

# COMPANY RESEARCH AND ANALYSIS REPORT

## AXXZIA Inc.

4936

Tokyo Stock Exchange Growth Market

18-Nov.-2022

FISCO Ltd. Analyst

**Hideo Kakuta**



FISCO Ltd.

<https://www.fisco.co.jp>

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## Summary

### **FY07/22 sales and profit were both record highs. Focusing on the development of the third main brand and Chinese EC platform diversification**

AXXZIA Inc. <4936> (hereafter, also “the Company”) is a cosmetics company with high growth potential that plans and manufactures made-in-Japan cosmetics and supplements in the high and medium price ranges, and sells them through e-commerce (hereafter, EC), mainly on the Chinese market. The Company name AXXZIA includes “XX” (the female chromosome) as a symbol of beauty, and presents “Asian Beauty” (ASIA→AZIA) from Japan to the world. Its main brands are AXXZIA and AGtheory, and the Company has succeeded in making hero products (hit products) of both Essence Sheet, an eye-care product, and AG Drink, a beauty supplement. In 2020, the Company won Rising Enterprise Award 2020 from Tmall (the Alibaba Group), China’s largest EC platform. In February 2021, in the 10th year since its foundation, the Company was listed on the Tokyo Stock Exchange (TSE) Mothers market, and then in April 2022 following the TSE’s reorganization of market categories, its listing was transferred to the Growth market. In April 2022, it made Huit laboratories, Inc. a consolidated subsidiary.

#### 1. Summary of FY07/22 results

In the FY07/22 consolidated results, net sales increased 42.0% year on year (YoY) to ¥8,215mn and operating income increased 18.1% YoY to ¥1,633mn, marking record high results. Also, net sales were 15.4% higher than the initial forecast, while operating income exceeded the initial forecast by 11.4%. In the priority market of Chinese EC (including cross-border EC), net sales rose 48.7% YoY to ¥6,088mn, a strong result that drove overall earnings. Despite the headwinds of the Shanghai Lockdown and tightened Chinese government restrictions, net sales increased due to up-front investments in advertising expenses as planned. In terms of the breakdown in the Chinese EC business, in addition to growth in the main channel of Tmall Global, contributions were made on top of that by sales on Douyin (the mainland China version of TikTok) which the Company opened a flagship store on in FY07/22. In terms of profits, SG&A expense ratio increased more than forecast as a result of implementing up-front investments as initially planned. However, the decline in the cost ratio and other factors caused profit to increase more than forecast, and the Company maintained a strong profit margin.

#### 2. FY07/23 results outlook

For the FY07/23 consolidated results, the Company is forecasting net sales of ¥10,351mn (up 26.0% YoY) and operating income of ¥1,818mn (up 11.3%), as it expects net sales to exceed ¥10bn due to the continuation of high growth. The Company aims for consistent expansion due to sales growth based on the growth of the high-performing Chinese EC business along with up-front investments (factories, R&D) targeting medium- to long-term business growth. Although SG&A expenses will increase, the Company is forecasting higher profit due to the increase in sales. While the Company is forecasting that the operating margin will decline 2.3 percentage points, this is largely due to the impact of the results of Huit Laboratories, Inc. In China, the Company’s priority market, there are some challenges from the macro perspective, including a dulling of economic growth and tightened restrictions due to China’s zero-COVID policy and other factors. On the other hand, however, from a micro perspective, the cosmetics products EC market, the Company’s targeted market, is growing markedly along with the diversification of EC platforms. Also, regarding regulations, the Company has thoroughly responded to cosmetic product registration (NMPA\*) and the like, and this is a relative strength of the Company. Based on the above factors, we at FISCO think there is a strong likelihood that the Company will achieve its net sales and operating income forecasts for FY07/23.

| \* Acronym for the National Medical Products Administration of China. It is the equivalent of a PMA from the FDA in the U.S. |

## Summary

### 3. Growth strategy

The Company has put in place basic strategic policies for FY07/23 in line with its medium- to long-term forecasts. In its brand strategies, the Company will strengthen development of its two main brands AXXZIA and AGtheory, as well as develop brands and turn them into hero products in the skin whitening market, a large market in which the Company is aiming to differentiate itself by fulfilling niche needs. In marketing strategies, the Company will deepen and diversify its Chinese EC channels and step up expansion into new regions, including within Japan. In particular, the Company will focus on Chinese EC platform development, after Douyin and Kuaishou which it opened flagship stores on in FY07/22. As policies for M&A and alliances, in addition to promoting synergies from the acquisition of Huit Laboratories, the Company will utilize its abundance of cash (¥6,389mn in cash and deposits at the end of FY07/22) for aggressive business expansion and revenue base diversification, as it promotes ongoing M&A and alliance efforts. With respect to M&A, the Company is targeting quality cosmetics businesses in order to rapidly accelerate and expand the domestic business.

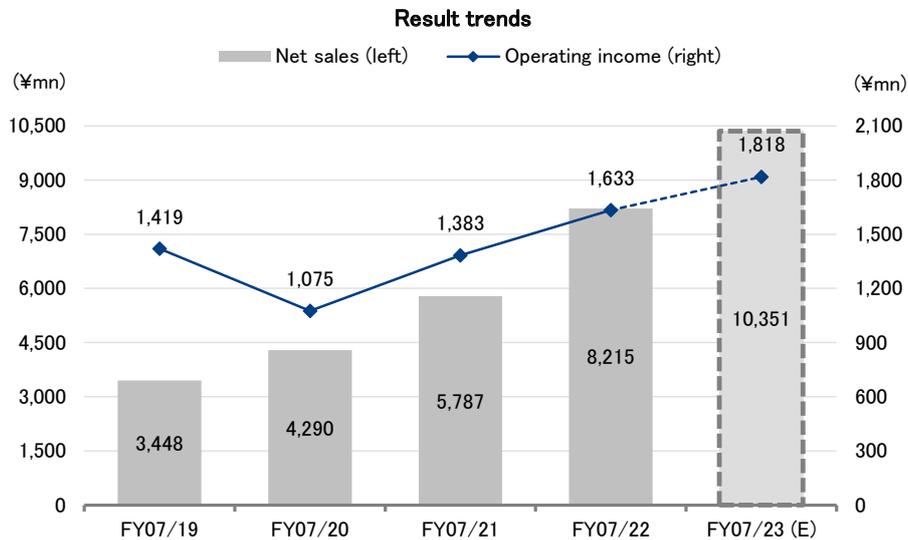
### 4. Shareholder return policy

In the near term the Company plans to prioritize securing internal reserves, but in the future it plans to continually return profits to shareholders while taking results and its financial condition into consideration. Based on the fact that it is rapidly growing in Asia, a market with potential, the investment stance in the near term is focused on capital gains, but over the long term the Company is establishing a foundation anticipating paying dividends, etc. in the future. Specifically, in May 2022 the Company newly established a shareholder benefits program in order to further improve its recognition and increase the number of shareholders. Also, the Company decided to submit a proposal to revise the Articles of Incorporation to allow the distribution of surplus in the form of dividends, etc. by a resolution of the Board of Directors to the General Shareholders' Meeting scheduled for October 2022. At FISCO, we expect the Company to realistically start paying a dividend around the time that it achieves a change in designation to the Prime market.

### Key Points

- Both sales and profits were record highs in FY07/22. Succeeded in growing sales in the core Chinese EC business due to aggressive upfront investment
- Forecasting net sales above ¥10bn in FY07/23 by maintaining high growth. Also carrying out upfront investment targeting medium- to long-term growth
- Focused on developing a third core brand and diversifying Chinese EC platforms
- Prioritizing internal reserves in the near term, but will establish a foundation for a flexible shareholder return policy

Summary



Source: Prepared by FISCO from the Company's financial results

## Company profile

### A high-growth company that sells cosmetics and supplement products made in Japan in the high and medium price ranges via EC in China

The Company is a cosmetics company with high growth potential that plans and manufactures made-in-Japan cosmetics and supplements in the high and medium price ranges and sells them through EC, mainly on the Chinese market. The Company name AXXZIA includes “XX” (the female chromosome) as a symbol of beauty, and presents “Asian Beauty” (ASIA→AZIA) from Japan to the world.. It is aiming to be a comprehensive beauty solution company that creates beauty and that can provide proposals tailored to customers’ wishes and realities.

Company profile

Since its foundation, the Company has been led by President and Representative Director Dan Taku. After graduating from China’s prestigious Xiamen University, he completed a post-graduate degree at the University of the Ryukyus. Then, after working as a systems engineer in a listed company, he launched a business in 2003. Subsequently, he accumulated experience including in beauty salon management and imports and exports of beauty devices, and in 2011, he established Orientina Cosme Co., Ltd. for the development and manufacture of cosmetics for beauty facilities (hereafter, salons), and then in 2012, the company name was changed to AXXZIA Inc. A turning point occurred in 2016. The sales launches of the AG Drink beauty supplement and the Essence Sheet eye-care product for BtoC coincided with the growth of China’s EC market and the Company succeeded in making them hero products. Subsequently, it skillfully conducted brand management, centered on the hero products, and grew to be a company with a lineup of 7 brands and more than 90 items. Also, in 2020 the Company won Rising Enterprise Award 2020 from Tmall, which is China’s largest EC platform. In February 2021 in the 10th year since its foundation, it was listed on the Tokyo Stock Exchange (TSE) Mothers market, and then in April 2022 following the TSE’s reorganization of market categories, its listing was transferred to the Growth market. In April of the same year, it acquired 100% of the shares and made a consolidated subsidiary of Huit laboratories. At the end of July 2021, the Group had a total of 115 employees, of whom, 73 employees (63.5%) were women. The ratio of women in managerial positions is 48.8% and the ratio of employees who are foreigners is 46.1%, and the Company has vitality through implementing diversity.

History

Date	Event
December 2011	Established Orientina Cosme Co., Ltd.
November 2012	Changed company name from Orientina Cosme Co., Ltd. to AXXZIA Inc.
September 2013	Launched Le Cier de L’aube, a skincare brand for beauty salons
May 2016	Launched AXXZIA Beauty Eyes, an eye care and skincare brand for the retail market
August 2016	Launched Venus Recipe, a supplement brand for retail the market
October 2016	Launched AXXZIA Beauty Eyes Essence Sheet, a skincare brand for the retail market
December 2016	Awarded 2016 Best of Venture Award by Beauty and Healthcare News Inc.
June 2017	Opened online shopping site
December 2017	Selected as and Awarded 2017 Growth Company Brand by Beauty and Healthcare News Inc.
April 2018	Established Xiaozhi Cosmetic (Shanghai) Inc. as a consolidated subsidiary
February 2019	Opened flagship store on Xiaohongshu (RED), one of China’s largest EC platforms
April 2019	Opened flagship store on Tmall Global, another of China’s largest EC platforms
February 2021	Listed on the Mothers market of the Tokyo Stock Exchange
May 2021	Opened flagship store on major Chinese mobile video app Douyin
April 2022	Made Huit Laboratories, Inc. a consolidated subsidiary
April 2022	Changed market designation to the Growth market of the Tokyo Stock Exchange
April 2022	Opened flagship store on major Chinese mobile video app Kuaishou

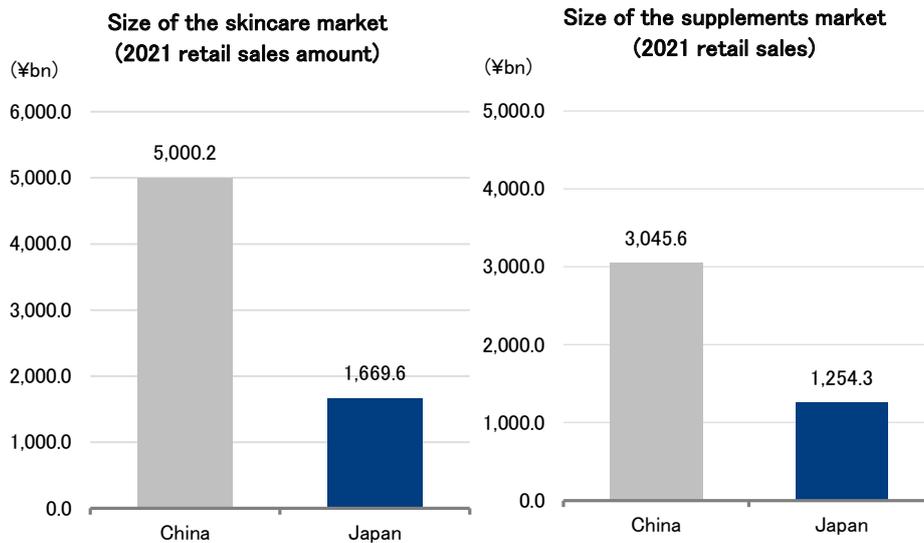
Source: Prepared by FISCO from the Company’s annual securities report, website, and news releases

## Market summary

### China’s cosmetics and supplements market is more than double the size of the market in Japan, and the growth potential is much higher

#### 1. Market size and growth potential (comparison of Japan and China)

The scale of the skincare market, which constitutes a large part of China’s cosmetics market that the Company targets, is growing greatly against the backdrop of the improved income level in China due to economic growth and the increase in its cosmetics-buying population. According to the Company, the scale of China’s skincare market was ¥5,000.2bn in 2021 (approximately 3.0x the size of the market in Japan), and the forecast five-year average growth rate through 2026 is 7.3%. On the other hand, the size of Japan’s skincare market is forecast to remain flat based on the fact that it has already matured. Likewise, the size of the supplements market was ¥3,045.6bn in 2021 (about 2.4x the size of the market in Japan), and the forecast five-year average growth rate through 2026 is 5.9%, while the Japanese market is forecast to move sideways. The environment is similar in the EC channel, which the Company focuses on. In China’s BtoC sales, the ratio of EC sales was 44.0% in 2020, and the shift to EC is expected to progress going forward. However, in Japan, the ratio of EC sales in 2021 was a low 8.8%.



Note: Used a 2021 average exchange rate of ¥1 = 0.059 yuan  
 Source: Prepared by FISCO from the Company’s results briefing materials

## 2. Competitive environment

In China's cosmetics market, the Company's products are known as made-in-Japan brands from a Japanese cosmetics company. The foundation of this category, which constitutes approximately one quarter of China's cosmetics market, was built over many years by companies such as Shiseido <4911>, Kosé <4922>, and FANCL<4921>, and in particular the functionality of Japanese products is highly evaluated in the skincare field and other fields. The Company competes with groups ranked 4th and lower, such as POLA ORBIS HOLDINGS <4927>. In the Chinese market, brands from Japanese and Western companies tend to be in the medium and high price ranges, brands from South Korean companies in the medium price range, and brands from Chinese companies in the low price range, and their respective positioning is different. Among them, in the medium and high price range categories, there are many companies that rely on retailers, particularly department stores, but the Company is developing its business centered on EC, thereby differentiating itself.

# Business description

**The Chinese EC business makes up more than 70% of sales. The Company possesses its own strengths in product development, manufacturing and sales to win in the Chinese market**

## 1. Main brands and products

### (1) AXXZIA

AXXZIA is one of the main brands for retailers, mainly of eye products, and the Company has succeeded in making Essence Sheet a hero product. It is a beauty serum that blends multiple beauty ingredients needed for the eyes, and is attached to the skin close to the eyes to provide the area with intensive care. As a result of becoming a hero product in the Chinese market, Essence Sheet's FY07/22 cumulative net sales were ¥3,407mn (41.5% of Company-wide net sales).

### (2) AGtheory

AGtheory, which is the second major brand for retailers, blends cosmetics with AG Drink as the core ingredient, and the Company succeeded in making it a hero product. It then created the AGtheory cosmetics brand series by combining the AG Drink (hero product) with cosmetics based on the same concept to target the existing loyal users of AG Drink. Incidentally, the features of AG Drink, which pursues "anti-saccharification" and has become a hero product, include that it stably ships 10,000 units a month and has a high ARPU (average revenue per user), and its FY07/22 net sales were ¥2,750mn (33.5% of Company-wide net sales). The percentage of net sales provided by the total sales of the 2 brands of AXXZIA and AGtheory (including AG Drink) was 74.9% (FY07/22).

### (3) Skin whitening-appeal field

In the skin whitening appeal field, the Company has positioned the cosmetics product sunscreen, the beauty supplement White Aminos, and its revamped product, Venus Recipe The White Drink, as up-and coming products, as it aims to establish a third core brand. These products are sold as BtoC brands in the mid- to high-price range (average sales price above ¥5,000) in both the Chinese market and the Japanese market. Net sales in FY07/22 were ¥983mn (12.0% of the Company's total sales), which represented a marked growth of 51.0% YoY. In particular, The White Drink, launched in February 2022, totaled ¥400mn in sales, as performance was strong, and it is on the way towards becoming a hero product.

Business description

**(4) Others**

Huit Laboratories' skincare base cosmetics product "LisBlanc" is sold as a BtoC brand in the mid- to high-price range (average sales price of ¥3,000).

**(5) Professional field**

"Le Ciel de L'aube," "Aither" and "THE B" are brands sold exclusively to salons (professional field). The brands sold exclusively to salons have been one of the Company's strengths and specialist fields since its foundation, and it sells them in the high price range (average unit price, ¥10,000 and higher).

The main product lineup

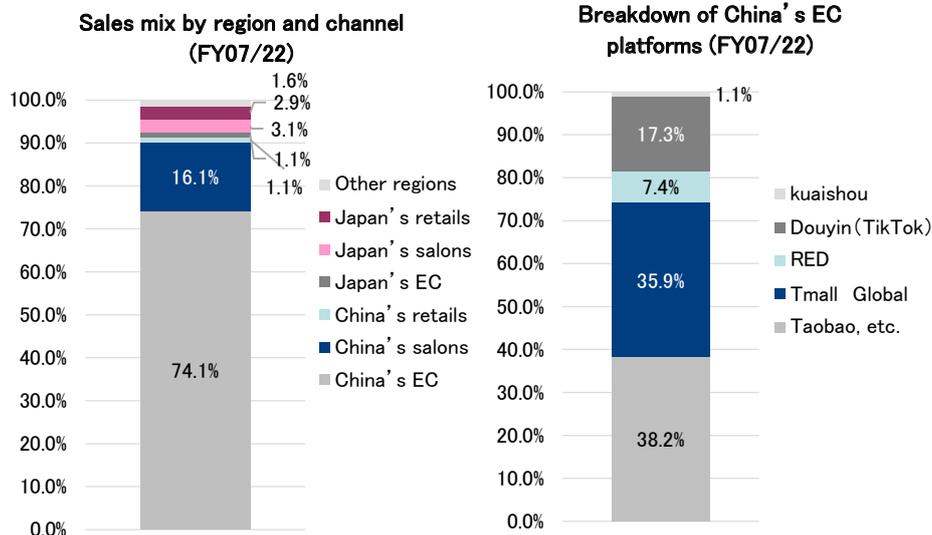


Source: The Company's financial results briefing materials

**2. Percentages of sales by region and channel**

The driving force behind the Company's growth is the success of the Chinese market, and in particular, the growth of EC in China. This is clear from the percentages of sales by region and by channel in the FY07/22 results, in which Chinese EC provided 74.1% (¥6,088mn). Breaking down Chinese EC, there are sales of the flagship store on Taobao, which is China's largest marketplace-type (CtoC) EC platform operated by the Alibaba Group (percentage of FY07/22 China EC sales = 38.2%) and sales of the flagship store on Tmall Global, which is a BtoC cross-border EC specialty mall operated by the Alibaba Group (35.9%), and both comprise a high ratio of sales. RED includes review and comments, the majority of which are by active female users (it is China's version of Instagram) and influencer marketing sales are active on it (7.4%). In addition to these, the video platform Douyin, the Chinese main store of TikTok and the mobile app, Kuaishou, on which the Company opened flagship stores in FY07/22, are growing remarkably. And attracting considerable attention from powerful sales channels (such as live commerce and interest EC). Of them, Douyin provides 17.3% of total net sales and its presence is increasing as the No.3 platform.

Business description



Source: Prepared by FISCO from the Company's financial results briefing materials

Summary of China's EC platforms on which the Company has opened stores

EC Platform	Features	No. of active users	The Company's net sales (¥mn)	% of net sales	YoY
Taobao, etc.	China's largest marketplace-type (C-to-C) platform operated by the Alibaba Group. Individuals can join as sellers and there are many products at reasonable prices.	740mn people	2,327	38.2%	7.8%
Tmall Global	A BtoC cross-border EC specialist mall operated by the Alibaba Group. Can purchase overseas products while being within China. Japanese products are very popular. It is limited to sales from companies to individuals and transactions are highly reliable.	(Can approach approximately 300 million members of the middle class)	2,185	35.9%	53.4%
RED (The majority of who are women)	Attracted attention as an app on which users can post photographs and comments (China's Instagram). Subsequently added EC functions similar to Amazon. Products are actively sold on it that utilize influencers, mainly skincare, makeup, fashion, and child-raising products.	85mn people	452	7.4%	0.2%
Douyin (TikTok)	An SNS specializing in video operated by ByteDance to which EC functions have been added by Douyin Dianshang. It uses video and live distribution to stimulate the consumers' potential desires for purchases and proposes products that they may want to buy (interest EC), and sales are growing.	Approximately 400mn people	1,054	17.3%	1,627.9%
Kuaishou	A short video app for mobile devices operated by Beijing Kuaishou Technology Co., Ltd. It was the leading short video app prior to Douyin becoming popular. It has a live commerce function, and sales are growing.	Approximately 320mn people	70	1.1%	-
<b>China's EC total</b>			<b>6,088</b>	<b>100.0%</b>	<b>48.7%</b>

Note: The Company's net sales are the FY07/22 results. Kuaishou had no results in the previous year  
 Source: Prepared by FISCO from the Company's financial results briefing materials and various materials

Among the percentages of net sales by region and by channel, the next highest is sales for salons in China at 16.1% (¥1,318mn). In FY07/22, these sales were impacted by the Shanghai lockdown, but there are more than 600 beauty salon customers and sales are steadily growing. The total of EC, sales in China to beauty salons, and retail have risen to 91.3% of total sales. On the other hand, the Japanese market has been impacted by the COVID-19 pandemic, and in particular retail sales have declined. However, the percentage of sales is on a rising trend at 7.1% (¥585mn) due to the consolidated of Huit Laboratories. Other than these, although it has a track record of sales in countries such as Canada, Germany, and Australia, it is currently refraining from active business development due to factors including travel restrictions due to COVID-19.

We encourage readers to review our complete legal statement on "Disclaimer" page.

## Business description

### 3. Business model

The Company's business model is optimized for the Chinese market. It is a process divided into four stages: (1) product development, (2) manufacturing, (3) sales, and (4) after-sales support, and each stage of the process has its own features.

#### (1) Product development

The Company can grasp consumer needs in a timely manner, such as through its strategic collaboration with Tmall and through test marketing with Taobao and others (via KOL [key opinion leaders] and local salons). From among these needs, the Company plans concepts for up to 200 items a year and mass produces around 20 items while repeatedly creating prototypes and conducting quality checks. In the EC channel, evaluations in the market can be confirmed quickly and it can also quickly make changes to or discontinue products. This kind of high-paced release cycle can be said to be a factor behind the Company being able to continuously create and develop hero products. One example of this is with AG Drink, one of the Company's core products. The Company has updated AG Drink five times since launching it in 2016, which shows the speed of the Company's cycle of reflecting customers' opinions in products. Also, another of the Company's strengths is that it performs in-house all of the functions necessary for cosmetics development, such as formulation development, container development, license confirmation and pharmaceutical affairs. In addition, with the move to make Huit Laboratories a subsidiary, the Company is planning to strengthen its R&D\*.

| \* Acronym for Research & Development. |

#### (2) Manufacture

The Company prioritizes made-in-Japan brands that are highly supported in China, outsources manufacturing to Japanese companies, and thoroughly applies quality-control standards at the same high level as production at its own plants. On the other hand, by making Huit laboratories a subsidiary, it has moved in-house one part of the manufacturing, and as a result it has acquired manufacturing expertise and it is also expected to reduce costs.

#### (3) Sales

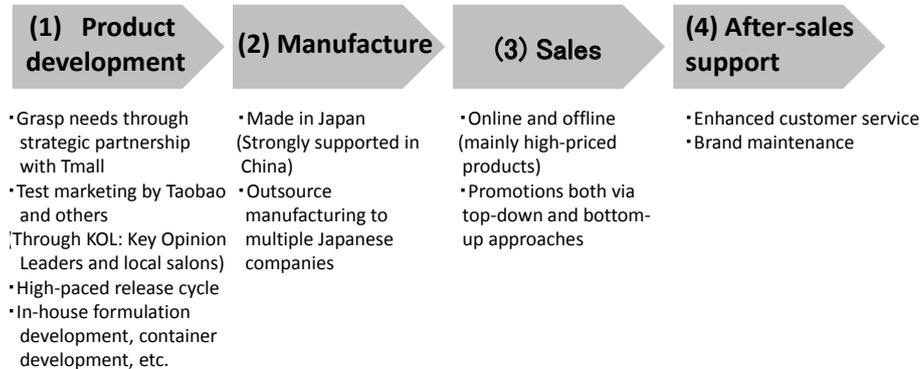
The Company is progressing in parallel online and offline (mainly high-priced items for salons) sales, which contributes to maintaining the brands. For sales channels and sales promotions, it is accumulating expertise in promotions for both the top-down type, centered on Tmall, and the bottom-up type, which mainly utilizes Taobao and RED.

#### (4) After-sales support

The Company's enhanced customer services have been highly evaluated for each channel. The Chinese market requires that measures be conducted against counterfeit products, diversion and unreasonably low-priced products, but in terms of the Company's initiatives to maintain its brands, it attaches a QR-code security label to all products and numbers them so that buyers can confirm that the product is genuine through numbering, and it has in place a system in which it can respond immediately to a problem at the time of distribution.

Business description

Business model for the China business



Source: Prepared by FISCO from interview

**4. Company's strengths**

The Company's strengths include that it targets the Chinese market as its main target, based on a feature of China where even medium- and high-price-range products can be sold via EC, and that based on these characteristics of China, it utilizes all of the channels in an integrated manner for sales-promotion support and sales. As the Company specializes in China, it can be said to have built competitive advantages over other Japanese companies.

The Company is utilizing its strengths in relation to China's unique approval system. The Chinese market has its own unique approval system, including requiring approval from NMPA, and as a result, it can be said that the barriers to enter the Chinese market are high. In response to this, the Company designs products that prioritize ingredients and formulations that the NMPA will approve. As a result, among its products developed for China, 82% have been registered by the NMPA (as of the end of April 2022), and the approval rate in the last 2 years has been 100% (generally, it is 20% to 30%) and its average application period is 3 months (generally, it is 6 months), and it is able to smoothly acquire approvals. Products not approved by the NMPA can still be sold on the Chinese market, but restrictions are placed on advertising for them, so EC stores find it difficult to handle these products.

In addition, with respect to marketing in the Chinese EC market, the Company has succeeded in increasing sales by controlling advertising expenses through the synergies of two-way marketing, using multiple major platforms belonging to the categories of top-down marketing and bottom-up marketing, respectively. In top-down marketing, the Company mainly uses Tmall for posting advertisements featuring actresses and other famous people, aiming to foster its brands and expand its name recognition. The Company's efforts have been positively evaluated by Tmall, and the two sides concluded a strategic alliance in 2020. As a result, the Company is now able to grasp needs and implement sales promotion initiatives using Tmall's big data.

Business description

Examples of marketing in China's EC market



Source: The Company's materials

Meanwhile, in bottom-up marketing, the Company has built a network of influencers and KOL on word-of-mouth sites and CtoC sites such as Taobao and RED. On Taobao, the Company has a network of more than 600 influencers/KOL, as well as a network of stores, and each person/store has anywhere from several tens of thousands to a million end users. It can be said that focusing on and nurturing the value of influencers and KOLs from an early stage has led to the Company's current brand recognition. Furthermore, in FY07/22, the Company opened flagship stores on Douyin, JD.com, and Kuaishou, and started developing new platforms. In particular, Douyin and Kuaishou are increasing their presence as sales channels, mainly among young people, and in addition to word-of-mouth and increased brand awareness, sales through the live streaming function can be expected. Chinese EC platforms have been developed mainly by the Alibaba Group, but recently they have been diversifying. The Company's ability to respond agilely to the changes in channels is another one of its strengths.

## Results trends

**In FY07/22 sales and profit both reached new record highs. Aggressive up-front investment drove successful growth in sales in Chinese EC, the Company's core market**

### 1. Summary of FY07/22 results

In FY07/22 consolidated results, net sales were ¥8,215mn (up 42.0% YoY), operating income was ¥1,633mn (up 18.1%), ordinary income was ¥1,746mn (up 27.4%), and profit attributable to owners of parent was ¥1,116mn (up 28.6%), as results were record highs. Net sales were 15.4% higher than the initial forecast, while operating income, ordinary income, and profit attributable to owners of parent ended up exceeding the Company's initial forecasts by 11.4%, 22.7%, and 20.1%, respectively.

## Results trends

**FY07/22 consolidated results**

(Unit: ¥mn)

	FY07/21		Initial forecast	FY07/22		Change		Beginning of year Ratio to forecast
	Results	Ratio to net sales		Results	Ratio to net sales	Amount	Ratio	
Net sales	5,787	100.0%	7,117	8,215	100.0%	2,428	42.0%	15.4%
Gross profit	4,075	70.4%	-	6,221	75.7%	2,145	52.7%	-
SG&A expenses	2,692	46.5%	-	4,587	55.8%	1,895	70.4%	-
Operating income	1,383	23.9%	1,466	1,633	19.9%	250	18.1%	11.4%
Ordinary income	1,370	23.7%	1,424	1,746	21.3%	376	27.4%	22.7%
Profit attributable to owners of parent	868	15.0%	930	1,116	13.6%	248	28.6%	20.1%

Source: Prepared by FISCO from the Company's financial results

Net sales in the priority Chinese EC market (including cross-border EC) were strong at ¥6,088mn, a 48.7% YoY increase, which drove overall net sales. Despite the headwinds from the Shanghai Lockdown and tightened Chinese government restrictions, net sales increased due to up-front spending on advertising as planned. In terms of the breakdown in the China EC business, in addition to 53.4% YoY growth in the main channel of Tmall Global to ¥2,185mn, an additional contribution of ¥1,054mn in net sales was made on top of that by Douyin, the mainland China version of TikTok, which the Company opened a flagship store on in FY07/22. Moreover, at all of the Big 3 EC events\*1 (W11, 3.8, and 618) in China the Company recorded record high performance (GMV\*2). Meanwhile, in Japan, net sales increased 52.7% YoY to ¥585mn due to the success from shifting to an EC strategy as well as the contribution to results from Huit Laboratories. By brand, the core AXXZIA brand saw net sales increase 38.9% YoY to ¥3,739mn, AGtheory saw net sales increase 38.5% YoY to ¥2,906mn, while skin whitening-appeal products (sunscreen, White Aminos and The White Drink) saw net sales increase 51.0% YoY to ¥983mn.

\*1 "W11" is China's largest EC sale to celebrate Singles' Day (November 11), "3.8" is an EC sale of products for women on March 8, International Women's Day, and "618" is an EC sale held around June 18 by Chinese EC site JD.com.

\*2 Acronym for Gross Merchandise Value.

In profits, the Company conducted upfront investments as planned, resulting in SG&A expenses increasing 70.4% YoY to ¥4,587mn. These included advertising expenses of ¥1,578mn (up 99.0% YoY) and payment fees of ¥1,252mn (up 86.9% YoY). Although the SG&A expense ratio increased more than forecast, profit increased more than forecast due to factors including the reduction in the cost ratio, as the Company maintained a high profit margin.

## The scale of assets grew due to the strong earnings. Cash and deposits are an abundant ¥6.3bn, so there are sufficient funds for additional M&A

### 2. Financial condition

Total assets at the end of FY07/22 were ¥10,053mn, an increase of ¥1,786mn YoY. Of these, current assets increased ¥1,105mn to ¥8,795mn due to an increase in cash and deposits (¥454mn) and an increase in products (¥424mn), while non-current assets increased ¥680mn to ¥1,257mn due to factors including an increase in property, plant and equipment (¥407mn). There was M&A activity during the fiscal year, but cash and deposits increased to ¥6,389mn due to strong earnings.

Results trends

Total liabilities increased ¥583mn to ¥1,657mn. Of these, current liabilities increased ¥285mn to ¥1,243mn as a result of a ¥79mn increase in short-term borrowings and a ¥83mn increase in the current portion of long-term borrowings, among other factors. Non-current liabilities increased ¥297mn to ¥414mn, due to factors including the ¥256mn increase in long-term borrowings. Although interest-bearing liabilities increased, the amount of ¥654mn is much less than the amount of cash and deposits (¥6,389mn). Total net assets increased ¥1,202mn to ¥8,396mn due to factors including the ¥1,100mn increase in retained earnings. The Company can be said to have sufficient funds to further advance M&A activity or alliances.

In terms of management indicators, in FY07/22 the current ratio was 707.4% and the equity ratio was 83.5%, so there was a high level of both short-term and long-term stability. Regarding profitability and efficiency, ROE was 14.3% and ROA was 19.1%, and ROS (return on sales) was 19.9%. These indicators fell slightly YoY but were still at high levels, as the Company has established a business model with a high level of management efficiency.

**Consolidated balance sheet and management indicators**

	(Unit: ¥mn)		
	End of FY07/21	End of FY07/22	Change
<b>Current assets</b>	7,690	8,795	1,105
Cash and deposits	5,935	6,389	454
Products	733	1,157	424
<b>Non-current assets</b>	577	1,257	680
<b>Total assets</b>	8,267	10,053	1,786
<b>Current liabilities</b>	958	1,243	285
Interest-bearing debt	72	235	162
<b>Non-current liabilities</b>	116	414	297
Interest-bearing debt	63	320	256
<b>Total liabilities</b>	1,074	1,657	583
<b>Total net assets</b>	7,193	8,396	1,202
Retained earnings	3,042	4,142	1,100
<b>Total liabilities and net assets</b>	8,267	10,053	1,786
<b>[Stability]</b>			
Current ratio	802.6%	707.4%	-95.2pt
Equity ratio	87.0%	83.5%	-3.5pt
<b>[Profitability/Efficiency]</b>			
ROE	18.4%	14.3%	-4.1pt
ROA	24.6%	19.1%	-5.5pt
ROS	23.9%	19.9%	-4.0pt

Source: Prepared by FISCO from the Company's financial results

## Results trends

## Forecasting net sales above ¥10bn in FY07/23 by maintaining high growth. Also carrying out upfront investment targeting medium- to long-term growth

### 3. Outlook for FY07/23

For the FY07/23 consolidated results, the Company is forecasting net sales of ¥10,351mn (up 26.0% YoY) operating income of ¥1,818mn (up 11.3%), ordinary income of ¥1,797mn (up 2.9%), and profit attributable to owners of parent of ¥1,172mn (up 5.0%). The Company expects net sales to exceed ¥10bn due to the continuation of high growth.

#### FY07/23 consolidated results forecasts

(Unit: ¥mn)

	FY07/22		FY07/23		Change	
	Results	Ratio to net sales	Forecast	Ratio to net sales	Amount	Ratio
Net sales	8,215	100.0%	10,351	100.0%	2,135	26.0%
Operating income	1,633	19.9%	1,818	17.6%	184	11.3%
Ordinary income	1,746	21.3%	1,797	17.4%	50	2.9%
Profit attributable to owners of parent	1,116	13.6%	1,172	11.3%	55	5.0%

Source: Prepared by FISCO from the Company's financial results

Net sales are expected to grow mainly in the Chinese EC business, which is performing well. Specifically, in addition to diversifying by advancing the development on Chinese EC platforms following Douyin and Kuaishou, which it opened flagship stores on in FY07/22, the Company will continue to solidify its brand position through the bottom-up approach (word-of-mouth, SNS, live commerce) which the Company has strength in. In terms of profit, the Company aims for consistent growth in business by implementing upfront investments (factories, R&D) targeting medium- to long-term growth. Although SG&A expenses will increase, the Company is forecasting higher profit due to the increase in sales. While the Company is forecasting that the operating margin will decline 2.3 percentage points, this is largely due to the impact of the results of Huit Laboratories, Inc. (expecting net sales of ¥790mn and operating income of ¥10mn).

In China, the Company's priority market, there are some challenges being observed from a macro perspective, including a dulling of economic growth and a tightening of restrictions due to China's zero-COVID policy and other factors. On the other hand, however, from a micro perspective, the cosmetics products EC market, the Company's targeted market, is growing markedly along with the diversification of EC platforms. Also, regarding regulations, the Company has thoroughly responded to cosmetic product registration (NMPA) and the like, and this is a comparative strength of the Company. Based on the above factors, we at FISCO think there is a strong likelihood that the Company will achieve its net sales and operating income forecasts for FY07/23.

## ■ Growth strategy

### **Focusing on developing the third core brand and diversifying Chinese EC platforms. Utilizing its abundant cash, aims to aggressively expand business and diversify its earnings foundation**

#### **1. Medium- to long-term plan and progress**

In December 2021, the Company announced a medium- to long-term plan. As medium-term goals of the three-year medium-term management plan, the Company established numerical targets for the plan's final fiscal year of FY07/24 of net sales of ¥11,200mn (average annual growth rate = 24.6%), operating profit of ¥2,800mn (26.5%), and operating margin of 25.0%. These are high targets, but the average growth rate in sales over the past four years (FY07/18 to FY07/22) has been 38.1%, so at FISCO we think that these targets are certainly achievable. In FY07/22, the first year of the plan, the sales growth rate was 42.0%, so things are progressing smoothly. Also, aiming to increase recognition and accelerate growth through aggressive investment in advertising, the Company's advertising cost to sales ratio was around 20%. The advertising cost to sales ratio in FY07/22 was 19.2%, resulting from executing investments as planned. The basic strategy is to continue to grow and expand while maintaining brand strength, and to ensure increased profits from higher sales through cost control, and to implement the (1) Brand Strategy (expand mainstay products and nurture products within existing brands); (2) Marketing Strategy (deepen involvement in the Chinese market and diversify sales channels); and (3) Business Alliances/M&A (Strengthen product development capabilities and reinforce the domestic market). For FY07/26, the Company has established targets of net sales of ¥20bn and an operating margin of at least 20%.

#### **2. Strategic basic policies (FY07/23)**

In accordance with the medium- to long-term plan, the Company established strategic basic policies for FY07/23. While continuing the basic policy of implementing the brand strategy and marketing strategy centered on China EC, the Company once again emphasized that it would strengthen R&D as well investment in human resources, and advance M&A/alliances with the aim of further diversifying the business and earnings foundation.

Growth strategy

**Strategic basic policy (FY07/23)**

Basic policy	Key matters	Summary
<b>Brand strategy</b>	Launch brand series and develop hero products	<ul style="list-style-type: none"> <li>• Grow and nurture products for the skin whitening market into hero products</li> </ul>
	Prompt registration of cosmetics and brand protection	<ul style="list-style-type: none"> <li>• Develop products on the premise of registering them with NMPA in China to ensure approval is obtained smoothly</li> <li>• Thorough countermeasures against imitation products</li> </ul>
	Bolster R&D by building new laboratories	<ul style="list-style-type: none"> <li>• Plans to build new laboratories (research facilities) in order to expand function as a manufacturer.</li> </ul>
<b>Marketing strategy</b>	Diversify and deepen Chinese EC channels	<p><b>[Diversify]</b> Develop on Chinese EC platforms following Douyin and Kuaishou which it worked on in FY07/22</p> <p><b>[Deepen]</b> Establish a brand position through a bottom-up approach (word-of-mouth, SNS, live commerce)</p>
	Step up entry into new areas (explore expansion into regions other than China)	<ul style="list-style-type: none"> <li>• Strengthen SNS information dissemination in Japan and develop physical stores (Haneda Airport Garden, major department stores)</li> <li>• Proactively expand into other regions (Australia, Canada, Southeast Asia, etc.)</li> </ul>
<b>M&amp;A/alliance policy</b>	Strengthen and realize synergies for manufacturing/R&D	<ul style="list-style-type: none"> <li>• Leverage Huit Laboratories to strengthen utilization of manufacturing and research facilities, and timely manufacturing and development of group products</li> <li>• Grow revenue by taking on contracted manufacturing from other companies</li> </ul>
	Expand domestic business and secure sales channels	<ul style="list-style-type: none"> <li>• Target quality cosmetics businesses for M&amp;A to bolster and expand domestic business in a timely manner</li> </ul>
	Increase revenue by bolstering sales of quality Japanese products in the Chinese market	<ul style="list-style-type: none"> <li>• Promote alliances with quality domestic manufacturers and provide Chinese expansion/marketing support leveraging AXXZIA's Chinese sales network</li> </ul>

Source: Prepared by FISCO from the Company's financial results briefing materials

**(1) Brand strategy**

In its brand strategies, the Company will strengthen its two main brands of AXXZIA and AGtheory, as well as develop brands and turn them into hero products in the skin whitening market, a large market in which the Company is aiming to differentiate itself by fulfilling a niche need. The Company is steadily growing The White Drink, which was renewed and market launched in February 2022, as a candidate to be the third core product. In order to further increase recognition and promote continued growth, the Company plans to aggressively invest in advertising with an advertising cost to sales ratio of around 20%.

The Company is planning to establish new laboratories (research facilities) to expand its functions as a manufacturer by utilizing the functions of Huit Laboratories, which was made a consolidated subsidiary in the previous fiscal year. At FISCO, we believe that the product development cycle will be faster and more efficient, which will strengthen the brand.

**(2) Marketing strategy**

The Company will step up expansion into other areas (including Japan) while diversifying and deepening Chinese EC channels. The Company also plans to reinforce the business structure and hire aggressively for this purpose. In terms of the diversification of Chinese EC channels, the Company will implement EC platform development in China, continuing on from Douyin and Kuaishou, for which it opened flagship stores on in FY07/22. This will lead to reducing the risk arising from depending too much on a particular channel. In terms of deepening the Chinese EC channels, the Company will continue to establish the brand's position through a bottom-up approach (word of mouth, SNS, and live commerce), as well as analyze customer segments and approach potential customers using big data, along with promoting DtoC.

As a domestic marketing strategy, in FY07/22, the Company began subscription trials as well as began appointing famous people as brand ambassadors. In FY07/23, based on the efforts in the previous fiscal year, the Company will strengthen messaging on Japanese SNS and operate physical stores (Haneda Airport Garden, major department stores). The Company also plans to aggressively expand into other regions such as Australia, Canada and Southeast Asia, centering on EC channels.

## Growth strategy

**(3) M&A and alliance policy**

Aiming to promote synergies from the acquisition of Huit Laboratories and carry out aggressive business expansion and revenue base diversification, the Company will utilize its abundant cash (¥6,389mn in cash and deposits at the end of FY07/22) to continue to promote M&A and alliances. In terms of synergies from the acquisition of Huit Laboratories, the Company will increase the utilization of factories and research facilities to quickly manufacture and develop Group products. The Company will also seek revenue growth through contract manufacturing from other companies.

Regarding M&A, the Company will target quality cosmetics businesses for M&A in order to rapidly accelerate and expand the domestic business. With respect to alliances, the Company will target high quality domestic manufacturers and provide marketing support for their rollout in China, leveraging its Chinese sales network to increase revenue.

## Shareholder return policy

### **While currently prioritizing securing internal reserves, will establish the foundation for implementing flexible shareholder return measures**

The Company's basic shareholder return policy is to strengthen profitability and to continuously and stably pay a dividend. However, it is currently in a growth process and in order to expand the business in the future and to enhance the financial base, it is prioritizing securing internal reserves and has not paid a dividend since it was founded. With respect to its abundant funds, in the short term, the Company will utilize the funds for investment in brand development, bolstering R&D, strengthening manufacturing, and M&A alliances, and it does not plan to pay a dividend in FY07/23. However, in May 2022 it newly established a shareholder benefits program in order to further enhance recognition and increase the number of shareholders. Every year at the end of July, shareholders holding at least 100 shares will receive a gift of the Company's products according to the number of shares they hold.

Although the Company will prioritize securing internal reserves in the near term, in the future the Company plans to continuously return profits to shareholders while taking results and its financial condition into consideration. The Company is rapidly growing in the Asia market, which has untapped potential, so the investment stance over the near term will mainly be for the purpose of capital gains, but the Company is building a foundation in anticipation of providing dividends, etc. in the future. Specifically, the Company decided to submit a proposal to revise the Articles of Incorporation to allow the distribution of surplus in the form of dividends, etc. by a resolution of the Board of Directors to the General Shareholders' Meeting scheduled for October 2022. At FISCO, we expect the Company to realistically start paying a dividend around the time that it achieves a change in designation to the Prime market.



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■ For inquiry, please contact: ■

FISCO Ltd.

5-13-3 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062

Phone: 03-5774-2443 (IR Consulting Business Division)

Email: [support@fisco.co.jp](mailto:support@fisco.co.jp)