J. Front Retailing

Summary of Q&A session at

Earnings call for the third quarter (Q3) of the fiscal year ending February 29, 2024

Date and time: 15:30 – 16:10 on Tuesday, December 26, 2023

Q. I understand that the Q3 results were almost in line with the plan, but I would like to know whether gross sales, gross profit, SG&A expenses, operating profit, and business profit are above or below the plan, and also progress by segment.

A. I think it is easier to understand progress by segment by looking at business profit. Our core businesses—department store business and shopping center business—are performing above the plan. As for challenges, the top line and profits of the payment and finance business are below expectations
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Q. Although figures have been announced through the first half of December, I don't think the trend has changed that much from the 3Q, so I feel that it will not be too difficult to achieve the full-year forecast. However, the yen may appreciate a little, and since the hurdles for the previous year will gradually increase from about January or February, I would like to know, for example, what are you paying close attention to in the department store business going forward, or conversely, what feedback you are getting?

A. As of the October announcement, inbound sales at Daimaru Matsuzakaya Department Stores are estimated to be just under 30 billion yen in the second half of the year, or an average of about 5 billion yen per month. But as I explained earlier, Q3 results were just under 6 billion yen.

Inbound sales are expected to grow steadily in the 4Q. On the other hand, domestic sales, including gaisho sales, were generally in line with the plans for Q3, and although total sales have not been revised, we believe there is room for an upward swing in light of the progress in Q3.

Department store sales, driven by luxury goods and high-end watches, are generating solid gross profit, but the profit margin is below the plan. We will strive to secure sales and gross profit, including in December and January, when sales and profits contributions are significant, to achieve the business profit target for the second half of the fiscal year.

Q. When look at Q3 as a single period, why was there an 8.7% decline in total sales for the Payment and Finance Business? The decline was considerably larger than in the first half of the fiscal year, with business profit slightly down by less than 500 million yen in the Q3 alone. If this pace continues in Q4, I wonder if the payment and financing business will offset the upturn in department stores and PARCO. Please explain in detail.

A. The Q3 results for the payment and finance business were harsh, with a decline in both sales and profits. As I mentioned in my presentation, the use of cards in department stores and by gaisho customers is increasing, so commission fees themselves are rising. On the other hand, the challenge is that the acquisition of new customers is not progressing as planned, which also translates into a decrease in annual card membership fees. In addition, a new point service called "QIRA points" was introduced as a JFR card when the card was renewed in January 2021, and the use of these QIRA points has been increasing. As a result, the point lapse rate has been lower than initially expected, leading to a decrease in sales revenue in the form of negative sales due to increased point expenses.

Q. Does that mean that for a while after the renewal of the card, you attracted more members than expected and the card switchover was smooth, but after a year, membership withdrawals increased due to the increase in membership fees, and conversely, the newly

launched QIRA points are being used more frequently, leading to a large negative impact on sales?

A. It was originally anticipated that the number of card accounts, especially for low-activity members, would decline as a result of the card renewal. On the other hand, before and after the card renewal, annual membership fee income grew significantly, and transaction volume per account increased, leading to increased efficiency.

The challenge is to acquire new customers, and the first step is to work with department stores to acquire cardholders. The number of department store app members reached 2.09 million in the Q3, but less than half of them have both the app and the card. We believe it is important to encourage these app members to hold JFR cards.

In addition, it is important to consolidate the Group's cards, including PARCO's. Although currently investment is ahead of schedule, we recognize the need to expand the customer base of the group and its credit card members.

Q. In other words, the payment and finance business was initially profitable as planned in the mid-term business plan. Now, since there are areas where you are somewhat off your estimates, as you move forward with the development of basic infrastructure, will you be presenting a more medium- to long-term picture in the next medium-term business plan? I think this is an important part of the portfolio, so I would appreciate your cooperation.

A. Yes, I understand.

Q. Real estate lease revenues have grown considerably, which is probably higher than planned and is contributing to profit. But was the reason for this is the strong performance of GINZA SIX? As this is a higher growth rate than the annual forecast, is it correct to recognize this as an upward trend?

A. The largest share of real estate lease revenue comes from GINZA SIX and the Daimaru Shinsaibashi store, so they are the contributing factors.

Q. First, profits by segment are shown on page 4 of the reference material, but there is a large deviation in the adjusted business profit from the previous year, both for the three-month period and for the nine-month total. What is the explanation for this and why is it increasing?
**Added after QA*

A. The increase in the adjustment of business profit in Q3 is due to the adjustment of unrealized profit on software related to a new accounting system at JFR (non-consolidated), personnel expenses at JFR (non-consolidated), and a 400 million yen increase in expenses associated with the renovation of the new accounting system and unification of groupware, which are common infrastructure for the group.

On the other hand, the upward adjustment in operating profit in the Q3 (non-consolidated) was due to a gain of approximately 700 million yen from the transfer of shares in SLH.

Q. In your explanation of the payment and finance business, I believe you mentioned that operating profit decreased due to an increase in fraudulent card use. Please explain whether this negative impact is a temporary decrease in the Q3, whether it will continue in the future, or whether they are bunched together and come out in the 3Q results? If this is a one-time cost, I would like to know the amount as well. Or if there is any insurance that would reimburse us?

Ａ．As for expenses associated with card fraud, this is not a one-time event, but rather an occurrence that includes Q1, Q2, and Q3. The cumulative total for the March to November period in the third quarter is approximately 270 million yen. This is not a sudden increase from this year, but rather a doubling of the pace from approximately 130 million yen in FY2022 and less than 100 million yen in FY2021.

This is said to be an industry issue, including our company, and the damage caused by this kind of abuse, including so-called phishing scams, is increasing. The negative impact of this on profit and loss is gradually increasing.

As for countermeasures, we are currently working on system modifications to review the payment flow for customers, although we will naturally conduct awareness raising activities toward customers about this issue. We believe that there will be a certain amount of impact on the current fiscal year, including the Q4, but we will work to reduce these costs by taking measures in the next fiscal year and beyond.

Q. On page 4 of the earnings presentation, between consolidated operating profit and operating profit, you mention other operating expenses, but I believe that at the time of the Q2 results, the forecast for other operating expenses was changed from the initial 3 billion yen to 5.7 billion yen. As a result, only 2.9 billion yen was recorded for the nine-month period, so I would like to know what other operating expenses are expected in Q4.

Ａ．Other operating expenses, the portion that corresponds to an extraordinary loss in Japanese GAAP terms, are included in the figures announced in October, assuming a certain amount of loss on disposal of fixed assets and impairment losses.

As you are aware, in the current medium-term business plan, we have been proceeding with management structural reforms while identifying problem businesses and stores. We are currently discussing the next medium-term business plan, and we have included a certain amount of money in the plan, assuming that we will take actions as necessary in conjunction with the mid-term outlook for each business and store. However, at this point, we have no major plans, including for the Q4.

Q. This fiscal year is the final year of the current medium-term business plan. Are you aware that the various numerical targets you originally set, such as ROE of 7% and ROIC of 5%, are fully achievable given the current progress of your business performance? If so, although of course the situation is that cash has increased significantly because of the sale of investment securities holdings, is my understanding correct that there is no change in the current financial policy, which is to go one step further from the current policy of a dividend payout ratio of 30% or more, in light of the increase in cash and deposits?

Ａ． It is safe to say that the series of performance targets announced in October are on track at this point. On the other hand, we are currently discussing the next medium-term business plan with regards to the return ratio and other matters. As you pointed out, our current basic policy is to maintain a consolidated dividend payout ratio of 30% or more. But as we look ahead to the next medium-term business plan and the year 2030, we will be looking to expand not only our core businesses but also our payment and finance business and our developer business. The Board of Directors is currently discussing cash allocation, including investment in each of these businesses. We would like to issue a firm policy in April, including the purpose of your comments.

Q. Just for the record, what is your opinion of the current dividend payout ratio of 30% or more. From your company's perspective, is it low or high in terms of the current balance sheet and the current direction of business performance?

A． Currently, our policy is to maintain a dividend payout ratio of 30% or more, but due to the COVID-19 pandemic, we are aware that we are in fact returning more than 30% of our profits to shareholders. However, we would like to discuss the future policy itself and the total return ratio, including share buybacks, in management before issuing a statement.

Q. Understood, since the P/B ratio has been below 1x for quite a long time, I would like to ask for various positive considerations.

A． I understand

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