

LIFULL Co., Ltd. (2120)
Edited Transcript
Earnings Briefing for the Nine-month Period Ended June 30, 2018

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Venue: LIFULL headquarters

Corporate Participants:

Takashi Inoue, *President and CEO*

Takashi Yamada, *Director, General Manager of LIFULL HOME'S Business Department*

President of LIFULL Marketing Partners Inc.

Yosuke Hisamatsu, *Director, Manager of Contents Strategy Division, LIFULL HOME'S Business Department*

Kazuhiko Abe, *Managing Officer, General Manager of Group Company Business Development Department*

Keizo Tsutsui, *Managing Officer, Manager of Executive Office*

Yuji Ito, *Managing Officer, Deputy General Manager of LIFULL HOME'S Business Department,*

Division Manager of New UX Development Division, LIFULL HOME'S Business Department

Attendees: 64 people

Presentation

Takashi Inoue, President and CEO

■ Today's Key Points

1. FY2018/9 Q3 : Revenue JPY 26,015 million (+8.6% YoY), EBITDA JPY 4,439 million (+56.9% YoY)

2. Revised full-year forecast for FY2018/9 Revenue JPY 34,000 million (Change -17.1%)

EBITDA JPY 5,190 million (Change -13.7%)

Execute an investment strategy and structural reform to achieve mid-to-long term growth

3. KPI : Steady growth in no. of customers although withdrawing from the renovation business JPY 26,728 million (+2.6% YoY)

ARPA (Average Revenue Per Agent) improvement initiative in progress JPY 83,044 (-0.2% YoY)

4. Overseas Business : Expected to grow significantly following Mitula Group Limited acquisition (“Mitula”)

■ Consolidated Results for FY2018/9 Q3

For the nine-month period ended June 30, 2018, revenue was ¥26,015 million (+8.6%), EBITDA was ¥4,439 million (+56.9%) and net profit was ¥2,274 million (+104.85). Revenue increased and grew rapidly across all segments.

Advertising expenses were ¥8,515 million (+10.6%) with continual investment. Other SG&A decreased to ¥3,860 million (-8.1%) because temporary expenses for the transfer of the head office were included in the previous fiscal period.

In terms of expenses-to-revenue ratios, the ratio of advertising expenses increased to 32.7% (+0.6 percentage points), the ratios of cost of sales and other SG&A decreased to 28.3% (-3.9pt) and the ratio of personnel expenses decreased to 21.9% (-2.0 pt). As a result, the ratio of EBITDA improved to 17.1% (+5.3 pt).

In sales by segment, HOME'S Services Business recorded ¥21,638 million (+7.7%). Small-scale local business operators increased, and the sluggish growth of ARPA is an issue. We intend to promote monetization. The Overseas Business recorded ¥2,802 million (+13.1%), and the Other Business including new business recorded ¥1,573 million (+13.4%). They grew steadily.

In segment income and loss, due to the temporary cost decrease and SG&A cost control, among other initiatives, HOME'S Services Business recorded ¥3,284 million (+¥1,564 million, +90.9%). The Overseas Business recorded ¥264 million (+¥118 million, +81.9%), mainly due to improvements in the personnel expenses of Trovit. Income increased significantly.

In the condensed statements of financial position and goodwill, current assets increased 18.7% with the revenue increase. Short-term loans will be fully repaid at the end of July.

With respect to the situations of cash flows, cash and cash equivalents increased ¥2,122 million, to ¥7,136 million.

■ Mid-to-long Term Growth Strategy

The mid-term management targets are revenue of ¥50 billion level and an EBITDA margin of around 20% in the fiscal year ending September 30, 2020.

The growth image of revenues is the accumulation of the HOME'S Services Business and growth of the Overseas Business as the pillar in the medium to long term, and investment in the Other Business.

In the growth image of income, the area in which investment should be made is the HOME'S Services Business of

Japan, followed by the Overseas Business. The initial investment will be made in the HOME'S Services Business, and then in the regional revitalization business including the so-called "Akiya Bank" and the so-called "Minpaku," the private residence taking lodgers temporarily to increase revenues. At the same time, in the area of advanced technology application such as internal system investment to increase productivity, real estate tech and artificial intelligence(AI), research and development investment will be continued.

In terms of promotion, Mr. Yuto Nagatomo, a professional soccer player, has assumed the position of "LIFULL ambassador" and "Chief of Global HQ" and will contribute to raising LIFULL brand awareness for the year from October 1, 2018.

The utilization of AI/big data/block-chain and other advanced technologies will be promoted.

On August 1, 2018, the "AI Strategy Office" that reports directly to the CEO was established. Data analysts and AI human resources will be gathered there to build a future business model. In addition, a consortium to share real estate information utilizing the block-chain will be established. The number of participants in this plan will be increased. Moreover, there will be participation in the Seven & i Data Lab, which was reported on the front page of *Nihon Keizai Shimbun*.

Changes in the mid-to-long term growth strategy are the implementation of restructuring to enhance competitiveness and the concentration of resources in the growing areas.

In the HOME'S Services Business, Reform, which was a non-profitable business, and LIFULL Remodel, which is a subsidiary that conducts the prime contract work of Reform, will be terminated. For the stronger growth of stronger departments, the media of the rental and business solution (BS) department were integrated. In strengthening media capability, the renovation of LIFULL HOME'S platform was advanced and development has commenced.

In the Overseas Business, resources will be concentrated mainly on Trovit and Mitula. The International Division in Japan was dissolved and the business was withdrawn from Australia and Germany, which were the locations of business expansion for the operation of the portal sites.

The business forecasts for the fiscal year ending September 30, 2018 were revised; however, the mid-term plan will be implemented without change.

On page 19 of the Earnings Presentation, issues relating to internal causes and responses to changes in the external environment are broadly divided and stated. With respect to the HOME'S Services Business, which is the main business, we consider that there are generally issues of internal causes. First, for <optimization of the structure>, divisions will be integrated and the sales capability will be enhanced. Although new product groups have been created, the spread among the member stores all over Japan is still considered to be weak. In addition, it will be strengthened to increase ARPA. In <improvement of productivity>, revenue and profitability per worker will be visualized in relation to individuals, departments and business by introducing the daily profitability management system. With this measure, PDCA will be implemented at high speed. It will start from October. In <improvement of efficiency>, knowledge about how to use marketing budgets and to what advertising how much budget will be allocated has been accumulated, and thus optimization will be able to be proceeded with. To provide more advanced services, AI will be utilized in services inside and outside the company. To raise the CVR of inquiry, the renewal of the sites will be conducted. By making such internal efforts, although a downward revision was regrettably made recently, recovery will be possible in the short term.

Another issue is changes in the external environment, especially SEO. Due to the impact of the change of the algorithm of Google, the number of natural inflows needs to change. In the past, catch-up continued without stopping. The input of more resources, the improvement of contents, the automatic creation of a landing page according to the individual and other measures will be promoted to increase natural inflow.

With respect to the business forecast, the cost of sales will decrease 23.7% because the growth of LIFULL Marketing Partners is quite weak. With respect to SG&A, personnel expenses are difficult to control; however, by controlling advertising expenses, operating expenses and other expenses, the resulting EBITDA margin will be improved to 15.3%.

With respect to revenues by service, the forecasts are ¥28,100 million in the HOME'S Services Business (-16.0% in comparison with the forecast at the beginning of the fiscal year; the same shall apply hereinafter), ¥3,800 million in the Overseas Business (-21.4%), and ¥2,100 million in the Other Business (-22.9%).

In the acquisition of Mitula, the current plan is that the shares will be acquired in October. The impact on the mid-term plan is being carefully examined and will be disclosed in a timely manner.

● HOME'S Services Business

In Q3, the number of customers decreased due to the withdrawal of the renovation business. However, ARPA remained almost the same. To improve ARPA, the operational support business for customers, which was separated, has been integrated into the Rental Division since July. By providing one-stop media and operational support and focusing on strong sales expansion, the ARPA of the operational support area as well as that of the media will be raised.

With respect to the total quantity of information listed on KPI, while improving the accuracy of information, an overwhelming quantity of 6.7 million pieces of information is maintained.

“LIFULL HOME’S PRICE MAP” has been available throughout Japan since May 18. With this service, the capability to attract customers will be increased.

In application, the new service “hold up your smartphone and search” was input. With this service, by holding up a smartphone toward any scenery in the town, vacant properties, if any, will be displayed in AR and specific information on them will be presented owing to the recent advancement of augmented reality (AR), virtual reality (VR) and other xR technologies. Currently, the service handles one million properties for rent, newly built condominiums and second-hand apartments nationwide.

In real estate tech, “3D Model House” will be released in August. The service of viewing with the use of a smartphone and a pair of VR goggles from a remote location will be implemented.

To make more global investment, a partnership was established with 台湾房屋(Taiwan Realty), one of the largest real estate companies in Taiwan that has 400 stores in Taiwan. A Japanese affiliate has already been launched. For investors from Taiwan, a real estate brokerage service in Japan will be supported.

Promotions are conducted via cross-media in versatile ways. Each result is analyzed in detail, and PDCA is conducted at all times.

● Overseas Business

Currently, both revenue and profit are led by Trovit. Mitula, which is to be turned into a subsidiary, recorded revenue of about ¥2.8 billion and EBITDA of about ¥0.9 billion (results for the fiscal year 2017). By turning Mitula into a subsidiary, as the aggregation site of real estate, the overwhelming top position will be secured globally. Through this multiplication, we intend to grow the Overseas Business significantly.

(*In this material, the exchange rate for the Japanese yen to the Australian dollar is 82.6 yen to 1 Australian dollar.)

With respect to the results of the Overseas Business, the revenue of Trovit for the latest Q3 of the fiscal year ending September 30, 2018 was about ¥980 million. The portion of the Other Business is very small. The operating profit of Trovit was about ¥260 million. In PPA and the International Business Division, mainly personnel expenses of about ¥100 million were spent. However, the International Business Division was dissolved in April. In the latest Q3, expenses in relation to the acquisition of Mitula in an amount of ¥200 million were included.

The growth strategy of Trovit is to increase traffic first. Customer attraction is strengthened in various ways, such as SEO via multi-channels, fee-charging customer attraction and e-mail marketing. UI is then improved to raise CVR. Based on these actions, the sales capability is enhanced to increase advertising revenue. The development of new customers and the improvement of the unit price are encouraged. In addition, through the input of new products, actions are taken to realize change from the low unit price of CPC to a higher unit price.

Mitula is listed on the Australian stock exchange. Its base is in Madrid, Spain. It provides an aggregation service of real estate information in more than 50 countries around the world. Although its business includes cars and work, its main business area is real estate. In the past five years, sales and EBITDA grew about nine times and twelve times, respectively. The EBITDA margin is around 35%. Its business model is extremely profitable.

Trovit and Mitula are both based in Spain. The plan is to integrate the companies’ management in future to combine their respective strengths for the creation of synergy.

In the improvement of traffic, for example, the expertise of both companies is integrated to further strengthen the inflow in SEO. Both sites are already strong and rank high, and thus the companies will be integrated, but the websites will remain separate. They will each secure higher ranks in SEO to prevent loss. According to the SimilarWeb survey, the traffic share will expand rapidly from 26% to 68% in Chile, from 55% to 85% in Italy and from 53% to 90% in Mexico. These countries (Chile, Italy and Mexico) rank high in the revenue of both companies. Accordingly, an impact on revenue and profits can be expected.

With respect to the improvement of sales per customer, by taking advantage of the overwhelming traffic that both companies receive, we would like to become the price leader. By turning Mitula into a subsidiary, the ability to attract customers will increase and the sales capability will be strengthened. The range of traffic, advertising revenue and new product development will then be expanded to increase revenue/profit.

From CPC, in which the unit price is cheap, the unit price will be raised by advertising revenue such as e-mail marketing and retargeting. In addition, it is planned to raise the unit price further by customer transfers of higher quality CVR from inquiries to contracts, customer transfers based on contracts according to the countries and business areas, and customer transfers to the secondary market such as housing loans/mortgage brokers/insurance/moving companies.

As a result, with respect to revenue/EBITDA, as stated on page 45, our expectation is that revenue will be ¥8.2 to ¥8.7 billion, cost reduction by synergy will be ¥200 to ¥300 million, and EBITDA after the integration will be ¥2.4 to ¥2.9 billion. (*When both companies are consolidated on a full-year basis with the fiscal year-end of December.)

The net profit of Trovit for the fiscal year 2017 was about ¥600 million. It is expected to increase to ¥1.6 to ¥1.9 billion.

By issuing common shares, there will be dilution of a maximum of 15.6%. However, net profit will be able to be increased by 20% to 25% through consolidated integration. This is a very good deal for both us and the other party, and thus the procedures are being undertaken in a cordial manner.

● Overseas Business

With respect to the results of the Other Business, the revenues of the four companies that were established in the incorporation-type company split, LIFULL FinTech, LIFULL MOVE, LIFULL senior and LIFULL SPACE, grew steadily. Other new business also gradually accumulated revenues.

With respect to operating profit, the four existing companies produced profits of ¥110 million in the Q3 of the fiscal year ending September 30, 2018. The other business is in the investment phase, and thus the profits above were offset by the deficit of ¥110 million. By gradually increasing new business monetized, however, we will work so that this field can also contribute to profits.

Questions and Answers

*For the sake of accuracy, portions of the Q&A session have been corrected or revised. To see the actual events of the day, please watch the video on our web site.

Q1. It appears that based on the subtraction of the results until the Q3 from the downward revision of the current fiscal period, the revenue of the HOME'S Services Business for the Q4 is stated as a decrease from the previous year. Was there anything that changed significantly from July to September? I would like to ask whether the results will actually be at this level.

A1. (Takashi Yamada) We take the downward revision of the business results very seriously. We cannot optimistically provide figures in the middle of the downward trend, and thus we provided very strict and certain forecasts including the transactions accumulated currently. In that sense, for the Q4, we would like to ask for your understanding of a slightly underestimated forecast. It is the second busy season toward September. Actions for the acquisition of responses, including the realization of more efficient promotion, have been implemented. We will work to produce better results than the forecasts.

Q2. The number of affiliated realtors on page 57 includes mainly rentals/second-hand purchases. It appears that negative results quarter on quarter were recorded for the first time in many years. I thought that the figures for the Q2 were slightly higher. It appears that recently, the two-dimensional expansion in the number of affiliated realtors of rental/second-hand real estate purchases of the HOME'S Services Business has been limited. I would like to ask about its background.

A2. (Takashi Yamada) The change in the number of affiliated realtors is attributable partly to the decrease of Reform. I have already talked about the strengthening of the internal system. Currently, the inflow of the response and the creation ability have dropped, and thus in the appropriation of sales resources, the up-selling of existing clients is prioritized over new development. We would like to ask for your understanding that it is under control.

Q3. Based on the current situations of the two questions above, about what percentage do you think the organic sales growth rate of the HOME'S Services Business should now be? In addition, conversely, if it is not enough, what elements are now missing? And when will the ideal growth rate be recovered? What do you think?

A3. (Takashi Inoue) With respect to the organic growth of the HOME'S Services Business, I intend to start providing support for shoring up and structural reform myself. My aim is for the organic sales growth rate of about 15% to be recovered. With respect to the approximate timeframe for the recovery, I think that the internal factors will be bigger than the external factors. Structural reform, the strengthening of the sales system, the improvement of growth per person and other actions will not take a lot of time, so I would like to undertake them at an early stage in order to achieve the medium-term plan.

Q4. In a follow-up to the first question, when comparing the trends for the Q3 and Q4, is it not necessary to think that new factors with a negative impact on the revenue growth have arisen from July to September? With respect to the

number of affiliated realtors, the impact of Reform occurred in the Q3. Can I take the view that it will increase at the same rate of growth as before in the Q4?

A4. (Takashi Yamada) At the present time, in comparison with the Q3, I do not think that there are any negative factors regarding the revenue for the Q4. Some clients are showing signs of reducing advertisements. From what I have heard, however, there is no significant impact. With respect to the affiliated realtors, we are not currently focusing on the acquisition of the number. I think that in terms of whether the rate of progress recovers in the Q4, it is still that point which should be grown.

A4. (Takashi Inoue) I would like to contribute some additional information. There are no factors that will cause a decrease in revenues in the Q4. However, advertising expenses will be used more in investment in the Q4 than in the Q3, and thus profits will fall to that extent. The affiliated realtors may be asked to join an industrial association in the course of local development. However, this rarely contributes to revenues, and thus rather than increasing them, we would like to steadily increase the number of customers who are charged fees. Accordingly, the mode has been changed somewhat.

Q5. On page 44, there was a statement that you would like to increase overseas sales per customer to advertising and a higher level. Currently, with respect to Trovit and Mitula, what are the sales per customer and the percentages of the lower case and the higher case? What outlook do you have with respect to the future actions in the medium to long term?

A5. (Takashi Inoue) Currently, the largest share is (1) CPC, which accounts for about 70%. The other was occupied by Google AdSense. (2) advertising revenue and (3) transactions will be developed in the future. The present stage is (1). First, the unit price at this stage will be increased by achieving overwhelming traffic. The expansion of (2) and (3) is then planned.

Q6. Your company used real estate and tech from the beginning. Recently, the number of companies expressing real estate tech in relation to real estate for revenues has been increasing. LIFULL HOME'S of your company mainly handles the actual demand. I think that the business of real estate for revenue has been proceeding steadily. Will it be emphasized further? Since growth can be achieved with the actual demand, will it be deepened further? What is your view regarding real estate for revenues?

A6. (Takashi Inoue) It is the area that I want to grow. In addition to real estate investment in Japan, I want to capture the global market for real estate investment as a platform. Recently, the approval of the type II financial license of the subsidiary engaging in crowd funding, which is called LIFULL Social Funding, was delayed against the background of a range of problems with bitcoin companies and real estate crowd funding. This state in which funds cannot be gathered online and invested in real estate and regional revitalization has continued for about a year. In relation to this, before it becomes possible to obtain the type II license, the results are produced in proprietary trading. Preparations for the formulation of the fund and other products have already been made.

In the Overseas Business, although it is a small start-up, we made an investment in BitOfProperty of Singapore (https://lifull.com/wp-content/uploads/2018/03/release_20180329_en.pdf). In this business, the system for global real estate investment using virtual currency and tokens has already been made. Only one transaction was actually conducted; however, the gathering of investors was completed and the state of management has commenced. From this, we intend to take know-how and systems into our business.

In conclusion, Mitula and Trovit will be integrated and the global network will be expanded into 63 countries. Meanwhile, real estate investment products that are made into small ones through the issue of tokens will become able to be purchased around the world. A trial will be conducted both in Japan and for regional revitalization. The pieces of the puzzle have been arranged.

Q7. From June 15, the new law for the so-called "Minpaku," the private residences taking lodgers temporarily, took effect. Your company has 49% of the equity of Rakuten LIFULL STAY. How is the progress in the middle of the business? I heard that the number of Airbnb properties decreased sharply. Your company made a lawful start. I also heard that there was a delay due to problems in the municipalities, among other reports. Is this business still promising?

A7. (Takashi Inoue) The new law took effect on June 15, and in "Vacation Stay," which is operated by Rakuten LIFULL STAY, a joint venture with Rakuten, the number of registrations as of today's date is 2,140 properties, the number of those already approved is 1,780 properties, and the number of those offered on the website is just under 1,000 properties. On the other hand, I understand that the 60,000 rooms on Airbnb reduced to 15% to 20% of that number. Currently, due to the additional ordinances of each municipality, demand for presence in the case that only notification should be required at the desk, demand for materials because they are not sufficient, and other similar causes, the acceptance of notification at the administration desk remains undone. In relation to these situations, some time ago,

the Japan Tourism Agency issued an official notice to each municipality, demanding the operation of the ordinances and the desk work that did not contradict the original gist of the new law for the *Minpaku*. I expect progress to occur going forward.

Q8. Of the causes for the downward revision of the business results, with respect to the fall in the number of customers attracted from the search engines below the estimate, the impact of the change in the algorithms was referred to in the domestic/overseas business. This state was overcome again and again in the past; however, speaking of the current fiscal year only, although certain forecasts are provided until the Q4, an outlook for a slight slowdown is presented. In comparison with the changes made in the past and countermeasures, among other matters, will the impact of this change be severe for your company, or will it take time to respond to it? Do you have such a recognition? I would like to confirm this.

A8. (Takashi Inoue) I will provide answers for both the domestic business and the overseas business. In the domestic business, the change of the algorithms will not be as severe. However, there are many competitors with strength in SEO. Among them, our company is competing fiercely. We recognize that internally, the response to it was a little slow. We therefore intend to input resources for recovery.

A8. (Keizo Tsutsui) In the Overseas Business, there are many countries into which Trovit is expanding, and the situations differ from country to country. This is because when Google undertakes an update, the same update is not necessarily implemented all around the world, and the standards are also different. Accordingly, I think that this reason is reflected. With respect to Trovit, the AB test was conducted on a daily basis, and various improvement measures were implemented finely as well as the use of AI. Among the countries whose revenue is high, a quick recovery was made in Italy, where the business was struggling. The situations were relatively positive.

A8. (Takashi Inoue) Trovit alone has three vertical sites: real estate/recruitment/second-hand. The business is conducted in 57 countries. Accordingly, about 180 sites are in operation. Mitula also has the same scale. As a result, while operating over 300 sites all over the world in future, at each site, know-how will accumulate endlessly through automatic processing of what pages will be automatically created and shown for which keywords. And what ultimately wins will be deployed in other countries. This is the mechanism that will be created. In that sense, rather than any one specific thing, broad knowledge will be able to be accumulated. Accordingly, in relation to this, we have future confidence in this field.

Q9. I heard that there is an intention to recover the organic growth rate of the HOME'S Services Business to around 15%. And at the same time, the President said that during the course of changing the organization so that it is able to provide one-stop services, the focus would be on the sales expansion of the operation support service, which is not revenue from media. In the course of the recovery to 15%, I think that the percentage of operation support, not the existing media field, will increase. I would like to ask whether you think that of the business of your company group, in the future HOME'S Services Business, the weight of media revenues and the weight of the operation support service and the business mix will change, and if they do change, what do you think the level of profitability will be?

A9. (Takashi Inoue) With respect to the breakdowns of the 15% growth, we do not explain anything clearly, but the media will still be the main part. In terms of the ratio, the projection of between 9:1 and 7:3 will be approximately appropriate.

Q10. I heard about the difference in the fiscal year of Mitula. At the present time, assuming a neutral case without the immediate outcome of synergy, what contribution to revenues is expected in the next fiscal year and the fiscal year after that?

A10. (Keizo Tsutsui) Mitula is listed on the exchange in Australia. The forecasts for 2020 are not provided. The image is shown on page 45. The period is 12 months after the completion of MA, so the data is almost the sum of Mitula and Trovit for 2019.