ARATA CORPORATION / 2733

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Research Coverage Report by Shared Research Inc.

INDEX

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

Executive summary

Business overview

- ARATA CORPORATION mainly wholesales everyday items and cosmetics, which it buys from manufacturers. The goods are delivered to the company's logistics centers, where they are sorted and dispatched to retailers to whom they are sold. The company is one of just two major Japanese wholesalers specializing in everyday items, the other being PALTAC (TSE1: 8283). These two companies have a combined market share of nearly 50%. ARATA handles around 100,000 items such as cosmetics (Health & Beauty product category), detergents, and paper products bought from some 1,200 Japanese and overseas manufacturers. The company wholesales these products to Japanese retailers (around 45,000 stores operated by 3,500 companies, including almost all domestic drugstores, supermarkets, and DIY centers). In FY03/20, ARATA posted sales of JPY796.2bn, and we estimate this figure would be around JPY1tn on a retail basis (converted to instore retail prices). The volume of items it handles is equivalent to that of top-10-ranking retailers in Japan. Upon receiving an order from a retailer, the company's role is to deliver the right quantity of the right products to the right location at the right time.
- Over the past five years, the company's GPM trended slightly over 10%. Shared Research thinks the company has four major sources of added value: First, it has the logistics capabilities to respond accurately to small-lot orders. Second, because the company handles such a wide range of items, it can serve as a one-stop wholesaler. Third, the company can offer proposals that connect manufacturer promotions with instore retail methods. Fourth, the company has a vast store of transaction data, which it sometimes sells to retailers and manufacturers.
- ARATA was formed in 2002 as a result of the business combination of three wholesalers. The company thinks of the first 15 years since its formation as its first stage, and positions FY03/18 to FY03/20, the period of its current medium-term management plan, as the time for stepping up to the second stage of growth. During this stage, it intends to pursue new possibilities in the wholesaling industry.

Trends and outlook

- Full-year FY03/20 results were sales of JPY796.2bn (+5.5% YoY), operating profit of JPY9.3bn (+4.9% YoY), recurring profit of JPY10.1bn (+7.4% YoY) and net income of JPY7.2bn (+4.2% YoY). GPM decreased from 10.4% in FY03/19 to 10.3% in FY03/20, but the SG&A ratio (SG&A expenses to sales) fell from 9.2% to 9.1% over the same period as a result of limiting the YoY rise in SG&A expenses to 4.6%. While logistics costs increased, ARATA was able to limit the rise in indirect expenses through the consolidation of operations and other means, and this contributed to the improved SG&A ratio. In Q4 alone, sales rose 10.2% YoY on sharp growth in sales of paper products amid the novel coronavirus pandemic.
- Forecast for FY03/21: For FY03/21 the company forecasts sales of JPY810.0bn (+1.7% YoY), operating profit of JPY10.2bn (+9.4% YoY), recurring profit of JPY10.8bn (+6.2% YoY), net income of JPY7.3bn (+1.5% YoY), and EPS of JPY428.0. The company had originally decided not to publish an outlook for the year, but has now announced an earnings forecast based on the situation in Q1. The company anticipates that sales of infection-mitigating products such as masks, disinfectants, and hand soaps will remain high. In line with its strategy up to this point, it also aims to increase sales of cosmetics, which have relatively high profit margins.
- In August 2020, the company announced a new medium-term management plan (FY03/21 to FY03/23). For FY03/23, it is targeting sales of JPY845.0bn (CAGR of 2.0% over three years), operating profit of JPY11.5bn (7.2%), recurring profit of JPY12.0bn (5.8%), ROE of over 9% but less than 10% (8.8% in FY03/20), and an equity ratio of 33–35% (33.2%). The company aims for competitive sales activities and low-cost operations. To do so, it will focus on product development and retail space proposals founded on marketing efforts that reflect the digital technology-driven changes in consumer lifestyles and values. It will also make use of the labor-saving logistics centers that leverage the latest technology.

Strengths and weaknesses

Shared Research thinks the company's strengths are: 1) the logistics capabilities to deliver the right quantity of the right products to the right location at the right time, 2) the ability to advise retailers about how to create highly effective retail spaces, and 3) the information it accumulated leveraging handling volume that would rank the company as a top-10 retailer on an instore retail price conversion basis (based on Shared Research estimates). We believe ARATA's weakness are its 1) relatively high logistics costs owing to its history of business combinations, 2) weak development capabilities overseas, where the company sees upstream and downstream growth opportunities, and 3) limited ability to respond to changing commercial channels amid the spread of e-commerce (see "Strengths and weaknesses" section for more details).

Key financial data

Income statement (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Est.
Sales	**606,705**	**616,327**	**651,954**	**638,792**	**676,743**	**704,610**	**732,914**	**754,447**	**796,227**	**810,000**
YoY	0.8%	1.6%	5.8%	-2.0%	5.9%	4.1%	4.0%	2.9%	5.5%	1.7%
Gross profit	**69,033**	**64,286**	**66,730**	**64,613**	**70,731**	**73,068**	**76,475**	**78,197**	**81,833**	**-**
YoY	-9.6%	-6.9%	3.8%	-3.2%	9.5%	3.3%	4.7%	2.3%	4.6%	-
GPM	11.4%	10.4%	10.2%	10.1%	10.5%	10.4%	10.4%	10.4%	10.3%	-
SG&A expenses	**64,859**	**60,560**	**62,258**	**62,152**	**65,032**	**65,684**	**67,618**	**69,305**	**72,507**	**-**
YoY	-14.7%	-6.6%	2.8%	-0.2%	4.6%	1.0%	2.9%	2.5%	4.6%	-
SG&A ratio	10.7%	9.8%	9.5%	9.7%	9.6%	9.3%	9.2%	9.2%	9.1%	-
Operating profit	**4,174**	**3,726**	**4,472**	**2,461**	**5,699**	**7,384**	**8,857**	**8,892**	**9,326**	**10,200**
YoY	-	-10.7%	20.0%	-45.0%	131.6%	29.6%	19.9%	0.4%	4.9%	9.4%
OPM	0.7%	0.6%	0.7%	0.4%	0.8%	1.0%	1.2%	1.2%	1.2%	1.3%
Recurring profit	**3,915**	**3,605**	**4,388**	**2,469**	**5,811**	**7,842**	**9,439**	**9,429**	**10,124**	**10,750**
YoY	-8.0%	-7.9%	21.7%	-43.7%	135.4%	35.0%	20.4%	-0.1%	7.4%	6.2%
RPM	0.6%	0.6%	0.7%	0.4%	0.9%	1.1%	1.3%	1.2%	1.3%	1.3%
Net income	**1,628**	**1,768**	**2,435**	**1,124**	**3,244**	**4,863**	**6,361**	**6,903**	**7,191**	**7,300**
YoY	60.4%	8.6%	37.7%	-53.8%	188.6%	49.9%	30.8%	8.5%	4.2%	1.5%
Net margin	0.3%	0.3%	0.4%	0.2%	0.5%	0.7%	0.9%	0.9%	0.9%	0.9%
Per share data (split-adjusted; JPY)										
Shares outstanding (ex. treasury shares; mn)	15.4	15.4	15.4	15.4	15.4	14.7	16.7	17.7	17.1	-
EPS	105.6	114.7	158.0	73.0	210.4	331.0	399.1	397.7	413.0	428.0
EPS (fully diluted)	-	-	-	-	-	294.9	377.8	381.2	391.3	-
Dividend per share	40.0	40.0	50.0	50.0	55.0	65.0	75.0	80.0	85.0	90.0
Book value per share	3,068	3,180	3,309	3,496	3,628	4,055	4,285	4,547	4,861	-
Balance sheet (JPYmn)										
Cash and cash equivalent	9,985	8,108	10,965	11,800	14,119	13,693	17,826	19,798	18,547	
Total current assets	**143,020**	**145,806**	**158,015**	**143,906**	**151,873**	**153,455**	**171,256**	**175,156**	**181,744**	
Tangible fixed assets	44,897	45,980	48,772	51,896	50,841	50,248	51,041	49,022	48,940	
Investments and other assets	10,332	10,804	10,124	11,890	13,194	15,695	17,905	15,776	15,321	
Intangible fixed assets	4,255	4,108	4,289	4,147	3,781	3,576	3,495	3,659	3,706	
Total assets	**202,506**	**206,699**	**221,202**	**211,840**	**219,689**	**222,974**	**243,698**	**243,614**	**249,712**	
Short-term debt	42,934	35,380	37,069	35,271	38,017	28,147	32,653	17,945	22,700	
Total current liabilities	**115,798**	**116,515**	**122,910**	**122,414**	**129,756**	**124,003**	**145,831**	**129,829**	**136,239**	
Long-term debt	29,042	30,904	38,048	27,157	24,215	27,930	14,648	21,861	18,981	
Total fixed liabilities	**39,384**	**41,140**	**47,251**	**35,515**	**33,992**	**39,358**	**26,394**	**33,269**	**30,571**	
Total liabilities	**155,182**	**157,655**	**170,161**	**157,929**	**163,748**	**163,361**	**172,226**	**163,099**	**166,811**	
Shareholders' equity (adjusted)	47,306	49,023	51,017	53,897	55,923	59,605	71,462	80,499	82,890	
Total net assets	**47,324**	**49,044**	**51,041**	**53,911**	**55,941**	**59,613**	**71,472**	**80,515**	**82,901**	
Total interest-bearing debt	68,707	62,566	70,872	58,637	58,982	52,569	43,640	36,524	37,739	
Statement of cash flows (JPYmn)										
Cash flows from operating activities	-720	9,959	1,481	21,955	7,594	12,637	11,649	9,513	5,262	
Cash flows from investing activities	-4,575	-4,054	-5,878	-6,775	-3,360	-3,155	-2,924	-880	-2,742	
Cash flows from financing activities	5,257	-7,699	7,246	-13,990	-1,791	-9,948	-4,501	-6,678	-3,833	
Finantial ratios										
ROA (RP-based)	2.0%	1.8%	2.1%	1.1%	2.7%	3.5%	4.0%	3.9%	4.1%	
ROE	3.5%	3.7%	4.9%	2.1%	5.9%	8.4%	9.7%	9.1%	8.8%	
Equity ratio	23.4%	23.7%	23.1%	25.4%	25.5%	26.7%	29.3%	33.0%	33.2%	

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

Recent updates

Highlights

On October 8, 2020, Shared Research updated the report following interviews with ARATA CORPORATION.

On September 16, 2020, the company announced a comprehensive business alliance with Chinese company Guangzhou Public Investment Holding Group Co., Ltd (GPIHG).

The company has entered into a comprehensive business alliance agreement with GPIHG in China, which operates business spanning the entire supply chain, from manufacture and wholesale of everyday items to B2C sales on its e-commerce site. The company operates a wholesale business primarily for home goods through subsidiary Kairaotai (Shanghai) Trading Co., Ltd., but the company thought that with the globalization of the business environment it would take time to become competitive and achieve growth under its current structure. As a future growth strategy, the company decided that it required a partner company with which it could collaborate in good faith on business operations from manufacture to sale, and arrived at this comprehensive business alliance. GPIHG aims to enhance operational management by incorporating the wholesale category strategy and management know-how cultivated by the company over many years, in order to achieve further growth in the Chinese market.

The business alliance comprises the following five main points: 1) the sale in China of quality products manufactured in Japan; 2) doing business with outstanding factories in China; 3) the sale in Japan of quality products manufactured in China; 4) the procurement of quality products from countries other than Japan or China; and 5) the implementation of quality logistics and supply chain management through both Japan and China.

The company expects the impact of the alliance on its FY03/21 results to be minor. If it becomes apparent that the alliance will have a significant impact on results, the company will make prompt disclosure to that effect.

On August 4, 2020, the company announced earnings results for Q1 FY03/21; see the results section for details.

For previous releases and developments, please refer to the “News and topics” section.

Trends and outlook

Quarterly trends and results

Cumulative	FY03/19				FY03/20				FY03/21	FY03/21	
(JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	% of Est.	FY Est.
Sales	191,872	381,081	578,125	754,447	195,393	406,341	601,901	796,227	211,915	26.2%	810,000
YoY	4.4%	3.1%	3.2%	2.9%	1.8%	6.6%	4.1%	5.5%	8.5%		1.7%
Gross profit	19,865	39,204	59,427	78,198	20,295	41,435	61,766	81,833	21,835		
YoY	3.3%	2.5%	2.6%	2.3%	2.2%	5.7%	3.9%	4.6%	7.6%		
GPM	10.4%	10.3%	10.3%	10.4%	10.4%	10.2%	10.3%	10.3%	10.3%		
SG&A expenses	17,379	34,726	52,499	69,306	17,804	36,399	54,512	72,507	18,344		
YoY	3.6%	2.8%	2.9%	2.5%	2.4%	4.8%	3.8%	4.6%	3.0%		
SG&A ratio	9.1%	9.1%	9.1%	9.2%	9.1%	9.0%	9.1%	9.1%	8.7%		
Operating profit	2,486	4,478	6,928	8,892	2,491	5,036	7,254	9,326	3,490	34.2%	10,200
YoY	1.2%	0.1%	0.0%	0.4%	0.2%	12.5%	4.7%	4.9%	40.1%		9.4%
OPM	1.3%	1.2%	1.2%	1.2%	1.3%	1.2%	1.2%	1.2%	1.6%		1.3%
Recurring profit	2,551	4,673	7,285	9,429	2,693	5,403	7,940	10,124	3,669	34.1%	10,750
YoY	-5.6%	-3.5%	-1.9%	-0.1%	5.6%	15.6%	9.0%	7.4%	36.2%		6.2%
RPM	1.3%	1.2%	1.3%	1.2%	1.4%	1.3%	1.3%	1.3%	1.7%		1.3%
Net income	1,760	3,332	5,208	6,903	2,070	3,861	5,827	7,191	2,476	33.9%	7,300
YoY	-1.9%	3.1%	0.1%	8.5%	17.6%	15.9%	11.9%	4.2%	19.6%		1.5%
Net margin	0.9%	0.9%	0.9%	0.9%	1.1%	1.0%	1.0%	0.9%	1.2%		0.9%

Quarterly	FY03/19				FY03/20				FY03/21
(JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Sales	191,872	189,209	197,044	176,322	195,393	210,948	195,560	194,326	211,915
YoY	4.4%	1.7%	3.6%	2.0%	1.8%	11.5%	-0.8%	10.2%	8.5%
Gross profit	19,865	19,339	20,223	18,771	20,295	21,140	20,331	20,067	21,835
YoY	3.3%	1.6%	2.9%	1.2%	2.2%	9.3%	0.5%	6.9%	7.6%
GPM	10.4%	10.2%	10.3%	10.6%	10.4%	10.0%	10.4%	10.3%	10.3%
SG&A expenses	17,379	17,347	17,773	16,807	17,804	18,595	18,113	17,995	18,344
YoY	3.6%	1.9%	3.3%	1.1%	2.4%	7.2%	1.9%	7.1%	3.0%
SG&A ratio	9.1%	9.2%	9.0%	9.5%	9.1%	8.8%	9.3%	9.3%	8.7%
Operating profit	2,486	1,992	2,450	1,964	2,491	2,545	2,218	2,072	3,490
YoY	1.2%	-1.2%	-0.2%	1.8%	0.2%	27.8%	-9.5%	5.5%	40.1%
OPM	1.3%	1.1%	1.2%	1.1%	1.3%	1.2%	1.1%	1.1%	1.6%
Recurring profit	2,551	2,122	2,612	2,144	2,693	2,710	2,537	2,184	3,669
YoY	-5.6%	-1.0%	1.2%	6.4%	5.6%	27.7%	-2.9%	1.9%	36.2%
RPM	1.3%	1.1%	1.3%	1.2%	1.4%	1.3%	1.3%	1.1%	1.7%
Net income	1,760	1,572	1,876	1,695	2,070	1,791	1,966	1,364	2,476
YoY	-1.9%	9.5%	-5.0%	46.6%	17.6%	13.9%	4.8%	-19.5%	19.6%
Net margin	0.9%	0.8%	1.0%	1.0%	1.1%	0.8%	1.0%	0.7%	1.2%

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

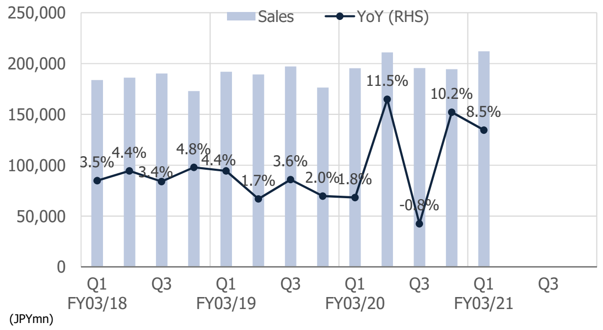
Seasonality: Sales and operating profit tend to be higher in Q3 (October–December) than in the other quarters, because product volume increases due to the year-end holiday shopping season and other factors.

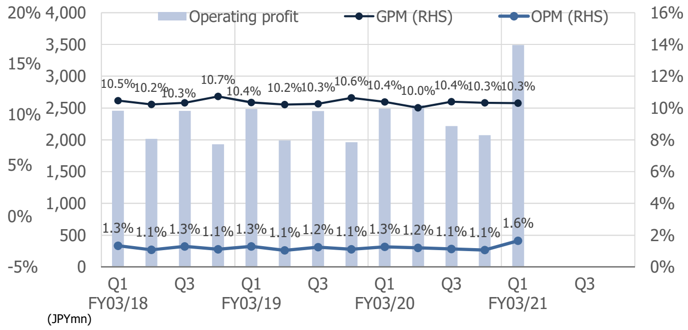
Q1 FY03/21 results (out August 4, 2020)

Summary

- Q1 FY03/21 results: Sales were JPY211.9bn (+8.5% YoY), operating profit was JPY3.5bn (+40.1% YoY), recurring profit was JPY3.7bn (+36.2% YoY), and net income was JPY2.5bn (+19.6% YoY). Although economic activity was subdued and inbound demand was curtailed due to the impact of the COVID-19 pandemic, Q1 results grew YoY thanks to the large variety of daily necessities ARATA handles, and the robust sales of infection-prevention items and home consumption-related goods. Gross profit increased 7.6% YoY, and the gross profit margin was 10.3%, slightly lower than the previous year (10.4%). The SG&A expenses were up 3.0% YoY, and the operating profit margin was 1.6%, higher than the previous year (1.3%).
- Forecast for FY03/21: The company forecasts sales of JPY810.0bn (+1.7% YoY), operating profit of JPY10.2bn (+9.4% YoY), recurring profit of JPY10.8bn (+6.2% YoY), net income of JPY7.3bn (+1.5% YoY), and EPS of JPY428.0. The company had originally decided not to publish an outlook for the year but has now announced a forecast of results based on the situation in Q1. Q2 sales are estimated at JPY208.1bn (-1.4% YoY), with operating profit estimated at JPY2.2bn (-13.2% YoY). The forecast for 2H sales are JPY390.0bn (in line with the previous year) and operating profit is JPY4.5bn (+4.9% YoY). The annual dividend forecast is JPY90 per share, revised upward from the original forecast of JPY85 per share.
- Medium-term management plan: At the same time as the Q1 financial results, the company announced a new medium-term management plan (FY2021 to FY2023). For FY03/23, the management is targeting sales of JPY845.0bn (CAGR of 2.0% over three years), operating profit of JPY11.5bn (7.2%), recurring profit of JPY12.0bn (5.8%), ROE of over 9% but less than 10% (8.8% in FY03/20), and an equity ratio of 33–35% (33.2%). The company aims for competitive sales activities and low-cost operations. To do so, it will focus on product development and retail space proposals founded on marketing efforts that reflect the digital technology-driven changes in consumer lifestyles and values. It will also make use of the labor-saving logistics centers that leverage the latest technology.

Sales (left); Operating profit and profit margins (right)





Source: Shared Research based on company data

By product category

Sales by product category

Sales by category	FY03/19				FY03/20				FY03/21
Quarterly (JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Total sales	191,872	189,209	197,044	176,322	195,393	210,948	195,560	194,326	211,915
YoY	4.4%	1.7%	3.6%	2.0%	1.8%	11.5%	-0.8%	10.2%	8.5%
Health & Beauty	59,217	59,854	61,897	56,869	60,927	65,560	63,373	60,113	65,004
YoY	10.6%	5.6%	5.4%	3.7%	2.9%	9.5%	2.4%	5.7%	6.7%
% of total sales	30.9%	31.6%	31.4%	32.3%	31.2%	31.1%	32.4%	30.9%	30.7%
Household	26,494	26,548	29,257	23,334	27,702	30,460	28,471	25,359	31,642
YoY	4.1%	2.8%	7.2%	4.4%	4.6%	14.7%	-2.7%	8.7%	14.2%
% of total sales	13.8%	14.0%	14.8%	13.2%	14.2%	14.4%	14.6%	13.0%	14.9%
Home Care	22,133	18,077	13,242	15,880	20,911	19,488	13,194	15,491	24,639
YoY	0.7%	-5.5%	-0.1%	-1.8%	-5.5%	7.8%	-0.4%	-2.4%	17.8%
% of total sales	11.5%	9.6%	6.7%	9.0%	10.7%	9.2%	6.7%	8.0%	11.6%
Paper Products	36,444	35,521	39,133	36,222	36,967	42,302	37,408	45,473	38,648
YoY	-1.1%	-1.6%	2.2%	0.8%	1.4%	19.1%	-4.4%	25.5%	4.5%
% of total sales	19.0%	18.8%	19.9%	20.5%	18.9%	20.1%	19.1%	23.4%	18.2%
Home Goods	12,151	13,229	15,248	11,617	12,794	14,802	14,954	12,732	14,255
YoY	-1.5%	-3.0%	-2.2%	-7.2%	5.3%	11.9%	-1.9%	9.6%	11.4%
% of total sales	6.3%	7.0%	7.7%	6.6%	6.5%	7.0%	7.6%	6.6%	6.7%
Pet Goods, other	35,433	35,976	38,268	32,396	36,089	38,336	38,161	35,158	37,724
YoY	5.6%	3.7%	3.3%	4.2%	1.9%	6.6%	-0.3%	8.5%	4.5%
% of total sales	18.5%	19.0%	19.4%	18.4%	18.5%	18.2%	19.5%	18.1%	17.8%

Source: Shared Research based on company data
Note: Figures for FY03/19 have been retroactively adjusted to reflect partial adjustments by the company to product categories in FY03/20.
Note: Figures may differ from company materials due to differences in rounding methods.

Q1 FY03/21 sales were up in all product categories. Sales in mainstay Health & Beauty (e.g., cosmetics, hair/body care products, and health products) were JPY65.0bn (+6.7% YoY). While sales of cosmetics were sluggish, sales for the category were up on a significant increase in hygiene product sales as the wearing of masks became commonplace and many adopted a habit of diligently disinfecting their hands with hand sanitizer. Sales in Household (e.g., laundry detergents and kitchen detergents) were JPY31.6bn (+14.2% YoY). It appears that people are doing laundry and cleaning more frequently since time spent at home has increased as well as hygiene awareness.

Sales in Home Care (including fragrances/deodorants and insect repellents) were JPY24.6bn (+17.8% YoY). Sales of pesticides were sluggish in Q1 FY03/20 due to unfavorable weather, but recovered to the typical level in Q1 FY03/21, which contributed to the YoY increase in the category sales. Sales in Paper Products (e.g., diapers and toilet paper) were JPY38.6bn (+4.6% YoY). While temporary panic buying has run its course, it appears that consumers are maintaining a certain level of inventory while continuing to purchase the amount they consume. Sales in Home Goods (e.g., kitchen consumables and toiletries) were JPY14.3bn (+11.4% YoY). Cooking-related products have become a driver of sales growth due to an expansion of at-home cooking-related demand. Sales in Pet Goods/Other were 37.7bn (+4.5% YoY).

We understand that the increase in sales was the result of the wide range of products that the company handles, along with its quick response in carrying out its role of connecting manufacturers and retailers.

By customer type

Sales by customer type

Sales by customer type Quarterly (JPYmn)	FY03/19 Q1	FY03/19 Q2	FY03/19 Q3	FY03/19 Q4	FY03/20 Q1	FY03/20 Q2	FY03/20 Q3	FY03/20 Q4	FY03/21 Q1
Total sales	191,872	189,209	197,044	176,322	195,393	210,948	195,560	194,326	211,915
YoY	4.4%	1.7%	3.6%	2.0%	1.8%	11.5%	-0.8%	10.2%	8.5%
Drugstores	93,862	91,728	94,822	87,943	96,433	101,650	96,511	97,317	106,313
YoY	6.4%	3.8%	6.7%	4.2%	2.7%	10.8%	1.8%	10.7%	10.2%
% of total sales	48.9%	48.5%	48.1%	49.9%	49.4%	48.2%	49.4%	50.1%	50.2%
DIY centers	32,667	31,461	33,168	26,927	31,830	34,064	31,168	29,758	34,363
YoY	4.7%	-0.4%	-0.9%	-1.4%	-2.6%	8.3%	-6.0%	10.5%	8.0%
% of total sales	17.0%	16.6%	16.8%	15.3%	16.3%	16.1%	15.9%	15.3%	16.2%
Supermarkets	23,569	23,481	24,622	22,118	23,368	26,250	24,107	24,858	26,063
YoY	1.9%	0.0%	1.9%	2.9%	-0.9%	11.8%	-2.1%	12.4%	11.5%
% of total sales	12.3%	12.4%	12.5%	12.5%	12.0%	12.4%	12.3%	12.8%	12.3%
Discount stores	13,642	14,139	14,767	13,183	14,328	16,124	14,800	14,250	14,788
YoY	2.1%	4.8%	4.6%	9.2%	5.0%	14.0%	0.2%	8.1%	3.2%
% of total sales	7.1%	7.5%	7.5%	7.5%	7.3%	7.6%	7.6%	7.3%	7.0%
General merchandising stores (GMS)	10,366	10,055	10,640	9,442	10,431	10,978	10,245	10,096	10,680
YoY	-5.8%	-7.3%	-2.8%	-3.3%	0.6%	9.2%	-3.7%	6.9%	2.4%
% of total sales	5.4%	5.3%	5.4%	5.4%	5.3%	5.2%	5.2%	5.2%	5.0%
Other	17,766	18,342	19,026	16,711	19,001	21,884	18,727	18,049	19,704
YoY	5.7%	0.5%	2.2%	-6.4%	7.0%	19.3%	-1.6%	8.0%	3.7%
% of total sales	9.3%	9.7%	9.7%	9.5%	9.7%	10.4%	9.6%	9.3%	9.3%

Source: Shared Research based on company data
Note: Figures for FY03/19 have been retroactively adjusted to reflect partial adjustments by the company to product categories in FY03/20.
Note: Figures may differ from company materials due to differences in rounding methods.

By customer type, supermarkets and drugstores drove sales in Q1. Sales to supermarkets increased significantly to JPY26.1bn (+11.5% YoY). It seems that consumers' tendency to refrain from going out as much as possible and to complete their shopping in their immediate neighborhoods has had an effect. Sales to drugstores were JPY106.3bn (+10.3% YoY). Sales to drugstore chains with many stores in central Tokyo stagnated due to a decrease in inbound demand, but sales to drugstore chains with many suburban stores were relatively strong. As for other customer types, sales to DIY centers were JPY34.4bn (+8.0% YoY), sales to discount stores were JPY14.8bn (+3.2% YoY), sales to general merchandising stores (GMS) were JPY10.7bn (+2.4% YoY), and sales to other customer types (including online and cross-border businesses) were JPY19.7bn (+3.7% YoY).

Cost drivers

In Q1 FY03/21, GPM was slightly down YoY to 10.3% (versus 10.4% in Q1 FY03/20). According to ARATA, the profitability of subsidiary Japell, which handles pet supplies, temporarily declined as the COVID-19 pandemic necessitated the cancellation of exhibitions that had been bringing in a certain amount of profit. However, the company has already implemented measures in response, and the decline in profitability is expected to be only temporary.

The company held SG&A expenses to JPY18.3 million yen (+3.0% YoY) in Q1. While sales increased 8.5% YoY, personnel expenses increased only 6.1% YoY, packing and transportation expenses increased only 5.5% YoY, and other expenses decreased 4.4% YoY. Utilization of temporary workers to meet an increase in logistics volume was a factor pushing up personnel expenses, but the company was able to control personnel expenses overall. Regarding packing and transportation expenses, the unit price of trucks has been on an uptrend due to labor shortages, but there is beginning to be room for price negotiations with logistics companies in light of slowdown of the economy as a whole. The main reason for the decrease in other expenses is that ARATA has used the COVID-19 pandemic as an opportunity to promote work style reforms, and as a result has been able to suppress travel/transportation expenses, entertainment expenses, and training expenses.

SG&A expenses

SG&A expenses Quarterly (JPYmn)	FY03/19 Q1	Q2	Q3	Q4	FY03/20 Q1	Q2	Q3	Q4	FY03/21 Q1
SG&A expenses	17,379	17,347	17,773	16,807	17,804	18,595	18,113	17,995	18,344
YoY	3.6%	1.9%	3.3%	1.1%	2.4%	7.2%	1.9%	7.1%	3.0%
Packing and transportation expenses	4,967	5,000	5,394	4,894	5,281	5,690	5,482	5,512	5,571
YoY	6.9%	5.9%	9.2%	8.1%	6.3%	13.8%	1.6%	12.6%	5.5%
Transportation and warehousing	3,788	3,843	4,073	3,667	3,962	4,326	4,159	4,246	4,249
YoY	5.7%	4.4%	7.0%	5.1%	4.6%	12.6%	2.1%	15.8%	7.2%
Distribution outsourcing	1,018	1,032	1,153	1,090	1,151	1,204	1,178	1,137	1,163
YoY	9.8%	12.9%	20.4%	21.4%	13.1%	16.7%	2.2%	4.3%	1.0%
Packing supplies	160	125	169	136	168	159	145	129	158
YoY	19.4%	-0.8%	-2.9%	-3.5%	5.0%	27.2%	-14.2%	-5.1%	-6.0%
Personnel expenses	7,547	7,474	7,500	7,164	7,579	7,959	7,690	7,681	8,045
YoY	2.4%	-2.0%	0.4%	-2.8%	0.4%	6.5%	2.5%	7.2%	6.1%
Other expenses	4,865	4,873	4,879	4,749	4,944	4,946	4,941	4,802	4,728
YoY	2.4%	4.3%	1.7%	0.5%	1.6%	1.5%	1.3%	1.1%	-4.4%

Source: Shared Research based on company data

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

Full-year FY03/21 company forecasts

	FY03/19			FY03/20			FY03/21		
(JPYmn)	1H	2H	FY	1H	2H	FY	1H Est.	2H Est.	FY Est.
Sales	**381,081**	**373,366**	**754,447**	**406,341**	**389,886**	**796,227**	**420,000**	**390,000**	**810,000**
YoY	3.1%	2.8%	2.9%	6.6%	4.4%	5.5%	3.4%	0.0%	1.7%
Cost of sales	341,877	334,372	676,249	364,906	349,488	714,394		-	-
Gross profit	**39,204**	**38,994**	**78,198**	**41,435**	**40,398**	**81,833**		**-**	**-**
YoY	2.5%	2.1%	2.3%	5.7%	3.6%	4.6%	-	-	-
GPM	10.3%	10.4%	10.4%	10.2%	10.4%	10.3%	-	-	-
SG&A expenses	34,726	34,580	69,306	36,399	36,108	72,507		-	-
YoY	2.8%	2.2%	2.5%	4.8%	4.4%	4.6%	-	-	-
SG&A ratio	9.1%	9.3%	9.2%	9.0%	9.3%	9.1%	-	-	-
Operating profit	**4,478**	**4,414**	**8,892**	**5,036**	**4,290**	**9,326**	**5,700**	**4,500**	**10,200**
YoY	0.1%	0.7%	0.4%	12.5%	-2.8%	4.9%	13.2%	4.9%	9.4%
OPM	1.2%	1.2%	1.2%	1.2%	1.1%	1.2%	1.4%	1.2%	1.3%
Recurring profit	**4,673**	**4,756**	**9,429**	**5,403**	**4,721**	**10,124**	**6,100**	**4,650**	**10,750**
YoY	-3.5%	3.5%	-0.1%	15.6%	-0.7%	7.4%	12.9%	-1.5%	6.2%
RPM	1.2%	1.3%	1.2%	1.3%	1.2%	1.3%	1.5%	1.2%	1.3%
Net income	**3,332**	**3,571**	**6,903**	**3,861**	**3,330**	**7,191**	**3,900**	**3,400**	**7,300**
YoY	3.1%	14.1%	8.5%	15.9%	-6.7%	4.2%	1.0%	2.1%	1.5%
Net margin	0.9%	1.0%	0.9%	1.0%	0.9%	0.9%	0.9%	0.9%	0.9%

Source: Shared Research based on company data

In FY03/21, the company forecasts sales of JPY810.0bn (+1.7% YoY), operating profit of JPY10.2bn (+9.4% YoY), recurring profit of JPY10.8bn (+6.2% YoY), net income of JPY7.3bn (+1.5% YoY), and EPS of JPY428.0. ARATA set its initial forecast as "TBD," but announced the above forecast on August 7 after taking into account the situation up to end-Q1. The company revised its annual dividend forecast upward to JPY90 per share from the initial forecast of JPY85 per share.

ARATA says it expects a gradual recovery in consumer activity, but was somewhat conservative in its forecast. The company's medium-term management plan calls for a CAGR for sales of 2.0% over the three years from FY03/21 to FY03/23, which is slightly more conservative than the FY03/21 forecast. The Q2 estimates—calculated from the company forecast—are for sales of JPY208.1bn (-1.4% YoY) and operating profit of JPY2.2bn (-13.2% YoY). In 2H, the company expects sales of JPY390.0bn (flat YoY) and operating profit of JPY4.5bn (+4.9% YoY).

In Q2, the company expects sales to be down YoY due to reactionary falloff from the rush demand in September 2019 before the consumption tax hike (implemented in October 2019). However, it is possible that sales will not fall as much as expected since product sales through August appear to be somewhat brisker than anticipated. In 2H, ARATA forecasts 2–3% YoY sales growth in Q3, and sales decline of around 2% YoY in Q4. The forecast of a YoY increase in Q3 was made in light of the decrease in demand after the consumption tax hike in Q3 FY03/20, while the forecast of a YoY decrease in Q4 was made in light of the sharp increase in sales of paper products related to COVID-19 in Q4 FY03/20.

By product category, ARATA expects cosmetics sales to gradually recover from its Q1 slump. The company sees the prospects of recovery in lip products as unlikely since the wearing of masks has become widespread, but says there is a gradual expansion in sales of eye makeup and skin care products. Cosmetics is a highly profitable product category, and an area in which the company places strategic emphasis, targeting growth. ARATA says it expects high, stable demand for products that mitigate infection risk such as masks, disinfectants, and hand soaps given the widespread adoption of mask-wearing and practice of hand sanitization. On the other hand, despite a strong performance through Q1 from products in the Household category such as laundry detergents and kitchen detergents and products in Home Goods such as cooking utensils, the company expects demand for these products will run its course and slow. ARATA plans to strengthen display proposals at retail stores in order to increase sales of products that are highly profitable for both retailers and wholesalers and are in strong demand from consumers.

The company expects a slight rise in GPM in FY03/21 compared to FY03/20. The company aims to gradually raise the profit margin by making sales floor proposals to retailers such as drugstores for products that enjoy strong consumer demand and can secure relatively high GPMs (cosmetics, products aimed at mitigating infection risk, Home Goods). The company is proactively starting to do business with more mid-sized manufacturers in Japan, with which it has had low transaction volume so far. It is also expanding its products aimed at mitigating infection risk.

ARATA expects SG&A expenses to increase by some 2% YoY. The company is using the opportunity presented by the implementation of COVID-19 countermeasures to review its sales activities and internal operations, and holding many meetings (between the head office and branch offices; between branch offices) online. ARATA expects to be able to suppress travel/transportation expenses compared to a typical year. In addition, truck freight costs have been on the rise due to labor shortages, but the company says there is room for negotiation due to slowdown in the economy as a whole. The company is also considering consolidation of its delivery partners in efforts to limit logistics cost increases.

Initial company forecast and results

Results vs. Initial Est. (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Sales (Initial Est.)	609,000	628,000	622,000	640,000	643,000	679,000	719,000	760,000	771,000
Sales (Results)	606,705	616,327	651,954	638,792	676,743	704,610	732,914	754,447	796,227
Results vs. Initial Est.	**-0.4%**	**-1.9%**	**4.8%**	**-0.2%**	**5.2%**	**3.8%**	**1.9%**	**-0.7%**	**3.3%**
Operating profit (Initial Est.)	400	-	4,700	4,550	4,250	6,600	8,100	9,700	9,300
Operating profit (Results)	4,174	3,726	4,472	2,461	5,699	7,384	8,857	8,892	9,326
Results vs. Initial Est.	**943.5%**	**-**	**-4.9%**	**-45.9%**	**34.1%**	**11.9%**	**9.3%**	**-8.3%**	**0.3%**
Recurring profit (Initial Est.)	4,300	4,800	4,400	4,400	4,300	6,700	8,300	10,000	10,000
Recurring profit (Results)	3,915	3,605	4,388	2,469	5,811	7,842	9,439	9,429	10,124
Results vs. Initial Est.	**-9.0%**	**-24.9%**	**-0.3%**	**-43.9%**	**35.1%**	**17.0%**	**13.7%**	**-5.7%**	**1.2%**
Net income (Initial Est.)	1,440	2,000	1,900	1,900	1,900	3,600	5,200	6,500	6,500
Net income (Results)	1,628	1,768	2,435	1,124	3,244	4,863	6,361	6,903	7,191
Results vs. Initial Est.	**13.1%**	**-11.6%**	**28.2%**	**-40.8%**	**70.7%**	**35.1%**	**22.3%**	**6.2%**	**10.6%**

Source: Shared Research based on company data

Medium-term outlook

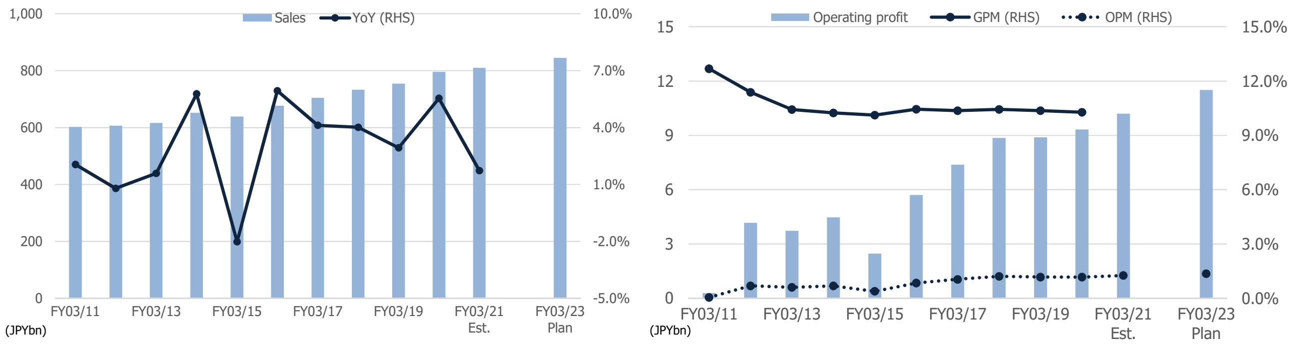
(JPYmn)	FY03/20 FY	FY03/21 Est.	FY03/23 Medium-term plan	3-year CAGR	FY03/30 Long-term vision	10-year CAGR
Sales	**796,227**	**810,000**	**845,000**	**2.0%**	**1,000,000**	**2.3%**
YoY	5.5%	1.7%	-		-	
Operating profit	**9,326**	**10,200**	**11,500**	**7.2%**	**-**	
YoY	4.9%	9.4%	-		-	
Operating profit margin	1.2%	1.3%	1.4%		-	
Recurring profit	**10,124**	**10,750**	**12,000**	**5.8%**	**-**	
YoY	7.4%	6.2%	-		-	
Recurring profit margin	1.3%	1.3%	1.4%		-	
ROE	8.8%	-	Over 9%, less than 10%		-	

Source: Shared Research based on company data

In August 2020, ARATA announced a new medium-term management plan (covering FY03/21 to FY03/23). For FY03/23, the plan targets sales of JPY845.0bn (three-year CAGR of 2.0%), operating profit of JPY11.5bn (7.2%), recurring profit of JPY12.0bn (5.8%), ROE of over 9% but less than 10% (versus 8.8% in FY03/20), and an equity ratio of 33–35% (versus 33.2% in FY03/20).

Previous medium-term management plan: Announced in May 2017, the previous medium-term management plan covered FY03/18 to FY03/20. The plan's slogan was "ARATA's second stage: pursuing new possibilities in wholesaling with a view to 10 years in the future." It specifically aimed to: 1) continue devising growth strategies, 2) lay the groundwork for the future, and 3) further strengthen the management base. The plan initially targeted sales of JPY760bn, recurring profit of JPY10bn, and net income of JPY6bn. In FY06/20, the company achieved these targets with sales of JPY796.2bn, recurring profit of JPY10.1bn, and net income of JPY7.2bn.

Sales (left) and operating profit and profit margins (right)



Source: Shared Research based on company data

The basic strategy of the current medium-term management plan is to achieve competitive sales activities and low-cost operations through marketing (product development and sales floor proposals) that takes into account changes in lifestyle and values due to progress of digital technology, and through labor-saving logistics centers using the latest technology. In following this strategy, the company plans to work on 1) expansion of growth potential, 2) improvement in productivity, and 3) strengthening management soundness.

Expansion of growth potential

ARATA plans to expand growth potential through rearrangement of the business and product composition and reinforcement of retail support and overseas business. The company handles about 100,000 items, mainly daily necessities. It expects relatively fast market expansion in the areas of health, hygiene, and cosmetics, and has confidence in its ability to secure profitability in these areas. The company aims to increase transaction volume by providing support to retailers. This includes providing information on top-selling products based on vast amounts of transaction data, proposing display configurations to stores, and providing promotional point-of-purchase (POP) displays (in-store advertising materials).

Although there is no change in ARATA's stance to center its business on the products of major manufacturers, the company intends to expand sales by selling company-exclusive products and enhancing its planning and development capabilities for products developed in-house that fill gaps in the company's product lineup (using outsourced production). Up until this point, ARATA has introduced unscented fabric softener "Fabrush" and deodorant mist "Yakuyou 24stock" to the market. The company plans to strategically strengthen its proprietary products in part because they have the effect of boosting customer retention.

Regarding sales channels, ARATA plans to strengthen its response to diversification of distribution, first and foremost through the e-commerce business. The company's main sales channels are drugstores, DIY centers, supermarkets, discount stores, and general merchandise stores (GMSs); its e-commerce business is small. The company has grown by leveraging the expansion of the drugstore industry's share of the retail industry. In the future, it aims to make the e-commerce business a major sales channel. However, simply aiming to cover demand in Japan entails constraints on growth. The company thus targets overseas expansion as well, keeping the ASEAN and China markets in its sights.

Improvement in productivity

Anticipating sales expansion, ARATA aims to improve profitability by increasing productivity. The current medium-term plan lays out a policy of improving productivity with the keywords of standardization, IT, and outsourcing. Specifically, the company's measures include: 1) reducing variable costs with the latest IT and reorganizing logistics centers; 2) optimizing the allocation of personnel by forecasting logistics work volumes; 3) optimizing freight rates by improving loading efficiency; 4) standardizing and systematizing (RPS and loose coupling) back office functions and reducing fixed expenses through outsourcing; and 5) reducing fixed expenses through telework (from home), mobile work, and work at satellite offices.

Regarding the reorganization of logistics centers, the focus is on the construction of logistics centers that cover Greater Tokyo and the Kansai area. The company has confirmed that the introduction of the latest IT and equipment at its Kyushu Minami Logistics Center has improved productivity, including reducing the number of employees needed. It thus aims to improve productivity by making its logistics centers more efficient.

One of ARATA's priorities is to improve loading efficiency and optimize freight rates. Logistics efficiency has been deteriorating due to labor shortages and other factors. In FY03/15, packing and transportation expenses were 2.51% of sales, but rose to 2.76% in FY03/20. The company plans to keep logistics expenses in check by implementing initiatives to improve delivery efficiency, and strengthening cooperation with major delivery companies to improve loading efficiency.

Wholesalers of daily necessities must continuously strive to improve productivity as it is generally considered a low-margin business. At present, ARATA has not indicated expected levels of productivity improvement for individual product categories. It will thus be necessary to pay attention to the company's earnings results to confirm the effect of productivity improvement measures.

Strengthening management soundness

The medium-term management plan has set growth in the equity ratio and ROE by reducing total assets as priority issues. The company targets an equity ratio of 33–35% (33.2% in FY03/20) and an ROE of over 9% but less than 10% (8.8%). In the wholesaling industry, the balance sheet tends to expand as business grows. ARATA says it will improve accounts receivable, inventory, and accounts payable while reviewing fixed assets and implementing flexible capital policy. However, the financial function of the wholesaling industry (collecting funds from retailers and sending money to manufacturers) has often been touted as one of its important functions. Trying to forcibly shorten the collection period for accounts receivable may affect business. How the company will go about reducing total assets warrants attention moving forward.

Financing plan

The company expects to secure operating cash flow of over JPY35bn in three years if the medium-term management plan progresses smoothly. It plans approximately JPY30bn for capex. Main investment projects are: 1) strengthening of logistics: construction of new distribution centers in Greater Tokyo and the Kansai area, and labor-saving equipment at existing distribution centers; 2) automation-related system investment: expenditures for an automatic ordering system based on shipment volume forecast by AI, and automation of operations using RPA and AI optical character recognition (AI-OCR); 3) improvement of the telework environment; 4) strengthening of the BCP system: investment in information security and emergency backup systems; 5) enhancement of the management and sales support systems; 6) strengthening of product development capabilities in health, hygiene, and cosmetics; and 7) strengthening of the field business (store support) and customer analysis functions. The company particularly emphasizes investment in logistics. It has 11 large distribution centers nationwide, each with annual shipments of over JPY15bn. Including small distribution centers, the company has 43 locations nationwide (five in Hokkaido, five in Tohoku, 12 in Greater Tokyo, five in Chubu, four in Kansai, seven in Chugoku/Shikoku, and five in Kyushu). ARATA's logistics capacity in Greater Tokyo is approaching full, and the company aims to get an early start in expanding it.

Logistics network

Source: Company materials

During the three years under the current medium-term plan, the company plans to pay about JPY5bn in dividends as shareholder returns, based on its policy of paying stable dividends.

"2030 Future Vision"

Amid difficulty in projecting the near-term earnings outlook owing to the novel coronavirus pandemic, ARATA unveiled its "2030 Future Vision" in May 2020, outlining the direction the company wishes to take over the next 10 years, prior to announcing its medium-term management plan. This new management vision identifies "sales in excess of JPY1tn" as an earnings target, but sets no other quantitative objectives.

The "2030 Future Vision" has its roots in ARATA's basic policy on corporate social responsibility (CSR), informed in turn by the company's management philosophy of "continuing to serve the world." The three pillars of the company's basic policy on CSR are: 1) building a strong foundation by forming relationships of trust with all stakeholders; 2) taking a rational approach to boosting the efficiency of the overall supply chain; and 3) implementing business strategies that enrich the everyday lives of consumers while also ensuring that employees derive fulfilment from their jobs.

The message underlying the new management vision is one of "changing lives by fulfilling dreams," leveraging the abilities of the company to fulfill mankind's shared dream of continuing to lead prosperous and comfortable lives.

In terms of the quantitative value it offers, ARATA regards sales of JPY1tn as a mere point along the way toward further growth (sales in FY03/20 amounted to JPY796.2bn). It intends to cultivate its ability to generate profit and increase profitability and productivity through aggressive investment in logistics, IT, and personnel, with the aim of creating a virtuous cycle that can generate returns at an early stage. Qualitatively, ARATA believes its value to society lies in being a company that: 1) provides job satisfaction to employees, 2) contributes to supply chain optimization, 3) delivers rich and comfortable lives to consumers, and 4) operates in an environmentally friendly manner.

Strategy for realizing future vision is to act as "comprehensive producer of comfortable lifestyles"

ARATA is a wholesaler dealing primarily in daily necessities. In its "2030 Future Vision," though, the company aspires to become a "comprehensive producer of comfortable lifestyles," performing all manner of roles beyond that of distribution industry intermediary, and fulfilling the function of producer across the entire supply chain. More specifically, it aims to produce 1) items, 2) retail spaces, and 3) marketing.

Item producer: ARATA seeks to further flesh out its already broad array of products. In addition, the company aims to strengthen its capacity for planning and developing differentiated merchandise and collaborate with manufacturers and retailers in building a system supporting an abundant supply of appealing products. By selecting and handling appealing products, the company strives to gain advantage over competitors.

Retail space producer: In addition to building on its existing strength in providing brick-and-mortar stores with proposals for the creation of appealing retail spaces as well as follow-up support, ARATA seeks to expand the scope of this value-adding expertise to encompass all manner of retailers, including those operating online and overseas.

Marketing producer: As a wholesaler acting as intermediary between manufacturers and retailers, ARATA possesses a wealth of real-time information spanning the entire supply chain. Through value-adding analysis of this data, the company seeks to devise attractive proposals that bring enjoyment to consumers' shopping experience.

Historical medium-term plans

Medium-term management plans	Targets and results (JPYbn)				Key initiatives
FY03/06–FY03/08 (out Feb. 2005)		FY03/05 Est.	FY03/08 Init. Target	FY03/08 Act.	Strengthen wholesale capabilities, and improve financial structure - Enhance expertise in the five major categories - Offer standardized services throughout the nation - Raise market share further in the Kanto and Kansai regions
	Sales	420.5	520.0	551.8	
	RP	8.0	9.0	1.9	
FY03/08–FY03/10 (out Mar. 2007)		FY03/07 Est.	FY03/10 Init. Target	FY03/10 Act.	Grow into a locally-rooted nationwide wholesaler - Enhance organizational integration and build a low-cost management structure - Further reduce assets to build an efficient business structure - Improve profitability by enhancing wholesale capabilities
	Sales	511.6	557.0	589.9	
	RP	1.4	4.9	3.9	
FY03/10–FY03/12 (out May 2009)		FY03/09 Act.	FY03/12 Init. Target	FY03/12 Act.	Strengthen ARATA brand - Enhance sales and store-based marketing capabilities - Bolster category management capability through group management - Build a nationwide optimized logistics network - Establish corporate governance structure and enhance management base
	Sales	569.7	600.0	606.7	
	RP	2.3	5.8	4.3	
FY03/12–FY03/14 (out May 2011)		FY03/11 Act.	FY03/14 Init. Target	FY03/14 Act.	Grow into a next-generation wholesaler - Enhance value-added offerings suitable to a next-generation wholesaler (Improve sales support capabilities collaborating with other industries; expand services for sales and logistics) - Expand and develop markets (promote group synergies; develop overseas businesses) - Renovate cost structure (integrate and optimize internal operations; rebuild group logistics networks)
	Sales	601.9	650.0	652.0	
	RP	4.3	8.0	4.4	
FY03/15–FY03/17 (out May 2014)		FY03/14 Act.	FY03/17 Init. Target	FY03/17 Act.	Build a new structure for a next-generation wholesaler - Adopt profit management by company to enhance profitability - Bolster product development leveraging ARATA's group-wide sales capabilities and network - Strengthen profitability by enhancing expertise of sales, sales promotion, and store managing groups - Gain earnings through investing management resources in overseas businesses and tighten profit management - Propose products for e-commerce; improve logistics structure - Integrate internal operations to office work center and procurement center to promote reduction of overhead
	Sales	652.0	670.0	704.6	
	RP	4.4	6.7	7.8	
FY03/18–FY03/20 (out May 2017)		FY03/17 Act.	FY03/20 Init. Target	FY03/20 Act.	ARATA Second Stage: Looking a decade ahead, pursue new possibilities in the wholesale business - Continue formulating growth strategies - Lay the foundation for the future - Further strengthen the management base
	Sales	704.6	760.0	796.2	
	RP	7.8	10.0	10.1	
	Net income	4.9	6.0	7.2	
FY03/21–FY03/23 (out Aug 2020)		FY03/20 Act.	FY03/23 Init. Target	FY03/23 Act.	Aim for competitive marketing and low-cost operation with product development and store layout proposal capabilities, and labor-saving logistics center - Further develop growth potentials - Improve productivity - Further enhance sound management
	Sales	796.2	845.0	-	
	RP	9.3	11.5	-	
	Net income	10.1	12.0	-	

Source: Shared Research based on company data

Business

Business model

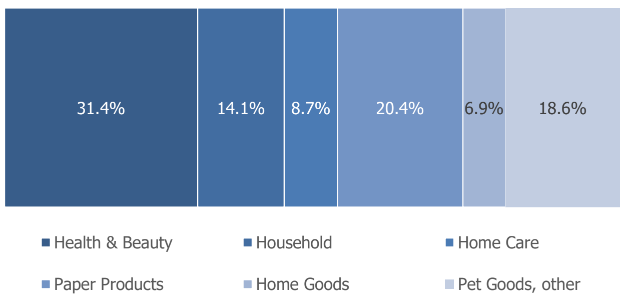
ARATA mainly wholesales everyday items and cosmetics, which it buys from manufacturers. The goods are delivered to the company's logistics centers, where they are sorted and dispatched to retailers to whom they are sold. The company handles around 100,000 items (such as cosmetics and other Health & Beauty products, detergents, paper products), which it buys from some 1,200 Japanese and overseas manufacturers. The company wholesales these products to almost all Japanese retailers (around 45,000 stores operated by 3,500 companies, including drugstores, supermarkets, and DIY centers). Upon receiving an order from a retailer, the company's role is to deliver the right quantity of the right products to the right location at the right time. The company has systems in place to handle detailed customer orders, including orders as small as a single toothbrush.

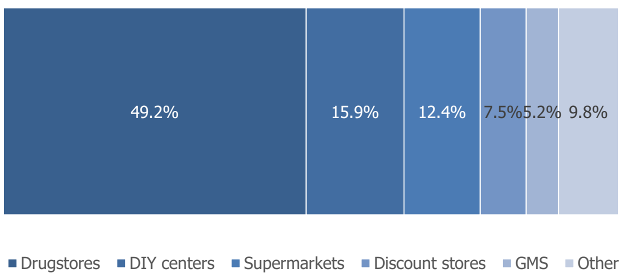
In FY03/20, the company posted sales of JPY796.2bn, which we estimate would be about JPY1tn on a retail basis (converted to instore retail prices). The volume of items it handles is comparable to that of top-10-ranking retailers in Japan.

The company breaks down the products it handles into six categories: 1) Health & Beauty (31% of sales in FY03/20): cosmetics, cosmetic accessories, bathwater additives, body cleansers, hair-care products, oral-care products, and health foods; 2) Paper Products (20%): baby products, baby diapers, nursing care items, adult diapers, sanitary goods, tissue paper, and toilet paper; 3) Household (14%): laundry detergent, kitchen cleansers and dish soap, and household cleansers; 4) Home Care (9%): fragrances and deodorizers, insect repellants, insecticides, incenses and candles for home altars, dry cell batteries and products that use them, recording media, lighting, electrical products, OA products, and photo-related products; 5) Home Goods (7%): kitchen consumables, products used on sinks, cleaning supplies, storage supplies, seasonal products, storage products, cooking items, tabletop items, and picnic supplies; 6) Pet Goods/Other (19%): pet supplies, stationery, toys, and auto products. The company's wide range of products excludes foods, apparel, consumer electronics, PCs, and mobile devices, which all vary in distribution channels.

The company sells its products to drugstores (49% of sales in FY03/19), DIY centers (16%), supermarkets (12%), discount stores (7%), GMSs (5%), and others (10%). Previously, convenience stores were among its important customers, but this sales channel has shrunk since Circle K Sunkus and FamilyMart merged and changed their procurement policies. The company does little business with online retailers, which are in the "Other" category. The company is not highly dependent on any individual business partner. Tsuruha Holdings (TSE1: 3391) accounted for 12.5% of sales in FY03/20, and is the only company to account for more than 10%.

Sales mix by product category (left) and sales mix by customer type (right) (FY03/20)

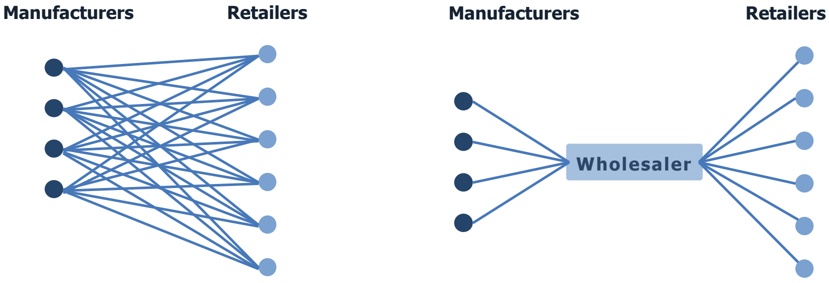




Source: Shared Research based on company data

The company's GPM is generally between 10% and 11%. The average over the past five years was 10.4%, with 10.5% being the highest (in FY03/16) and 10.3% the lowest (in FY03/20). Shared Research thinks the company has four major sources of added value: First, it has the logistics capabilities to respond accurately to small-lot orders. Second, because the company handles such a wide range of items, it can serve as a one-stop wholesaler. Third, the company has the ability to make proposals that connect manufacturer promotions with instore retail methods. Fourth, the company has a vast store of transaction data (available for free or for a fee to retailers and manufacturers) that it can use to identify what is being sold and where, at any particular time.

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



Source: Shared Research

Accurate deliveries from logistics centers a source of added value

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

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

For small-lot deliveries, the company relies on human capabilities and mechanical checks to ensure that operations are efficient and mistakes are kept to a minimum. ARATA has introduced AiMAS, picking carts equipped with scales, at its logistics centers. Employees follow the instructions on a cart's screen, taking products off shelves and placing them on the cart. A bar code confirms that the correct products are taken, and the cart senses the weight of the cart before and after the product(s) have been added to confirm that the quantity is correct. The company uses such systems to make deliveries, in quantities as small as a single toothbrush, to 45,000 stores operated by some 3,500 companies, with a misdelivery rate of less than 1/100,000.

The Kyushu Minami center, the company's newest facility, has an AI-equipped depalletizing robot. Due to the sheer number of items the company handles, the task of locating the right container of goods from the vast number of containers stacked on pallets, and placing it on the conveyers for shipping yielded a number of permutations so large that robot programming was impracticable. For that reason, until recently, the company relied on humans for this task. However, the company has eliminated the need to program the robot by using a system comprising 2D/3D cameras and deep learning functionality, improving operational speed. As a result, work that previously required six employees can now be handled by one. The company makes capital investments of JPY3.0–5.0bn per year; by using state-of-the-art distribution systems, it aims to handle more quantity without increasing the total number of employees, while ensuring accurate and efficient deliveries.

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

Source: Shared Research based on company materials

Information system that facilitates one-stop service

The company has an information system to ensure the accuracy of orders it places and receives for the 100,000 items it handles. It uses an electronic data interchange (EDI) backbone provided by Planet (TSE JASDAQ Standard: 2391). Investors in Planet include manufacturers of everyday items such as Lion (TSE1: 4912) and Unicharm (TSE1: 8113), as well as Intec (now TIS [TSE1: 3626]). Planet was established to create systems for communicating data between wholesalers and manufacturers of everyday items, sundries, and cosmetics. ARATA has been working with Planet on EDI backbone development since that company's establishment, helping it create a framework for accurately handling information regarding the placement and receipt of orders between manufacturers and distributors. Planet also provides a supplementary service for small and medium-sized manufacturers without the wherewithal to install the EDI backbone. The service helps ensure the accuracy of information ARATA exchanges with these manufacturers, as well.

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

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

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

Advice on creating successful retail spaces

Shared Research understands that the company stands out in the industry for its ability to make proposals that connect manufacturer promotions with instore retail methods. Facilitating such proposals is Dentsu Retail Marketing (DRM), an equity-method affiliate the company established in November 2006 along with Dentsu Tec Inc., a subsidiary of Dentsu (TSE1: 4324), NEC (TSE1: 6701), and Dai Nippon Printing (TSE1: 7912). Dentsu is a leading advertising agency with the top domestic market share and handles the creation of TV and online ads for many companies including manufacturers. ARATA has a 21.6% stake in

DRM (previously 20%). DRM's services include consulting on the analysis and use of customer purchasing data, planning and creating sales promotional tools tailored to store- or region-specific demand, managing instore product displays, and putting sales promotion tools in place in stores. Through DRM, the company works to maximize the combined effectiveness of different types of advertising and instore retail spaces. Recently, the company has been stepping up its efforts to create spaces in tie-ups with regional TV stations and newspaper advertisements. In addition to advertising products nationwide, the company creates plans to capitalize on regional events and proposes to retailers plans that link the three: special events, ads, and products. In May 2020, ITOCHU Corporation (TSE1: 8001) also took a stake in DRM.

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

The company's SG&A ratio (SG&A expenses to sales) is generally between 9% and 10%. Over the past five years, the ratio has averaged 9.3%, with a high of 9.6% in FY03/16 and a low of 9.1% in FY03/20. Of this figure, salaries and allowances have been the largest component, averaging 2.8% of sales during the period, followed by packing and transportation expenses, at 2.6%. Sales grew 17.7% from JPY676.7bn in FY03/16 to JPY796.2bn in FY03/20. The number of employees (consolidated basis) increased a modest 2.4% from 2,914 at end-FY03/16 to 2,984 at end-FY03/20, and salaries and allowances were up slightly. Administrative division productivity improved thanks to consolidation of business centers, adoption of robotic process automation (RPA), and a complete overhaul of operation manuals. Packing and transportation expenses, meanwhile, rose due to higher freight volumes and trended upward as a percentage of sales due to higher freight rates.

OPM was 0.4% in FY03/15, 0.8% in FY03/16, 1.0% in FY03/17, 1.2% in FY03/18, 1.2% in FY03/19, and 1.2% in FY03/20. Through FY03/18, gross profit rose in tandem with sales, with the GPM rising because sales grew faster than SG&A expenses. Packing and transportation expenses rose, but the company was able to maintain the overall profit margin by controlling the rise in salaries and allowances and other personnel costs.

Business breakdown

Sales by category (JPYmn)	FY03/12 Act.	FY03/13 Act.	FY03/14 Act.	FY03/15 Act.	FY03/16 Act.	FY03/17 Act.	FY03/18 Act.	FY03/19 Act.	FY03/20 Act.
Total sales (new categories)							**732,914**	**754,447**	**796,227**
YoY							-	2.9%	5.5%
Health & Beauty							223,800	237,837	249,973
YoY							-	-	5.1%
% of total sales							30.5%	31.5%	31.4%
Household							100,899	105,633	111,992
YoY							-	-	6.0%
% of total sales							13.8%	14.0%	14.1%
Home Care							70,553	69,332	69,084
YoY							-	-	-0.4%
% of total sales							9.6%	9.2%	8.7%
Paper Products							147,167	147,320	162,150
YoY							-	-	10.1%
% of total sales							20.1%	19.5%	20.4%
Home Goods							54,082	52,245	55,282
YoY							-	-	5.8%
% of total sales							7.4%	6.9%	6.9%
Pet Goods, other							136,410	142,073	147,744
YoY							-	-	4.0%
% of total sales							18.6%	18.8%	18.6%
Total sales (old categories)	**606,705**	**616,327**	**651,954**	**638,792**	**676,743**	**704,610**	**732,914**	**754,447**	**796,227**
YoY	0.8%	1.6%	5.8%	-2.0%	5.9%	4.1%	4.0%	2.9%	5.5%
Health & Beauty	181,028	180,304	186,283	181,492	196,853	212,207	225,283		
YoY	3.9%	-0.4%	3.3%	-2.6%	8.5%	7.8%	6.2%		
% of total sales	29.8%	29.3%	28.6%	28.4%	29.1%	30.1%	30.7%		
Toiletary	159,510	160,467	169,839	163,503	162,333	169,312	175,291		
YoY	2.4%	0.6%	5.8%	-3.7%	-0.7%	4.3%	3.5%		
% of total sales	26.3%	26.0%	26.1%	25.6%	24.0%	24.0%	23.9%		
Paper Products	127,376	128,777	138,652	135,584	145,872	146,026	147,245		
YoY	-5.9%	1.1%	7.7%	-2.2%	7.6%	0.1%	0.8%		
% of total sales	21.0%	20.9%	21.3%	21.2%	21.6%	20.7%	20.1%		
Home Goods	43,004	45,498	48,833	47,440	50,021	51,912	54,285		
YoY	1.0%	5.8%	7.3%	-2.9%	5.4%	3.8%	4.6%		
% of total sales	7.1%	7.4%	7.5%	7.4%	7.4%	7.4%	7.4%		
Pet Goods, other	95,787	101,281	108,347	110,773	121,664	125,153	130,810		
YoY	2.0%	5.7%	7.0%	2.2%	9.8%	2.9%	4.5%		
% of total sales	15.8%	16.4%	16.6%	17.3%	18.0%	17.8%	17.8%		

Source: Shared Research based on company data
Note: FY03/19 figures have been retroactively adjusted to reflect partial adjustments by the company to product categories in FY03/20. Accordingly, there are no YoY figures.

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

Market and value chain

Sales rising slightly more than drugstore sales

Drugstores are the company's largest customers, by percentage of sales. The top-selling product categories reflect this: Health & Beauty (mainly cosmetics and oral-care products) and Paper Products (mainly baby diapers, sanitary goods, and toilet paper) are sold in drugstores. Total drugstore sales across Japan have grown by a CAGR of 4.8% between FY2014 and FY2019 (from JPY6.1tn to JPY7.7tn). The company's sales have climbed by a CAGR of 4.5%, from JPY638.8bn in FY03/15 to JPY796.2bn in FY03/20. The company's sales have grown at roughly the same rate as that of drugstores.

Looking at trends in the drugstore industry, large drugstores have been seeking to increase sales by aggressively opening new stores and through acquisitions. Meanwhile, small and medium-sized drugstores have been closing, accounting for a shrinking market share. ARATA delivers products to all the big drugstores in Japan. These drugstores make up a growing share of the market, driving up the company's sales. By customer type, ARATA's sales to drugstores have been rising at a CAGR of 6.0%, outpacing the growth rate of the drugstore industry itself. Major drugstores have established many tax-free stores to capture increasing demand from inbound tourists. ARATA thinks its ability to abundantly supply these stores with items popular among inbound tourists has contributed to its increase in sales.

However, the company has not benefited completely from sales growth in the large-drugstore subset. Sales at the six largest drugstores in Japan grew at a CAGR of 7.9% between FY2014 (JPY2.5tn) and FY2019 (JPY3.7tn), rising faster than ARATA's sales. The reason is that large drugstores have accelerated growth by stocking food items, which make up only a tiny proportion of the company's products.

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

Among drugstores, the company's sales to Tsuruha Holdings make up more than 10% of total sales, requiring a separate breakdown in its annual securities report. (In FY03/20, sales to Tsuruha were JPY99.9bn, or 12.5% of FY03/20 sales).

Sales growth ratios

(JPYtn)	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	CAGR FY2014–2019
Sales: Total drugstores	6.07	6.13	6.49	6.85	7.27	7.69	4.8%
YoY	1.0%	1.1%	5.9%	5.5%	6.2%	5.7%	
Sales: Six major drugstores	2.51	2.80	2.95	3.20	3.45	3.68	7.9%
YoY	3.9%	11.5%	5.3%	8.5%	7.6%	6.8%	
PALTAC (8283) (JPYbn)	794.2	860.4	922.1	966.7	1,015.3	1,046.4	5.7%
YoY	-4.5%	8.3%	7.2%	4.8%	5.0%	3.1%	
ARATA (JPYbn)	638.8	676.7	704.6	732.9	754.4	796.2	4.5%
YoY	-2.0%	5.9%	4.1%	4.0%	2.9%	5.5%	
Drugstore sales	293.0	311.9	331.3	349.9	368.4	391.9	6.0%
YoY	0.1%	6.4%	6.2%	5.6%	5.3%	6.4%	
Other sales	345.8	364.9	373.3	383.0	386.1	404.3	3.2%
YoY	-3.7%	5.5%	2.3%	2.6%	0.8%	4.7%	

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

The company also sells product to other customer types, so sales growth is affected by their performance, as well. Over the past five years, ARATA's sales to discount stores have risen by a CAGR of 6.7%. Among key customers, store numbers have grown, and discount stores have also benefited from increased demand from inbound tourists. On the other hand, sales to DIY centers have risen 2.1%, sales to supermarkets have risen 2.8%, and sales to general merchandise stores (GMSs) have fallen 1.7%. Sales to convenience stores are no longer on a meaningful scale, falling as convenience stores have restructured and changed their procurement policies.

Sales by customer type

Sales by customer type (JPYmn)	FY03/12 Act.	FY03/13 Act.	FY03/14 Act.	FY03/15 Act.	FY03/16 Act.	FY03/17 Act.	FY03/18 Act.	FY03/19 Act.	FY03/20 Act.
Total sales	**606,705**	**616,327**	**651,954**	**638,792**	**676,743**	**704,610**	**732,914**	**754,447**	**796,227**
YoY	0.8%	1.6%	5.8%	-2.0%	5.9%	4.1%	4.0%	2.9%	5.5%
Drugstores		272,929	292,880	293,028	311,892	331,310	349,940	368,355	391,911
YoY		-	7.3%	0.1%	6.4%	6.2%	5.6%	-	6.4%
% of total sales		44.3%	44.9%	45.9%	46.1%	47.0%	47.7%	48.8%	49.2%
DIY centers		115,295	120,156	112,415	116,301	117,565	123,558	124,223	126,820
YoY		-	4.2%	-6.4%	3.5%	1.1%	5.1%	-	2.1%
% of total sales		18.7%	18.4%	17.6%	17.2%	16.7%	16.9%	16.5%	15.9%
Supermarkets		84,050	86,825	85,880	86,393	88,414	92,264	93,790	98,583
YoY		-	3.3%	-1.1%	0.6%	2.3%	4.4%	-	5.1%
% of total sales		13.6%	13.3%	13.4%	12.8%	12.5%	12.6%	12.4%	12.4%
Discount stores		39,970	42,766	42,961	48,354	50,678	53,054	55,731	59,502
YoY		-	7.0%	0.5%	12.6%	4.8%	4.7%	-	6.8%
% of total sales		6.5%	6.6%	6.7%	7.1%	7.2%	7.2%	7.4%	7.5%
General merchandising stores (GMS)		47,211	49,242	45,540	45,791	47,061	42,557	40,503	41,750
YoY		-	4.3%	-7.5%	0.6%	2.8%	-9.6%	-	3.1%
% of total sales		7.7%	7.6%	7.1%	6.8%	6.7%	5.8%	5.4%	5.2%
Convenience stores		11,331	9,904	9,554	8,481	5,763			
YoY		-	-12.6%	-3.5%	-11.2%	-32.0%			
% of total sales		1.8%	1.5%	1.5%	1.3%	0.8%			
Other		45,541	50,181	49,414	59,531	63,819	71,539	71,842	77,659
YoY		-	10.2%	-1.5%	20.5%	7.2%	2.8%	-	8.1%
% of total sales		7.4%	7.7%	7.7%	8.8%	9.1%	9.8%	9.5%	9.8%

Source: Shared Research based on company data
Note: FY03/19 figures have been retroactively adjusted to reflect partial adjustments by the company to customer types in FY03/20. Accordingly, there are no YoY figures.

Competitors

ARATA's main competitor is PALTAC (TSE1: 8283). Both companies are large wholesalers that handle cosmetics and everyday items and focus mainly on drugstores. The third-largest company in the industry, Chuo Bussan Corporation, is the main company operated by CB Group Management (TSE1: 9852), and has sales of JPY146.8bn (FY03/20). ARATA and PALTAC together account for the lion's share of everyday-item wholesale in Japan, with a combined market share of nearly 50%. The companies are similar in that overseas sales account for less than 10% of the total, and that OPM levels are lower than either upstream manufacturers or downstream drugstores.

Sales by customer type

ARATA (2733)	FY03/19		FY03/20	
	(JPYmn)	% of sales	(JPYmn)	% of sales
Sales	**754,447**	**100.0%**	**796,227**	**100.0%**
Drugstores	368,355	48.8%	391,911	49.2%
DIY centers	124,223	16.5%	126,820	15.9%
Discount stores	55,731	7.4%	59,502	7.5%
Supermarkets (SMs), GMS	134,293	17.8%	140,333	17.6%
Convenience stores	-	-	-	-
Other	71,845	9.5%	77,661	9.8%
Gross profit	**78,197**	**10.4%**	**81,833**	**10.3%**
SG&A expenses	69,305	9.2%	72,507	9.1%
Packing and transportation expenses	20,255	2.7%	21,965	2.8%
Salaries and allowances	20,008	2.7%	20,333	2.6%
Provision for bonuses	1,395	0.2%	1,449	0.2%
Retirement benefit expenses	940	0.1%	1,013	0.1%
Other	10	0.0%	4,988	0.6%
Operating profit	**8,892**	**1.2%**	**9,326**	**1.2%**
Depreciation	4,455	0.6%	4,281	0.5%
EBITDA	**13,347**	**1.8%**	**13,607**	**1.7%**

PALTAC (8283)	FY03/19		FY03/20	
	(JPYmn)	% of sales	(JPYmn)	% of sales
Sales	**1,015,253**	**100.0%**	**1,046,412**	**100.0%**
Drugstores	638,883	62.9%	663,366	63.4%
DIY centers	93,409	9.2%	95,622	9.1%
Discount stores, other	69,908	6.9%	76,272	7.3%
SMs, SSMs, GMS	92,020	9.1%	89,274	8.5%
Convenience stores	75,064	7.4%	75,146	7.2%
Export, other	45,969	4.5%	46,729	4.5%
Gross profit	**79,645**	**7.8%**	**81,527**	**7.8%**
SG&A expenses	54,246	5.3%	56,818	5.4%
Distribution expenses	11,062	1.1%	12,458	1.2%
Salaries and allowances	17,051	1.7%	17,246	1.6%
Provision for bonuses	1,713	0.2%	1,601	0.2%
Retirement benefit expenses	1,253	0.1%	1,099	0.1%
Other	23,167	2.3%	24,414	2.3%
Operating profit	**25,399**	**2.5%**	**24,708**	**2.4%**
Depreciation	4,493	0.4%	5,059	0.5%
EBITDA	**29,892**	**2.9%**	**29,767**	**2.8%**

Source: Shared Research based on company data. SSMs refers to “super supermarkets.”

Different customer bases

In FY03/20, PALTAC had sales of JPY1.0tn, compared with JPY796.2bn for ARATA. Drugstores account for a high percentage of products delivered by both companies, but this ratio is higher for PALTAC than for ARATA (more than 60% vs. under 50%). Matsumoto Kiyoshi is PALTAC’s major drugstore client, accounting for a little less than 10% of total sales.

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

Although the companies have different strengths, their market shares are stable. As the table at the start of this section shows, CAGR for sales over the past five years has been 5.7% at PALTAC versus 4.5% for ARATA, with favorable drugstore sales contributing relatively more to PALTAC.

Different cost structures

In FY03/20, ARATA had a GPM of 10.3%, versus 7.8% at PALTAC. Although the companies use different methods for booking sales and expenses, based on the data released in the annual securities reports, we have drawn the conclusion that customers view ARATA to be providing greater added value.

ARATA has an SG&A ratio of 9.1%, versus 5.4% for PALTAC. ARATA explains this difference as being the cost necessary to create and maintain added value. According to their annual securities reports, distribution-related costs (called “packing and transportation expenses” at ARATA, “distribution expenses” at PALTAC) were 2.8% of sales at ARATA, versus 1.2% for PALTAC. ARATA, which was formed through mergers, has many small logistics centers, whereas PALTAC has more large-scale logistics centers, which are more efficient. HR-related costs (the sum of salaries or salaries and allowances, provision for bonuses, and retirement benefit costs) was 2.9% for ARATA, vs. 1.9% for PALTAC. Shared Research believes ARATA has room to improve its distribution and HR efficiency.

Holdings of business partners’ shares

ARATA holds significant amounts of equity in business partners as policy shareholdings, as does PALTAC. According to their annual securities reports, in FY03/20 ARATA held JPY8.4bn worth of shares in 101 companies; PALTAC held JPY22.1bn in shares of 59 companies. Most of these shares are in the companies’ suppliers (manufacturers) or customers (drugstores and other retailers).

Strengths and weaknesses

Strengths

- **Logistics capabilities:** After the company receives an order from a retailer, it works to efficiently deliver the right quantity of the right products to the right location at the right time. ARATA handles around 100,000 items (such as cosmetics and other Health & Beauty products, detergents, and paper products), most of which it buys from around 1,200 Japanese and overseas suppliers. The company wholesales these products to around 45,000 stores operated by 3,500 companies, including drugstores, supermarkets, and DIY centers, covering almost all retail subsectors in Japan. We understand that this variety of items is attractive for retailers, as it allows them to order everything they need from one supplier. Despite repeated attempts by retailers to have manufacturers deliver to them directly, successes with this approach have been few. This situation creates an effective barrier to entry.
- **Ability to propose solutions:** For retailers, creating effective retail spaces is vital. ARATA can assist in this, as it knows what products peer retailers are selling in large volumes and how. The company uses this knowledge to propose new ideas to retail stores about how to create on-trend retail spaces. When a retailer introduces a new cosmetic product, for example, the company might suggest the retailer collaborate with the manufacturer to create an instore space with a TV commercial tie-in. (This approach enables the manufacturer to deliver sales promotion materials along with the product.) The company works with Dentsu Retail Marketing, a 21.6%-owned equity-method affiliate, to create regional sales promotion campaigns linked with regional TV commercials. This capability sets ARATA apart from peers. Dentsu, a business partner in these services, is a leading advertising agency with top domestic market share and handles the creation of TV and online ads for many companies including manufacturers.
- **Accumulated information:** We estimate that the sheer volume of the products ARATA handles would place it among Japan's top-10-ranking retailers (on an instore retail price basis). The company has thus accumulated a large amount of up-to-date data on retail orders (what is selling well, and where and what changes are occurring). Accurate information on what products are selling well (and which are not) at other companies is valuable for retailers. For the manufacturers as well, ARATA has information on peer products being sold at the retailers (what is selling, under what sort of a promotion plan and retail space design). Such information could at times be more valuable to manufacturers than the results of their own field research and can also be useful for their product development.

Weaknesses

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

Historical results and financial statements

Income statement

Income statement (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Sales	**606,705**	**616,327**	**651,954**	**638,792**	**676,743**	**704,610**	**732,914**	**754,447**	**796,227**
YoY	0.8%	1.6%	5.8%	-2.0%	5.9%	4.1%	4.0%	2.9%	5.5%
Cost of sales	537,672	552,041	585,224	574,179	606,012	631,542	656,439	676,249	714,394
Gross profit	**69,033**	**64,286**	**66,730**	**64,613**	**70,731**	**73,068**	**76,475**	**78,197**	**81,833**
GPM	11.4%	10.4%	10.2%	10.1%	10.5%	10.4%	10.4%	10.4%	10.3%
SG&A expenses	64,859	60,560	62,258	62,152	65,032	65,684	67,618	69,305	72,507
SG&A ratio	10.7%	9.8%	9.5%	9.7%	9.6%	9.3%	9.2%	9.2%	9.1%
Operating profit	**4,174**	**3,726**	**4,472**	**2,461**	**5,699**	**7,384**	**8,857**	**8,892**	**9,326**
YoY	-	-10.7%	20.0%	-45.0%	131.6%	29.6%	19.9%	0.4%	4.9%
OPM	0.7%	0.6%	0.7%	0.4%	0.8%	1.0%	1.2%	1.2%	1.2%
Non-operating income	949	942	927	944	977	1,158	1,195	1,189	1,287
Non-operating expenses	-1,208	-1,063	-1,011	-936	-865	-700	-613	-652	-489
Interest income	8	6	7	6	6	7	7	6	7
Dividend income	98	111	113	120	128	148	161	172	154
Interest expenses	-824	-774	-712	-661	-554	-436	-325	-217	-181
Equity in earnings of affiliates	12	14	9	27	17	26	14	8	6
Forex gains (losses)	-	-	-	-	-	-	-	-	-
Recurring profit	**3,915**	**3,605**	**4,388**	**2,469**	**5,811**	**7,842**	**9,439**	**9,429**	**10,124**
YoY	-8.0%	-7.9%	21.7%	-43.7%	135.4%	35.0%	20.4%	-0.1%	7.4%
RPM	0.6%	0.6%	0.7%	0.4%	0.9%	1.1%	1.3%	1.2%	1.3%
Extraordinary gains	3	22	611	148	69	51	411	1,239	874
Gain on sale of fixed assets	-	1	74	-	3	50	361	160	338
Other	3	21	537	148	66	1	50	1,079	536
Extraordinary losses	208	84	268	124	188	416	168	516	352
Loss on disposal of fixed assets	101	12	29	114	96	305	4	157	316
Loss on retirement of fixed assets	30	11	42	10	64	27	16	6	21
Impairment losses	-	-	57	-	26	7	103	-	-
Loss on valuation of securities	28	27	138	-	1	-	43	2	14
Other	77	61	140	-	2	77	45	353	15
Income taxes	2,081	1,772	2,294	1,376	2,458	2,624	3,319	3,244	3,462
Implied tax rate	56.1%	50.0%	48.5%	55.2%	43.2%	35.1%	34.3%	32.0%	32.5%
Net income attributable to non-controlling interests	-	2	-	-8	-10	-9	2	4	-7
Net income attributable to owners of the parent	**1,628**	**1,768**	**2,435**	**1,124**	**3,244**	**4,863**	**6,361**	**6,903**	**7,191**
YoY	60.4%	8.6%	37.7%	-53.8%	188.6%	49.9%	30.8%	8.5%	4.2%
Net margin	0.3%	0.3%	0.4%	0.2%	0.5%	0.7%	0.9%	0.9%	0.9%

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

Over the past five years, sales have grown by a CAGR of 4.5%, although sales declined in FY03/15, affected by a consumption tax hike in Japan. After that, sales have grown each year. By customer type, sales to drugstores and discount stores have continued to drive overall growth, while growth in sales to DIY centers, supermarkets, and GMSs have been relatively low.

The company's GPM is generally between 10% and 11%. The average over the past five years was 10.4%, with 10.5% being the highest (in FY03/16) and 10.3% the lowest (in FY03/20). The SG&A ratio is generally between 9% and 10%. Over the past five years, the ratio has averaged 9.3%, with a high of 9.6% in FY03/16 and a low of 9.1% in FY03/20. Of this figure, salaries and allowances have been the largest component, averaging 2.8% of sales during the period, followed by packing and transportation expenses, at 2.6%. Although sales have continued to grow, sales and allowances have fallen slightly as a percentage of sales. Packing and transportation expenses have been up due to higher freight volumes and trended upward as a percentage of sales due to higher freight rates.

OPM was 0.8% in FY03/16, 1.0% in FY03/17, 1.2% in FY03/18, 1.2% in FY03/19, and 1.2% in FY03/20. In FY03/17, non-operating income and expenditures was a net positive at JPY458mn, rising to JPY582mn in FY03/18 and remaining positive at JPY537mn in FY03/19 and JPY798mn in FY03/20. This increase was due mainly to a decline in interest payments, as interest-bearing debt decreased. The recurring profit margin was 1.1% in FY03/17, exceeding 1% for the first time since FY03/04.

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

Balance sheet

Balance sheet (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
ASSETS									
Cash and deposits	9,985	8,108	10,965	11,800	14,119	13,693	17,826	19,798	18,547
Notes and accounts receivable	78,328	82,592	89,542	82,649	86,133	82,212	97,321	98,763	102,234
Inventories	30,907	31,009	30,981	28,072	27,971	29,556	29,997	30,804	31,617
Accounts receivable–other	18,719	17,953	20,222	17,650	19,877	23,939	22,827	22,825	25,582
Other	5,081	6,144	6,305	3,735	3,773	4,055	3,285	2,966	3,764
Total current assets	**143,020**	**145,806**	**158,015**	**143,906**	**151,873**	**153,455**	**171,256**	**175,156**	**181,744**
Buildings and structures	18,972	18,201	19,828	22,730	21,415	21,829	22,983	21,906	21,917
Land	19,996	19,997	19,853	20,540	21,330	21,004	20,461	19,936	19,553
Other	5,929	7,782	9,091	8,626	8,096	7,415	7,597	7,180	7,470
Total tangible fixed assets	**44,897**	**45,980**	**48,772**	**51,896**	**50,841**	**50,248**	**51,041**	**49,022**	**48,940**
Goodwill	1,874	1,524	1,093	661	230	7	-	14	7
Other	2,381	2,584	3,196	3,486	3,551	3,569	3,495	3,645	3,699
Total intangible assets	**4,255**	**4,108**	**4,289**	**4,147**	**3,781**	**3,576**	**3,495**	**3,659**	**3,706**
Investment securities	5,301	5,314	6,631	8,426	9,732	11,713	13,539	11,153	10,960
Deferred tax assets	2,171	1,266	541	308	347	327	480	572	551
Other	2,860	4,224	2,952	3,156	3,115	3,655	3,886	4,051	3,810
Investments and other assets	**10,332**	**10,804**	**10,124**	**11,890**	**13,194**	**15,695**	**17,905**	**15,776**	**15,321**
Total fixed assets	**59,486**	**60,893**	**63,187**	**67,934**	**67,816**	**69,519**	**72,422**	**68,458**	**67,968**
Total assets	**202,506**	**206,699**	**221,202**	**211,840**	**219,689**	**222,974**	**243,698**	**243,614**	**249,712**
LIABILITIES									
Accounts and notes payable	58,081	65,031	69,039	68,989	72,135	76,579	89,112	90,031	90,153
Short-term debt	42,934	35,380	37,069	35,271	38,017	28,147	32,653	17,945	22,700
Accounts payable–other	7,962	8,682	10,037	9,681	10,200	10,884	12,783	12,883	14,090
Other	6,821	7,422	6,765	8,473	9,404	8,393	11,283	8,970	9,296
Total current liabilities	**115,798**	**116,515**	**122,910**	**122,414**	**129,756**	**124,003**	**145,831**	**129,829**	**136,239**
Long-term debt	29,042	30,904	38,048	27,157	24,215	27,930	14,648	21,861	18,981
Deferred tax liabilities for land revaluation	860	-	-	648	517	1,052	944	442	222
Retirement benefit liabilities	7,479	7,977	6,589	4,898	6,478	7,276	7,535	7,724	7,867
Other	2,003	2,259	2,614	2,812	2,782	3,100	3,267	3,242	3,501
Total fixed liabilities	**39,384**	**41,140**	**47,251**	**35,515**	**33,992**	**39,358**	**26,394**	**33,269**	**30,571**
Total liabilities	**155,182**	**157,655**	**170,161**	**157,929**	**163,748**	**163,361**	**172,226**	**163,099**	**166,811**
NET ASSETS									
Shareholders' equity	46,930	48,078	49,894	51,108	53,181	55,474	65,861	76,259	79,252
Accumulated other comprehensive income	376	945	1,123	2,789	2,742	4,131	5,601	4,240	3,637
Subscription rights to shares	-	-	-	-	-	-	-	-	-
Non-controlling interests	18	21	24	14	18	8	10	16	11
Total net assets	**47,324**	**49,044**	**51,041**	**53,911**	**55,941**	**59,613**	**71,472**	**80,515**	**82,901**
Working capital	51,154	48,570	51,484	41,732	41,969	35,189	38,206	39,536	43,698
Total interest-bearing debt	68,707	62,566	70,872	58,637	58,982	52,569	43,640	36,524	37,739
Net debt (net cash)	58,722	54,458	59,907	46,837	44,863	38,876	25,814	16,726	19,192

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

Although the scale of sales is large, at fiscal year-end the company maintains cash and deposits worth only about 0.3 months' sales, as its business model requires little cash on hand. Trade receivables (notes and accounts receivable) exceed trade payables (notes and accounts payable), but by a small margin. Inventory turnover is around 0.5 months. As of end-FY03/20, the company had JPY43.7bn in working capital.

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

Interest-bearing debt has fallen between end-FY03/12 and end-FY03/20 (from JPY68.7bn to JPY37.7bn). Shared Research understands the company includes convertible bond-type bonds with share acquisition rights within interest-bearing debt.

Cash flow statement

Cash flow statement (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Cash flows from operating activities (1)	-720	9,959	1,481	21,955	7,594	12,637	11,649	9,513	5,262
Pre-tax profit	3,709	3,543	4,731	2,493	5,691	7,477	9,682	10,152	10,646
Depreciation	3,348	3,631	3,975	4,317	4,526	4,452	4,353	4,455	4,281
Impairment losses	27	-	57	-	26	7	103	-	-
Amortization of goodwill	419	423	431	431	431	223	7	7	7
Gain on negative goodwill	-	-	-	-	-	-	-26	-	-
Change in working capital	-7,067	1,533	-3,094	12,316	-202	6,500	-2,956	-977	-4,980
Income taxes	-1,939	-1,851	-2,039	-1,386	-1,806	-3,097	-2,539	-3,685	-3,525
Cash flows from investing activities (2)	-4,575	-4,054	-5,878	-6,775	-3,360	-3,155	-2,924	-880	-2,742
Purchase of tangible/intangible fixed assets	-4,034	-3,843	-6,338	-7,289	-3,392	-3,093	-5,086	-3,198	-3,475
Proceeds from sale of tangible/intangible fixed assets	14	103	380	94	74	212	2,031	703	735
Free cash flow (1+2)	-5,295	5,905	-4,397	15,180	4,234	9,482	8,725	8,633	2,520
Cash flows from financing activities	5,257	-7,699	7,246	-13,990	-1,791	-9,948	-4,501	-6,678	-3,833
Net increase in short-term borrowings	-600	-8,400	500	-3,400	4,400	-5,340	1,913	-10,600	1,040
Net increase in long-term borrowings	6,923	1,989	6,306	-10,334	-3,555	-6,124	-3,858	-2,413	356
Proceeds from issuance of, and redemption of, bonds	-	-	1,978	1,475	-500	5,480	-500	3,979	-
Issuance of bonds	-	-	2,478	1,975	-	5,980	-	5,979	-
Redemption of bonds	-	-	-500	-500	-500	-500	-500	-2,000	-
Proceeds from issuance of shares	-	-	-	-	-	-	-	3,061	-
Acquisition of treasury shares	-	-3	-2	-370	-2	-2,123	-9	-5	-3,999
Disposal of treasury shares	-	-	-	368	-	-	-	1,517	997
Dividends paid	-538	-616	-617	-771	-1,171	-910	-1,101	-1,389	-1,417

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

Cash flows from operating activities

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

Cash flows from investing activities

Investments in tangible and intangible fixed assets vary between JPY3.0bn and more than JPY7.0bn, when payments rise to account for major expenditures as logistics centers. The company is thinking of establishing the tentatively named Tokyo Metropolitan Area Logistics Center, which would become operational between 2021 and 2022. The company expects possible investment of JPY8bn as it purchases land, buildings/structures, and machinery and equipment for that center.

Cash flows from financing activities

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

The company has not indicated a specific target for its dividend payout ratio. This ratio was 26.1% in FY03/16, 19.6% in FY03/17, 18.8% in FY03/18, 20.1% in FY03/19, and 20.6% in FY03/20.

Profitability and safety analysis

Profit margins (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Gross profit	69,033	64,286	66,730	64,613	70,731	73,068	76,475	78,197	81,833
GPM	11.4%	10.4%	10.2%	10.1%	10.5%	10.4%	10.4%	10.4%	10.3%
Operating profit	4,174	3,726	4,472	2,461	5,699	7,384	8,857	8,892	9,326
OPM	0.7%	0.6%	0.7%	0.4%	0.8%	1.0%	1.2%	1.2%	1.2%
EBITDA	7,522	7,357	8,447	6,778	10,225	11,836	13,210	13,347	13,607
EBITDA margin	1.2%	1.2%	1.3%	1.1%	1.5%	1.7%	1.8%	1.8%	1.7%
Net margin	0.3%	0.3%	0.4%	0.2%	0.5%	0.7%	0.9%	0.9%	0.9%
Financial ratios									
ROA (RP-based)	2.0%	1.8%	2.1%	1.1%	2.7%	3.5%	4.0%	3.9%	4.1%
ROE	3.5%	3.7%	4.9%	2.1%	5.9%	8.4%	9.7%	9.1%	8.8%
Total asset turnover	323.8%	312.8%	318.6%	298.6%	312.6%	326.6%	331.1%	323.3%	326.8%
Working capital	51,154	48,570	51,484	41,732	41,969	35,189	38,206	39,536	43,698
Current ratio	123.5%	125.1%	128.6%	117.6%	117.0%	123.8%	117.4%	134.9%	133.4%
Quick ratio	92.4%	93.3%	98.2%	91.6%	92.6%	96.6%	94.6%	108.9%	107.4%
OCF / Current liabilities	-0.6%	8.6%	1.2%	17.9%	6.0%	10.0%	8.6%	6.9%	4.0%
OCF / Total liabilities	-0.5%	6.3%	0.9%	13.9%	4.6%	7.7%	6.8%	5.8%	3.2%
Cash conversion cycle (days)	5.89	6.95	6.38	5.32	3.02	0.63	-1.36	-0.91	0.04
Change in working capital	6,852	-2,584	2,914	-9,752	237	-6,780	3,017	1,330	4,162

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

Historical performance

Full-year FY03/20 results (out May 11, 2020)

Summary

- Full-year FY03/20 results: Sales were JPY796.2bn (+5.5% YoY), operating profit was JPY9.3bn (+4.9% YoY), recurring profit was JPY10.1bn (+7.4% YoY), and net income was JPY7.2bn (+4.2% YoY). Results were modestly ahead of company forecasts (sales: JPY771.0bn, operating profit: JPY9.3bn, recurring profit: JPY10.0bn, net income: JPY6.5bn). GPM decreased from 10.4% in FY03/19 to 10.3% in FY03/20, but the SG&A-to-sales ratio fell from 9.2% to 9.1% over the same period as a result of limiting the YoY rise in SG&A expenses to 4.9%. While logistics costs increased, ARATA was able to limit the rise in indirect expenses through the consolidation of operations and other means, and this contributed to the improved SG&A ratio.
- In Q4, sales were JPY194.3bn (+10.2% YoY). Although GPM deteriorated YoY (10.3% compared with 10.6% in Q4 FY03/19), the SG&A-to-sales ratio was also lower (9.3% compared with 9.5% in Q4 FY03/19), and as a result, operating profit increased 5.5% YoY to JPY2.1bn. Over the quarter, sales of paper products increased amid the novel coronavirus pandemic, and the company believes the resulting change in product mix was the reason GPM deteriorated.
- Shareholder returns: The annual dividend for FY03/20 will be JPY85.0 per share, up from JPY80.0 per share in FY03/19. The payout ratio is 20.6%. Under its policy to maintain stable dividends, the company is forecasting an annual dividend of JPY85.0 per share for FY03/21. Regarding the acquisition of treasury stock announced in August (maximum 800,000 shares [4.5% of the total number of shares outstanding], total acquisition cost: JPY3.0bn, acquisition period: August 5, 2019 to January 31, 2020), the company had purchased 747,300 shares at a cost of JPY3.0bn by January 31. In February, the company also disposed of treasury stock (220,000 shares of common stock [1.2% of shares outstanding] for a total disposition amount of JPY997mn [JPY4,535 per share] to be put towards a Board Benefit Trust (BBT) for executive compensation over the next five fiscal years).
- FY03/21 company forecasts are undetermined. This is because, with no end in sight to the novel coronavirus pandemic, the company cannot currently determine the impact it will have on earnings. Consequently, it has also postponed announcing its new medium-term management plan commencing FY03/21. At present, it plans on disclosing FY03/21 forecasts and the new medium-term plan at the time Q1 results are announced.

Sales by product category

Sales by product category: Sales were driven by Paper Products, and there was also strong growth in the Health & Beauty and Household categories. Sales were up 5.1% YoY to JPY250.0bn in Health & Beauty (cosmetics, oral care products, etc.), up 6.0% YoY to JPY112.0bn in Household (laundry and kitchen detergents, etc.), down 0.4% YoY to JPY69.1bn in Home Care (fragrances, deodorants, insect repellants, etc.), up 10.1% YoY to JPY162.2bn in Paper Products (diapers, toilet paper, etc.), up 5.8% YoY to JPY55.3bn in Home Goods (kitchen supplies, toiletries, etc.), and up 4.0% YoY to JPY147.7bn in Pet Goods/Other.

In Health & Beauty, an area of focus under the company's growth strategy, ARATA saw benefits from the April 2019 integration of Fashion Arata, a former subsidiary. In Household, the company continued to report brisk sales of large-volume refillable products, while in Q4 it also registered increased sales of high-performance detergents with an antibacterial effect. Even in normal circumstances demand in the Paper Products category is comparatively stable, and in FY03/20 sales were further buoyed by a spike in demand ahead of the October 2019 consumption tax hike, and bulk buying of certain products as the novel coronavirus disease spread.

In Q4, in addition to sales rising 25.5% YoY in Paper Products due to the novel coronavirus pandemic, growth in sales was also comparatively strong in Health & Beauty (+5.7% YoY), Household (+8.7% YoY), Home Goods (+9.6%), and Pet Goods/Other

(+8.5%). Home Care sales dipped 2.4% YoY, as a comparatively cool summer and warm winter respectively led to weakness in insecticide and disposable body warmer sales.

As a company that handles daily necessities, ARATA firmly believes that its social mission is to ensure a stable supply of products to consumers. In order to restore stability to the supply of toilet paper and tissue paper, which at one point were the subject of panic buying on account of the pandemic, the company sought to minimize in-store stock shortages by swiftly renting additional warehouses to improve distribution, and expanding its fleet of delivery vehicles to enable more frequent deliveries.

The company reported a GPM of 10.3% for Q4, down from 10.6% a year earlier. It attributed this decline to an increase in the sales weighting for low-margin paper goods, from 20.5% in Q4 FY03/19 to 23.4%. According to ARATA, the GPM was flat YoY for Home Goods and Pet Goods/Other, but higher YoY for Paper Goods, Health & Beauty, Household, and Home Care.

Whereas many companies reported lower sales of cosmetics in Q4, sales in ARATA's Health & Beauty category increased YoY. Within the category, sales of cosmetics per se increased also, albeit at a low rate relative to other products in this category. This growth was a reflection of ARATA identifying cosmetics as an area of strategic importance, toward which end it has worked to secure new wholesale customers, and also is due to the high weighting of domestic demand for cosmetic products handled by ARATA, which accordingly have remained relatively immune to the recent fall in inbound demand.

Sales by customer type

Sales by customer type: Sales increased across all categories over FY03/20, including to mainstay drugstores. Sales were up 6.4% YoY to JPY391.9bn to drugstores, 2.1% YoY to JPY126.8bn to DIY centers, 5.1% YoY to JPY98.6bn to supermarkets, 6.8% YoY to JPY59.5bn to discount stores, 3.1% YoY to JPY41.8bn to GMSs, and 8.1% YoY to JPY77.7bn to customers in the "Other" category (including online retailers and cross-border e-commerce businesses).

In Q4, sales were up 10.7% YoY to drugstores, 10.5% YoY to DIY centers, 12.4% YoY to supermarkets, 8.1% YoY to discount stores, 6.9% YoY to GMSs, and 8.0% YoY to customers in the "Other" category. The company reported strong sales growth in every sales channel.

SG&A expenses

SG&A expenses rose 4.6% YoY to JPY72.5bn in FY03/20, below the 5.5% increase reported for sales. Although packing and transportation expenses were 8.4% higher YoY at JPY22.0bn (due to a steep increase in distribution expenses), growth in personnel expenses and other expenses both were kept to rates smaller than the increase in sales (+4.1% YoY to JPY30.9bn and +1.4% YoY to JPY19.6bn).

In Q4, SG&A expenses increased 7.1% YoY to JPY18.0bn. Packing and transportation expenses rose a sharp 12.6% YoY to JPY5.5bn, as amid short supply, the company handled more large-volume, low-priced items such as toilet paper, while also temporarily renting warehouse space in order to stabilize supply, and expanding its fleet of delivery vehicles to enable more frequent deliveries (as of May 2020, the company had vacated these temporary warehouses). Personnel expenses rose by 7.2% YoY to JPY7.7bn, as the company also took on more temporary workers (including warehouse staff) as a means of stabilizing supply. In short, ARATA did not stint from investing in fulfilment of its social mission.

Cumulative Q3 FY03/20 results (announced February 5, 2020)

Summary

- Cumulative Q3 results: Sales were JPY601.9bn (+4.1% YoY), operating profit was JPY7.3bn (+4.7% YoY), recurring profit was JPY7.9bn (+9.0% YoY) and net income attributable to owners of the parent was JPY5.8bn (+11.9% YoY). Cumulative Q3 sales improved YoY despite a tough operating environment in Q3, including a slump in of seasonal products due to a relatively warm winter and a reactionary decline in demand following last-minute spending ahead of the consumption tax hike. Distribution-related expenses increased in accordance with higher sales, but the company's ability to curtail the rise in indirect expenses contributed to operating profit growth. The company has made no changes to its full-year FY03/20 forecasts. Cumulative Q3 progress rates against full-year forecasts were 78.1% for sales (76.6% in cumulative Q3 FY03/19), 78.0% for operating profit (77.9%), and 89.6% for net income (75.4%).

- ▷ Q3 (October–December) results: Q3 sales were JPY195.6bn (-0.8% YoY), operating profit was JPY2.2bn (-9.5% YoY), and net income was JPY2.0bn (+4.8% YoY). Sales tracked above prior-year levels through the first half of October, supported by orders from retailers (drugstores and so forth) whose inventories had been depleted by rush demand at end-September, ahead of the October consumption tax hike. From the second half of October, sales fell below the previous year's levels owing to a snapback decline in demand, but December sales were on par with the year-earlier level, according to the company. This seems to suggest that the consumption tax hike no longer is impacting demand. The Q3 gross profit margin of 10.4% was above the previous year's 10.3%, as the higher consumption tax rate appears to have had little impact on transaction prices, and moreover there was an increase in the sales weighting of the Health & Beauty segment (which includes high value-added, profitable merchandise such as cosmetics). SG&A expenses were 1.9% higher YoY, due to increases in personnel and logistics expenditure, and the ratio of SG&A expenses to sales rose to 9.3% from 9.0% a year earlier.
- ▷ Sales by customer type: Q3 sales were up 1.8% YoY to JPY96.5bn to mainstay drugstores, down 5.4% YoY to JPY31.2bn to DIY centers, down 2.4% YoY to JPY24.1bn to supermarkets, up 0.5% YoY to JPY14.8bn to discount stores, and down 4.6% YoY to JPY10.2bn to GMSs. In the "Other" category (including online retailers and cross-border e-commerce businesses), sales were down 2.1% YoY to JPY18.7bn. The increase in sales to drugstores continued even amid sluggish demand after the consumption tax hike, and was due in part to higher sales of cosmetics to chains that previously handled only a small volume of such products.
- ▷ Sales by product category: Sales in Q3 were up 3.8% YoY to JPY63.4bn in Health & Beauty, which includes cosmetics and oral care products, down 2.6% YoY to JPY28.5bn in Household, which includes clothing and kitchen detergents, down 0.1% YoY to JPY13.2bn in Home Care, which includes fragrances, deodorants, and insect repellants, down 4.3% YoY to JPY37.4bn in Paper Products, which includes diapers and toilet paper, down 8.5% YoY to JPY15.0bn in Home Goods, which includes kitchen supplies and toiletries, and essentially flat (+0.0% YoY) at JPY38.2bn in Pet Goods/Other. Increased business with drugstores contributed to growth in Health & Beauty sales.
- ▷ Industry realignment: Consolidation is ongoing in the drugstore industry, which is a key sales channel for Arata. In January 2020, Matsumotokiyoshi Holdings (3088, TSE-1) and Cocokara Fine (3098, TSE-1) signed an agreement concerning a business and capital alliance in the lead-up to a merger that is scheduled to take place in October 2021. Shared Research understands that Arata is a leading supplier for Cocokara Fine, but has limited dealings with Matsumotokiyoshi in Japan. Arata regards this kind of industry consolidation as an opportunity to secure new business and further increase its exposure to the drugstore sector. Cocokara Fine also has plans to form a business alliance with H2O Retailing (8242, TSE-1), and form a joint venture with H2O Retailing subsidiary Izumiya Co., Ltd., to sell pharmaceuticals, cosmetics, and so forth. This, too, has potential to boost ARATA's market share.
- ▷ Next medium-term business plan: Arata is expected to unveil a new business plan in May 2020, as FY03/20 is the final year of the current medium-term plan. Growth strategies for the next ten years are likely to be a key focus of the new business plan.

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

1H FY03/20 results

Summary

- **1H FY03/20 results:** Sales were JPY406.3bn (+6.6% YoY), operating profit was JPY5.0bn (+12.5% YoY), recurring profit was JPY5.4bn (+15.6% YoY), and net income attributable to owners of parent was JPY3.9bn (+15.9% YoY). Results outperformed initial forecasts (sales: JPY394.0bn, operating profit: JPY4.9bn). As well as ongoing aggressive sales activities toward achieving medium-term plan targets, increased transactions relating to rushed demand prior to the consumption tax hike was a contributing factor to outperformance. The company has made no changes to its full-year FY03/20 forecasts. Against full-year forecasts, 1H sales reached 52.7% of the target, operating profit 54.2%, and net income 59.4%. Q2 (July–September) results were sales of JPY210.9bn (+11.5% YoY), operating profit of JPY2.5bn (+27.8% YoY), and net income of JPY1.8bn (+13.9% YoY).
- **Sales by customer type:** Sales increased across all customer types in Q2 due in part to the rushed demand prior to the consumption tax hike. Sales were up 10.8% YoY to JPY101.7bn to mainstay drugstores, up 8.0% YoY to JPY34.1bn to DIY centers, up 12.8% YoY to JPY26.3bn to supermarkets, up 14.3% YoY to JPY16.1bn to discount stores, and up 8.1% YoY to JPY11.0bn to GMSs. In the "Other" category (including online retailers and cross-border e-commerce businesses), sales were up 18.7% YoY to JPY21.9bn. Growth was relatively high in sales to discount stores, supermarkets, and drugstores.
- **Sales by product category:** Sales also increased across all product categories in Q2. Sales were up 11.5% YoY to JPY65.6bn in Health & Beauty, up 14.9% YoY to JPY30.5bn in Household, up 8.0% YoY to JPY19.5bn in Home Care, up 19.2% YoY to JPY42.3bn in Paper Products, up 1.6% YoY to JPY14.8bn in Home Goods, and up 7.1% YoY to JPY38.3bn in Pet Goods/Other. Growth in sales was relatively high in Paper Products (all types of baby diapers, toilet paper, etc.), Household (laundry detergent, kitchen cleansers, etc.), and Health & Beauty (cosmetics, oral-care products, etc.).
- **Operating profit up 27.8% YoY:** Gross profit increased 9.3% YoY to JPY21.1bn in Q2, while GPM deteriorated slightly YoY to 10.0% (from 10.2% in Q2 FY03/19). The dip in GPM was mainly caused by the fact that sales growth from rush demand preceding the October consumption tax hike was concentrated in low-margin products. It appears GPM is rising in product categories designated as areas of focus in the company's strategy. On the other hand, SG&A expenses increased just 7.2% YoY to JPY18.6bn, with the SG&A expenses to sales ratio improving YoY to 8.8% (from 9.2% in Q2 FY03/19). Although distribution-related expenses increased in accordance with higher sales, efforts to control the rise in indirect expenses contributed to improving the SG&A ratio.
- **Shareholder returns:** There is no change in the annual dividend forecast of JPY85 per share in FY03/20 (JPY40 per share in 1H, JPY45 per share in 2H). Regarding the acquisition of treasury stock announced in August (maximum 800,000 shares [4.5% of the total number of shares outstanding], total acquisition cost: JPY3.0bn, acquisition period: August 5, 2019 to January 31, 2020), the company had purchased 430,900 shares at a cost of JPY1.6bn by October 31.

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

Measures to capture rush demand

Sales expanded a substantial 11.2% YoY in Q2 FY03/20 (July–September) to JPY211bn. Chain stores, the company's main customers, implemented sales promotions in an attempt to capture rush demand preceding the October consumption tax hike. The company was able to capture the surge in demand by implementing measures to meet the specific needs of each customer type before the tax hike went into effect. It secured ample stocks of popular products in advance, ensured it had sufficient inventory to meet the temporary swell in logistics demand, and made prior arrangements with delivery companies to ensure its delivery capabilities would be able to keep up with demand.

Sales by customer type

Sales were up 10.8% YoY to JPY101.7bn to mainstay drugstores, up 8.0% YoY to JPY34.1bn to DIY centers, up 12.8% YoY to JPY26.3bn to supermarkets, up 14.3% YoY to JPY16.1bn to discount stores, and up 8.1% YoY to JPY11.0bn to GMSs. In the "Other" category (including online retailers and cross-border e-commerce businesses), sales were up 18.7% YoY to JPY21.9bn. Growth was relatively high in sales to discount stores, supermarkets, and drugstores.

From the company's perspective, the expansion in sales through the first half of September was not as sharp as before the previous consumption tax hike in March 2014. However, according to the company, sales surged dramatically in the second half of September so that customers' inventory levels were short by the end of the month. Inbound orders were relatively high through the first half of October, but declined afterward due to the expected recoil in consumer demand.

The company estimates rush demand will account for JPY17bn plus (=JPY210.9bn – 189.2bn x 1.022) in FY03/20, assuming it grows at its typical rate of growth during the year (2.2%, according to company forecasts).

Sales by product category

Sales were JPY65.6bn in Health & Beauty (+11.5% YoY), JPY30.5bn in Household (+14.9%), JPY19.5bn in Home Care (+8.0%), JPY42.3bn in Paper Products (+19.2%), JPY14.8bn in Home Goods (+1.6%), and JPY38.3bn in Pet Goods/Other (+7.1%).

Sales growth in Paper Products (all types of diapers, toilet paper, etc.), Household (laundry detergent, kitchen cleansers, etc.), and Health & Beauty (cosmetics, oral-care products, etc.). We infer that consumers' stocks of these products has increased. The company's medium-term plan calls for strategically expanding sales in the Health & Beauty, Home Goods, and Pet Goods/Other categories. Growth in these categories in Q2, however, was not so much the result of strategic intent as it was of the impact of rush demand.

Slight decline in GPM

In Q2, gross profit increased 9.3% YoY to JPY21.1bn and GPM fell 0.2pp YoY to 10%. The dip in GPM was mainly caused by the fact that sales growth from rush demand preceding the increase in consumption tax was concentrated in low-margin products. However, it appears GPM is rising in product categories designated as areas of focus in the company's strategy (Health & Beauty, Home Goods, etc.). It appears the company's initiatives to raise GPM are steadily having the desired effect. It is possible that GPM could rise if the post-tax-hike slump causes a decline in the portion of sales occupied by low-margin products and the GPM for the company's strategic products continues to climb.

SG&A expenses

SG&A expenses rose 7.2% YoY to JPY18.6bn. The SG&A-to-sales ratio improved to 8.8% from 9.2% in Q2 FY03/19. Logistics costs rose due to factors such as higher sales, measures to handle rush demand, and more expensive shipping costs. On the other hand, the company held back on personnel expenses and other expenses, which contributed to the decline in the SG&A-to-sales ratio.

Initiatives for long-term growth

ARATA explained its recent initiatives, based on its medium-term plan, in its 1H results briefing. The most striking initiative was the company's plan to increase joint development projects with manufacturers to produce ARATA-exclusive products sold as private brands.

Up until this point, the company has sought to develop private brand products that were more affordably priced than the corresponding national brands. It has recently shifted focus to developing unique products that will be recognized by consumers for the added value they provide. According to the company, unscented softener Fabrush, one of the products it developed in the past, has received positive reviews from consumers. The manufacturers of large national brands sell many types of scented softeners, but unscented softeners were new to the market and customers recognized the value they offered.

ARATA has also started applying its skill in proposing solutions for retail spaces, honed through experience in handling cosmetics, to home goods (cooking items). For many years, the company has purchased products from a large number of cooking item manufacturers, including SMEs, and sold them to supermarkets, general merchandise stores (GMSs), and drug stores. It is now focused on cooperating with manufacturers to develop products with a unified design theme, and plans to promote retail space solutions that display sets of these products. The aim is to increase the number of items consumers purchase by improving the attractiveness of cooking item sales spaces in supermarkets, GMSs, and drug stores.

Fabrush unscented softener (left) and cooking items (right)

Source: Company data

The company discussed other initiatives including: 1) introducing robotic process automation (RPA) to increase the efficiency of company operations (The company saved 11,000 hours/year of labor in 1H, mainly in indirect operations. It is targeting 26,000 hours/year by end-FY03/20); 2) improving supply chain efficiency (Cooperate with manufacturers on programs to increase logistics efficiency and reduce standby time and handling time for truck drivers); and 3) strengthening the domestic e-commerce business and overseas business (including cross border e-commerce; Sales at the Business Development Division, which manages both businesses, grew by 32% YoY).

FY03/20 is the last year of ARATA's current medium-term plan (FY03/18–FY03/20). The company plans to announce its new medium-term plan in May 2020.

Q1 FY03/20 results

Summary

- Q1 FY03/20 results: Sales were JPY195.4bn (+1.8% YoY), operating profit was JPY2.5bn (+0.2% YoY), recurring profit was JPY2.7bn (+5.6% YoY), and net income attributable to owners of parent was JP2.1bn (+17.6% YoY). The company has made no changes to its 1H and full-year FY03/20 forecasts. Against 1H forecasts, Q1 sales reached 49.6% of the target, operating profit reached 50.8%, and net income reached 60.9%. Against full-year forecasts, sales reached 25.3%, operating profit reached 26.8%, and net income reached 31.8%. The company also announced plans for the acquisition of treasury stock (maximum of JPY3.0bn).
- Sales by customer type: Sales to mainstay drugstores were up 2.7% YoY to JPY96.4bn, sales to discount stores were up 5.0% YoY to JPY14.3bn, and sales to GMSs were up 0.6% YoY to JPY10.4bn. In contrast, sales to DIY centers were down 2.6% YoY to JPY31.8bn, and sales to supermarkets were down 0.8% YoY to JPY23.4bn. Performance by customer type also affected overall sales. In the "Other" category (including online retailers and cross-border e-commerce businesses), sales were up 7.0% YoY to JPY19.0bn.

- ▷ Sales by product category: Sales rose 2.9% YoY to JPY60.9bn in Health & Beauty, 4.6% YoY to JPY27.7bn in Household, 5.3% YoY to JPY12.8bn in Home Goods, and 1.9% YoY to JPY36.1bn in Pet Goods/Other. Sales growth centered on key areas outlined in the medium-term management plan. On the other hand, sales fell 5.5% YoY to JPY20.9bn in Home Care.
- ▷ Operating profit slightly up: Gross profit increased 2.2% YoY to JPY20.3bn and GPM improved slightly YoY to 10.4%. The company notes that this improvement in GPM was attributable to enhanced sales in high margin categories. Shared Research believes that H&B and Household goods are the most competitive categories in the company with a higher gross profit margin than other categories. Therefore gradual improvement in profitability in these areas is likely to have underpinned the improvement in GPM. SG&A expenses were up 2.4% YoY to JPY17.8bn. Growth in personnel expenses was held down to only 0.4% YoY, but packing and transportation expenses increased by 6.3% YoY. The company secured modest growth in operating profit, which increased 0.2% YoY to JPY2.5bn. Non-operating income and expenditures also improved mainly on the absence of arrangement fees for committed credit lines. Extraordinary gains/losses improved with the booking of gain on the sale of securities (JPY388mn). Following on from FY03/19, sales of shares in business partners continued to improve asset efficiency.
- ▷ Acquisition of treasury stock: Arata Corporation announced the acquisition of treasury stock for the purpose of implementing a more flexible capital policy, enhancing shareholder returns, and improving capital efficiency. The acquisition will be limited to 800,000 shares (4.5% of the total number of shares outstanding) and a total acquisition of JPY3.0bn. The acquisition period will run from August 5, 2019 to January 31, 2020. Shared Research thinks that the company’s confidence in achieving the performance targets set in the medium-term management plan and growth for the rest of the year has increased because 1) the company indicated in its medium-term management plan that it will maintain ROE of over 9% but less than 10%, and 2) Q1 results were in line with plan.
- ▷ Industry reorganization: Industry restructuring is currently underway in the drugstore industry, which forms the company's principal customer base. In particular, Sugi Holdings (TSE1: 7649) and Matsumotokiyoshi Holdings (TSE1: 3088) have made a merger approach to cocokara fine (TSE1: 3098). The company’s the securities report shows that Arata Corporation has policy shareholdings in cocokara fine and Sugi Holdings on the basis that these are deemed to be important business partners. There is no disclosure for Matsumotokiyoshi Holdings, and transaction volume with Matsumotokiyoshi Holdings is likely to be small. The company views industry restructuring as an opportunity to increase its market share as changes occur in the industry. cocokara fine intends to disclose the results of its review of a potential capital and business alliance after mid-August 2019.

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

Other information

History

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

Source: Shared Research based on company materials

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

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

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

In November 2006, ARATA established Dentsu Retail Marketing in collaboration with three other companies: Dentsu Tec, a subsidiary of Dentsu (TSE1: 4324), NEC (TSE1: 6701), and Dai Nippon Printing (TSE1: 7912). (Initially, ARATA held 20% of this company, an equity-method affiliate. Its equity stake is now 21.6%.) In April 2007, ARATA established ISM Corporation as a subsidiary. Its goal in setting up these companies was to help ARATA evolve from an entity connecting manufacturers and retailers into a company that could make useful proposals to retailers on creating effective retail spaces, adding value to the wholesale business.

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

News and topics

May 2020

On **May 12, 2020**, the company announced a third-party allotment of its equity-method affiliate, Dentsu Retail Marketing Inc.

The company's equity-method subsidiary, Dentsu Retail Marketing (DRM), will carry out a capital increase via third-party allotment of new shares with ITOCHU Corporation (TSE1: 8001) as the subscriber and a share transfer among shareholders. This will reduce the company's shareholding from 36.0% to 21.6%.

The company established DRM in 2006 with the Dentsu Group (TSE1: 4324). In collaboration with DRM subsidiary ISM Corporation, the companies have been providing retailers with proposals to create strong selling sales floors based on data. In the retail industry, there is an increasing amount of available data, and the demand for advanced marketing that leverages data and technology is growing. In addition, an increasing number of companies are using business process outsourcing (BPO) services for in-store sales promotion. With ITOCHU’s participation in DRM, the company plans to strengthen its services to meet these demands.

The company formulated a long-term vision of where it should be 10 years from now, with "storefronts" as the keyword of the vision. The company plans to deepen cooperation with the new DRM to strengthen its business. After the third-party allotment and share transfer, the shareholding ratios will be 53.3% for Dentsu Tec, 21.6% for ARATA, 20.0% for ITOCHU, and 5.1% for NEC (TSE1: 6701).

April 2020

On **April 7, 2020**, the company made an announcement concerning the impact of the novel coronavirus disease (COVID-19) outbreak to date.

Business operation status

The company has promoted flexible work arrangements for its employees according to their job duties. Measures include encouraging employees to commute at different times (thus avoiding the press of rush hour) or work from home. So far there has been no significant effect on business operations, including dealing with manufacturers and retailers. In addition, there has been no change to ARATA’s financial position as of April 7, and the company has been able to continue business without any issues, including for the health of its distribution center employees.

Impact on business performance

Due to a request from the government to refrain from going out stemming from the spread of COVID-19, many people’s activities are mainly limited to the home. Since the company delivers daily necessities (detergent, toilet paper, sanitizer, masks, shampoo, etc.) to retailers, business performance is not easily affected by short-term economic fluctuations. At present, there has been no significant impact on results. The company’s business structure has been organized so that it can handle any situation.

Concerning the FY03/20 financial results announcement

The financial results announcement for FY03/20 is scheduled for May 11, although the actual results briefing has been canceled. It is possible the announcement will be delayed due to delays in accounting and audits. The social and business environment is changing due to the impact of COVID-19, and Arata is continuing to scrutinize the effect on its FY03/21 earnings (and corresponding forecasts). The company says it will promptly report any serious issues that may arise within the business itself, or any changes it observes that are likely to have a significant effect on the business environment or the company’s performance.

March 2020

On **March 30, 2020**, Shared Research updated the report following interviews with the company.

Main points from the interview are outlined as follows:

1) Due to the spread of the novel coronavirus, some product groups are generating more demand than planned. These items mainly include a) those related to prevention of infections (e.g., face masks, alcohol disinfectants, and hand soaps), and b) paper goods such as toilet paper, tissue paper, and wet wipes. These trends have been seen not only in the company's mainstay business selling to drugstores, but also in its sales to home improvement stores, supermarkets/general merchandise stores, and discount stores. The supply system for paper goods has already stabilized after experiencing a temporary surge in demand due to hoarding. However, it is still difficult to secure a sufficient number of face masks to meet demand, and manufacturer production capacity of alcohol disinfectants and hand soaps is limited. It is currently not possible to procure these goods in quantities that meet the demands of retailers.

2) The company says that sales in its areas of focus, such as Health and Beauty (including cosmetics), have been strong. Although the number of foreign visitors to Japan is decreasing due to the spread of the novel coronavirus, the company expects the impact on its earnings to be minor since many of its products target domestic consumers.

3) Logistics costs seem to be higher than planned, affected by a temporary increase in demand for products with low transportation efficiency (low sales and gross margin per product volume) such as toilet paper. However, the increase in logistics costs is likely to be offset by the rise in gross profit.

Corporate governance and top management

Corporate governance

Form of organization and capital structure	
Form of organization	Company with Audit & Supervisory Board
Controlling shareholder and parent company	None
Directors and Audit & Supervisory Board members	
Number of directors under Articles of Incorporation	15
Number of directors	9
Directors' terms under Articles of Incorporation	1 year
Chairman of the Board of Directors	Chairman
Number of outside directors	3
Number of independent outside directors	3
Number of members of Audit & Supervisory Board under Articles of Incorporation	5
Number of members of Audit & Supervisory Board	4
Number of outside members of Audit & Supervisory Board	2
Number of independent outside members of Audit & Supervisory Board	2
Other	
Participation in electronic voting platform	Y
Providing convocation notice in English	Y
Implementation of measures regarding director incentives	Performance-linked compensations
Eligible for stock option	-
Disclosure of individual director's compensation	None
Policy on determining amount of compensation and calculation methodology	In place
Corporate takeover defenses	None

Source: Shared Research based on company materials (as of June 2020)

Top management

Chairman of the Board: Nobuyuki Hatanaka (born August 1, 1949)

Joined Tomen Corporation in 1972. In June 1974, entered Shukosha K.K., becoming a director in November, being appointed managing director in 1983, vice president in 1988, and president in 1998. In 2002, appointed representative director and chairman of Itoyasu Co., Ltd.; appointed representative director and chairman of SISCO Co., Ltd., in 2004; appointed representative director, vice president and executive officer of ARATA in 2006; and appointed representative director, president, and executive officer in 2007. In 2008, appointed representative director and chairman of Fashion Arata Corporation. Appointed representative director, chairman, and CEO of ARATA in 2017. Appointed Chairman of the Board in 2019.

Representative Director and President: Hiroaki Suzaki (born October 25, 1955)

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

Representative Director and Executive Vice President: Yoichi Suzuki (born April 23, 1953)

Joined Ito-I Co., Ltd. in 1980. Appointed director of ARATA in 2002. Appointed senior managing director and general manager of operations in 2004; appointed representative director, senior managing executive officer, general manager of administration, and head of the internal control office in 2007; appointed representative director, executive vice president, and general manager of administration in 2009; appointed representative director, executive vice president, general manager of administration, and general manager of systems in 2015. In 2018, appointed representative director, executive vice president, and general manager of administration.

Dividend policy

Per-share data (split-adjusted; JPY)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Shares outstanding (ex. treasury shares, mn)	15.4	15.4	15.4	15.4	15.4	14.7	16.7	17.7	17.1
EPS	105.6	114.7	158.0	73.0	210.4	331.0	399.1	397.7	413.0
EPS (fully diluted)	-	-	-	-	-	294.9	377.8	381.2	391.3
Dividend per share	40.0	40.0	50.0	50.0	55.0	65.0	75.0	80.0	85.0
Payout ratio	37.9%	34.9%	31.6%	68.5%	26.1%	19.6%	18.8%	20.1%	20.6%
Book value per share	3,068	3,180	3,309	3,496	3,628	4,055	4,285	4,547	4,861

Source: Shared Research based on company materials

The company has a basic policy of maintaining stable dividends, deciding the figure after taking into overall consideration performance during each fiscal year, as well as financial condition, and future development plans. The company has not set a specific target for the dividend payout ratio. This ratio was 26.1% in FY03/16, 19.6% in FY03/17, 18.8% in FY03/18, 20.1% in FY03/19, and 20.6% in FY03/20. The company plans to pay JPY90 per share in FY03/21, representing a payout ratio of 21.0%.

Major shareholders

Top shareholders	Shares held ('000)	Shareholding ratio
Otowasyokusan Co., Ltd.	1,081	6.2%
The Master Trust Bank of Japan, Ltd. (Trust account)	1,033	5.9%
Japan Trustee Services Bank, Ltd. (Trust account)	946	5.4%
ARATA Employee Shareholding Association	904	5.2%
Northern Trust Co. (AVFC) Re Fidelity Funds (Standing proxy: The Hongkong and Shanghai Banking Corporation Limited, Custody Department)	637	3.7%
STATE STREET BANK AND TRUST CLIENT OMNIBUS	600	3.4%
Lion Corporation	481	2.8%
Nobuyuki Hatanaka	459	2.6%
Trust & Custody Services Bank, Ltd. (Trus account E)	369	2.1%
Government of Norway (Standing proxy: Citibank N.A. Tokyo Branch)	361	2.1%
SUM	6,875	39.5%

Source: Shared Research based on company materials (as of end-March 2020)

Employees

Number of employees	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Consolidated	2,977	2,960	2,924	2,917	2,914	2,926	3,023	3,016	2,984
Temporary staff (average)	4,648	4,935	5,287	5,174	5,091	5,052	5,255	5,219	5,151
Parent	2,209	2,174	2,102	2,083	2,056	2,047	2,096	2,061	2,112
Temporary staff (average)	4,052	4,290	4,647	4,505	4,446	4,339	4,444	4,408	4,491

Source: Shared Research based on company materials

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

Key group companies

Name	Location	Voting rights	Category	Business
Japell Co., Ltd.	Kasugai	100%	Subsidiary	Wholesaling of pet-related products
Japell Partnership Service Co., Ltd.	Kasugai	100%	Subsidiary	Retail sales of pet-related products, grooming services, recruitment of franchise stores
Pet Library Ltd.	Komaki	100%	Subsidiary	Sales of pets, pet food and pet goods, pet grooming, boarding–related services
Mobby Co., Ltd.	Hiratsuka	100%	Subsidiary	Online sales of pet-related products
ISM Corporation	Tokyo	80%	Subsidiary	Store management company
Living Arata Co., Ltd.	Higashi Osaka	100%	Subsidiary	Wholesaling of home goods
ARATA (Shanghai) Trade Co., Ltd.	Shanghai	100%	Subsidiary	Wholesaling of home goods mainly
Japell (Hong Kong) Co., Limited	Hong Kong	100%	Subsidiary	Retailing, wholesaling, and import/export sales of pet-related products, as well as other related services
Arata (Thailand) Co., LTD.	Bangkok	49%	Subsidiary	Wholesale business in Thailand
SIAM ARATA CO., LTD.	Bangkok	75%	Subsidiary	Wholesale business in Thailand
DENTSU RETAIL MARKETING INC.	Tokyo	22%	Equity-method affiliate	Overall retail marketing, including market analysis, sales promotion plans, retail merchandising, and evaluation of marketing effects
Asahi Keshohin Hanbai Co., Ltd.	Urasoe, Okinawa	49%	Equity-method affiliate	Wholesale of cosmetics, perfumed soap, tooth paste, food and beverages, textile products, and miscellaneous goods

Source: Shared Research based on company materials

Profile

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

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cocokara fine Inc.
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FaithNetwork Co., Ltd.
Ferrotec Holdings Corporation
FIELDS CORPORATION
Financial Products Group Co., Ltd.
First Brothers Col, Ltd.
FreeBit Co., Ltd.
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Gamecard-Joyco Holdings, Inc.
GameWith, Inc.
GCA Corporation
Good Com Asset Co., Ltd.
Grandy House Corporation
Hakuto Co., Ltd.
Hamee Corp.
Happinet Corporation
Harmonic Drive Systems Inc.
HENNGE K.K.
Hope, Inc.
HOUSEDO Co., Ltd.
H2O Retailing Corporation
IDOM Inc.
IGNIS LTD.
i-mobile Co.,Ltd.
Inabata & Co., Ltd.
Infocom Corporation
Infomart Corporation
Intelligent Wave, Inc.
ipet Insurance CO., Ltd.
Itochu Enex Co., Ltd.
JAFCO Co.,Ltd.
JMDC Inc.
JSB Co., Ltd.
JTEC Corporation
J Trust Co., Ltd
Japan Best Rescue System Co., Ltd.
JINS HOLDINGS Inc.
JP-HOLDINGS, INC.
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Kanamic Network Co.,LTD
Kawanishi Holdings, Inc.
KFC Holdings Japan, Ltd.
KI-Star Real Estate Co., Ltd.
KLab Inc.
Kondotec Inc.
Kumiai Chemical Industry Co., Ltd.
Lasertec Corporation
Locondo, Inc.
LUCKLAND CO., LTD.
MATSUI SECURITIES CO., LTD.
Media Do Co., Ltd.
Medical System Network Co., Ltd.
MEDINET Co., Ltd.
MedPeer,Inc.
Mercuria Investment Co., Ltd.
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Net One Systems Co.,Ltd.
Nichi-Iko Pharmaceutical Co., Ltd.
Nihon Denkei Co., Ltd.
Nippon Koei Co., Ltd.
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NIPRO CORPORATION
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Toyo Tanso Co., Ltd.
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TSURUHA Holdings
VISION INC.
VISIONARY HOLDINGS CO., LTD.
World Holdings Co., Ltd.
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