Supplementary Material for the First Quarter of the Fiscal Year Ending February 28, 2021

Stock code: 2930
Kitanotatsujin Corporation
July 15, 2020

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Executive Summary

- Net sales were ¥2,268 million (down 5.0% year on year), and operating profit amounted to ¥561 million (up 1.4% year on year).
- Despite the impact of COVID-19 in March and April, the number of new customer acquisitions in May recovered to the level before the consumption-tax hike in October 2019 through measures such as raising the CPO limit.
- Achieved certain level of improvement in LTV through cross-selling measures for customers who are regularly busing products, as well as an improvement in customer service quality to promote service continuation

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Company Overview and Business Overview

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Company Overview

【Company Name】	Kitanotatsujin Corporation	
【Representative】	Katsuhisa Kinoshita, Representative Director & President	
【Capital Stock】	¥273,990,000 (As of May 31, 2020)	
【Officers and Employees, etc.】	172 people (As of May 31, 2020)	
【Incorporated】	May 1, 2002	
【Listing】	May 2012	Listed on Sapporo Securities Exchange, Ambitious Market
	March 2013	Upgraded to Main Market on Sapporo Securities Exchange
	November 2014	Listed on the Tokyo Stock Exchange, Second Section
	November 2015	Assigned to the Tokyo Stock Exchange, First Section

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Business Overview

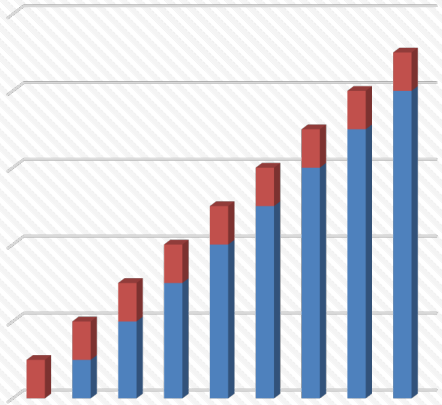
Product development based on feeling

- Established original product development standards with 750 items specifically designed for online sales and conduct a thorough monitor survey
- Only 2% of development projects meet these standards to be commercialized. A product will only be commercialized when an “astonishingly fine product” is created.
- Currently offering our original products that meet specific customer needs, including cosmetics, health foods, and miscellaneous goods (a total of 33 products)

北の快適工房 J NORTH FARM　北の快適工房 J NORTH FARM BEAUTY　北の快適工房 MEN

D2C* × Subscription

- Steadily growing business model
- Approximately 70% of net sales is from subscription purchases



Red: New sales

Blue: Subscription sales

*D2C stands for Direct to Consumer, which is a system to sell our products directly to consumers through e-commerce sites.

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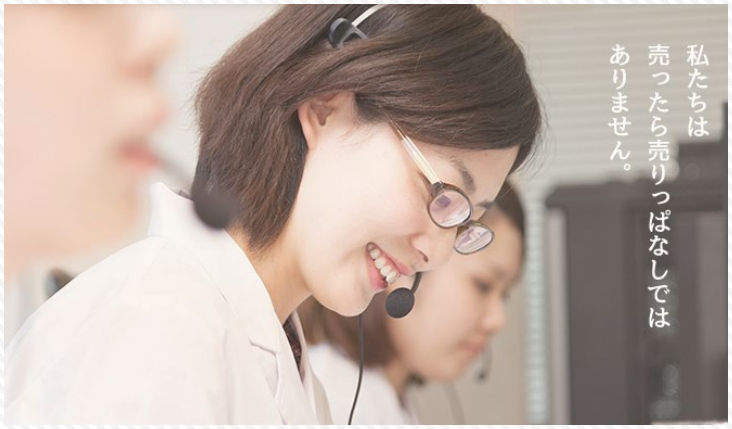
Thorough customer follow-up

Attentive after sales follow-up by in-house professional staff based on their expertise as a developer



Advertising optimization system

(1) Analyze daily accumulated data and calculate LTV*
(2) Set a CPO* limit for each product as the upper limit for advertising expenses
(3) Calculate and manage CPO on a daily basis by subdividing approximately 5,000 advertisements presented regularly into various segments.
(4) Automatically suspend advertisements that exceed the CPO limit

⇒ Develop a system where only profitable advertising will remain

* LTV stands for Life Time Value, which is the amount of lifetime net sales a customer will bring.
CPO stands for Cost Per Order, which is the amount of advertising expenses per order. For example, if advertising expenses are ¥1 million and the number of new customer acquisitions is 100, the CPO is ¥10,000.

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Five level profit management

- Visualize profits on five levels for “each product” -

Gross profit by product

Mandatory cost per order

Gross profit – order-linked costs = net gross profit (coined term)

Net gross profit - sales promotion expenses = sales profit (coined term)

Personnel expenses for each product

	Total of all products	Product (1) ×	Product (2) △	Product (3) ◎
Net sales	10,000	6,000	3,000	1,000
Profit (1) Gross profit or loss	4,400	2,500	1,200	700
Order-linked costs (enclosures, accessories, settlement charges, shipping fees, packaging materials, etc.)	600	300	200	100
Profit (2) Net gross profit	3,800	2,200	1,000	600
Sales promotion expenses (primarily advertising expenses)	1,800	1,500	200	100
Profit (3) Sales profit	2,000	700	800	500
ABC (Active Based Costing)	200	100	50	10
Profit (4) ABC profit	1,800	600	750	490
Operating expenses (rent expenses and indirect operating personnel expenses, etc.)	700	420	210	70
Profit (5) Operating profit for each product	1,100	180	540	420
Operating profit margin for each product	11%	3%	18%	42%

- The sales of Product (1) are increasing. However, this is due to spending more on sales promotion expenses, and profit is not high as much. Product (3) has low sales, but it has a high gross profit margin. It is making a lot of profit, since it does not spend much on ABC. However, it is easy to overlook this matter, since a product with low ABC is not often be discussed in the Company.
- By thoroughly managing this profit, it will be possible to maintain a high operating profit margin in the mass market.
- Based on results for the fiscal year ended February 29, 2020, operating profit per employee was ¥23.32 million, ROE was 54.2%, and operating profit margin was 28.9%.

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Significant success of "injectable cosmetics series" with total sales of approximately 17 million patches*1

*1 As of March 31, 2020 (research by the Company)

[No. 1] "HYALO DEEP PATCH" for wrinkles under the eyes and smile lines

[No. 2] "MIKEN DEEP PATCH" for the area between the eyebrows

[No. 3] "ODEKO DEEP PATCH" for the forehead

[No. 4] "CHEEK PORE PATCH" for the cheek pore zones*2

*2 Area where cheek pores are concentrated

[Characteristics]

- Apply the microneedle technology, which is also used in medical treatments.
- A new concept of cosmetic products to directly inject needle-shaped beauty ingredients into the skin ("injectable cosmetics")
- Established a dominant position in the microneedle cosmetics market in terms of price and quality

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Food with functional claims “KAITEKI OLIGO”

Our sales of oligosaccharide food for household use is the highest in Japan.*1

Improves bowel movements for people with constipation tendency (increase stool volume and frequency of bowel movements)

*1 Research by JMA Research Institute Inc. (May 2016). The annual sales up to the previous fiscal year of home use products sold in Japan, such as powder, granules and syrup products containing “oligos and oligosaccharides”

- Awarded the Monde Selection nine times
  (Awarded the Grand Gold Award eight times and the Gold Award one time between 2012 and 2020)
- The registration as a food with functional claims was accepted in May 2019.

→ Japan’s first food with functional claims containing five types of functional ingredients
Expecting an increase in sales going forward through an expansion of the extent of advertising expressions

- “OKOSAMAYOU KAITEKI OLIGO,” a product for children, was launched in February 2019.

*2 As of September 7, 2018 (research by the Company)

“EYE KIRARA,” one product sells every 27 seconds.*2

- Awarded the Gold Award of the Monde Selection for five consecutive years (2016 to 2020)
- Run in medical journals, representing a rare achievement for cosmetic products
- “MEN’s EYE KIRARA” for men was also launched in January 2019.

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Highlights for the First Quarter of the Fiscal Year Ending February 28, 2021

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Key Performance Highlights [Year on Year]

(Millions of yen)

	Results for the first quarter of the fiscal year ended February 29, 2020	Results for the first quarter of the fiscal year ending February 28, 2021	YoY changes	YoY %
Net sales	2,387	2,268	-118	-5.0%
Operating profit	553	561	+7	+1.4%
Operating profit margin	23.2%	24.7%	+1.5pt	
Ordinary profit	553	560	+7	+1.3%
Profit	385	389	+3	+1.0%

- Net sales decreased due to a decline in the number of new customer acquisitions
- Profits at each level were flat due to reduced advertising investment in response to the deterioration in the status of new customer acquisitions

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Key Performance Highlights [Progress against Forecasts]

(Millions of yen)

	Forecast for the fiscal year ending February 28, 2021	Results for the first quarter of the fiscal year ending February 28, 2021	Progress
Net sales	**8,227**	**2,268**	**27.6%**
Operating profit	**2,006**	**561**	**28.0%**
Ordinary profit	**2,007**	**560**	**27.9%**
Profit	**1,357**	**389**	**28.7%**

- Steady progress in net sales and profits at each level

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The number of new customer acquisitions

March and April

- Spread of COVID-19
- Decline in consumer confidence

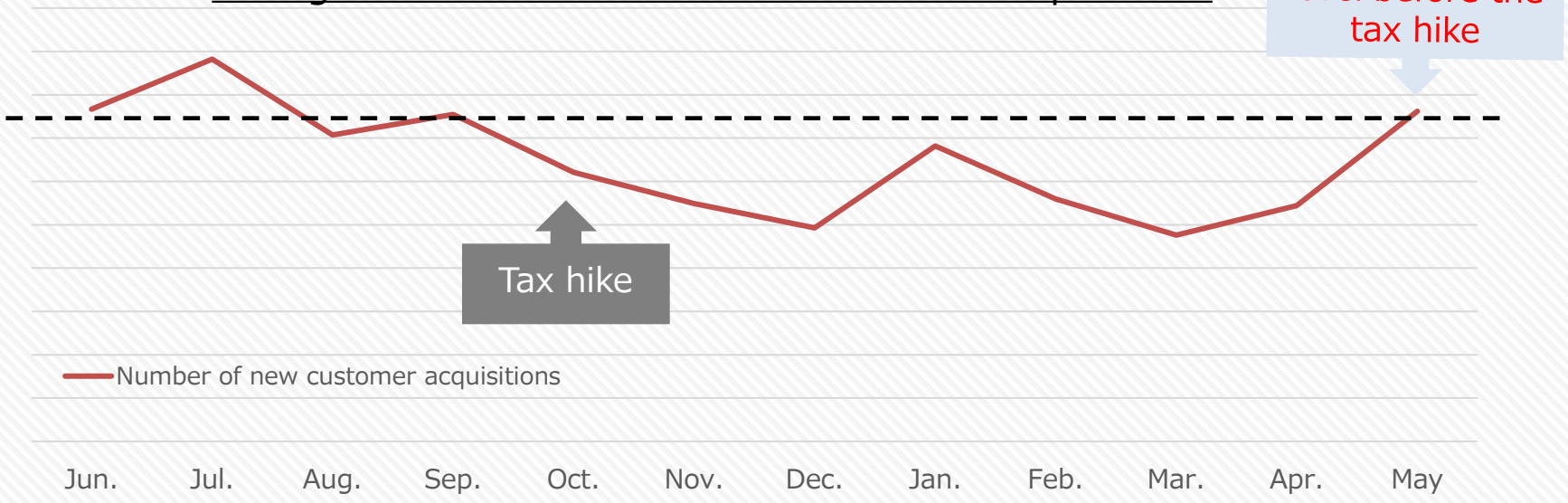
→ Fell below the initial plan

May

- Trend of a recovery in consumer confidence
- Raising the CPO limit

→ Exceeded the initial plan and returned to the level before the consumption-tax hike in October 2019

Changes in the number of new customer acquisitions



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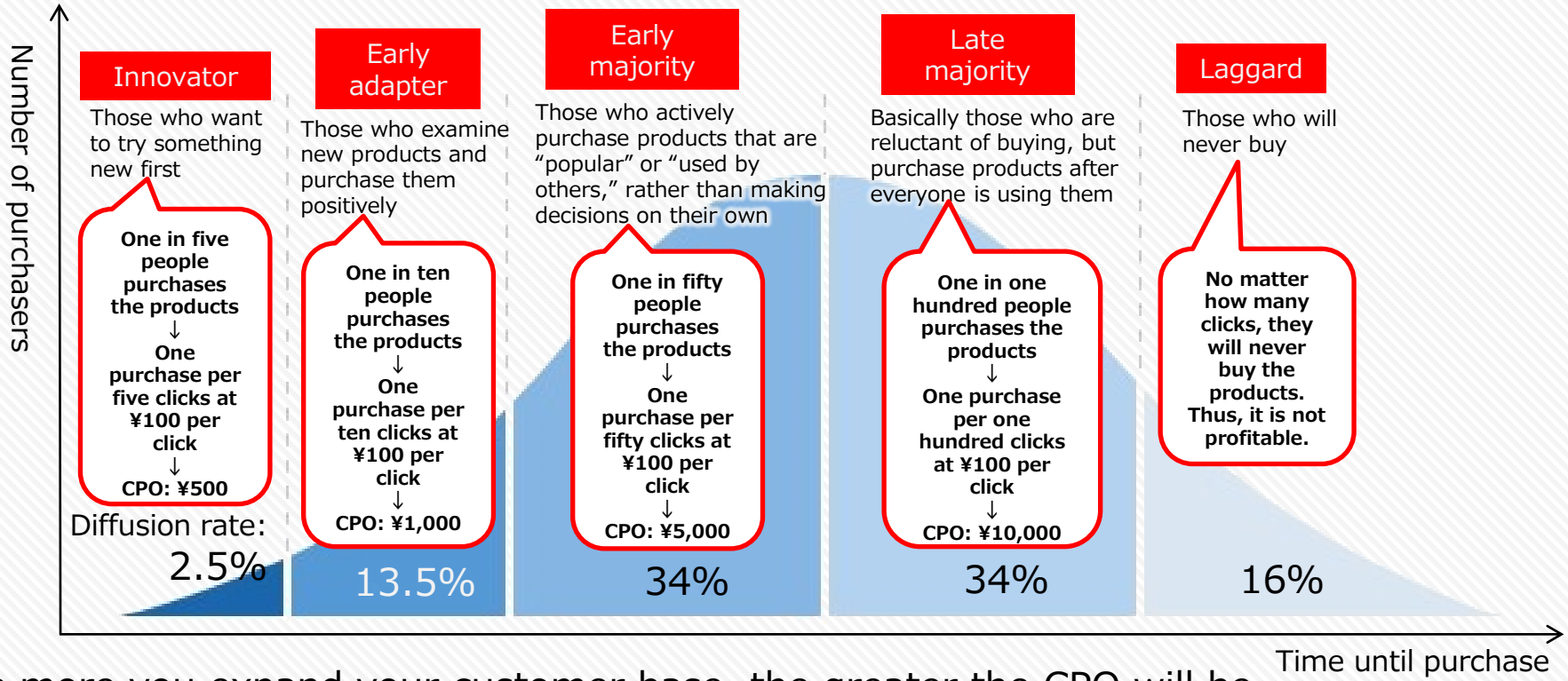
Correlation between CPO and the number of new customer acquisitions

- Profit = Number of new customer acquisitions × Profit per customer (LTV – CPO)

  Advertising expenses and the number of new customer acquisitions fall under the "law of diminishing returns," and CPO (acquisition cost per order) tends to increase as the number of new customer acquisitions increases.

Consumer distribution by innovator theory



The more you expand your customer base, the greater the CPO will be.

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Correlation between CPO and the number of new customer acquisitions

■ Profit = Number of new customer acquisitions × Profit per customer (LTV – CPO)

- Lowering the CPO increases profit per customer, but decreases the number of new customer acquisitions
- Higher CPO increases the number of new customer acquisitions, but decreases the profit per customer

→ It is important to find the most profitable CPO

Example) In the case of LTV of ¥10,000

Diminishing returns begin from here

CPO	¥3,000	¥4,000	¥5,000	¥6,000	¥7,000	¥8,000	¥9,000
Number of new customer acquisitions	100	120	150	200	250	270	300
Profit per customer	¥7,000	¥6,000	¥5,000	¥4,000	¥3,000	¥2,000	¥1,000
Profit	¥700,000	¥720,000	¥750,000	¥800,000	¥750,000	¥540,000	¥300,000

Most profitable profit per customer

Most profitable

Largest number of new customer acquisitions

→ In this case, it is most desirable to set the CPO limit to ¥6,000.

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Advertising investment efficiency, ROAS*

■ ROAS deteriorated due to failure in measures to raise the CPO limit.

May 2019	September 2019 (before the tax hike)	May 2020
ROAS 1.00	ROAS 1.17	ROAS 0.75
Number of new customer acquisitions: 37,000	Number of new customer acquisitions: 37,000	Number of new customer acquisitions: 38,000

(Premise)
We have assumed that the ROAS would deteriorate to a certain degree, because it has become more difficult to acquire new customers since we had added into the target consumers who are less willing to purchase compared to past targets in order to increase sales from the previous fiscal year.

(Background)

Past trends
Certain number of "orders that do not require advertising expenses" via search engines and malls that grow in proportion to advertising placement volume

Measures
Included "orders that do not require advertising expenses," etc. in the calculation of the CPO limit

→ Raised the CPO limit, but…

Result
The effect of the measures was weak. Although the number of new customer acquisitions increased, the increase was not enough to match the increase of CPO.

→ ROAS deteriorated, and profit margin declined.

→ Review the calculation method of the CPO limit, in order to increase net sales, while maintaining a high profit margin

* ROAS stands for Return On Advertising Spend, which is an indicator of advertising investment efficiency that measures how much sales are generated from advertising. If ¥1 million was used for advertising expenses, and sales was ¥900 thousand, the ROAS is 0.90. If ROAS is less than 1, the balance of income and expenditure at the first purchase will be negative. Meanwhile, if it is a subscription purchase, the balance will become positive as products are purchased continuously.

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Approach to existing customers who are regularly buying products

Implemented full-scale approach to existing customers who are regularly buying products during the first quarter under review

Specific measures (1) Cross-selling* to improve LTV

Certain achievements in improving LTV through cross-selling measures for existing customers

Illustration of cross-selling as reference

Facial cleanser

×

Lotion

(Example) Would you like some lotion as well?

*Cross-selling is a sales method to ask customers to purchase not only the products they are currently purchasing, but also other products.
In addition to improving LTV, customers will benefit from lower settlement charges and shipping fees.

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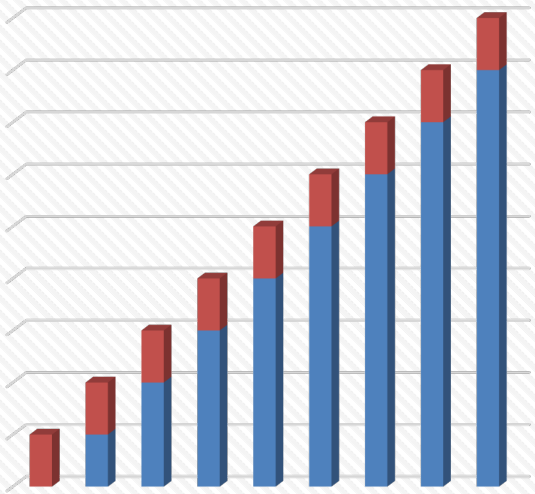
Approach to existing customers who are regularly buying products

Implemented full-scale approach to existing customers who are regularly buying products to increase the persistency rate during the first quarter under review

Specific measures (2)

Improving customer service quality



- Improve knowledge of in-house professional staff
- Improve services of telephone support

→ Improvement of customer satisfaction and the rate of continued subscription purchases

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Other measures

1 Full-scale implementation of approach to affiliates* by a dedicated team

- Affiliates were the main source of acquisition of new customers several fiscal years ago. At the time, SEO (Search Engine Optimization) was a major means. However, Google's update has slowed it down.
- Current affiliates are mainly "performance-based advertising agencies," where affiliates advertise using their own funds (ad-affiliates).
- Since the number of highly skilled affiliates has increased, the Company has once again reinforced efforts for affiliates.

2 Experimenting with TV advertisement in certain regions and magazine advertisement, including women's magazines

- Approach to customers who do not purchase products on the Internet
- Published in magazines: Josei Seven, CLASSY, STORY, Be Story, Oggi, etc.

* An online advertising method, where an affiliate posts advertisements about an advertiser's products and services on its blogs, websites, or other media. The advertiser pays a fee (commission) to the affiliate, if a viewer purchases the product through the link.

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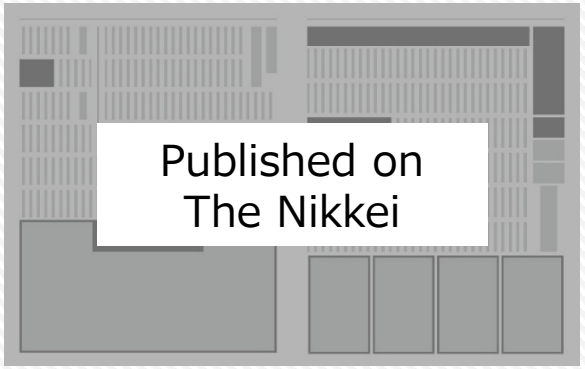
External evaluations and media publications

March 24, 2020	Ranked forth in the “Medium-sized Listed Companies (NEXT 1000) with High Five-year Average Operating Profit Per Employee” in The Nikkei nationwide edition
May 12, 2020	Published on the web media, “ShinR25,” which targets young business people with high motivation for growth, as “The Expert in Overcoming Recessions“
July 3, 2020	327 people participated in the Japan Management Consultants Association’s “Kitanotatsujin Seminar on Five Strategies to Surpass Competitors” (Participation fee: ¥45,000) Became a topic as the “Authority in Online Marketing”



Seminar on Five Strategies to Surpass Competitors

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Launched new products in the first quarter of the fiscal year ending February 28, 2021

"Injectable cosmetics series" No. 4

チークポアパッチ

CHEEK PORE PATCH

Launched in March 2020

[Quasi-drug]
Spots prevention peeling gel for men

PEEL SHOT

Launched in May 2020

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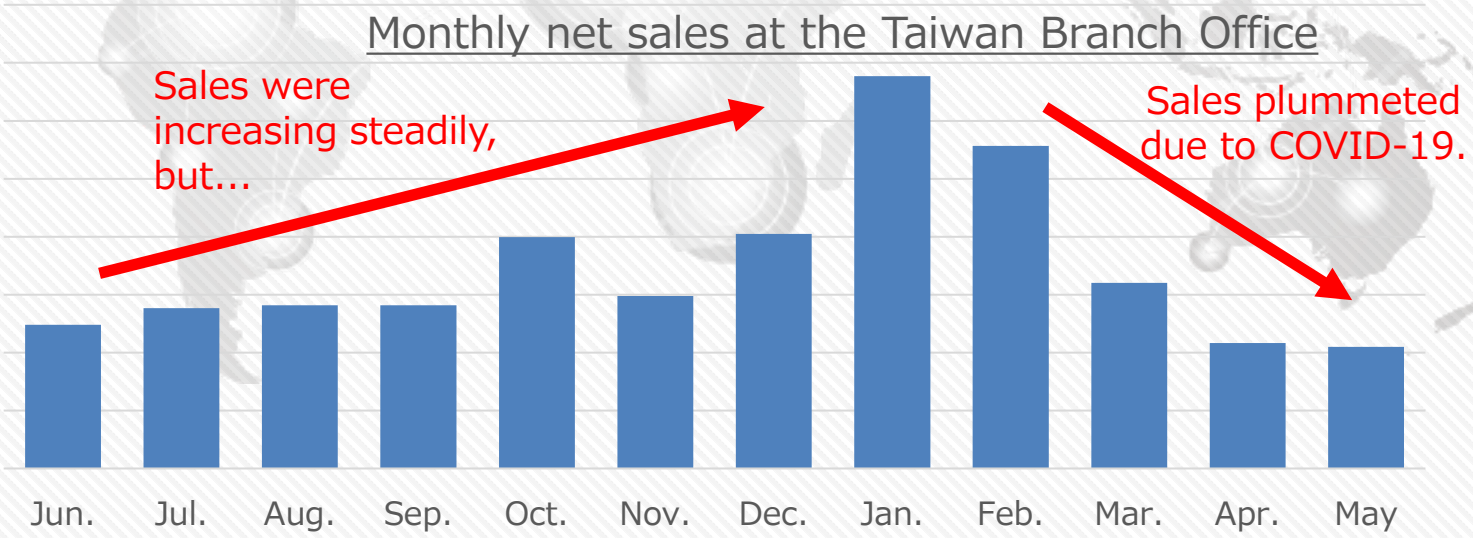
Overseas Business Development

- At the Taiwan Branch Office, which steadily increased sales during the previous fiscal year, sales growth slowed due to the impact of COVID-19.
  However, sales of the Taiwan Branch Office account for only a small portion of total sales and have a minor impact on the Company's overall business performance.

- During the first quarter under review, we have begun developing a system to expand our Taiwan Branch Office, such as hiring several full-time staff from Taiwan and providing training for them. We have also begun preparing for expanding into Asian countries other than Taiwan.



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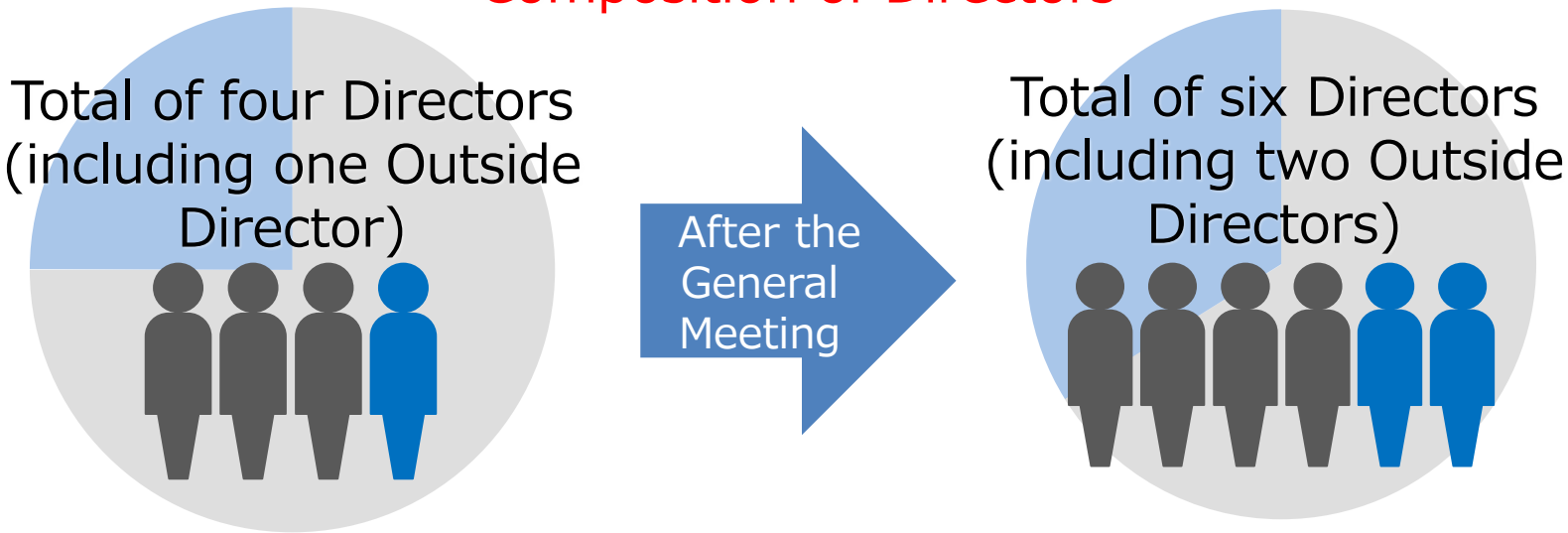
Corporate Governance System

- Mr. Shigeatsu Shimizu, Senior Managing Director, resigned at the conclusion of the Ordinary General Meeting of Shareholders in the previous fiscal year.
- Increased the number of Directors in order to strengthen the management system, and elected three Directors (including one Outside Director) at the said Ordinary General Meeting of Shareholders.

Composition of Directors



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Protection of intellectual property rights

(The Company's initiatives)
Mainly the "Office of Competition and Imitation Countermeasures" respects the intellectual property rights of the Company and other companies and promotes business activities in a fair competitive environment.

■ Topic: Settlement of a case seeking an order of provisional disposition

SNS adver-tising

(Background)
hugkumi+ inc., whose product "hugkumi Oligo" is a competitor of the Company's product "KAITEKI OLIGO," was displaying in their SNS advertising that the product could "fight off coronavirus by improving immunity from within your body."

北の達人コーポレーション Meister in the North

(Petition)
Misrepresentation of product quality and infringement of business interests
→ Petition filed at the Tokyo District Court

Tokyo District Court

(Result)
The court gave a nearly complete approval of the Company's claim, and a settlement was reached in court.
→ hugkumi+ inc. posted an apology on their website and SNS.

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Addressing issues

- Rebuilding the internal organizational structure for medium- and long-term growth -

Strengthening the Creative Department

- Build an education system by highly skilled personnel with abundant experience acquired by strengthening recruitment
- Continue to strengthen recruitment of experienced personnel who can be expected to contribute to business results in a short period of time and are industry-ready.

<Measure>

Representative Director & President, Mr. Kinoshita himself utilizes SNS, offers lectures and seminars to raise awareness of the Company within the industry.

<Progress>

Increase in the number of applications of talented personnel with abundant achievements and management experience, etc.
Confident in future recruitment of experienced personnel

Strengthening the Product Development Department

- Strengthen the recruitment of personnel from major cosmetics manufacturers, etc.
- Expansion of development product categories
- Revision of market research methods used as criteria for product development

→ Continue to strengthen development with “mass-market products, which can generate net sales of ¥5.0 billion to ¥10.0 billion from a single product” in mind

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Balance Sheets

(Millions of yen)

Subject/Section	Fiscal year ended February 29, 2020	Three months ended May 31, 2020	Changes	Changes (%)
(Cash and deposits)	4,088	3,639	-448	-11.0%
Current assets	5,521	5,098	-423	-7.7%
Non-current assets	380	341	-39	-10.4%
Total assets	5,902	5,439	-462	-7.8%
Current liabilities	1,554	1,008	-546	-35.1%
Non-current liabilities	–	–	–	–
Total liabilities	1,554	1,008	-546	-35.1%
Total net assets	4,347	4,430	+83	+1.9%
Total liabilities and net assets	5,902	5,439	-462	-7.8%

The main factors for the changes were a decrease in “Cash and deposits” and a decrease in “Current liabilities“ due to the payment of ¥553 million of income taxes payable.

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Understanding the Current Situation and Future Outlook

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Understanding the Current Situation and Our Future Initiatives

(Understanding the current situation)

The number of new customer acquisitions has recovered to the level before the tax hike, but...

- The calculation method of the CPO limit needs to be returned to the previous one, and ROAS needs to be improved.
- It is currently not clear when the issues concerning the Creative Department and the Product Development Department will be resolved.
- The timing of when COVID-19 will be contained also remains unclear.

→ Therefore, we must conservatively estimate the number of new customer acquisitions going forward.

(Our future initiatives)

- Utilize advertising placements and video advertisements on major media outlets, which we were not able to engage in due to lack of resources
- Continue to focus on strengthening the Creative Department and the Product Development Department

→ Increase the number of new customer acquisitions
The Company has not changed its forecast announced on April 14, 2020.

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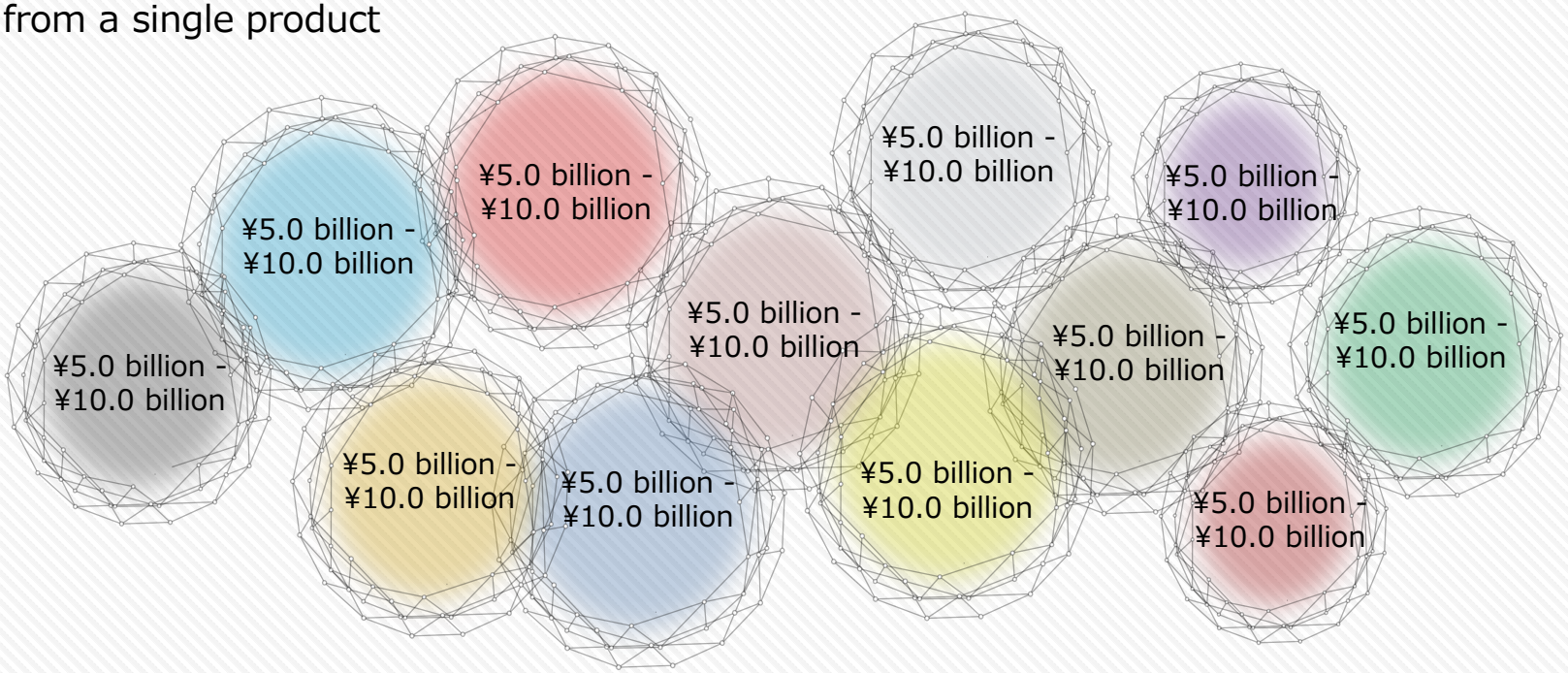
Future Strategies

<Current>

- Achieve net sales of ¥10.0 billion, while maintaining high profitability
- Acquire know-how to create a business of ¥4.0 billion to ¥5.0 billion from a single product

<Future>

Focus on the product development that can deploy multiple businesses of ¥5.0 billion to ¥10.0 billion from a single product in large mass markets



While focusing on sales promotion activities in Japan, we consider overseas expansion other than Taiwan, where business performance has expanded.
By utilizing platforms such as Google, Facebook, Twitter, Amazon, etc., achieve annual sales of ¥100.0 billion by developing businesses of ¥5.0 billion to ¥10.0 billion × Multiple markets.

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References

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History

May 2002:	Founded Hokkaidou.co.jp., Ltd., Osaka with capital stock of ¥10,000,000
September 2002:	To strengthen product development, moved Head Office to 2 Kita-1-jonishi, Chuo-ku, Sapporo, Hokkaido
May 2006:	To cope with expanding business, moved Head Office to 2 Kita-7-jonishi, Kitaku, Sapporo, Hokkaido
July 2007:	Began operation of health and beauty sales consolidation site “Kaiteki Friend Club (now “J North Farm”)“
March 2009:	Changed Trade Name to Kitanotatsujin Corporation
November 2010:	To cope with expanding business, moved Head Office to 1 Kita-7-jonishi, Kitaku, Sapporo, Hokkaido
February 2011:	The Company sold its website for sales of Hokkaido specialties with the aim of shifting to sales of health and beauty products, etc.
May 2012:	Listed on Sapporo Securities Exchange, Ambitious Market
March 2013:	Upgraded to Main Market on Sapporo Securities Exchange
November 2014:	Listed on the Tokyo Stock Exchange, Second Section
November 2015:	Assigned to the Tokyo Stock Exchange, First Section
December 2015:	Opened Taiwan Branch Office
January 2019:	Opened Korea Representative Office
February 2019:	Became a member of the Japan Business Federation (Keidanren)
March 2019:	To cope with expanding business, moved Head Office to 1 Kita-1-jonishi, Chuo-ku, Sapporo, Hokkaido
April 2019:	Opened Tokyo Branch Office in Chuo-ku, Tokyo
July 2019:	Designated as margin trading issues on the Tokyo Stock Exchange, First Section and Sapporo Securities Exchange
February 2020:	Increased the floor space of Tokyo Branch Office

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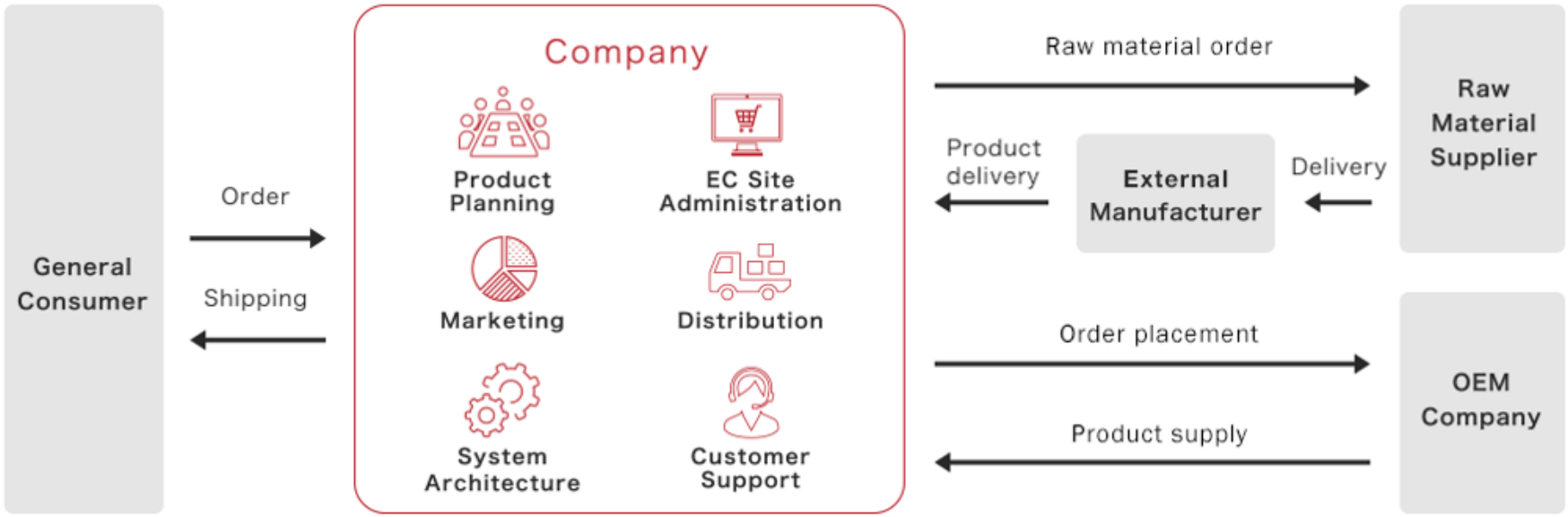
Main Business Structure



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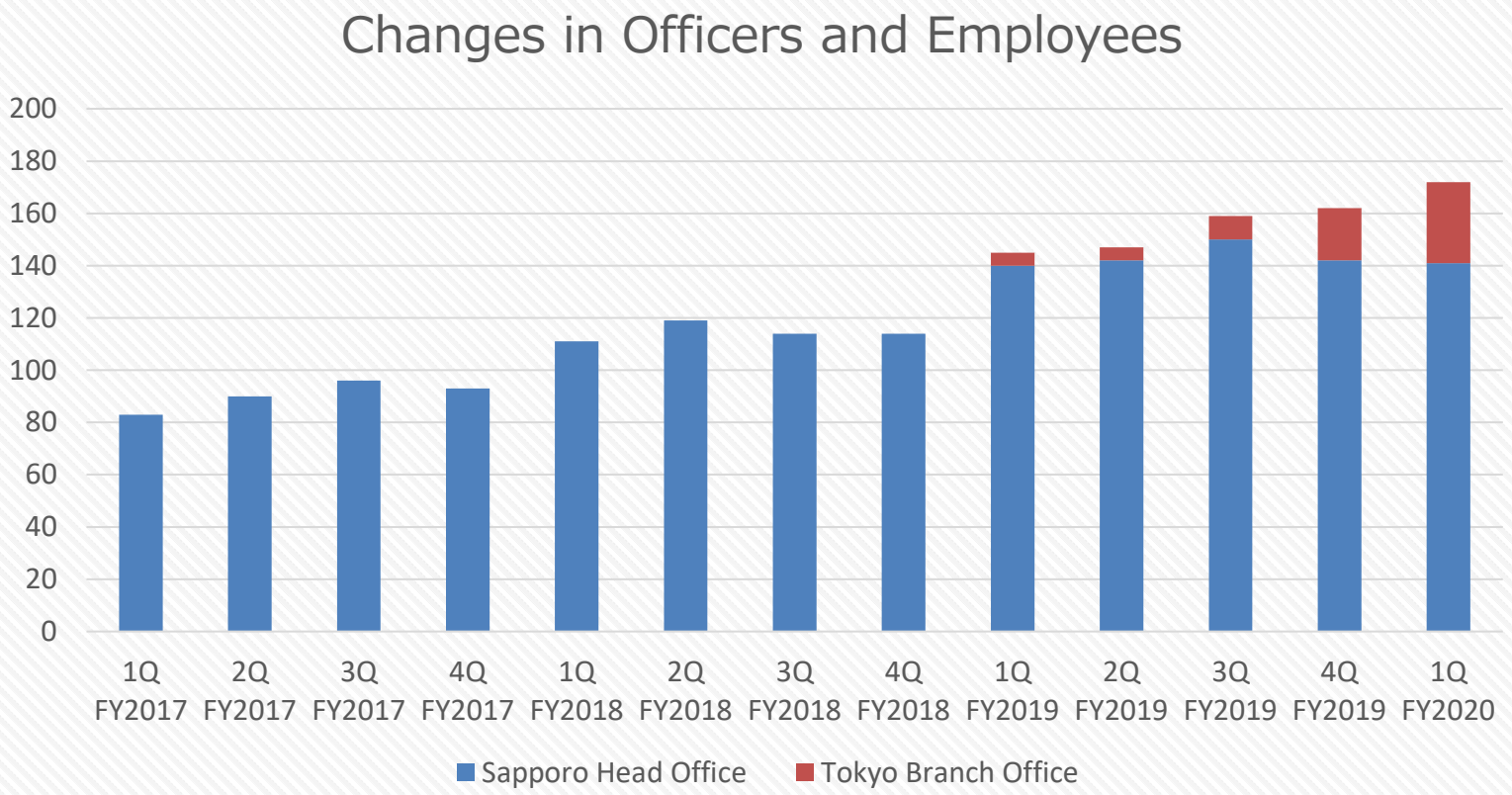
Personnel Changes



* Tokyo Branch Office was established in April 2019 at Nihonbashi, Chuo-ku, Tokyo

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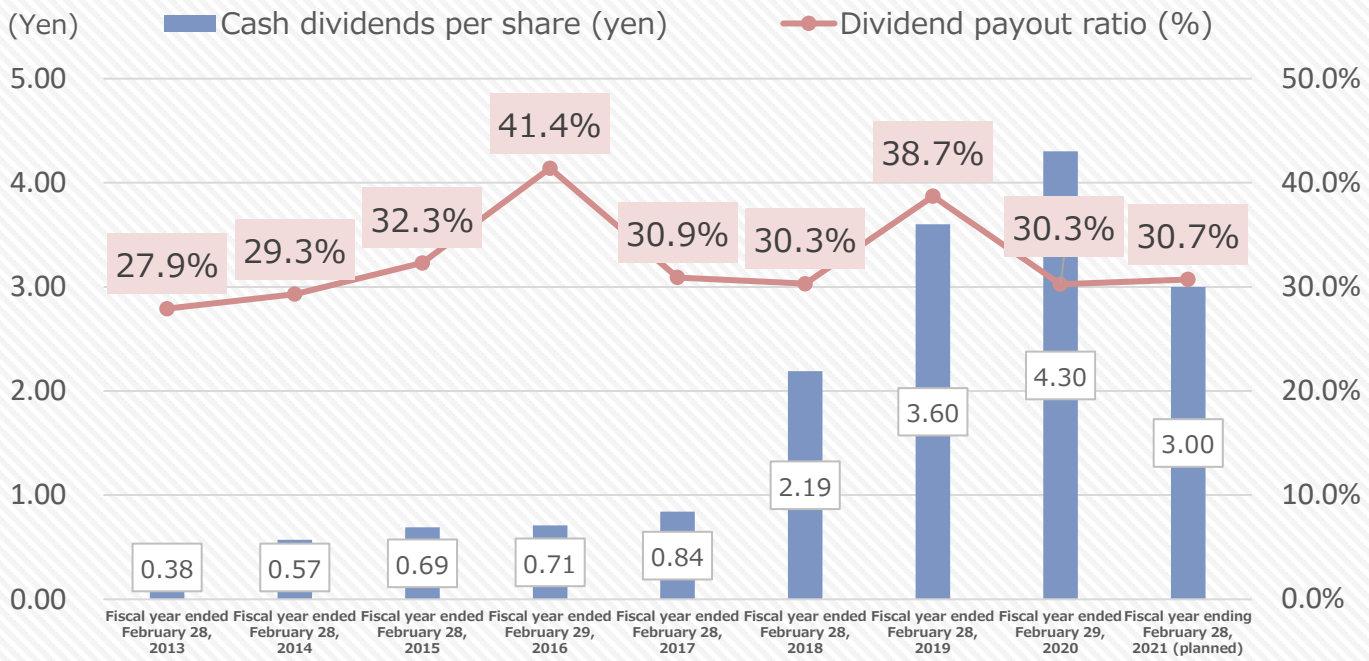
Actual and Projected Dividends

The Company is working to return profits to shareholders by paying dividends of approximately 30% of dividend payout ratio, taking into consideration the strengthening of its business foundation and the enhancement of its internal reserves. The Company expects to pay an interim dividend of ¥1.80, a year-end dividend of ¥1.20, and an annual dividend of ¥3.00 per share for the fiscal year ending February 28, 2021.



(Note) Cash dividends per share are translated based on the impact of the following six stock splits. (Fractions less than one sen are rounded up.)

A 4-for-1 stock split for common shares as of February 9, 2013
A 2-for-1 stock split for common shares as of January 3, 2014
A 2-for-1 stock split for common shares as of June 1, 2015
A 2-for-1 stock split for common shares as of April 1, 2017
A 2-for-1 stock split for common shares as of November 6, 2017
A 3-for-1 stock split for common shares as of February 15, 2018

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Other Indicators

	Fiscal year ended February 29, 2016	Fiscal year ended February 28, 2017	Fiscal year ended February 28, 2018	Fiscal year ended February 28, 2019	Fiscal year ended February 29, 2020
Equity ratio (%)	86.5	67.4	67.3	69.4	73.7
Dividend payout ratio (%)	41.4	30.9	30.3	38.7	30.3
Cash dividends per share (yen)	0.71	0.84	2.19	3.60	4.30
Number of shareholders	8,128	8,926	31,667	47,978	54,307

(Note) Cash dividends per share are translated based on the impact of the following stock splits:
(Fractions less than one sen are rounded up.)
A 2-for-1 stock split for common shares as of June 1, 2015
A 2-for-1 stock split for common shares as of April 1, 2017
A 2-for-1 stock split for common shares as of November 6, 2017
A 3-for-1 stock split for common shares as of February 15, 2018

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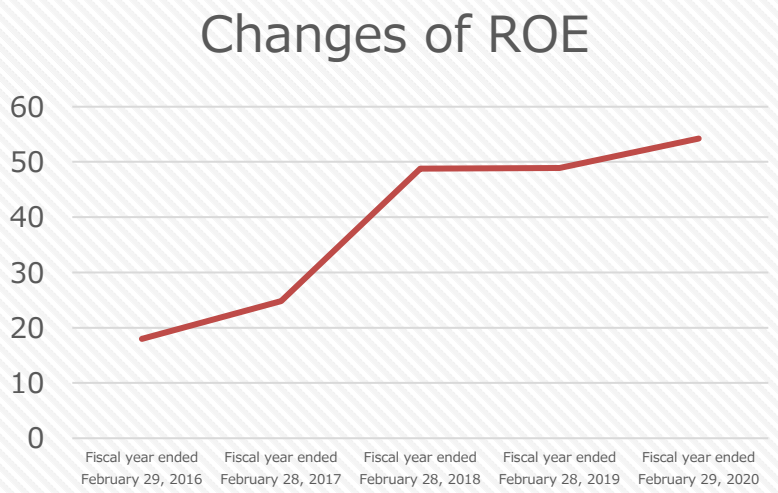
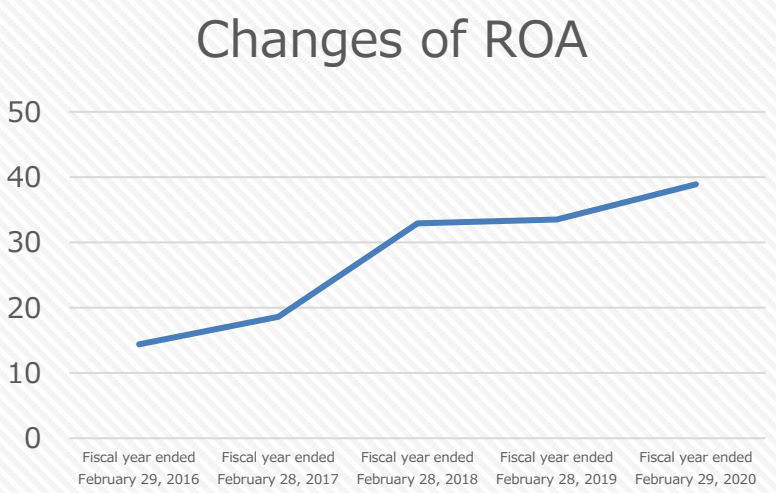
Changes of ROE and ROA

	Fiscal year ended February 29, 2016	Fiscal year ended February 28, 2017	Fiscal year ended February 28, 2018	Fiscal year ended February 28, 2019	Fiscal year ended February 29, 2020
ROE (return on equity)	18.0%	24.8%	48.8%	48.9%	54.2%
ROA (return on assets)	14.4%	18.6%	32.9%	33.5%	38.9%





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Major Awards Received

September 2019: Awarded the Internet Shopping Award in the “Asia Direct Marketing Vision 2019”

November 2018: Awarded the “Asia’s 200 Best Under A Billion” for the second time in the Asian edition of the U.S. economic magazine Forbes

February 2017: Special E-Commerce Promotion Award Recipient at “Japan Venture Awards 2017” hosted by the Organization for Small & Medium Enterprises and Regional Innovation, JAPAN (backed by The Small and Medium Enterprise Agency, Ministry of Economy, Trade and Industry, etc.)

September 2015: Japanese Representative Candidates Finalist for EY Entrepreneur of the Year 2015, an international award program for entrepreneurs

February 2014: Awarded the IT Management Award of the Minister of Economy, Trade and Industry Award

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Medium-term Management Plan

In the Internet industry in which the Company operates, the business environment is rapidly changing, and it is necessary to make swift and flexible management decisions in accordance with the business environment. Accordingly, the Company does not disclose its medium-term management plan.

The Company carries out the analysis of causes of divergence between the plans for a single fiscal year and its results on a regular basis, and discloses and explains the analysis results to stakeholders, including shareholders, through announcements of financial results, etc.

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