

LIFULL Co., Ltd. (TSE 2120)

Edit Transcript

Earnings Presentation For the Six-Month Period Ended March 31, 2018

(October 1, 2017 to March 31, 2018)

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Venue: LIFULL headquarters

Corporate Participants:

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Takashi Yamada, *Director, General Manager of LIFULL HOME'S Business Department*
Executive Vice President, LIFULL Marketing Partners Inc.

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Hidekazu Fukuzawa, *Deputy General Manager of Group Company Business Development Department*

Kazuhiro Yoshida, *Group Manager of IR Group, Group Company Business Development Department*

Presentation

Takashi Inoue, *President and CEO*

Moving on, I would now like to provide a brief overview of our business results for the fiscal period ended March 31, 2018.

[Index (Slide 1)]

Following the table of contents listed here on the Index slide, I will first touch on some key points of the fiscal period under review.

[Key Points (Slide 2)]

In the six-month period ended March 31, 2018, revenue increased 9.3% and EBITDA improved 28%.

As far as our acquisition of Mitula Group Limited is concerned, details are consistent with the explanation provided a moment ago.

Looking at certain key indicators, the number of clients has shown steady growth. ARPA, on the other hand, remains a challenge. While I will elaborate in more detail shortly, measures to increase ARPA are still in progress.

Turning to the topic of real estate aggregation, our efforts are again in line with earlier comments.

[Consolidated Results for FY2018/9 1H (Slide 3)]

[Condensed Statements of Income and Loss IFRS (Slide 4)]

Next, I would like to touch on LIFULL's consolidated results. As you can see from this condensed statement of income and loss, revenue increased across all segments, climbing 1 billion 506 million yen, or 9.3%, year on year, to 17 billion 669 million yen.

As far as selling, general and administrative expenses are concerned, the decline in other costs is especially noteworthy. Reflecting the absence of the temporary increase related to the relocation of our head office in the previous period, this downturn in other costs helped boost earnings.

As a result, EBITDA climbed 663 million yen, or 28%, year on year, to 3 billion and 33 million yen.

[Expense-to-Revenue Ratio IFRS (Slide 5)]

Taking a closer look at the expense-to-revenue ratio, advertising expenses increased. In contrast, cost of sales and other SG&A expenses declined. As a result, the EBITDA margin improved to 17.2%.

[Sales by Segment IFRS (Slide 6)]

Here on slide 6, we provide details of our performance by segment. Revenue in each of the HOME's Services, Overseas, and Others businesses improved and totaled 14 billion 805 million yen, 1 billion 819 million yen, and 1 billion and 45 million yen, respectively.

As indicated in the "main items" column on this slide, ARPA declined despite steady growth in the number of clients. Among a variety of measures aimed at improving ARPA, we will focus mainly on increasing the number inquiries by boosting traffic. This is expected to impact favorably on returns in the form of inquiry payment sales.

In addition, our efforts to provide services for realtors fell short of expectations. This was not from a media perspective, but more in terms of applications and system services. Our efforts to develop and expand sales of both are still in progress, and this is another reason for the decline in ARPA.

[Segment Income and Loss IFRS (Slide 7)]

From an income and loss perspective, revenue from the Overseas Business increased sharply due mainly to the decrease in Trovit's personnel expenses. Income in the HOME'S Services Business climbed 768 million yen to 2 billion 223 million yen and improved 127 million yen to 208 million yen in the Overseas Business.

[Reference: Condensed Statements of Profit and Loss (quarterly) IFRS (Slide 8)]

For reference and comparative purposes, we provide condensed statements of profit and loss for the January to March quarters of 2017 and 2018. While measures to increase ARPA are still in progress, profitability has improved considerably due to a variety of factors.

[Condensed Statements of Financial Position and Goodwill IFRS (Slide 9)]

As you can see from this condensed statement of financial position and goodwill, current assets as of March 31, 2018 grew 9.4% compared with the end of the previous year. This is largely in line with the increase in sales.

Liabilities, on the other hand, declined 2.1% owing mainly to the repayment of loans.

[Condensed Statements of Cash Flows IFRS (Slide 10)]

As far as the Company's cash flows are concerned, the balance of cash and cash equivalents stood at 5 billion 446 million yen as of March 31, 2018, down 600 million yen year on year.

Plans are in place to repay loans in full in June this year. At that point, LIFULL will transition to a debt-free financial position.

[Progress of Business Forecasts (Slide 11)]

Turning then to our progress compared with business forecasts, I direct your attention to slide 12.

[FY2018/9 Forecast and Progress IFRS (Slide 12)]

As I have mentioned, efforts to implement measures aimed at increasing ARPA are slightly behind schedule and still in progress.

Revenue results for the six-month period from October 1, 2017 to March 31, 2018 come in at 43.1% of forecasts for the full fiscal year ending September 30, 2018.

From a profit perspective, results have improved. EBITDA for the period under review comes in at 50.4% of the full fiscal year forecast and the EBITDA margin at 17.2%. The issue at hand for the second half therefore entails how best to align revenue results with forecasts.

At the right of the slide, we provide details of actual results by segment compared with full fiscal period forecasts. As you can see, revenue from the HOME'S Services and Overseas businesses came in at 44.3% and 37.6%, respectively.

As stated in the note at the bottom of the slide, details of the impact after acquiring Mitula Group Limited on forecasts for the full fiscal period have not been provided. We will disclose this information in a timely manner once determined and ask for your patience in this matter.

[Mid-Term Business Plan (Slide 13)]

Having touched earlier on LIFULL'S Mid-Term Business Plan, I will refrain from making any further comments here.

[Restructuring of the Business Strategy and the Organization (Slide 14)]

In a bid to enhance its competitive advantage, LIFULL is restructuring its business strategy and organization.

First, we will withdraw from unprofitable businesses in the HOME'S Services Business. In specific terms, we plan to terminate LIFULL HOME'S Renovation, a search site for construction companies that engage in property renovations, at the end of September this year.

Again, with an eye toward restructuring activities in the renovation and remodeling field, we also intend to terminate LIFULL Remodel, a joint-venture subsidiary and renovation contractor established to manage the outsourcing of subcontractors, during 2018, due to its unprofitable operations.

Furthermore, and as was mentioned earlier in the first half of this presentation, we will focus resources on Trovit and Mitula. In undertaking this roadmap, we have decided to terminate LIFULL AU Real Estate and LIFULL Immofinder, companies that were established from scratch in Australia and Germany as portal business sites.

Based on the aforementioned, our strategy then is to focus resources in an effort to increase competitiveness.

[Mitula Group Limited Acquisition: Impact on Current Fiscal Year and Mid-Term Management Plan (Slide 15)]

Having already touched on the acquisition of Mitula Group Limited in some detail, I will refrain from making any

further comments here.

[Business Standings (Slide 16)]

Drawing your attention to LIFULL'S mid-to-long term strategy roadmap, I direct you to slide 17.

[Mid-to-Long Term Strategy Roadmap (Slide 17)]

While I will comment on our domestic business strategy a little later, and as indicated by the diagram on this slide, we have classified LIFULL HOME'S mid-to-long term roadmap into the three core Database, Network, and Media strategies. Continuing to hone each of these strategies since our foundation, our growth depends on our ability to build a massive database, expand our network, and enhance our media power.

[Expanding the Client Network (Slide 18)]

From a network expansion perspective, the number of clients has grown steadily to 27,445. As indicated here on this slide, we have recently focused on expanding our client network in local regions and to include small-to-mid sized real estate companies, areas that have been neglected in the past. As a result, we have seen a subsequent downturn in ARPA.

To address this downturn, we are providing services for realtors by expanding our sales capabilities and continuing to enhance value by increasing the number of inquiries. Based on these endeavors, ARPA in the recent January to March quarter came in at 103,358 yen.

[Expanding the Number of Total Information Listed (Slide 19)]

Turning to our database, we also maintain an overwhelming volume of information listings, which currently stands at 7.16 million.

[Visualizing the Price Information – “PRICE MAP” (Slide 20)]

As a part of efforts to visualize price information, LIFULL's PRICE MAP is scheduled to provide nationwide coverage during May 2018.

On this basis, the visualization of property and pricing information is progressing steadily.

[Enhancing Media Power – LIFULL HOME'S Android App (Slide 21)]

As one measure aimed at enhancing media power, we have released an online application that utilizes state-of-the-art technology including AI. The application on offer learns as users view properties. By drawing on browsing as well as inquiry histories to ascertain tastes, this app can put forward tailor-made proposals that match the preferences of users.

[Enhancing Media Power – Improving Information Accuracy (Slide 22)]

Another aspect of efforts geared toward enhancing media power includes the improvement of information accuracy. Conscious of the need to maintain strict information integrity, steps have been taken to upgrade the Company's systems in a bid to detect and eliminate any false statements or bait-and-switch information.

While I will omit a detailed explanation, I draw your attention to the diagram at the left of the slide, which details this system upgrade and detection system.

As indicated in the diagram at the right of the slide, we are also coordinating with other online sites such as Rakuten to avoid any incidence of fraud. This coordination is also being used to prevent fraudulent orders.

[Enhancing Media Power – Promotions (Slide 23)]

Again, with the aim of enhancing our media power, we have rolled out “LIFULL HOME’S LIVE” as a new promotion concept.

Historically, real estate activities have been limited largely to over-the-counter contact. Customers were forced to use their weekends, with the explanation of important matters conducted on a face-to-face basis. At the same time, the process from property search to contract execution often necessitated multiple visits. Taking into consideration the considerable burden and inconvenience, LIFULL has worked diligently to utilize TV commercials as well as transportation advertising to vigorously promote the use of online tools to carry out real estate transactions.

[Making Real Estate Transactions Available Online – “LIFULL HOME’S LIVE” (Slide 24)]

We continue to promote LIFULL HOME’S LIVE as a medium for conducting real estate transaction online.

LIFULL HOME’S LIVE is a medium that connects client companies to customers. In addition to receiving explanations of important matters online, LIFULL HOME’S LIVE also allows customers to remotely view a property using their smartphone, iPad, or tablet device. As you can see from the selection of client comments listed at the right of the slide, LIFULL HOME’S LIVE provides a host of benefits. While improving business efficiency by consolidating certain operations, which are then handled by registered real estate brokers at a designated facility, LIFULL HOME’S LIVE also allows client companies to better serve customers. The ability to explain important matters online has, for example, made it possible to provide explanations and other services at such times as weekday evenings. Not only is this easing congestion during the busy weekend period, but also decentralizing operations thereby significantly improving business efficiency.

Hardly any of the initial concerns have come to fruition. And, as a result, LIFULL HOME’S LIVE is being extremely well received.

Both users and clients are fully embracing this service. Looking ahead, we hope to broaden the scope and coverage of LIFULL HOME’S LIVE even further.

[Revitalizing the Second-Hand Market (Slide 25)]

As the incidence of empty homes becomes an increasingly serious social issue nationwide, LIFULL recognizes the critical need to revitalize the second-hand market. Among a host of initiatives that include steps to establish a comprehensive database, engage in the training of personnel, apply crowd-funding, and develop new uses, LIFULL has collaborated with Japan’s Ministry of Land, Infrastructure, Transport and Tourism to first visualize the problem. In specific terms, we have applied our expertise to help set up the platform for a nationwide *Akiya* (vacant home) *Bank*.

Moving forward, energies will now be directed toward training personnel including producers and entrepreneurs, who will be dispatched to regional areas to promote the use of vacant homes.

Rounding out this cycle for revitalizing the second-hand market, attention will be placed on procuring finance through crowd-funding. The finance raised will be applied to renovations and the conversion of properties for a wide range of uses. This includes application as home-sharing facilities and restaurants geared toward generating additional income. In this manner, LIFULL is committed to creating a virtuous cycle as a part of its regional revitalization promotion project.

[LIFULL HOME'S *Akiya Bank* Official Release (Slide 26)]

As of May 2018, more than half, or 480, out of a total 900 local governments have registered as participants of the *Akiya Bank* service.

[RAKUTEN LIFULL STAY – “Vacation STAY” (Slide 27)]

Recognizing home-sharing as an excellent opportunity with respect to the use of vacant homes, preparations are progressing smoothly to establish RAKUTEN LIFULL STAY, a Vacation STAY rental and accommodation reservation site. Coinciding with the date the new law governing home-sharing operations will come into effect, this service is scheduled for release on June 15.

Despite an article in this morning's newspaper that home-sharing registration numbers are low, our findings indicate steady growth in the number of properties for monthly accommodation and budget hotel use as well as home-sharing as defined under the new law.

[Overseas Business (Slide 28)]

[Trovit X Mitula (Slide 29)]

Having touched earlier on LIFULL's overseas strategy, I will refrain from making any additional comments, and close this presentation of our business results.

[LIFULL Make every LIFE FULL (Slide 30)]

I would again like to open the floor to questions.

Questions and Answers

Q1. My question has two parts. Taking into consideration the decline in ARPA, it would appear that issues continue to linger with respect to services for realtors. Is this because of competition, or does it indicate that real estate brokers are yet to fully appreciate the additional convenience? What are your thoughts, and can you provide details of how you intend to respond?

My second question relates to the home-sharing market. Restrictions will be lifted on June 15. You have mentioned that the number of properties under management is exhibiting steady growth. How confident are you in the home-sharing market and the potential for success?

A1. (Takashi Inoue) Our efforts in the home-sharing field are through a joint venture with RAKUTEN. As the minority partner, we are not in a position to provide specific details. We have calculated backwards to identify forecast data based on the ability to secure a leading position in Japan over a fixed period of time. While these forecasts are essentially online based, we are confident that the RAKUTEN LIFULL STAY service will provide users with multiple options over a reasonable area.

I apologize for any ambiguity in my reply.

As far as ARPA is concerned, and as I mentioned a moment ago, there are two aspects to address: “traffic” and the business needs of “realtors.” From a “traffic” perspective, partner portal progress, steps to attract fee-paying customers, and branding including TV commercials are all, for the most part, in line with plans. Turning to natural inflow trends in connection with search engine optimization, or SEO, and in particular the impact on property leasing activities, conditions are improving at a rapid pace.

Activities that involve the leasing, purchase, and sale of properties incur fees depending on the type and nature of each inquiry. As traffic and inquiries increase so do sales expand. In the event that organic inflows fall short of expectations, then results tend to stall.

Accordingly, we balance the degree of aggression when attracting fee-paying customers with the level of organic improvement when working to improve traffic.

At this point, I would ask Mr. Yamada to fill in the details.

(Takashi Yamada) Commenting further on the need to address traffic, and as identified earlier in the context of Mitula and Trovit, the fields in which the LIFULL Group operates both on a global and domestic basis are experiencing extremely fierce competition from a Google platform perspective.

Against this backdrop, and impacted by a change in Google’s algorithm, we are initiating steps to address the slight delay compared with plans.

Looking at the business domain, we continue to confront a variety of issues. We are unable, for example, to boldly expand sales due to such concerns as system stability. Owing largely to associated changes in the work flow of real estate companies, we have seen minor delays in obtaining the necessary level of penetration compared with initial expectations.

Having said this, we are not just sitting on our hands, but are pursuing various avenues including new products. While also evaluating the possibility of taking on work flows in our own right, we have already initiated activities in partnership with certain majors and are looking to secure a recovery.

(Takashi Inoue) Having said that this will increase operating efficiency, we are aware that a certain amount of time is required before users are comfortable after introduction. Recognizing that orders have also been received despite some level of skepticism even prior to introduction, we understand the important need to provide an easier-to-use user interface. At the same time, and as Mr. Yamada has pointed out, we can also leverage the positive feedback for assuming operating responsibility on behalf of users. Looking ahead, we will therefore expand sales by pursuing both avenues. We will either provide the necessary systems when users assume direct responsibility or take on a direct role when users feel the task at hand to be a burden.

Q2. Looking at the Group’s restructuring plan, and on a personal note, I believe the decision to terminate the HOME’s business overseas is both wise and bold. I especially see merit in withdrawing from the renovation and renovation contractor fields. Having said this, I feel it is somewhat of a waste to close down the site in its entirety. This is particularly the case when considering long-term value.

Can you provide us with some background in the leadup to the Group’s decision to completely withdraw from the renovation domain?

A2. (Takashi Inoue) Renovation work is closely associated with our principal business and as such the decision to terminate our renovation site was not an easy one. Looking back, we took steps to increase earnings by revising our business model on several occasions. Despite these endeavors, our efforts to place this business on a growth trajectory have proven to be unsuccessful. This has led to persistent losses over a number of years.

Our difficulties in the renovation field can in part be attributed to the small size of construction companies. Even when fielding an inquiry, many construction companies do not have the staff to engage in meaningful follow-up. While every effort has been made to capitalize whenever possible, business has not gone well.

This outcome is not unique to the Company. Looking at our peers and other venture companies, renovation sites that are generating high earnings growth are few and far between.

Taking these factors into consideration, we decided that rather than continue the site business, we should in this instance terminate operations.

We have not, however, completely given up on the renovation field. We recognize the importance of putting forward some kind of service as a means to enhance user convenience. In this instance, we will completely clear the decks before starting from scratch, rethinking our approach, and once again taking up the challenge at some time in the future.

Q3. In an earlier question about ARPA, you mentioned that the business needs of realtors was one aspect that needed to be addressed. Do you have any concerns that realtors will be reluctant to allocate a portion of their budgets to administrative support-type services when conditions are tight?

May I also ask about cost savings in the 2H. Previously, you commented that the Company might pursue cost savings in such areas as personnel expenses in the event that sales and ARPA growth fell below expectations. With this in mind, what is your outlook for the 2H?

A3. (Takashi Inoue) When talking about services for realtors, the key issues are how best to increase efficiency and, for example, how to manage personnel expenses while improving the contract rate. Discussions with customers then move away from service use because of budget availability to the payment of system usage fees from a portion of the amount saved by reducing the time required to carry out overall operations through increased efficiency. Under this scenario, we do not see the lack of a budget as an impediment to progress.

As I mentioned during our previous presentation, we will to some extent control expenses in order to secure profits in the 2H in the event sales and ARPA growth are a little weak.

Our cost of sales is virtually zero and the vast majority of expenditures is selling, general and administrative expenses. On this basis, we believe that costs are controllable.

In addition, we see the change in our account settlement date as providing certain benefits. Wherever possible, we would like to refrain from controlling costs during the January, February and March busy period as the means to secure profits. Operations are more on an even keel during the second half April to September period. Controlling costs to secure profits during this period does not have as much of an impact as the busy period from a medium-to-long term perspective. Our goal is to engage in skillful control.

Our allotted time is now up and if there are no more questions, I would like to close today's proceedings.

Thank you for your patience and attention.