PREMIUM GROUP (7199 JP)

MEDIUM-TERM MANAGEMENT PLAN TARGET SOLELY ACHIEVED THROUGH GROWTH IN EXISTING BUSINESSES

QUARTERLY EARNINGS SUMMARY

3Q EARNINGS RESULT AND 4Q OUTLOOK

Premium Group reported FY20 Q1~Q3 cumulative pre-tax profit of ¥3,242mil (+159.6% YoY) on operating revenue of ¥10,173mil (+29.0% YoY). In 3Q alone, the firm saw pre-tax profit decline 7.8% YoY (-72.4% QoQ) to ¥190mil on operating revenue of ¥3,514mil (+30.1% YoY / flat QoQ) due to a ¥160mil cost incurred for investment in strategies for growth. Furthermore, there was an evaluation loss of ¥105mil on new shares issued by a Thai affiliated company.

In its core business, Automobile Credit, cumulative operating revenue for FY20 Q1~Q3 rose 18.2% YoY to ¥7,032mil and transactions rose 35.4% YoY to ¥129,269mil thanks to 1) higher transaction volumes with existing member dealers, 2) a boost in the number of sales staff, and 3) a rise in per-head transactions/month to ¥153mil (as of FY20 3Q) from ¥127mil a year ago. In 3Q alone, the Automobile Credit business reported operating revenue of ¥2,458mil (+23.3% YoY / +1.7% QoQ).

Increasing business with large-scale network stores (used car dealers) and cross-selling also help boost credit transactions. The number of network stores rose 12.1% YoY to 22,574 stores as of Dec 19. The rise in transactions/member store was achieved by activating dormant stores (adding more sales staff) and allocating marketing resources. These efforts resulted in loan receivables rising 28.6% YoY to ¥301,947mil – to surpass the ¥300,000mil benchmark for the first time. Premium has also managed to keep its default rate (0.97% (-0.02ppt YoY)) at low levels.

Premium's second pillar of business, Automobile Warranty, generated cumulative FY20 Q1~Q3 operating revenue of ¥2,716mil (+53.9% YoY), boosted by a 49.6% YoY improvement to ¥3,257mil in transactions. The firm's subsidiary EGS, acquired in April 19, contributed nearly 65% of the 49.6% growth in transactions. In 3Q alone, the segment generated operating revenue of ¥933mil (+52.9% YoY / +2.9% QoQ).

As of 3Q, the unrealised revenue – or the future profit potential – from financial guarantee contracts (from Automobile Credit) and deferred income (from Automobile Warranty), was ¥20,697mil (+21.1% YoY) and ¥4,184mil (+67.2% YoY), respectively, to total ¥24,881mil (+27.0 YoY).

So far this fiscal year, Premium Group has bought back 520,000 shares (at the cost of ¥1,199.9mil). Management wishes to use the treasury shares to fund its growth strategy which includes M&A.

EXECUTIVE SUMMARY

- Premium Group reported FY20 1~3Q cumulative results with pre-tax profit of ¥3,242mil (+159.6% YoY) on operating revenue of ¥10,173mil (+29.0% YoY).
- In 3Q alone, pre-tax profit fell 7.8% YoY / -72.4% QoQ due to growth-related investment (¥160mil) and a valuation loss of new shares issued by its affiliate company in Thailand (¥150mil).
- In the Automobile Credit segment, cumulative Q1~Q3 operating revenue improved 18.2% YoY and transactions hit ¥129,300mil (+35.4% YoY) thanks to 1) an increase in transactions by existing member dealers, 2) a rise in sales staff and 3) improved per-head transactions. Future income indicator, financial guarantee contracts, rose 21.1% YoY to ¥20,697mil
- In the Automobile Warranty segment, contributions from EGS, a subsidiary acquired in FY3/19 boosted operating revenue for the 9 months.
- The firm has achieved full-year pre-tax profit estimate in 3Q but did not revise up FY20 guidance. Given there has not been any earnings risk present, Premium is likely to exceed its FY20 guidance.
- Concurrent to the 3Q results release, Premium announced its first medium-term plan "Value Up 2023", which runs from FY3/21~FY3/23. The plan targets pre-tax profit of ¥5,600mil (3-year CAGR 21.6%) on operating revenue of ¥26,000mil (CAGR 23.9%). In the first year (FY3/21), pre-tax profit is estimated to fall to ¥2,400mil (-24% YoY) due to a one-off profit from insurance assets from the previous year.

PL Summary (Cumulative)							
(¥mil)	**FY3/19**				**FY3/20**		
	1Q	**2Q**	**3Q**	**4Q**	**1Q**	**2Q**	**3Q**
Operating Revenue	2,542	5,183	7,885	10,699	3,166	6,659	10,173
Automobile Credit revenue	1,939	3,953	5,947	8,095	2,158	4,574	7,032
% Total revenue	76.3	76.3	75.4	75.7	68.2	68.7	69.1
Guarantee Commission	289	594	913	1,247	383	853	1,351
GP - Automobile Credit	1,650	3,359	5,034	6,848	1,775	3,721	5,681
GPM - Automobile Credit (%)	85.1	85.0	84.6	84.6	82.3	81.4	80.8
Automobile warranty revenue	566	1,155	1,765	2,395	877	1,784	2,716
% Total revenue	22.3	22.3	22.4	22.4	27.7	26.8	26.7
Warranty cost	380	806	1,211	1,590	589	1,222	1,826
GP- Automobile Warranty	186	349	554	805	288	562	890
GPM - Automobile Warranty (%)	32.9	30.2	31.4	33.6	32.8	31.5	32.8
Impairment cost	335	777	1,092	1,581	34	23	56
Personnel cost	568	1,239	1,916	2,602	744	1,561	2,404
Other overheads	635	1,326	2,131	2,972	1,030	2,083	3,319
Operating profit	334	442	622	707	386	916	1,217

Source: Nippon-IBR based on Premium Group's presentation materials

Quarterly Revenue Trend									
(¥mil)	**FY3/19**				**FY3/20**				
	1Q	**2Q**	**3Q**	**4Q**	**1Q**	**2Q**	**3Q**	**YoY (%)**	**QoQ (%)**
Automobile Credit	1,939	2,014	1,994	2,148	2,158	2,416	2,458	23.3	1.7
Automobile Warranty	566	589	610	631	877	907	933	52.9	2.9

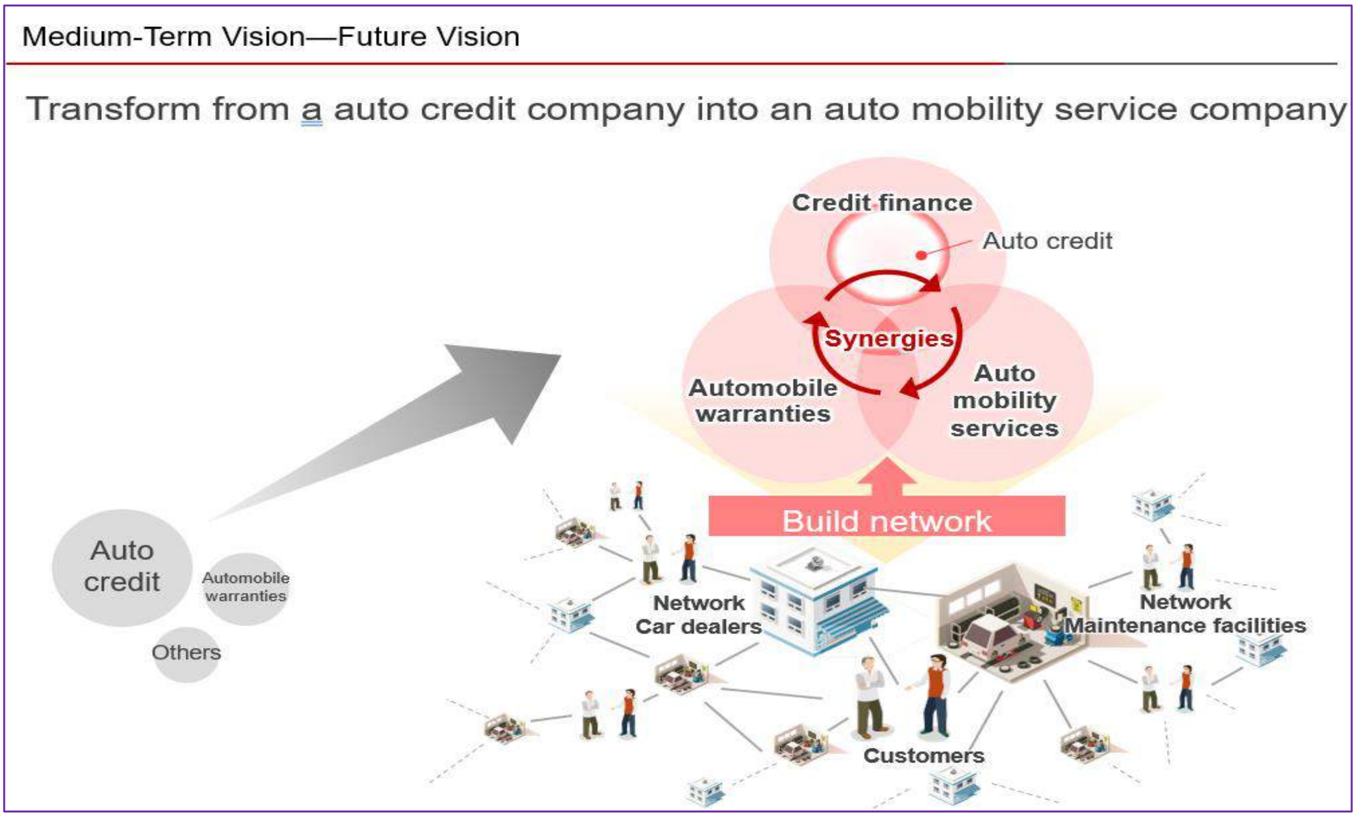
Source: Nippon-IBR based on Premium Group's presentation material

Premium revised up pre-tax profit guidance for FY20 at the 1Q result from ¥2,232mil to ¥3,141mil (+53.5% YoY) to reflect a one-off impact net gain of around ¥1,670mil for changes in accounting of estimates relating to insurance assets. This one-off impact to pre-tax profit was partially offset by strategic costs incurred to attain growth such as cost for marketing and sales promotion in core businesses (¥280mil), costs associated with M&As (¥160mil) and costs related to HQ such as moving to a new larger office (¥310mil). 3Q pre-tax profit has already overshot company's full-year guidance. According to Premium, the current business trend continues to be favourable in 4Q, however, the firm maintains the full-year pre-tax guidance as the possible upside does not meet the TSE's required disclosure rule. Cumulative 9-month operating revenue achieved 74.4% of the full-year company guidance ¥13,668mil (+27.8% YoY) which also remains unchanged. It is estimated that the firm spends the same level of cost for growth investment as in 3Q. Other than that, no further one-off costs have been incurred in 4Q. At this point in time, the firm does not recognise any risk of earnings shortfall to the full-year guidance.

MEDIUM-TERM MANAGEMENT PLAN TO MAR 23

Premium Group released its first 3-year management plan together with the FY20 3Q results. The foundation for the medium-term plan is to demonstrate management's risk awareness of the potential decline in the auto credit market. Growth in the used car market is somewhat linked to that of new car markets, but with some time lag. For the past 3 years, annual used car sales volumes have been stable at around 3mil units, with the market size estimated at around ¥3.5trn. For the next 3 years, it is assumed that the growth will remain flattish, or to decline gradually, as the new car market shrinks [NB: Japan's new car sales fell 1.5% YoY in CY19].

With Japan's ageing and declining population, demand for self-purchased cars is expected to slow eventually, though the demand for mobility services is likely to become the new norm. Premium Group's current business model is mainly associated with the domestic used car sales. Premium's focus is to transform the current business model and create a platform formed with various mobility services during the medium-term management plan.



Source: Premium Group "Medium-Term Management Plan Value Up 2023

The plan has two phases: Phase 1 – named "Value up 2023" – covers 3 years to Mar 2023.

Under Phase 1, the firm has two missions each of which can be further divided to three goals:

1. Providing the best finance by:
   - Growing existing businesses, i.e. auto credit and auto lease: Premium aims to achieve past 3-year CAGR of 22% or more in Automobile Credit over the 3-year period through increasing sales staff and sales offices – with plans to add 10 new locations to bring the total to 25. However, contributions from the Automobile Lease business – aimed at consumers – is not included in the medium-term growth projections.

   - Sourcing used cars through a subsidiary that specialises in collecting collateralised second-hand cars and making them fit for purpose again. Premium plans to wholesale such second-hand cars to its network dealers.

- Expanding existing businesses to shopping credit (shinpan) on higher-value items, such as solar power installation and other housing equipment. The firm is also considering entering into other credit businesses, for example, rent guarantee.

2. Providing quality service to the second-hand car platform value chain by:
   - Continuing to grow the existing Automobile Warranty business: Premium is looking for service revenue CAGR to grow in line with what it has achieved over the past few years (3-year CAGR to FY3/19 was ca. 14%). However, with auto warranty revenues growing at a rate of 50%+ so far this fiscal year, thanks to contribution from a newly added subsidiary EGS, it is likely that this business will be the main growth driver, which will take the 4-year CAGR to FY3/20 up to an impressive 22.1%.

     Premium reckons that used cars' life expectancy can be extended by providing services / products that can be guaranteed by warranty. Improved quality maintenance and servicing is likely to reduce the scrappage of used cars, which the firm identifies as an ESG-related business opportunity.

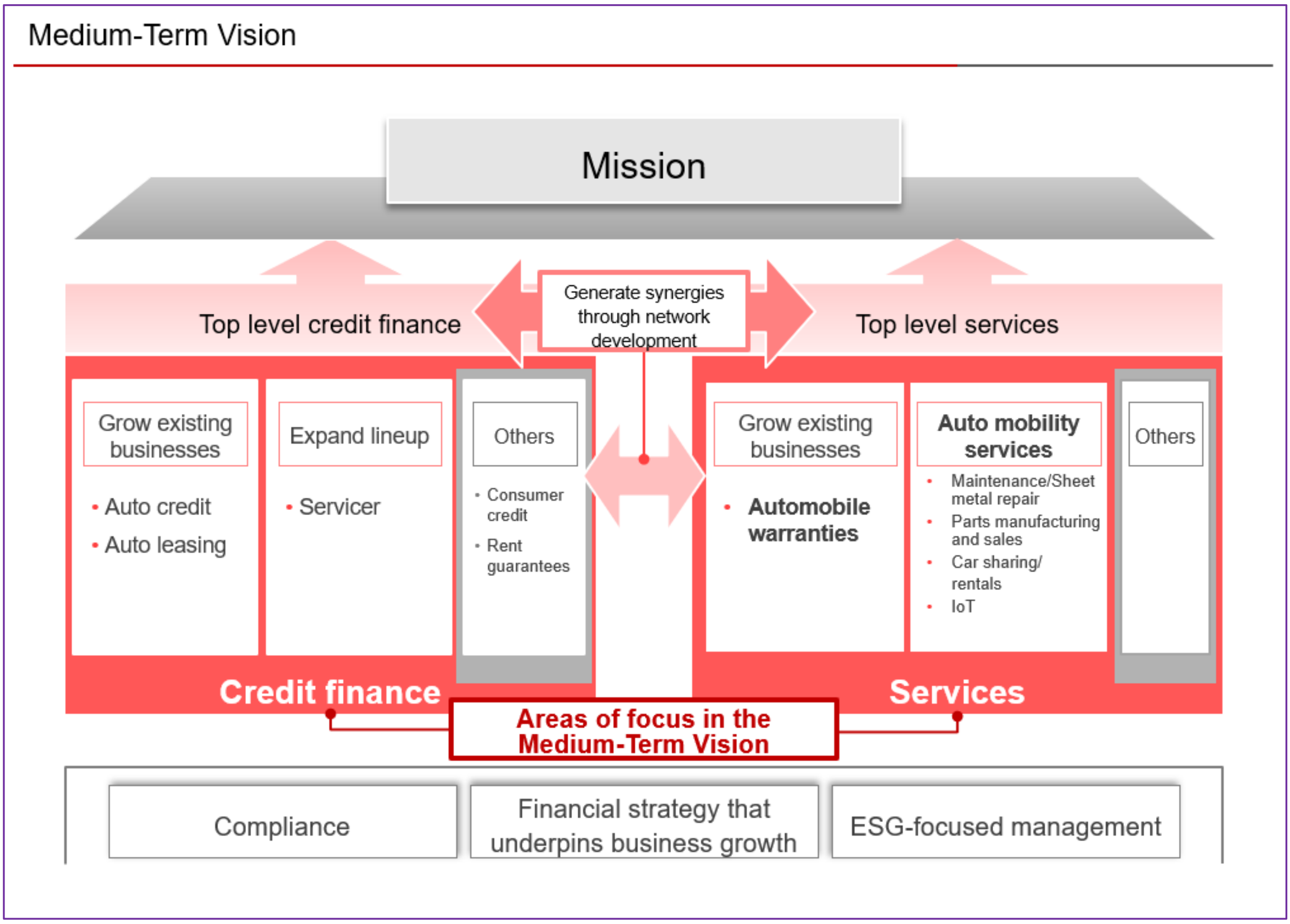
     Existing warranty products are all BtoC-based products. Premium aims to launch the new-type warranty products that also targets CtoC second-hand car transactions. Although it has not yet become a sizeable market, Premium's interest lies in providing warranties for those direct CtoC trades.

   - Auto Mobility Services – providing multiple services required to run the entire second-hand car value chain. Premium identifies those businesses as 3Rs – recycle, reuse and repair. The next 3 years are considered as a seed phase to build those businesses. No earnings contribution is expected in the current medium-term earnings estimates. Premium plans to start an auto parts recycling business through the acquired subsidiary that specialises in rebuilding and making fit for purpose used automobile components. Those recycled parts can then be wholesaled to Premium's network dealers and garages to service used cars. After establishing the second-hand parts market in Japan, Premium plans to expands its recycled parts business overseas. Cities like Dubai, Nairobi and Sao Paulo are known for their active recycled auto parts markets.

     The auto parts rebuilding subsidiary is just about break-even; therefore, Premium has not yet included any contribution to the medium-term management plan. Over the next 3 years, Premium's focus is to build a platform for the distribution of recycled auto parts. In the reuse business, the firm plans to wholesale used cars that the servicer subsidiary has collected from defaulted debtors to Premium's network dealers and garages.

   - Continuing to grow the existing repair business by expanding a network of member garages. 1The repair business will operate Premium's network garages, including its own FIXMAN garage in Hokkaido, providing environmentally-friendly support, such as using water-based paint, and human resources. Premium also aims to give support to other garages with expertise in improving service quality. The firm also plans to start its own road services. Out of the 3Rs, the repair business is the only service that is estimated to contribute to mid-term plan.

     Premium reckons that the Auto Mobility Service has a potential to achieve 3-year CAGR of above 30% in revenue. However, almost all the growth will come from repair services at its garages and from its SaaS-based software provider (for garages) subsidiary, Soft Planner. Soft Planner's software, such as GATCH, provides back office functions for garages such as MOT test bookings, service bookings, quoting / invoicing and controlling parts inventories. It is yet unknown when the recycle and reuse services to commence during this medium-term plan, therefore no contributions have been included in the figures.



Source: Premium Group "Medium-Term Management Plan Value Up 2023

Medium-Term Plan "Value Up 2023" Illustration

(¥mil)	Pre-Medium-term Management Plan					Value Up 2023			
	FY3/16	FY3/17	FY3/18	FY3/19	FY3/20	FY3/21	FY3/22	FY3/23	CAGR (%)
<IFRS>	Actual	Actual	Actual	Actual	CE & N-IBR Est	Nippon-IBR Estimate			
Operating Revenue	5,297	7,900	9,065	10,699	13,668	17,500	21,500	26,000	23.9
Automobile Credit	5,180	6,010	6,885	8,095	9,700	12,600	15,480	18,720	24.5
% total revenue	97.8	76.1	76.0	75.7	71.0	72.0	72.0	72.0	
Automobile Warranty	1,640	1,826	2,068	2,395	3,650	4,375	5,375	6,500	21.2
% total revenue	31.0	23.1	22.8	22.4	26.7	25.0	25.0	25.0	
Others (incl. Garage & Software)	0	63	112	209	318	525	645	780	34.9
% total revenue	0.0	0.8	1.2	2.0	2.3	3.0	3.0	3.0	
Pre-tax profit	579	1,297	1,979	2,097	3,141	2,400	3,600	5,600	21.3
Net profit attributed to the parent's shareholders	330	847	1,293	1,390	2,052	1,500	2,300	3,600	20.6

Source: Nippon-IBR
FY3/20 estimate for Automobile Credit is illustrated based on ca. 3.5~4% of previous year's loan balance
FY3/20 estimate for Automobile Warranty is illustrated based on assumption that 4Q revenue is flat QoQ
For all 3 segments, FY3/21-FY3/23 estimates are based on assumption that 1) target growth rate is similar to the past 3 years or more in each segment, 2) there is no major change in revenue breakdown.

In FY3/23, the final year of the Phase 1, Premium estimates pre-tax profit of ¥5,600mil (3-year CAGR +21.6%) on operating revenue of ¥26,000mil (CAGR +23.9%). In the first year (FY3/21), pre-tax profit is estimated to decline to ¥2,400mil from FY3/20 estimated pre-tax profit of ¥3,141mil as FY3/20 pre-tax profit was bolstered by accounting changes related to estimates for insurance cost.

SHAREHOLDER RETURN

Premium Group commits to maintain ca. 30% pay-out during the medium-term management plan. The firm wishes to increase its cash dividend every year upon achieving YoY growth in earnings. The remaining 70% will be reinvested to the growth strategy, which includes M&A.

Premium repurchased 520,000 shares at a cost of ¥1,200mil as of 15 Jan 20. Currently, the repurchased shares are held in treasury and will be used for M&A.

Due to liquidity issues (trading less than $3mil/day), as well as numbers of shareholders, Premium's shareholder return policy appears more geared towards dividend payments rather than share buy-backs.

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