# Estore Corporation (TSE Standard/4304)

**A pioneer in EC support.**
**The trend of digital transformation (DX) is a great business opportunity, and the company is expected to make a leap forward.**

KAsset Representative
Market analyst
Kenichi Hirano

## Corporate profile

| | |
|---|---|
| Location | Toranomon, Minato-ku, Tokyo |
| Representative | Kenichi Ishimura, President and CEO<br>Yoichi Yanagida, President and COO |
| Established | 1999 |
| Capital | 768 million yen |
| Listed | September 19, 2001 |
| URL | https://estore.co.jp/ |
| Business | Information & Communication |

## Stock price data (closing price as of December 19)

| | |
|---|---|
| Stock price | 1,407 |
| Number of shares outstanding | 5,636,636 shares |
| Market cap | 7,931 million yen |
| Dividend per share (est.) | 50.0 yen |
| PER (est.) | 8.8x |
| Actual PBR | 2.8x |

## Executive Summary


* The Estore Group provides e-commerce support to companies. It is a pioneer and a leader of “corporate e-commerce support.” The group consists of Estore, which is a holding company, and four consolidated subsidiaries. Its strength is its one-stop service, including the production and operation of EC sites, marketing support, and payment settlement services.

* Since its inception, the company has supported “corporate EC sites” rather than “shopping malls” in the EC industry, and it now has a 25% market share for establishing corporate EC sites. In the rapidly changing IT industry, the company has grown by constantly predicting such changes and providing timely services. In the current era of rapid digitalization, the company is aggressively pursuing M&A and business alliances under the keywords of “sophistication & comprehensive services” in order to survive the DX competition. In this fiscal year, the company made SHIFFON Co., Ltd. (now SHIFFON) a subsidiary and launched a hands-on incubation (HOI) business in addition to its existing services.

* In 2Q of FY 3/2023, the company posted net sales of 2.85 billion yen (up 0.3% YoY) and operating income of 250 million yen (down 54.3% YoY) as the latest performance. The sharp decline in profit was due to aggressive upfront investment in the development of new functions, development costs for large-scale projects and temporary costs such as M&A expenses. In the second half of the fiscal year, performance is expected to grow significantly due to the Christmas and New Year gift season, which tends to increase EC consumption every year, as well as the contribution of the new subsidiary SHIFFON.

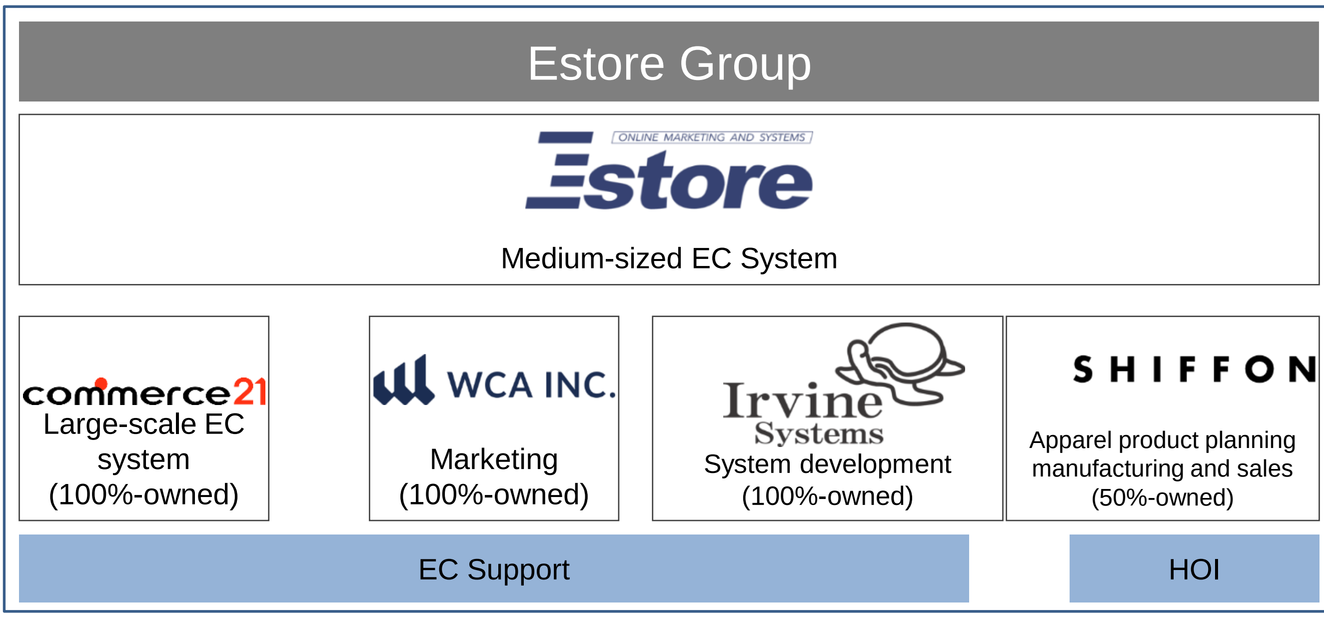
* The EC market expanded due to the restrictions on going out amid the COVID-19 pandemic. Spending through EC remains firm, and enterprises’ willingness to invest in DX is strong. It is certain that the EC market will continue to expand, so the business environment is favorable. However, competition is projected to intensify. The company aims to ride the wave of DX and achieve significant growth by expanding its lineup of services in markets where it can read market trends that are changing at a tremendous pace and maximize the synergy among group companies. In the fiscal year ending March 2025, the final year of the medium-term management plan, the company expects net sales of 10.1 billion yen and operating income of 2.1 billion yen.

* The company is expected to be a rising star in 2023 as it engages in “corporate EC site” support business, which increases customer profits by “providing customers with all the EC solutions (systems, marketing, and payment settlement) they need,” which can be called “true DX” to triumph in the unified commerce market.

# Overview/History

## ■ Overview

The group's primary business is to support companies' own e-commerce sites. As of November 2022, the group consists of Estore, which is a holding company, and four consolidated subsidiaries. The services they offer include (1) EC systems, (2) payment settlement services, and (3) marketing services. The company's strength lies in its ability to provide one-stop services to increase the competitiveness of customers' own EC sites. In the current fiscal year, the company is launching a hands-on incubation (HOI) business with the aim of turning its accumulated know-how into their "own business" rather than just "providing support."




## ■ History

Kenichi Ishimura, the current representative director and CEO, founded the company in February 1999 to support "online specialty shops." At that time, EC was in its infancy, and Rakuten and an NTT-related company were the only two companies operating EC shopping malls, while the company was the only company providing corporate EC support. The company is a pioneer in corporate EC support, being the first in Japan to offer the "shopping cart" function as seen in many EC sites. The IT world is changing rapidly, and technology and services are destined to face fierce competition. The company has always grasped these changes accurately and has changed its main services, such as the provision of rental servers and marketing support, over a span of almost seven years. Through a series of capital and business alliances, the company provided three services (system, marketing, and payment settlement) until 2019 with Estore only. However, in order to change itself in the era of paradigm shift where society is drastically changing, the company has been conducting M&A successively, starting with Commerce21 Corporation (hereinafter "C21") in 2020, followed by WebCrew Agency Inc. (hereinafter "WCA"), and Irvine Systems, Inc. Through these acquisitions, the company has established a structure that allows the group to provide consistent support for e-commerce sites, including production, operation, payment settlement and marketing. Furthermore, in August 2022, the company acquired SHIFFON, an apparel business, as a consolidated subsidiary, and launched a hands-on incubation (HOI) business.

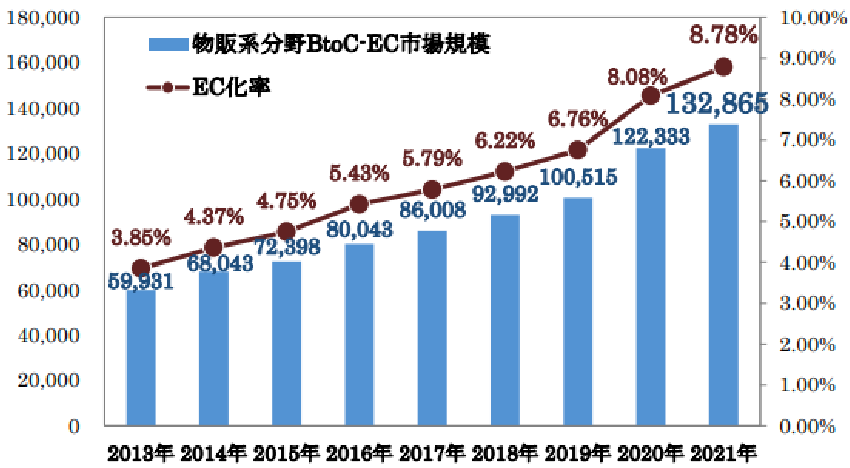
# Business Environment

According to the statistics by the Ministry of Economy, Trade and Industry, the B2C-EC market size in the goods sales sector in 2021 was 13.3 trillion yen, up 1.5 trillion yen from the previous year, and EC adoption rate was 8.78%, up 0.7 points. Compared to 2020, when the EC market expanded significantly owing to a rise in demand from people staying home due to the spread of COVID-19, the growth rate is slightly lower, but EC adoption rate is increasing, which indicates that consumption at EC sites appears to have taken root.

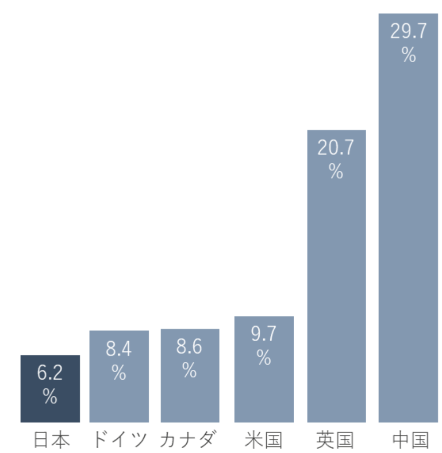
Despite continued strong growth, Japan's EC adoption rate is still in the 8% range, lagging behind other developed countries, as shown in the chart below. Therefore, there is ample room for growth in Japan's EC market, which is expected to grow to at least 18%.

The B2C-EC market for goods sales can be divided into "platforms" and "corporate EC," and it is estimated that major EC platforms account for about 70% of this market. While opening a store or displaying items on a major EC platform has the advantage of attracting a large number of customers, there are fees, competitors, and restrictions on access to customer information. On the other hand, corporate e-commerce enables direct promotion of a brand's worldview and access to consumer information. However, it requires technology and know-how, so it is not easy. Nevertheless, from a quantitative perspective, B2C (D2C), where companies sell directly through their own EC sites, is expected to grow. This is the reason why the company focuses on corporate EC sites. In the current era of declining population and digitalization, corporate EC sites are a necessity for companies seeking to improve management efficiency, and full-scale growth is just beginning.

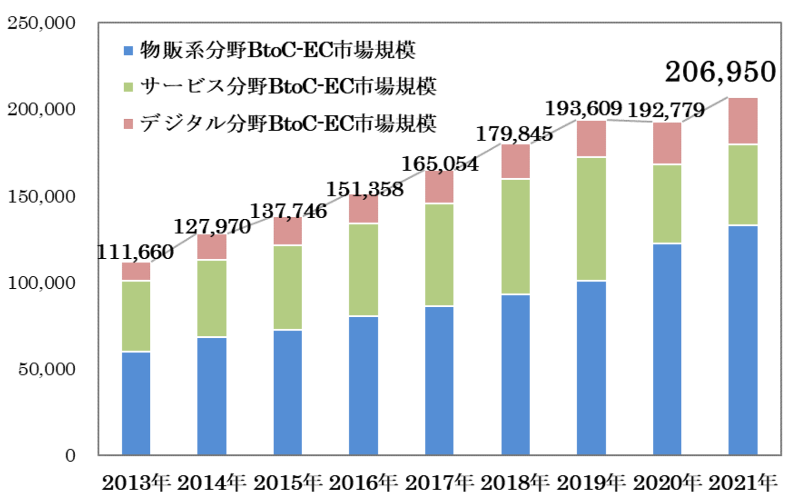
◻ Yearly changes in the size of the B2C-EC market for goods sales and EC adoption rate
(Unit: 100 million yen)




◻ Global EC adoption rate (B to C) 2018




◻ Yearly changes in the size of the B2C-EC market and EC adoption rate (Unit: 100 million yen)

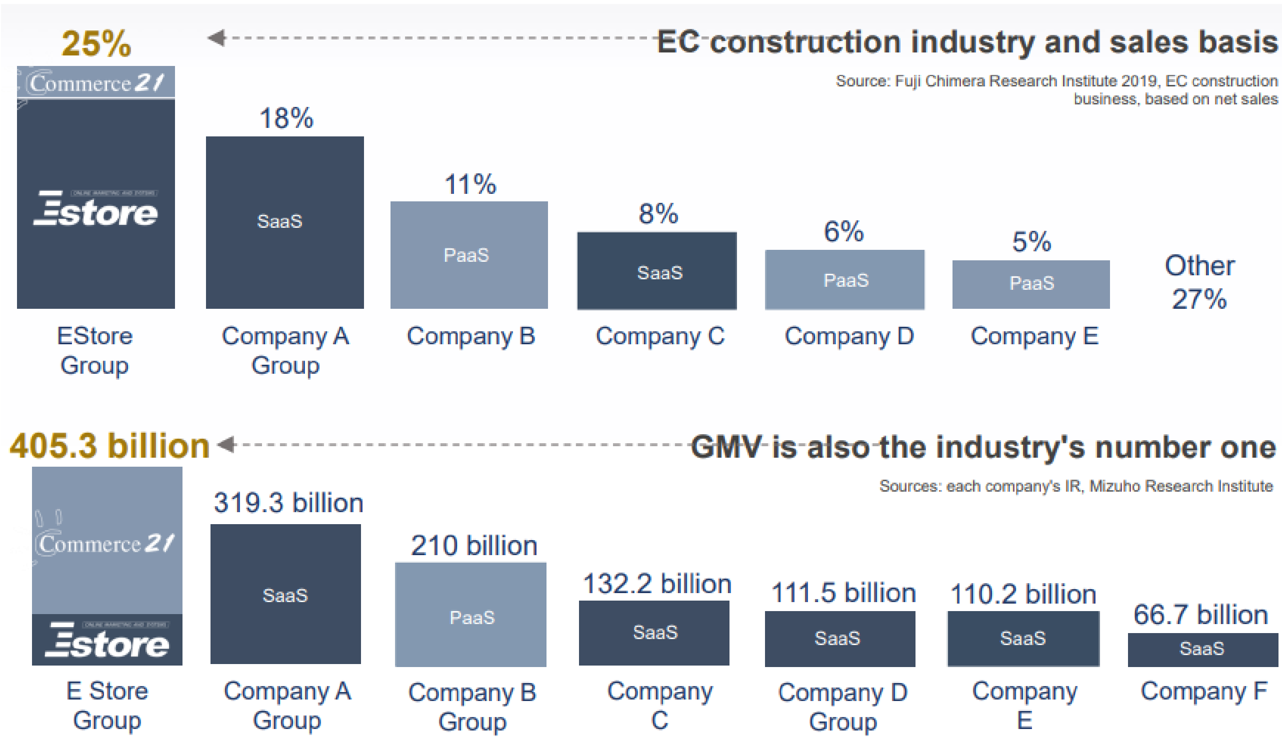



Source: Ministry of Economy, Trade and Industry

# Position in the Industry

■ Position in the industry

Since the start of its business, the company has been providing EC support to its customers, and boasts the industry's top market share for corporate EC site production at 25% (based on sales) and the industry's top GMV (Gross Merchandise Value) at 405.3 billion yen. (from the medium-term management plan released in 2020)

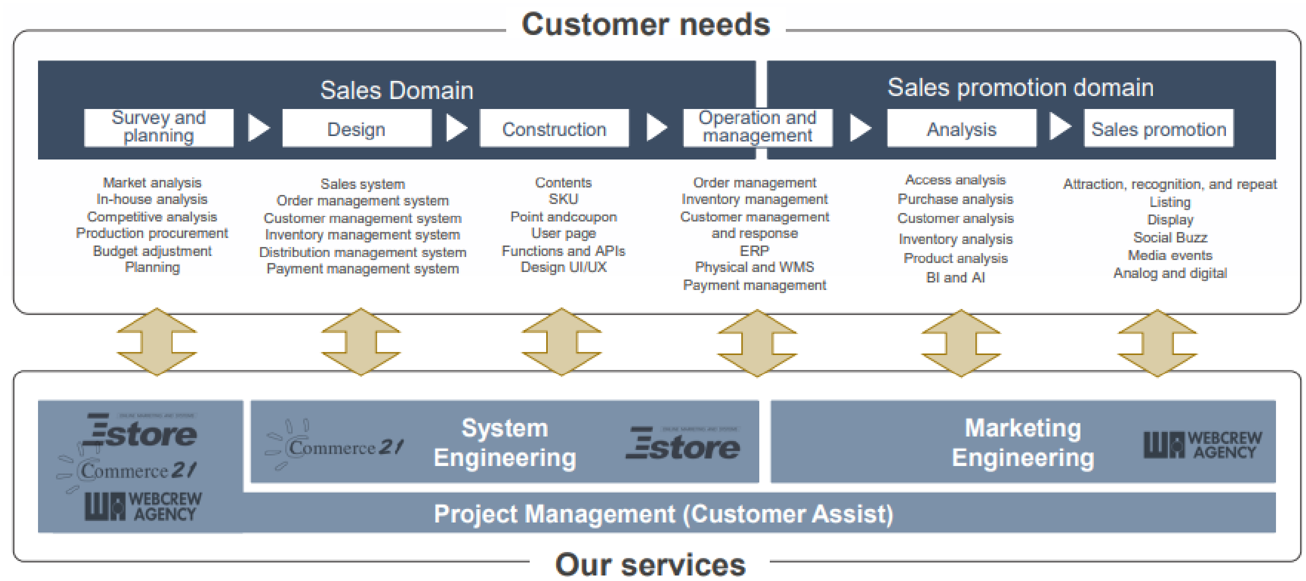



Major customers include a number of Japanese companies. (from the supplementary financial data)

# Business Model

## ■ Revenue structure

The company provides three services: EC systems, payment settlement services, and sales promotion strategy proposal & sales promotion agency services. As shown in the figure below, the company's involvement in the production of EC systems can lead to the provision of other services such as payment settlement and sales promotion, creating a revenue structure that cyclically generates synergetic effects among services.




While many competitors respond to customer needs only partially, the company can provide a one-stop service from the sales domain, including market analysis and system development, to the sales promotion domain based on payment settlement and purchase data analysis. Since information is not fragmented, they are able to respond precisely to customer needs. This comprehensive capability is their greatest strength and is the reason why the company is the industry leader.

## ■ Revenue model of each service

There are two EC systems: "Shopserve" provided by Estore and "Sell-side Solution" developed on consignment by C21. The former is a SaaS-type EC site production system for small and medium-sized companies, featuring stable operations and an overwhelming API. The latter is a PaaS-type system that can generate significant recurring revenues through maintenance, operation, and additional development after initial development. More than 10% of the best 100 Japanese companies in terms of sales are their customers.

The payment settlement service is a business based on settlement agency commissions with a linear revenue model in which revenue is generated according to the number of customers and the amount of business flow.

Marketing is a business that supports customer acquisition and website production with the aim of increasing client companies' EC sales and improving operational efficiency. This is a business model with high recurring revenues: the higher the retention rate, the lower the customer acquisition cost per customer, and the longer the retention, the higher the order amount.

# Business Model

| | Group companies | Services |
|---|---|---|
| EC system | Estore | Cloud EC system |
| | C21 | Dedicated EC system construction and packaged EC system |
| Payments, etc. | Estore | Provision of pay-as-you-go services such as settlement services |
| Sales promotion proposals | Estore<br>C21 | Consulting |
| Sales promotion agency | WCA | Mass marketing (acquisition of new customers)<br>Direct marketing (making repeat customers) |

In addition to these, SIFFON, an apparel planning and sales company, was made a consolidated subsidiary in August 2022 and the HOI business was launched in earnest. This business aims to improve profitability by acquiring companies that can be expected to achieve significant results by strengthening e-commerce services. Although performance is expected to fluctuate depending on the availability of projects and the speed at which performance improves, the business is basically expected to improve profitability and provide a significant return.

# Performance Trends

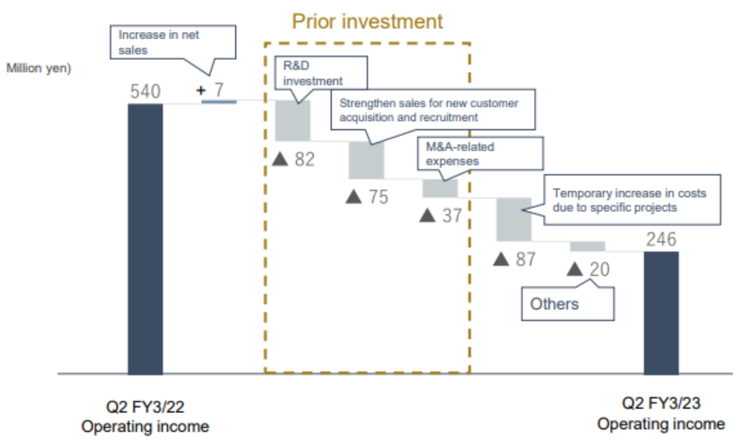
The performance has been strong. During the COVID-19 ciricis from 2020 to 2021, the e-commerce market expanded dramatically due to so-called "stay-at-home" spending. After the government lifted restrictions on going out, the growth in the e-commerce market has moderated, but the number of e-commerce users has spread and its spending has been growing steadily. Companies have been forced to be aware of the e-commerce and digital transformation trends and have a strong appetite for investment. In this environment, the Company's performance has also shown steady growth as an industry leader, although profits have fluctuated due to development investment and M&As.

| (Million yen) | 2019.3 | 2020.3 | 2021.3 | 2022.3 | 2023.3 (Forecast) |
|---|---|---|---|---|---|
| Net sales | 4,932 | 4,852 | 10,504 | * 5,746 | 9,600 |
| Operating income | 515 | 478 | 906 | 1,051 | 1,250 |
| Operating income margin (%) | 10.4 | 9.9 | 8.6 | 18.3 | 13.0 |
| Ordinary income | 582 | 526 | 1,073 | 1,078 | 1,270 |
| Net income | 409 | 367 | 482 | 677 | 800 |

*The decline in sales in 3/22 was due to the switch from the gross amount to the net amount. Sales increased by 6% in the previous presentation.

In the current period, the second quarter of the fiscal year ending March, e-commerce spending has been moderated, but supported by client companies' DX investments, the Company secured sales of 2.85 billion yen, an increase of 0.3% year-on-year. However, operating income fell sharply to 250 million yen (-54.3%). This was due to one-time factors such as aggressive investment in the development of new functions, as well as higher development costs in 1H due to M&A expenses and some large-scale projects (see diagram below). Differences from the plan do not appear to be significant.

□ Factors behind changes in operating income (from the financial results briefing materials)




□ Comparison of 1H Results

| (Million yen) | 2022.3 | | 2023.3 | |
|---|---|---|---|---|
| | 1H | 2H | 1H | YoY (%) |
| Net sales | 2,842 | 2,904 | 2,849 | 0.3 |
| Operating income | 540 | 511 | 246 | -54.3 |
| Operating income margin (%) | 19.0 | 17.6 | 8.6 | |
| Ordinary income | 540 | 538 | 168 | -68.9 |
| Net income | 348 | 329 | 92 | -73.6 |

The performance is expected to grow significantly in the second half of the year due to the Christmas and New Year gift season, which in previous years has tended to increase demand for e-commerce spending, as well as the contribution of the new subsidiary SHIFFON.

# Capital Policy

■ Summary

The consolidation of SHIFFON on August 31, 2022 has resulted in a significant rise in assets/liabilities. The balance of assets increased by 3.78 billion yen from the end of the previous fiscal year.
On the other hand, both short-term and long-term borrowings have increased as the acquisition of shares of the new subsidiary was compensated for by bank loans.
Free cash flow, calculated by subtracting investment cash flow from operating cash flow, is also negative at this point in time due to an increase in investment.

☐ Consolidated balance sheet for Q2 FY3/23 (from the financial results presentation)

(Million yen)

| | | | |
|---|---|---|---|
| Current assets | 8,075 | Current liabilities | 6,543 |
| Major items | | Major items | |
| Cash and deposits | 4,628 | Notes payable, accounts payable and accrued liabilities | 1,724 |
| Notes, accounts receivable and contract assets | 2,282 | Short-term and current portion of loans | 1,930 |
| Merchandise | 818 | Deposits received | 2,189 |
| | | Non-current liabilities | 2,383 |
| Non-current assets | 3,912 | Net assets | 3,061 |
| Tangible and intangible | 2,275 | Shareholders' equity | 2,551 |
| Investment and others | 1,237 | Others | 509 |
| Total assets | 11,987 | | 11,987 |

(Total assets at the end of March 2022: 8,211)

Liabilities

Long-term debt: 1,590 million yen

Convertible bonds: 510 million yen

M&A of SHIFFON is expected to take 2 steps, acquiring 50% in August 2022, and acquiring an additional 20% in June 2023. For the time being, the Company's policy is to prioritize upfront investment for growth.

# Mid-term Plan

## ■ Management policy

There has been no change in the basic policy of “corporate EC support” since the company’s establishment. In a digital society inundated with information, the amount of information exceeds the amount that can be digested. Under such circumstances, consumers need information necessary for their lives, and businesses need information for their operations. Consumers seek product lineups and price competitiveness from “mall stores,” while they seek specialization and quality from “corporate EC sites.” Therefore, the company, whose customers are “corporate EC” operators, will focus on ARPU (Average Revenue Per User) and LTV (Life Time Value), although it is necessary to acquire new customers.

## ■ Mid-term plan

As the paradigm shift in society progresses rapidly and DX becomes inevitable, the growth of the EC market, which is positioned at the center of this shift, is expected to accelerate. In addition, the fusion of physical stores and EC (unified commerce) is expected to progress, and the trend of DX is a great opportunity for growth. In its medium-term management plan (FY 3/2021 to FY 3/2025), the company is actively pursuing business alliances and M&A to accelerate its growth as a comprehensive solution provider for EC, offering “more sophisticated and comprehensive services.” As mentioned above, this fiscal year, the company acquired SHIFFON as a subsidiary and launched a new HOI business on a full-scale basis. This business will contribute to the company’s performance from the second half of the year.

Target figures in the medium-term management plan are described below. The company aims to double net sales to 10.1 billion yen and quadruple operating income to 2 billion yen from FY 3/2021. The ratio between the EC support business and the HOI business is 75:25.

□ Medium-term performance forecast (from the medium-term management plan)

| | | FY2020 New Accounting Standards | | | | FY2024 New Accounting Standards | | | |
|---|---|---|---|---|---|---|---|---|---|
| Sector | | Net sales | Operating income | Operating income margin | Profit Portfolio | Net sales | Operating income | Operating incomc margin | Profit Portfolio |
| EC support | System: PaaS | 1.9 billion yen | 120 million yen | 6% | 19% | 4.4 billion yen | 600 million yen | 15% | 28% |
| EC support | System: SaaS | 2.44 billion yen | 490 million yen | 20% | 80% | 2.6 billion yen | 800 million yen | 30% | 38% |
| EC support | Marketing | 740 million yen | 10 million yen | 1% | 1% | 1.6 billion yen | 200 million yen | 12% | 10% |
| Hands-on DX | | – | – | – | – | 1.5 billion yen | 500 million yen | 34% | 24% |
| Total (before depreciation of goodwill) | | 5.08 billion yen | 620 million yen | 12% | | 10.1 billion yen | 2.1 billion yen | 21% | |
| After the depreciation of brick | | | 500 million yen | 10% | | | 2 billion yen | 20% | |
| After M&A 1-time expenses | | | 400 million yen | ← After temporary expenses such as office integration | | | | | |

Excluding the special factors in 2020 and 2021 (the demand by people staying at home during the COVID-19 pandemic), the B2C-EC market has grown at an average annual rate of over 8% since 2015. Despite being a pioneer, the company’s growth rate was lower than that of the market, because Estore had been providing services all by itself until 2020 as mentioned above. However, with the establishment of a one-stop service structure through M&A after 2020, the company expects its growth rate to increase in the future.

Considering the acceleration of corporate investment in DX as a chance to make a leap forward, the company plans to continue to aggressively pursue business alliances and M&A opportunities, and expects to see large returns from its HOI business. The company aims to make a leap forward as a provider of comprehensive solutions for supporting EC.

# Issues and Risks

System development is indispensable for the company, which operates in the IT market where technological innovation advances rapidly. Securing and training system engineers and sales staff is also a challenge. In addition, securing personnel with strong marketing and consulting skills is an important issue in order to expand the HOI business as M&A will increase as well as to increase the satisfaction of EC system customers.

In addition, it appears that the introduction of payment services to C21's customers is not progressing as initially planned, and if it does not progress as expected, it will be necessary to cover its shortfalls by other service areas to achieve the goals of the medium-term management plan.

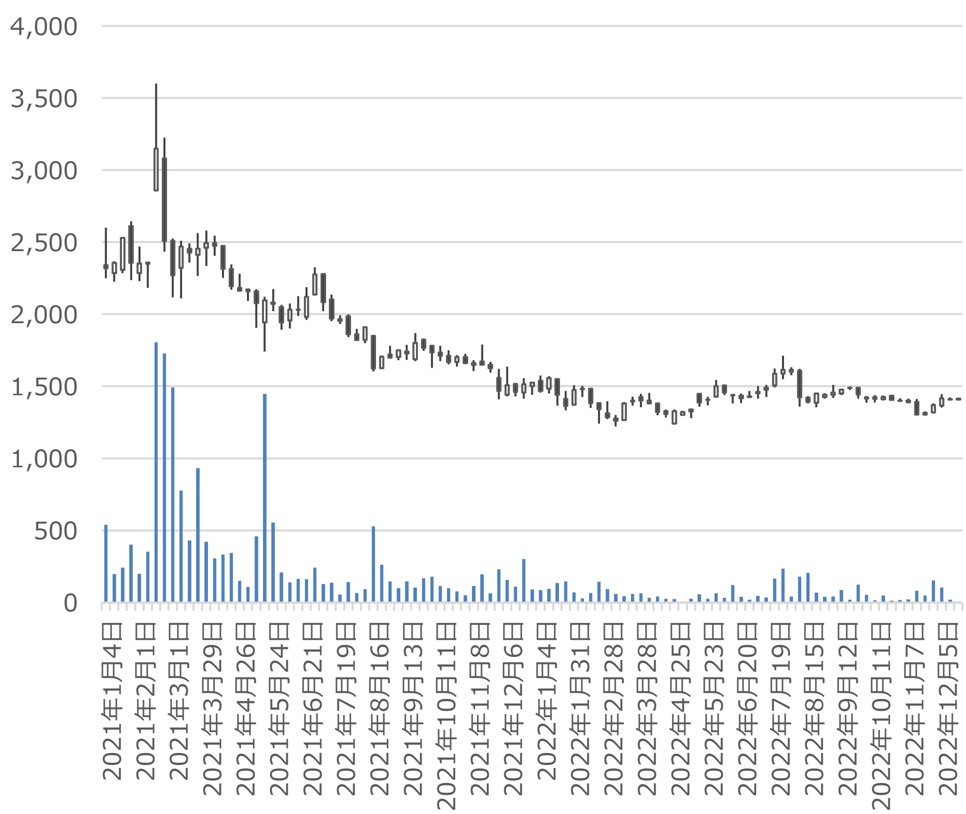
If the results of M&A are less than expected, the company's financial condition may deteriorate and should be monitored closely.

# Stock Price Analysis

The company's consolidated results in the second quarter of the fiscal year ending March 31, 2023 showed a slight increase in net sales to 2,849 million yen, but operating income fell 54.3% year on year to 246 million yen, ordinary income fell 68.9% year on year to 168 million yen, and net income fell 73.5% year on year to 92 million yen, resulting in a sharp drop in profits, which led to a nosediving stock price. However, we believe this is a good time to purchase its stock. The first reason is that the significant decrease in profit in the second quarter was due to the strengthening of sales activities to acquire blue-chip customers, recruiting activities to strengthen the personnel structure, and M&A-related expenses. The company's full-year consolidated forecasts for 2023 remain unchanged, calling for net sales of 9.6 billion yen (up 67.0% YoY), operating income of 1,250 million yen (up 18.9% YoY), ordinary income of 1,270 million yen (up 17.8% YoY), and net income of 800 million yen (up 18.1% YoY). Secondly, the dividend is still scheduled to be increased by 10 yen/share to 50 yen/share, showing continuous dividend increase from 29 yen/share in 2020. It is noteworthy that the company has never decreased the dividend amount. The dividend yield as of December 2 was 3.65%, making it a growing stock. Thirdly, the company is expanding its business domain by linking systems and marketing. The company's main business is to provide customers with EC solutions (systems, marketing, and payment settlement) in a single package, which can be called "true DX," and support "corporate EC" to increase customers' profits. This business structure was reinforced by acquiring WCA, which operates marketing business. In addition, the synergetic effects with another group company C21, which excels at planning EC infrastructure and consulting, would strengthen the company. The EC industry is entering the era of unified commerce, and "sophisticated and comprehensive services" are at the center of this era. We believe that the company will be the winner in such an era. In this sense, the share price of 1,407 yen as of December 19, 2022, after a prolonged slump from the high of 3,600 yen on February 15, 2021, does not make sense. We would like to expect much from it, as a promising stock in 2023.

| Stock price (historical) | |
|---|---|
| Year's high | 1,712 |
| Year's low | 1,222 |
| All-time high | 590,000 |
| All-time low | 620 |

Share price trends (weekly)



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