Message from the CFO

We will rapidly transform our business model to focus on intellectual creation driven by intangible assets.

Difficulty in Accomplishing Major Medium-Term Management Plan Targets Due to COVID-19 Pandemic

In the fiscal year ended March 31, 2020, the fourth year of the medium-term management plan, performance with regard to the key performance indicators (KPIs) of the plan was as follows: earnings per share (EPS) of ¥117.6, ¥5.1 lower than targeted; return on equity (ROE) of 8.8%, 0.4 percentage point less than our target; and return on invested capital (ROIC) of 3.7%, 0.1 percentage point below the target. In this manner, performance with regard to all KPIs fell below targets due to the impacts of the global COVID-19 pandemic, which occurred near the end of the fiscal year. Moreover, the pandemic reduced consolidated operating income by ¥1.3 billion through a ¥1.5 billion reduction in Retailing segment income coupled with a ¥0.2 billion increase in FinTech segment income.

The FinTech segment actually posted higher operating income as a result of the pandemic as we continued to record recurring revenue while a significant drop in new card issuance costs was seen. The impacts of the pandemic are expected to weigh even more heavily on the fiscal year ending March 31, 2021, the final year of the medium-term management plan. We have therefore judged that it will be difficult to accomplish the targets set for the plan's KPIs, namely EPS, ROE, and ROIC, in this year. We apologize for the disappointment this news causes.

MARUI GROUP will launch a new medium-term management plan in the fiscal year ending March 31, 2022. We hope to accomplish the goals of the current medium-term management plan, specifically EPS of ¥130 or more, ROE of 10% or more, and ROIC of 4% or more, as quickly as possible under the new plan.

Ongoing Corporate Value Creation through Earnings Structure Transformation

Regardless of the unfortunate performance, we were able to make steady progress in transforming our business model and earnings structure and in transitioning toward our target balance sheet based on the medium-term management plan. As a result, we have nearly completed the development of a structure that displays our desired corporate value, by which I refer to a structure in which ROIC exceeds weighted average cost of capital (WACC) and ROE surpasses cost of shareholders' equity on a consistent basis.

The most important goal of our earnings structure transformation is to be able to show growth in recurring gross profit and contracted future recurring gross profit,*[1] which are important KPIs for management emphasizing lifetime value (LTV). Recurring revenue contributes to improvements in LTV. This form of profit has come to represent 65% of total gross profit, a level nearly double that seen before the start of the current medium-term management plan. Meanwhile, contracted future recurring gross profit, which represents gross profit to be recorded in future fiscal years, increased to a level that is 2.7 times greater than the amount of recurring gross profit recorded in the fiscal year ended March 31, 2020. This earnings structure is resilient to major risk factors, like the COVID-19 pandemic, and means that we should be less impacted by such occurrences than we would under our prior structure.

At the same time, we steadily moved forward with capital measures aimed at accomplishing our target balance sheet, resulting in a decrease in WACC and consequently a rise in corporate value through both improved profitability and reduced cost of capital. Furthermore, as recurring gross profit is recorded as the total for both the Retailing and FinTech segments, it is an ideal indicator for MARUI GROUP as it emphasizes LTV in its management through a business merging retailing and finance.

*1 Referred to as "contracted future recurring revenue" until the fiscal year ended March 31, 2020, to reflect future recurring revenue based on revenue as displayed on financial statements; referred to as "contracted future recurring gross profit" in this report to reflect future recurring revenue based on gross profit

Fiscal Year Ended March 31, 2020

ROIC **3.7%**	> WACC **3.0%**
ROE **8.8%**	> Cost of shareholders' equity **6.9%**

Increasing of Investment in Intangible Assets

In tandem with the implementation of our medium-term management plan, we have also been increasing investment in intangible assets for the purpose of fueling future growth. In the fiscal year ended March 31, 2020, investments in intangible assets amounted to ¥15.0 billion, twice as much as investments in stores and other tangible assets. Breaking down these investments in intangible assets, we directed ¥8.7 billion toward new business development, primarily through investments in start-up companies; ¥3.1 billion to software; and ¥3.2 billion to human resource development and R&D investments, which, although being recorded as expenses on the financial statements, are viewed as investments by us. Often times, we invest in start-up companies for the purpose of collaboration with the main businesses of the Retailing and FinTech segments, and we therefore anticipate returns through our business activities. However, we have also set an internal rate of return (IRR)*[2] of 10% or more as a hurdle rate out of consideration for financial returns. The IRR on the ¥7.1 billion in investments conducted prior to March 2020 was 34%, greatly surpassing this hurdle rate. Software investments, meanwhile, have produced an exceptional rate of return on investment of 313% due in part to the fact that we conduct development in-house, which not only speeds up development but also creates such returns for our business. Human resource development and R&D investments include the cultivation of our IT staff and the secondment of employees to start-up investees, efforts we anticipate will increase corporate value over the medium-to-long term. These investments also contribute to ongoing improvements in operating income per employee, which was 1.7 times higher in the fiscal year ended March 31, 2020, than it was in the fiscal year ended March 31, 2015.

*2 Rate calculated using recent procurement prices for applicable marketable securities and based on amounts if listed stocks were to be sold at the end of the respective fiscal year

Investments in Intangible Assets (FY2020)

	Amount	Major Successes
New business fields	¥8.7 billion	IRR of 34% from investments in start-up companies
Human resource development / R&D	¥3.2 billion	Operating income per employee of ¥8.02 million (1.7 times higher than in FY2015)
Software	¥3.1 billion	Return on investment of 313%
Total	¥15.0 billion	

Outlook for the Next Medium-Term Management Plan

ROE was around 5% prior to the establishment of the current medium-term management plan, but the earnings structure transformations and capital measures conducted under the plan caused this indicator to rise to 9.1% in the fiscal year ended March 31, 2019, and 8.8% in the fiscal year ended March 31, 2020, coming in just below 10% in both years. Based on these trends, we will look to achieve an optimal capital allocation assuming ROE of 10% or more under the next medium-term management plan.

A central pillar of investment under the next medium-term management plan will be co-creative investment in start-up companies and other targets. In the new plan, we intend to double such investments from the level of the current plan, ¥30.0 billion over a five-year period. We can improve our success rate in co-creative investments by pursuing earnings contributions to our main business through collaboration with investees while also providing them access to our stores and other resources to stimulate their growth. We aim to maintain an IRR of 10% or more for financial returns through this approach. Moreover, by positioning co-creative investments as a central pillar of growth investments, we hope to create a situation in which ROE stays above 10% and ROE consistently exceeds cost of shareholders' equity. In existing businesses, investments will rise in the FinTech segment centered on software investment while investments in renovations in the Retailing segment will decrease as the transition to fixed-term rental contracts is winding down. As a result, overall investments in existing businesses will decline.

Taking this approach, investments in intangible assets, such as co-creative investments and software investments, will likely rise to account for around 80% of total growth investments under the next medium-term management plan. Through these investments, we will rapidly transform our business model to focus on intellectual creation driven by intangible assets.

Hirotsugu Kato
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In charge of IR, Finance, Sustainability, and ESG Promotion
President and Representative Director, D2C & Co. Inc.
Director, tsumiki Co., Ltd.

Business Merging Retailing and Finance, and Earnings Structure

Since its founding as a company selling furniture on installment payments in 1931, MARUI GROUP has continued to evolve its distinctive business model merging retailing and finance. Today, our operations are divided into the Retailing segment and the FinTech segment, but these segments share the same customer base, making for a model that is conducive to generating synergies. This business model merging retailing and finance also has a uniquely ideal earnings structure in which the earnings structures of both of our segments compensate for the deficiencies of the other segment's model while capitalizing on its strengths.

Business Merging Retailing and Finance

Building appealing stores increases revenues from fixed-term rental contracts while also enhancing our ability to draw customers, which in turn benefits credit card operations by creating more opportunities to recruit new cardholders. Furthermore, as we issue cards on-the-spot in stores, customers often use them right away, which effectively increases active user rates and card revenues. The higher card revenues can be reinvested in retail stores. Through this process, MARUI GROUP's business model generates an ideal virtuous cycle (see Figure 1). Our value journey can be explained by looking at how this business model functions across a timeline (see Figure 2).

Our relationships with customers generally begin in stores, and around 400,000 customers apply for credit cards at our stores every year, often times using them immediately. This process allows for smooth, low-cost recruitment activities and is a significant benefit of our store operations. Stores also serve as venues for ongoing contact, which can create lifelong relationships with customers while encouraging them to upgrade to Gold cards. This multitude of unique advantages is a major characteristic of MARUI GROUP's business model merging retailing and finance.

Figure 1: MARUI GROUP's Business Model

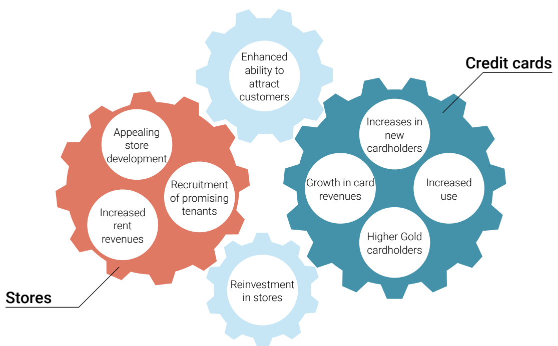
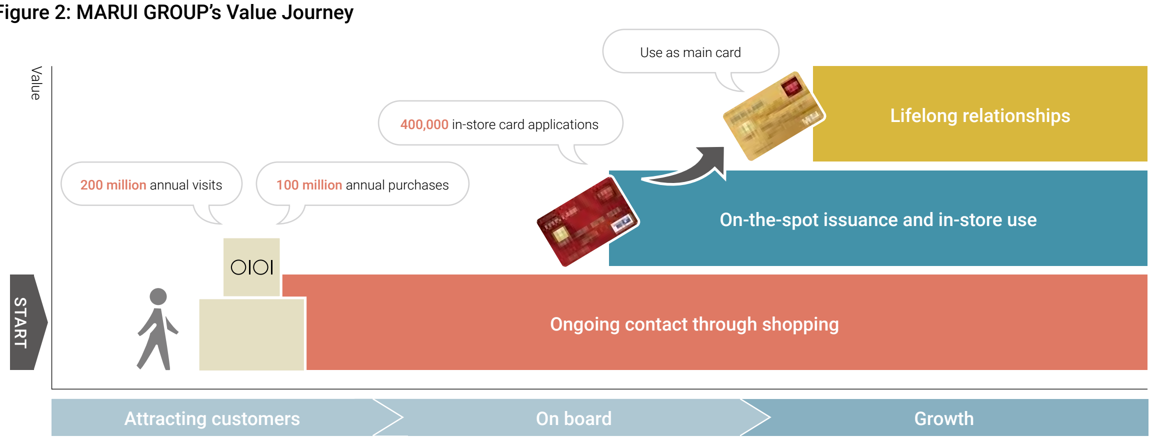


Figure 2: MARUI GROUP's Value Journey



Earnings Structure Based on Distinctive Business Model

MARUI GROUP's distinctive business model merging retailing and finance has an earnings structure that is equally unique (see Figure 3). In our credit card operations, the issuance costs and other initial expenses associated with new cards means that money is actually lost on new cardholders in their first few years. However, once these cardholders start generating profit, this profit can be anticipated to continue growing steadily thereafter. In the Retailing segment, meanwhile, we expect consistent earnings and cash flows following the completion of the transition to fixed-term rental contracts. The combination of these two structures is MARUI GROUP's earnings structure. The consistent retail revenues ensure the Company does not incur overall losses no matter how much profit may be lost on new cardholders in their first year while card revenues continue to grow after they climb into the positive. This earnings structure of MARUI GROUP's business model merging retailing and finance is one of the factors behind the Company's continuously high profit growth.

Changes in Earnings Structure and Clear Indicators for LTV Emphasizing Management Growth of Recurring Gross Profit

Another major characteristic of MARUI GROUP's business model merging retailing and finance is how increases in customer contact points are effective at driving improvements in LTV. Increases in ongoing transactions also spur growth in LTV. MARUI GROUP displays the revenue produced through those ongoing transactions via the indicator of recurring gross profit. The transition to fixed-term rental contracts in the Retailing segment and measures for enhancing rent guarantee and other operations in the FinTech segment are contributing to increases in recurring gross profit. As a result, recurring gross profit rose to ¥131.1 billion in the fiscal year ended March 31, 2020, representing 65% of total gross profit (see Figure 4). Recurring gross profit has grown rapidly over the past five years in both amount and portion of total gross profit, compared to recurring gross profit representing less than 50% of total gross profit prior to the start of the current medium-term management plan.

Figure 3: Earnings Structure Based on Distinctive Business Model

Unique structure combining high growth potential of credit card business with consistent revenues from fixed-term rental contracts

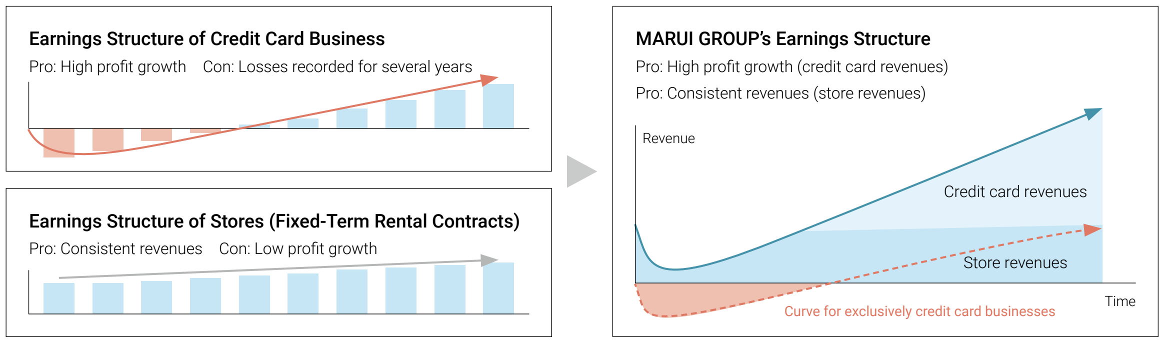
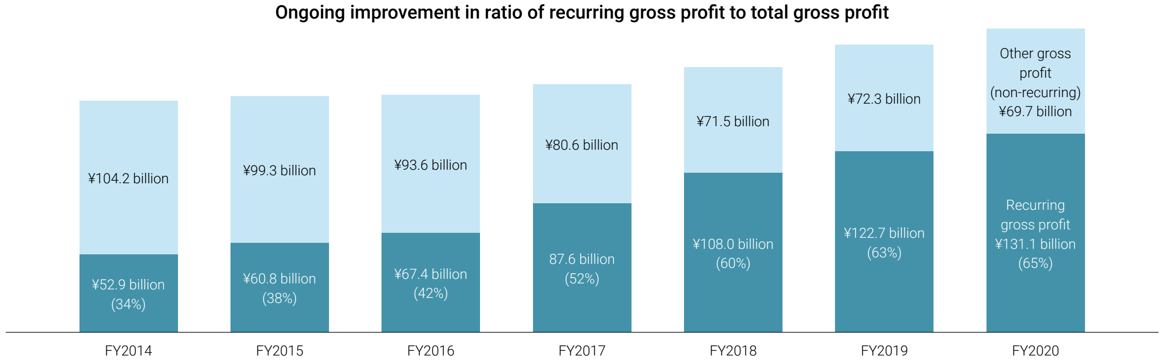


Figure 4: Ratio of Recurring Gross Profit to Total Gross Profit*

Ongoing improvement in ratio of recurring gross profit to total gross profit



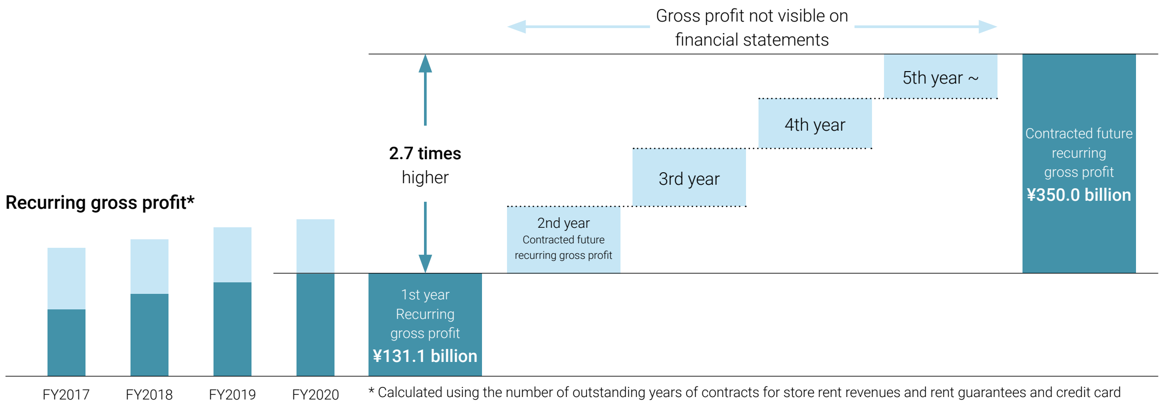
* Gross profit includes selling, general and administrative expenses paid by business partners.

Expansion of Contracted Future Recurring Gross Profit and Resilience

Recurring gross profit represents profit that has already been generated. However, ongoing transactions also entail profit that will be generated in future fiscal years based on contracts. This profit does not appear on the financial statements for a given fiscal year, but it is still an incredibly important indicator of revenue stability and growth potential. For this reason, MARUI GROUP displays this profit through the indicator of contracted future recurring gross profit. On March 31, 2020, contracted future recurring gross profit amounted to ¥350.0 billion, 2.7 times higher than the amount of recurring gross profit recorded in the fiscal year ended March 31, 2020. This figure indicates that the Company has already secured nearly three years' worth of future revenue, which has greatly increased the stability and growth potential of our revenue. This stability makes for improved resilience in times of crisis, such as during the COVID-19 pandemic (see Figure 5). Using finance charges on revolving and installment payments, the primary form of earnings in the FinTech segment, as an example, revolving and installment payment transactions are projected to decline by between ¥30.0 billion and ¥60.0 billion in the fiscal year ending March 31, 2021, due to the impacts of the pandemic. Regardless, earnings from these transactions are anticipated to be up year on year. The reason for this projection is that roughly 70% of finance charges on revolving and installment payments for the fiscal year will be attributable to contracted future recurring gross profit that is already contracted at the beginning of the fiscal year (see Figure 6).

Figure 5: New Financial Indicator—Contracted Future Recurring Gross Profit

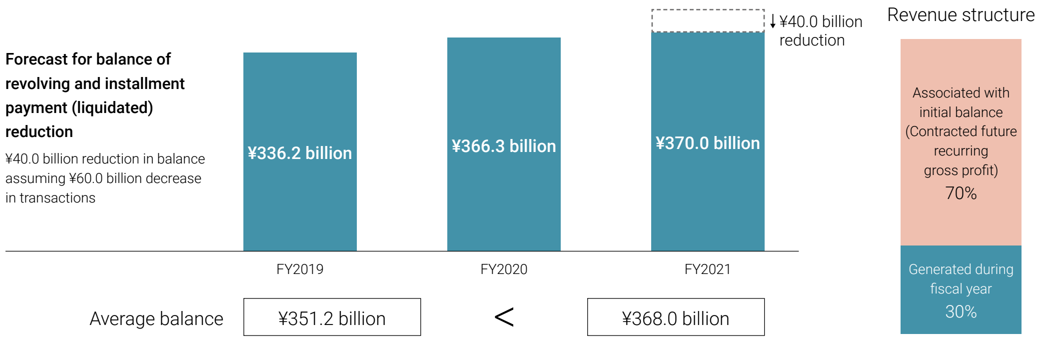
Contracted future recurring gross profit = Recurring gross profit that can be expected to recur in subsequent years after initial transaction



* Calculated using the number of outstanding years of contracts for store rent revenues and rent guarantees and credit card expiration dates for affiliate commissions (fixed payments)

Figure 6: Mechanism Increasing Finance Charges on Revolving and Installment Payments

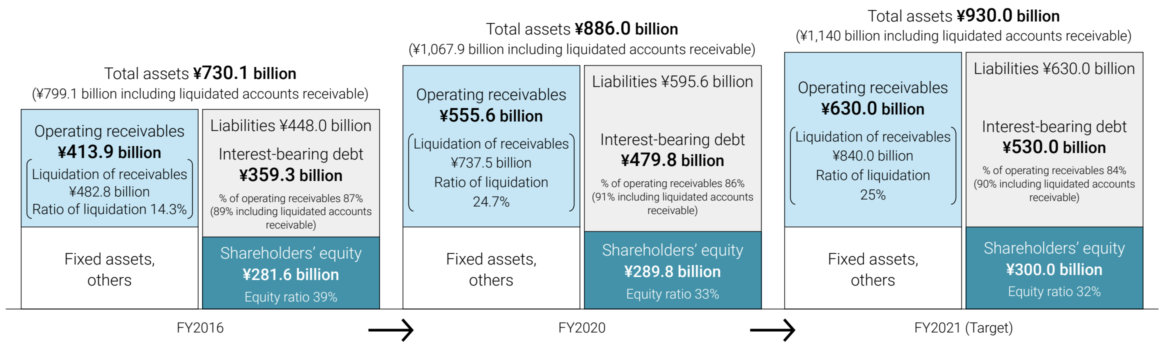
Revolving and installment payment transactions projected to decrease by ¥30.0–¥60.0 billion in FY2021 due to COVID-19 pandemic, but revenue from finance charges to increase as 70% will be attributable to balance at beginning of year



Capital Measures for Achieving Targeted Balance Sheet

The medium-term management plan slated to conclude with the fiscal year ending March 31, 2021, defines a target balance sheet. Achieving this balance sheet will entail procuring funds through interest-bearing debt in response to increases in operating receivables and other capital measures, seeking a level of interest-bearing debt equivalent to roughly 90% of operating receivables, and maintaining an equity ratio of approximately 30% (see Figure 7). After the establishment of the plan, operating receivables increased to a degree that exceeded initial expectations due to growth in the FinTech segment, creating the possibility for excessive growth in interest-bearing debt. For this reason, the Company decided to begin systematically liquidating operating receivables in the fiscal year ended March 31, 2019, targeting a ratio of liquidation of 25%. In the fiscal year ended March 31, 2020, the ratio of liquidation was 24.7%. This level will be maintained in the fiscal year ending March 31, 2021, while net assets are kept below ¥1.0 trillion to maintain the ideal equity ratio of approximately 30%.

Figure 7: Balance Sheet



Creation of Corporate Value through Earnings Structure Transformation and Capital Measures—Development of Structure with ROIC Exceeding WACC and ROE Surpassing Cost of Shareholders' Equity Consistently

The growth of recurring gross profit and other transformations to MARUI GROUP's earnings structure together with capital measures aimed at achieving the targeted balance sheet are leading to the development of a structure in which ROIC exceeds WACC and ROE surpasses cost of shareholders' equity consistently. In the fiscal year ended March 31, 2020, ROIC came to 3.7%, exceeding WACC, which was 3.0%, for the fourth consecutive year, despite the decrease in income due to the COVID-19 pandemic. In addition, ROE surpassed cost of shareholders' equity for the second consecutive year, with figures of 8.8% for the former and 6.9% for the latter (see Figure 8).

Figure 8: ROIC, WACC, ROE, and Cost of Shareholders' Equity