2,782	2,800
YoY	-10.2%	3.8%	11.6%	29.2%	48.5%	18.9%	-27.2%	22.9%	16.9%	0.6%
OPM	9.0%	9.9%	11.5%	12.3%	12.3%	15.5%	11.4%	11.1%	9.7%	9.7%
Non-operating income	28	79	61	114	63	49	93	149	57	-
YoY	-52.5%	181.5%	-22.4%	86.4%	-44.7%	-22.4%	90.2%	60.3%	-61.6%	-
% of sales	0.3%	0.7%	0.6%	0.9%	0.3%	0.3%	0.6%	0.7%	0.2%	-
Non-operating expenses	260	169	151	185	211	265	60	87	302	-
YoY	-26.3%	-35.1%	-10.7%	22.5%	14.1%	25.4%	-77.3%	45.4%	246.5%	-
% of sales	2.3%	1.6%	1.5%	1.5%	1.2%	1.5%	0.4%	0.4%	1.0%	-
Rcurring profit	775	954	1,075	1,434	2,087	2,442	1,969	2,441	2,537	2,700
YoY	-6.3%	23.1%	12.8%	33.3%	45.6%	17.0%	-19.4%	24.0%	3.9%	6.4%
RPM	7.0%	9.0%	10.6%	11.7%	11.5%	14.2%	11.6%	11.4%	8.8%	9.3%
Net income	673	773	948	1,347	1,541	1,551	1,142	1,547	1,810	1,500
YoY	20.8%	14.7%	22.7%	42.0%	14.4%	0.6%	-26.3%	35.4%	17.0%	-17.1%
Net margin	6.0%	7.3%	9.4%	11.0%	8.5%	9.0%	6.8%	7.2%	6.3%	5.2%

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

Per-share data (JPY)

Per-share data (split-adjusted; JPY)	FY12/10 Parent	FY12/11 Parent	FY12/12 Parent	FY12/13 Parent	FY12/14 Parent	FY12/15 Parent	FY12/16 Parent	FY12/17 Parent	FY12/18 Parent	FY12/19 Par. Est.
Shares issued (year-end)	12,576	12,576	12,576	12,576	12,576	12,576	12,576	12,576	12,941	
EPS	54.8	62.90	77.20	109.7	125.5	126.32	93.06	126.08	145.47	118.76
EPS (fully diluted)	-	-	-	-	-	-	-	-	145.46	-
Dividend per share	0.00	0.00	0.00	25.00	36.00	39.00	39.00	40.00	46.00	40.00
Book value per share	750.6	813.5	890.8	1000.5	1100.9	1191.4	1245.1	1332.9	1484.44	-

Source: Shared Research based on company data

Notes: Figures may differ from company materials due to differences in rounding methods.
The company conducted a 50-for-1 stock split on August 31, 2011. BPS and EPS have been adjusted.

Balance sheet

Balance sheet (JPYmn)	FY12/10 Parent	FY12/11 Parent	FY12/12 Parent	FY12/13 Parent	FY12/14 Parent	FY12/15 Parent	FY12/16 Parent	FY12/17 Parent	FY12/18 Parent
Current assets	4,929	5,504	5,753	10,828	10,115	9,122	12,169	17,532	25,948
Cash and deposits	1,034	2,819	3,085	3,591	5,432	6,415	7,159	6,594	9,673
Inventories	2,810	1,704	1,814	6,321	3,714	1,855	4,232	10,063	15,347
Other	1,085	981	854	916	969	852	778	875	928
Fixed assets	13,772	11,762	12,860	12,189	9,423	10,191	11,623	12,372	11,915
Tangible fixed assets	12,524	10,529	10,888	10,544	8,169	8,871	10,005	10,648	9,742
Intangible fixed assets	228	152	103	84	67	86	107	135	178
Investments and other assets	1,019	1,081	1,869	1,562	1,188	1,234	1,511	1,589	1,995
Total assets	18,701	17,266	18,612	23,017	19,539	19,313	23,792	29,905	37,862
Current liabilities	2,137	2,138	1,780	3,207	2,463	2,881	4,959	5,692	6,607
Interest-bearing debt	1,154	1,046	815	1,792	461	690	2,516	2,719	3,516
Other	983	1,092	966	1,415	2,002	2,191	2,443	2,973	3,091
Fixed liabilities	7,350	5,141	5,898	7,528	3,562	1,806	3,549	7,862	12,505
Interest-bearing debt	5,925	4,160	4,730	6,045	2,298	621	2,016	5,912	9,893
Other	1,425	981	1,167	1,483	1,264	1,185	1,533	1,950	2,613
Total liabilities	9,486	7,278	7,678	10,735	6,025	4,686	8,508	13,553	19,113
Total net assets	9,215	9,987	10,935	12,282	13,514	14,626	15,284	16,351	18,750
Total liabilities and net assets	18,701	17,265	18,613	23,017	19,539	19,313	23,792	29,905	37,862

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

Cash flow statement

(JPYmn)	FY12/10 Parent	FY12/11 Parent	FY12/12 Parent	FY12/13 Parent	FY12/14 Parent	FY12/15 Parent	FY12/16 Parent	FY12/17 Parent	FY12/18 Parent
Cash flows from operating activities	2,533	2,641	443	1,014	7,123	3,941	-709	-2,993	-2,381
Cash flows from investing activities	-588	1,080	-489	-2,764	146	-1,069	-1,544	-1,424	-484
Cash flows from financing activities	-2,713	-1,937	311	2,256	-5,429	-1,888	3,000	3,855	5,944

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

Financial indicators

	FY12/10 Parent	FY12/11 Parent	FY12/12 Parent	FY12/13 Parent	FY12/14 Parent	FY12/15 Parent	FY12/16 Parent	FY12/17 Parent	FY12/18 Parent
ROA (RP-based)	3.4%	4.3%	5.3%	6.5%	7.2%	8.0%	5.3%	5.8%	5.3%
ROE	7.6%	8.0%	9.1%	11.6%	11.9%	11.0%	7.6%	9.8%	10.3%
Inventory turnover	2.8	3.6	4.3	2.2	2.7	4.3	4.0	2.2	1.7
Tangible fixed assets turnover	0.9	1.0	0.9	1.2	2.2	1.9	1.7	2.0	3.0
Current ratio	230.7%	257.4%	323.2%	337.6%	410.7%	316.7%	245.4%	308.0%	392.7%
Equity ratio	49.3%	57.8%	58.8%	53.4%	69.2%	75.7%	64.2%	54.7%	49.5%

Source: Shared Research based on company data

Historical performance

Full-year FY12/18 results

Overview

FY12/18 results: Sales of JPY28.8bn (+34.2% YoY), operating profit of JPY2.8bn (+16.9% YoY), recurring profit of JPY2.5bn (+3.9% YoY), and net income of JPY1.8bn (+17.0% YoY). Both the Property Management and Property Revitalization & Liquidation segments posted higher sales and profit. Recurring profit increased at a slower rate than operating profit due to increased commission fees paid and other factors. Net income rose YoY on a decrease in total income taxes.

Performance by segment

Property Management segment

Sales of 25.1bn (+28.1% YoY) and segment profit of JPY3.4bn (+9.9% YoY)

The company intensified the opening of a new type of indoor storage facilities with land at income-producing properties. This makes it possible to open facilities in densely populated areas where it was impossible to open facilities of the conventional outdoor storage container type, and unearthing new customer demand. Further, the company attracted demand from investors wishing to purchase nonresidential investment real-estate and sold storage facilities with land by establishing two private funds.

Self-storage management

Sales of JPY11.3bn (+13.9% YoY), gross profit of JPY2.5bn (-5.9% YoY), GPM of 22.0% (-4.6pp YoY), operating profit of JPY1.5bn (-18.4% YoY), and OPM of 12.9% (-5.1pp YoY)

Sales were up on an increase in the total number of storage units and a higher occupancy rate. As of end December 2018, the total number of storage units was 91,545 (+12.2% YoY), including 69,120 outdoor (+8.7% YoY) and 22,425 indoor storage units (+24.7% YoY). The occupancy rate was 75.6% (versus 73.3% at end December 2017). Gross profit declined. The GPM fell due to marketing measures to raise the occupancy rates at properties completed in FY12/16 and FY12/17, building verification expenses for outdoor warehouses (excluding storage facilities with land), and booking of allowance for subleasing losses. Regarding the outdoor warehouses (excluding storage facilities with land) completed in FY12/16 and FY12/17, as a result of having increased the number of facilities, facility opening standards in some regions fell, causing occupancy rates to drop in those regions. From FY12/19 onward though, the company says it will be able to improve occupancy rates without having to implement marketing measures through the establishment of more stringent opening standards. Operating profit fell on higher SG&A expenses accompanying sales growth.

Self-storage brokerage

Sales of JPY11.9bn (+54.4% YoY), gross profit of JPY2.4bn (+40.6% YoY), GPM of 20.0% (-2.0pp YoY), operating profit of JPY1.4bn (+75.0% YoY), and OPM of 11.6% (+1.4pp YoY)

Sales growth was attributed to the sale of storage facilities with land, with Arealink selling 38 such facilities (versus 15 in FY12/17). Gross profit increased on higher sales, but the GPM fell. The company says the decline in GPM was due to an unfavorable change in the sales mix with an increase in the share of storage facilities with land, which have a lower profit margin than outdoor storage facilities. Operating profit grew substantially thanks to only a 10.6% YoY increase in SG&A expenses versus a 40.6% rise in gross profit.

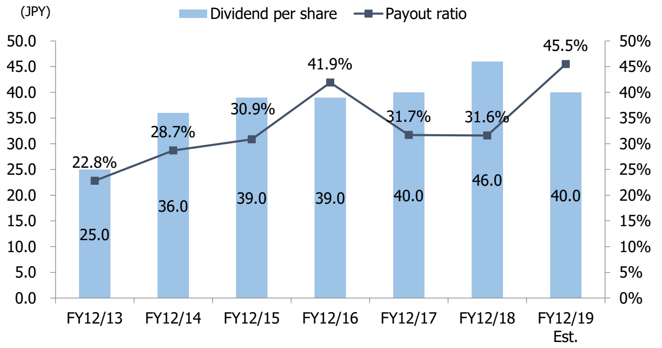
Property Revitalization & Liquidation segment

Sales of JPY3.7bn (+97.8% YoY) and segment profit of JPY651mn (+40.2% YoY)

The company has been focusing on the land rights management business, which is relatively unaffected by fluctuations in real estate prices, and engaging in the sale and purchase of land rights.

Shareholder returns

Dividends



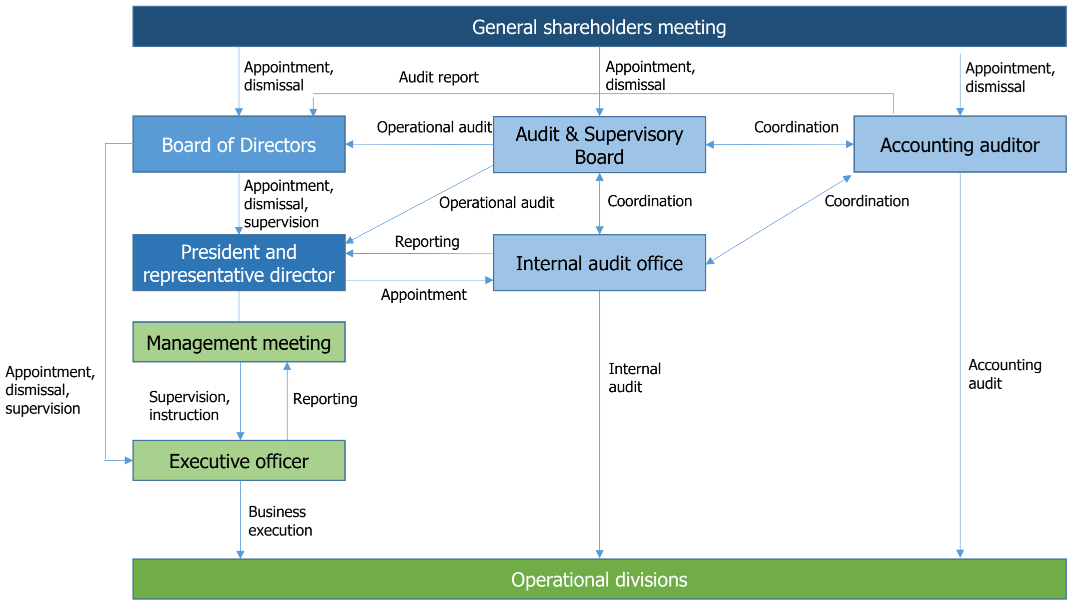
Source: Shared Research based on company data

Shareholders

Top shareholders	Shares held	Shareholding ratio
Naomichi Hayashi	2,813,660	22.27%
Goldman, Sachs & Co. Reg (Standing proxy: Goldman Sachs Securities Co., Ltd.)	1,217,554	9.63%
The Master Trust Bank of Japan, Ltd. (Trust account)	765,400	6.05%
Trust & Custody Services Bank, Ltd. (Trust B account)	467,700	3.70%
Japan Trustee Services Bank, Ltd. (Trust account)	399,700	3.16%
Niihama Iron Works Co., Ltd.	310,000	2.45%
Amix Co., Ltd.	250,000	1.97%
SMBC Nikko Securities Inc.	207,900	1.64%
THE BANK OF NEW YORK MELLON 140042 (Standing proxy: Mizuho Bank, Ltd. Settlement Department)	197,109	1.56%
Arealink Trade Partners Shareholding Association	184,100	1.45%
Sum	6,813,123	53.93%

Source: Shared Research based on company data (as of end December 2018)
Note: Excludes 309,931 shares of the treasury stock

Corporate governance



Source: Shared Research based on company data

Contact Details

Shared Research Inc.
3-31-12 Sendagi Bunkyo-ku Tokyo, Japan
https://sharedresearch.jp
Phone: +81 (0)3 5834-8787
Email: info@sharedresearch.jp