



**Hiroshi Aoi**

President and Representative Director  
Representative Executive Officer

**Message from the President**

# A Step toward a Future of Creating Corporate Value

**Emerging Issue**

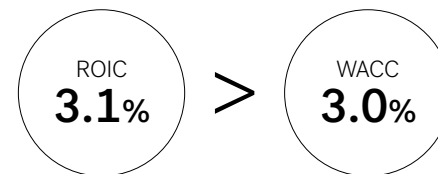
First, let me begin by discussing our performance in the fiscal year ended March 31, 2017, the first year of our current five-year medium-term management plan. During this year, we made smooth progress in advancing this plan, achieving earnings per share (EPS) of ¥80.2, an increase of 14% year on year, and return on equity (ROE) of 6.7%, up 0.7 percentage point. Both indicators met their targets. Operating income grew 6%, rising for the 8th consecutive year, to ¥31.3 billion, and a new record was set for cash dividends per share of ¥33, ¥11 higher than in the previous fiscal year. In addition, return on invested capital (ROIC) exceeded weighted average cost of capital (WACC) as a result of our financial strategies for achieving an optimal capital structure. Accordingly, we are at last poised to begin creating corporate value. Perhaps a more noteworthy accomplishment was MARUI GROUP's inclusion in all three of the

environmental, social, and governance (ESG) investment indexes adopted by the Government Pension Investment Fund of Japan in July 2017 (→P.134).

In this manner, MARUI GROUP took a step toward a future of creating corporate value during the fiscal year ended March 31, 2017. However, an issue also emerged. Our total shareholder return (TSR) for this year was a negative 4.5%, well below the Tokyo Stock Price Index average of 17%. Some may be curious why, despite a massive increase in per share dividends from ¥22 to ¥33 on the back of a large 14% rise in EPS, the Company's TSR fell below the market average.

The reason was most likely that investors and other stakeholders were unable to fully understand MARUI GROUP's corporate value, and therefore could not evaluate the Company properly. Based on our interactions with stakeholders to date, we have identified two causes for the difficulty in properly understanding and evaluating our corporate value.

Transition to a Structure in which ROIC Exceeds WACC  
(Fiscal year ended March 31, 2017)



Inclusion in ESG Investment and Socially Responsible Investment Indexes

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The first cause is trouble understanding the unique business model of MARUI GROUP. The second cause is our failure to clearly describe our future initiatives or, in other words, our measures for addressing risks. In *Co-Creation Management Report 2017*, we will endeavor to more thoroughly explain MARUI GROUP's business model and the opportunities and threats we face.

## 1. MARUI GROUP's Business Model

### Identity of *Euglena*

A major characteristic of MARUI GROUP is the unique business model merging retailing and finance that it has employed since its founding. For those of us on the inside of the Company, shaping our actions based on this model is a natural part of everyday business. However, when viewed from outside of the Company, this model has been difficult to understand, with the meaning of "merging retailing and finance" being particularly unclear. In fact, the most common question received from investors was whether MARUI GROUP was a retailer or a financial company. We would always respond to this question by saying "both," but, unfortunately, there were few who were able to fully grasp what we meant.

While this may be a bit of an unorthodox comparison, the situation was similar to someone asking a species of *Euglena* whether it is a plant or an animal. Faced with this

question, the organism would have to answer "both." Although the inquirer would understand better if the *Euglena* were to say "animal" or "plant," either answer would entail denying its own identity. The *Euglena* cannot do that, and neither can we. Just as *Euglena* species have distinctive value due to their combining the characteristics of both animals and plants, so too does MARUI GROUP derive its unique corporate value from blending retailing with finance.

### Reversal of Relationship between Retailing and Credit Cards

Let me go into a little more detail. MARUI GROUP was a retailer with approximately 6.4 million cardholders, and we grew by having loyal cardholders shop at Marui stores. Taking a different perspective, however, it could also be said that MARUI GROUP was a financial company with stores where roughly 200 million customers shopped each year. Either way, we have grown primarily through retailing operations by providing credit cards as a tool to offer customers greater convenience when shopping at Marui stores.

Today, we are witnessing a shift in consumption from goods to experiences, which has also made it necessary for us to change the relationship between retailing and credit cards. In light of this trend, we transformed our business model by transitioning away from our previous credit card, which was only usable at Marui stores, to a

new multipurpose card that can be used anywhere in the world. This new card was the EPOS card launched in 2006. Since issuing EPOS cards, our number of cardholders has increased by 1.6 times, from about 4.0 million to around 6.4 million, and card shopping transactions have risen by approximately 8 times, from ¥180.0 billion to ¥1,390.0 billion. Furthermore, although 100% of card transactions used to take place within Marui stores, this figure has since dropped below 10%. Previously, credit cards supported the growth of our retailing operations. However, as I have explained, this relationship has been reversed, and now our stores are supporting the growth of our credit card operations.

This change in business structure is most clearly apparent on our balance sheet. In the past, the land, structures, and other fixed assets that had supported MARUI GROUP's growth since its inception represented a majority of assets. Everything changed in the fiscal year ended March 31, 2014, when the balance of credit card operating receivables came to account for more than half of our assets. Since then, this balance has continued to rewrite record highs.

### Retailing and Finance— Two Sides of the Same Coin

What I want to make perfectly clear is that this change in business structure—this innovation—did not transform MARUI GROUP from a retailer to a financial company, but rather that it led to our using the stores of our retailing operations to drive the growth of our credit card operations. I mentioned that only less than 10% of total credit card transactions are conducted at Marui stores. However, approximately 80% of cardholders applied at Marui stores, clearly illustrating how both businesses are in a mutually complementary relationship and are intrinsically linked.

For example, you could say that retailing and finance are two sides of the same coin for MARUI GROUP. If you stand a coin on its edge and give it a spin, the spinning coin will appear to take the shape of a sphere. Our business model is like this spinning coin, with no heads or tails, just one sphere of retailing and finance.

By taking a snapshot in time of this sphere, we can report on our financial condition by showing the two circles, one for retailing and one for finance, that would be

visible in this picture. A great deal of information can be gleaned from this picture. One could take the perspective of looking at which circle is larger and which is smaller or which is heads and which is tails. However, we see such information as only supplementary and not as truly important to MARUI GROUP.

To MARUI GROUP, it is important for the "coin" to spin more smoothly, gain speed, and ultimately draw a more powerful and beautiful sphere.

For this reason, we do not segregate retailing and finance. Rather, we share human resources, stores, and data throughout our integrated business as we seek to improve corporate value by evolving our unique business model merging retailing and finance.

## 2. Opportunities and Threats Faced by MARUI GROUP

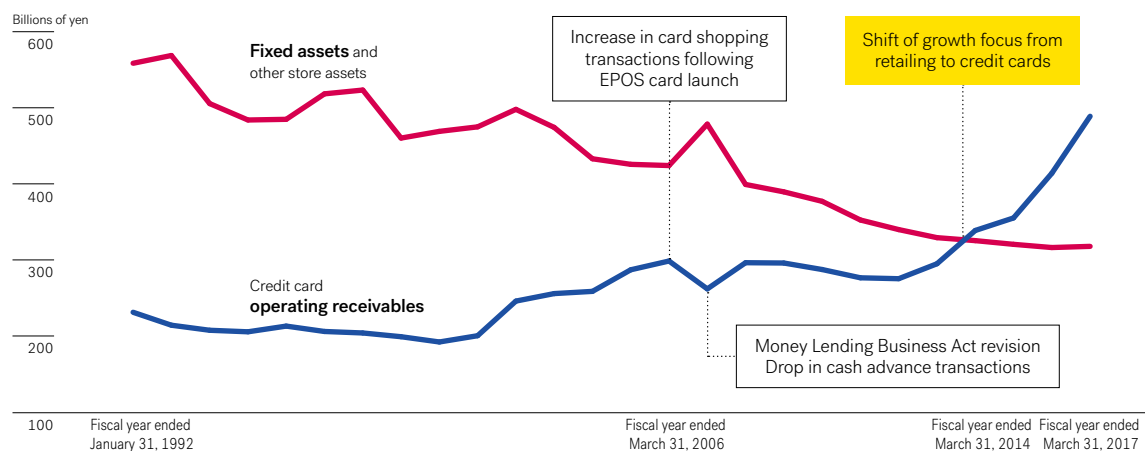
### Eight Operating Environment Changes over the Next Decade

The ability for MARUI GROUP's business model to continue creating corporate value into the future will hinge on our ability to furnish long-term responses to the changes in the operating environment that will be seen going forward.

I would therefore like to discuss the long-term operating environment changes we expect to see over the next decade. Specifically, we have identified eight major changes projected to occur. In this report, we will look at how these changes will unfold going forward, examine the opportunities and threats they will present for our business, and explain how MARUI GROUP intends to respond.

- (1) Transition to e-commerce
- (2) Shift from goods to experiences
- (3) Emergence of a sharing economy
- (4) Declining birthrate and aging population
- (5) Increase in demand from inbound travelers
- (6) Rise of cashless payment methods
- (7) Change of focus from saving to investment
- (8) End of era of low interest rates

### Balance Sheet Assets



### Opportunities and Threats for the Retailing Business

For the Retailing business, we see opportunities in the projected increase in demand from inbound travelers. However, we will also have to face numerous threats, the greatest of which may be the transition to e-commerce. As e-commerce becomes more prominent going forward, it can be expected that conventional retailing businesses selling goods at stores will begin to decline, a trend that is already apparent in the United States and China. This trend will be compounded by the shift from the consumption of goods to the consumption of experiences, which will decrease demand for goods. This decrease is currently visible with regard to apparel products, which have been undergoing a noted decline in demand in recent years.

At the same time, we project the emergence of a sharing economy. "Sharing" also means a reduction in the consumption of goods, making it a threat to retail businesses. Meanwhile, the declining birthrate and aging population will result in a decrease in the number of consumers.

We have formulated two main measures for responding to these changes. One measure is the transition to shopping centers and fixed-term rental contracts that we have been advancing under the medium-term management plan or, in other words, the transformation of our business model from focusing on a department store model to utilizing a real estate model. The other measure is the expansion of omni-channel retailing. The transition to shopping centers and fixed-term rental contracts entails deemphasizing apparel tenants, whose services will no

#### Opportunities and Threats to Be Faced by the Retailing Business over the Next Decade



doubt be replaced by e-commerce sales, to place more emphasis on tenants that provide dining, services, experiences, and other offerings that cannot be supplied via e-commerce. The expansion of omni-channel retailing will be conducted to deliver new value to consumers by evolving our retailing business in a manner that is complementary to e-commerce.

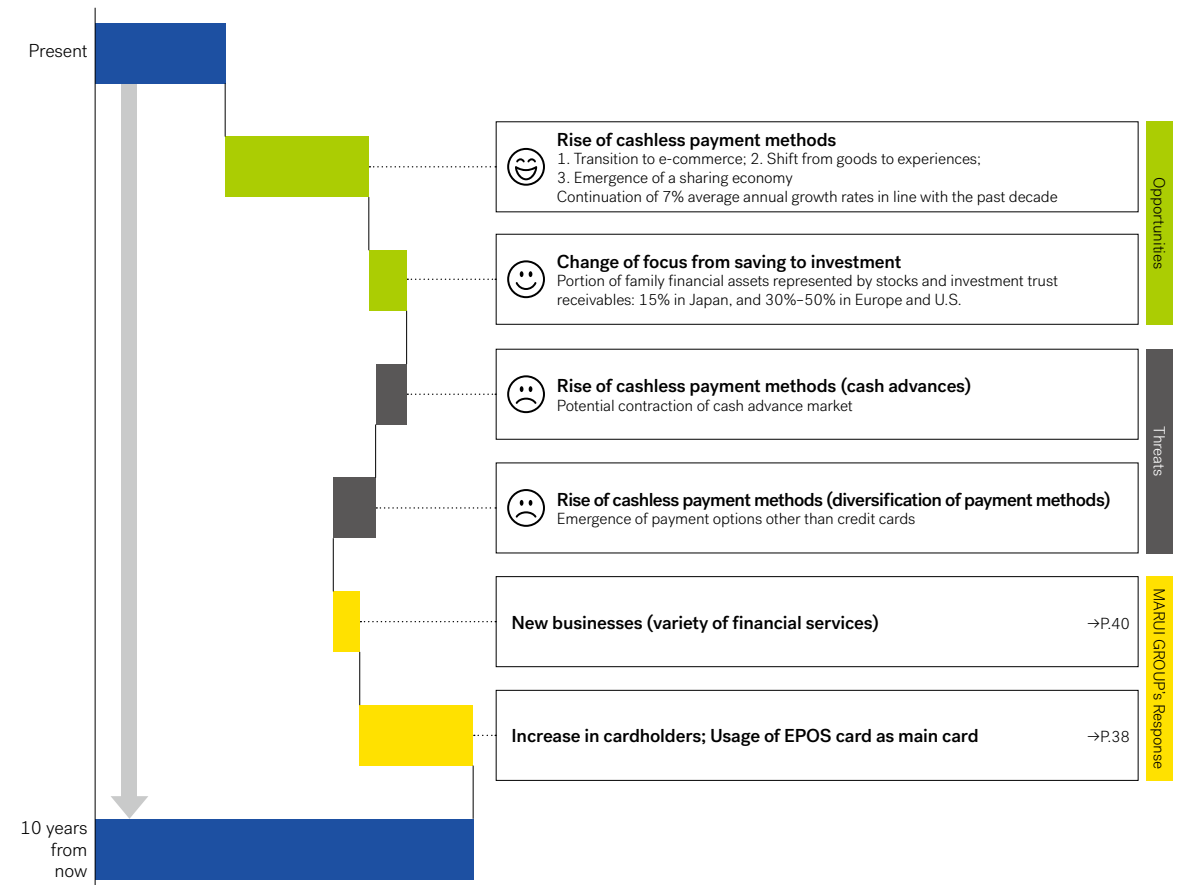
Meanwhile, we look to address the declining birthrate and aging population by expanding our customer base and increasing customer numbers through diversity and inclusion initiatives targeting customers. These initiatives will include providing products, commercial facilities, and services that can be enjoyed by all customers, regardless of their age; physical characteristics, or if they have a disability; or gender, which will entail catering to members

of the LGBT community. As for the emergence of a sharing economy, we will respond by creating new businesses to expand the scope of our operations.

### Opportunities and Threats for the FinTech Business

The greatest opportunities for the FinTech business will come from the rise of cashless payment methods. The transition to e-commerce, the shift from consumption of goods to consumption of experiences, and the emergence of a sharing economy will all contribute to the rise of cashless payment methods. Credit cards are a major component of the FinTech business. In the credit card market, the rise of cashless payments has contributed to the continuation of 7% average annual growth rates over the past decade.

#### Opportunities and Threats to Be Faced by the FinTech Business over the Next Decade



Note: Information on measures related to (B) End of era of low interest rates can be found on page 80.

We expect this 7% trend to be sustained going forward as infrastructure is installed in preparation for the Tokyo 2020 Olympic and Paralympic Games. On the other hand, the rise of cashless payments presents the threat of contraction in the cash advance market. In addition, technological progress could stimulate the diversification of payment methods and consequently detract from the credit card market.

Our responses to these trends include the shift in our business model from an in-house credit card to a multi-purpose credit card—the EPOS card—which took place in 2006, as well as the redefinition of our credit card services business as the FinTech business, which was described in our medium-term management plan. As the diversification of payment methods detracts from the credit card market, MARUI GROUP will evolve its operations into a FinTech business in order to transform this threat into an opportunity while at the same time expanding the scope of its business. This move will also enable us to take advantage

of the opportunities presented by the change in people's focus from saving to investment.

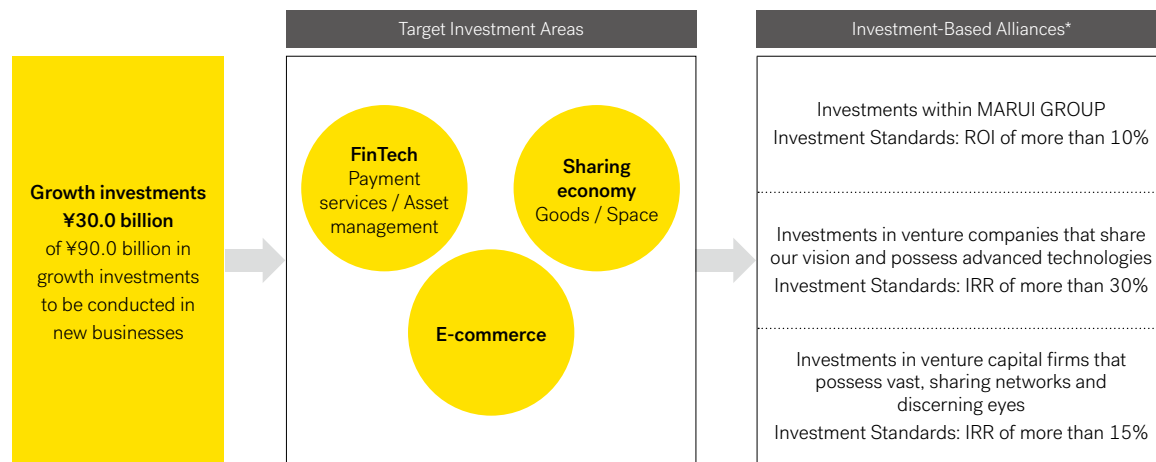
### Immunity to Downside Risks and Growth Investments

To summarize, we will first transition to a real estate model for stores in the Retailing business in order to part ways with the declining department store model. This transition will change the source of our earnings from product sales to rent revenues, effectively guaranteeing stable earnings that are almost completely unaffected by weather, trends, inbound demand, or other external factors. Moreover, by utilizing fixed-term rental contracts, we will be able to increase the value of our shopping centers by periodically replacing tenants, thereby realizing steady growth.

Compared to the prior department store model, this real estate model will lack in its ability to capitalize on upside risks. However, it will be almost immune to downside risks, which is our main aim. During past periods of

### Growth Investments under Medium-Term Management Plan (5 Years)

**Investment Policy**  
Rather than focusing on pure investment, engage in investments and alliances that contribute to expansion and innovation of main business



\* Investment in and collaboration with applicable companies to be conducted based on investment standards by the Research Department and the New Business Development Department

strong economic growth, department store models operating with consignment agreements were able to exploit upside risks over long periods of time. Today, the situation is quite the opposite. Not only are we in a period of low economic growth, but stores that sell products are also exposed to significant long-term risks arising from changes in consumer needs and the spread of e-commerce.

Next, we will pursue the creation of new value by transitioning to a business model that can grow by taking advantage of the e-commerce trend. Specifically, we will promote omni-channel retailing to build a complementary relationship between our retailing operations and our e-commerce operations and provide value that cannot be replaced solely by e-commerce. This approach will be adopted in all conventional, product-selling retailing operations, including Marui stores and private brands and even tenants. In addition, we will capitalize on the greater degree of freedom in stores granted by the real estate model to develop new, sharing businesses. These businesses will not be limited to sharing goods, but will also include sharing spaces to foster communities among customers and thereby respond to changes in lifestyles and needs.

Under the current medium-term management plan, we intend to invest ¥30.0 billion in new businesses leading up to the fiscal year ending March 31, 2021. We have already begun investments and collaboration aimed at advancing omni-channel retailing, sharing economy, and FinTech initiatives through open innovation.

### Forward-Looking Business Models

MARUI GROUP aims to develop an unprecedented, forward-looking retailing business model that is unlike department stores, shopping malls, train station buildings, fashion retail complexes, specialty shops, or anything else seen before. By evolving our retail stores from a forward-looking perspective, we anticipate that synergies can be created with our FinTech business. There is only one financial company in the world with stores where roughly 200 million customers shop each year, and that is MARUI GROUP. We plan to promote financial inclusion through the use of these stores, our approximately 6.4 million cardholders, and big data that links our retailing operations with our credit card operations. Simultaneously growing our credit card operations will create the

forward-looking business model we envision for our FinTech business.

Our quest to create value for the future has only just begun. In this report, we have taken every possible angle toward explaining the business model we are targeting, but I am aware that these explanations may still be insufficient. For this reason, we hope that investors will provide us with their frank opinions as professionals.

We also desire to co-create corporate value through engagement with our customers, business partners, members of local communities and the greater society, employees, and all of our other stakeholders. I look forward to your ongoing support and understanding.

August 2017

**Hiroshi Aoi**

President and Representative Director  
Representative Executive Officer

Messages from President Aoi can be accessed through the following links.

- Fiscal Year Ended March 31, 2015:  
Co-Creation Management Declaration  
[www.0101maruigroup.co.jp/en/ir/message/ceo\\_2015.html](http://www.0101maruigroup.co.jp/en/ir/message/ceo_2015.html)
- Fiscal Year Ended March 31, 2016:  
Co-Creation Management from a Corporate Value Perspective  
[www.0101maruigroup.co.jp/en/ir/message/ceo\\_2016.html](http://www.0101maruigroup.co.jp/en/ir/message/ceo_2016.html)

