NEXT Co., Ltd. (TSE1, 2120)

Takashi Inoue
President and CEO

Achieved a significant number of properties posted on our website: Addressing the challenge of maximizing the number of customer inquiries

(May 13, 2011, Tokyo)

◆Changed the pricing method from a pay-per-posting-based fee structure to a pay-per-inquiry-based fee structure

In the year ended March 31, 2011, NEXT recorded a year-on-year decline in sales and profit. However, excluding the Guarantor Operating Business from which the Company withdrew, sales for the year increased 4.6% compared with the year ended March 31, 2010. For the year ended March 31, 2011, sales stood at 10,738 million yen (a decline of 0.4% year on year) and operating profit totaled 1,749 million yen (a decline of 11.6% year on year). Net profit for the fiscal year under review amounted to 1,107 million yen (an increase of 7.9% year on year).

In January 2011, the pricing method for “HOME’S Rental & Real Estate Trade” and “HOME’S Real-estate Investment,” together constituting our main business lines, was changed from the previously-used pay-per-posting-based fee structure to the pay-per-inquiry-based fee structure. The number of properties posted on our website continued to grow strongly, allowing us to provide as many as 3.1 million pieces of property information at one time in early March 2011.

The entire revamp process for the local information website “Lococom” run by NEXT was completed in April 2011 following a significant business model change and a full website renovation that had been implemented since October 2010. This website revamp allowed us to start providing services through iPhone applications in addition to PCs and mobile phones, the existing vehicles for our services. In April 2011, Littel Co., Ltd., the entity equipped with natural language processing knowhow, was merged into NEXT through an absorption-type merger before being reorganized into the Littel Research Institute, the unit established as a research and development arm.

◆Negligible effects of the Great East Japan Earthquake on our business operations

As of March 31, 2011, the number of our affiliated stores in the Tohoku region stood at 149, or 1.6% of the total. Thus the Great East Japan Earthquake’s effects on our overall business were negligible. NEXT implemented a preferential program involving fee exemptions for affiliated stores remaining closed due to damage from the disaster, among those affiliated in the region. The real estate investment fair, previously scheduled for March 12, 2011, the day after the earthquake hit the country, was cancelled, which meant sales fell short of projections by 10 million yen or so. Soon after the earthquake, the levels of traffic also fell markedly, coupled with a decline in the number of inquiries, which resulted in the “HOME’S Rental & Real Estate Trade” falling short of projections by 30 million yen or so. Although the Real-estate Rents business is currently recovering, the recovery of the Real-estate Trade business has been somewhat slow.

Meanwhile, to assist with the disaster area reconstruction efforts, we launched the website “HOME’S Accommodation Search Assistance Program,” providing disaster victims with information on preferential lease properties. Separately, our local information website "Lococom" introduced a message board designed to supply information on disaster victims’ temporary accommodation. This message board currently provides room vacancy information registered by personal property owners willing to offer help and support to disaster victims.

◆Significantly increased advertising cost spending

Examining positive and negative contributing factors to sales in the year ended March 31, 2011 of 10,738 million yen (a decline of 41 million yen year on year), new detached houses made a particularly positive year-on-year contribution to sales in absolute terms. Meanwhile, new detached houses, custom-built houses and refurbished houses all showed meaningful year-on-year sales gains in percentage terms in the year. Sales in the “Rental & Real Estate Trade” business, the main business line, were more or less flat compared with the year ended March 31, 2010. The Company withdrew from the Guarantor Operating Business in the year ended March 31, 2011.

Operating profit of 1,749 million yen (a decline of 229 million yen year on year) for the year ended March 31, 2011 was the result of personnel costs declining by 76 million yen year on year and operating expenses decreasing by 202 million yen year on year, which more than offset a 534 million yen increase in advertising costs. Included in the financial statements for the year ended March 31, 2011 is an additional head office relocation cost of 53 million yen representing one-month office rent.

A decline in the number of affiliated stores to 9,564 (a decrease of 1,849 stores year on year) in the year ended March 31, 2011 was mainly attributable to our continued efforts to focus on our existing clientele to grow the number of properties posted on our website, while curbing the number of salespersons for new market development. Such efforts were made on the basis of the Company's earlier decision to change its key metric from the number of affiliated stores and sales per store to the number of properties posted on the website. Another main contributing factor to the decline in the number of affiliated stores was the increasing number of withdrawals from membership in response to the pricing method change implemented in the year.

For the year ended March 31, 2011, sales per store stood at 56,089 yen (a decrease of 768 yen year on year). That represented a sales decline caused by a growing tendency in March 2011 to refrain from moving in response to the March 11 earthquake, which more than offset a year-on-year gain recorded in the first two months of the January-to-March moving season. Sales per store as of January 31, 2011 stood at 59,686 yen (an increase of 6.6% year on year), and sales per store as of February 28, 2011 amounted to 59,415 yen (a gain of 5.3% year on year).

In relation to operating profit performance for the year ended March 31, 2011, sales and SG&A expenses declined in the year as a result of NEXT withdrawing from the Guarantor Operating Business through the sale of subsidiary NEXT Financial Services Co., Ltd. (NFS). In the year ended March 31, 2010, the Guarantor Operating Business posted 783 million yen in sales, 906 million yen in SG&A expenses and 123 million yen in operating loss.

Personnel costs for the year ended March 31, 2011 amounted to 3,507 million yen (a decline of 2.1% year on year). The average consolidated number of employees stood at 582 (a gain of 4 persons), including 23 new graduates (a decrease of 15 persons). Advertising costs for the fiscal year under review totaled 2,460 million yen (a gain of 27.8% year on year), including increased cost spending with a focus on listing advertising and SEO, the kinds of spending that contributes directly to attracting customers. In particular, in the quarter ended March 31, 2011, following the price method change, advertising cost spending increased by 404 million yen year on year (a gain of 72.5% year on year).

In the fiscal year under review, the Company recorded 1,107 million yen in net income (an increase of 7.9% year on year), including extraordinary losses consisting of 125 million yen in head office relocation cost, 22 million yen in prior-year depreciation costs due to the recognition of asset retirement obligations and 229 million yen in loss on sale of shares in NFS. In the year ended March 31, 2010, the Company posted 141 million yen in loss on impairment of Lococom.

As for the change in different cost items' percentage ratios of the total sales, cost and other SG&A expenses totaling 3,020 million yen (28.1% of the total sales) declined by 2.4 percentage points year on year, supported significantly by reduced expenses resulting from the Company's withdrawal from the Guarantor Operating Business. On the other hand, advertising costs of 2,460 million yen (22.9% of the total sales) and personnel costs of 3,507 million yen (32.7% of the total sales) grew by 4.5 percentage points year on year as a result of an increase in advertising cost spending. As a basic rule, we intend to maintain an advertising-costs-to sales ratio of approx. 20% and a personnel-costs-to sales ratio of approx. 30%.

◆A year-on-year sales growth achieved by the main services

Sales by service in the year ended March 31, 2011 show that, with the exception of the Guarantor Operating Business with 268 million yen in sales, from which the Company withdrew in the fiscal year under review, year-on-year sales growth was achieved by the Company's main services including real estate information services for which 10,407 million yen in sales was recorded (an increase of 4.5% year on year). "Others", amounting to 26 million yen in sales, comprised property and casualty insurance agency business, fee-charging employment agency business (downsized in September 2010) and “MONEYMO” and “eQOL Skincare,” as new business lines, among others.

The “Real-estate Rents and Trade” business, constituting a significant part of the real estate information services, posted 7,096 million yen in sales in the fiscal year under review (an increase of 1.2% year on year), which was more or less unchanged from the level recorded in the year ended March 31, 2010, as a result of the pricing method change implemented in the year. From quarters one through three, “Rental & Real Estate Trade” sales grew 5.9% year on year before declining 11.4% year on year in the fourth quarter following such pricing method change.

This represents a challenge that needs to be tackled in the coming months. New condominiums recorded 1,131 million yen in sales in the year ended March 31, 2011 (a gain of 6.7% year on year) with special programs and option sales doing well. Although the number of properties posted on our website fell year on year, affected by the prevailing market conditions, the number of customers continued to remain essentially flat. New detached houses posted 994 million yen in sales (an increase of 23.6% year on year) with the number of customers and properties growing 12.6% and 12.4% year on year respectively.

In the “Rental & Real Estate Trade” business, we experienced an increase in the number inquiries during the peak season from January onward, and sales per store showed a year-on-year growth for the year ended March 31, 2011.For the month of March 2011, the number of affiliated stores in the “HOME'S Rental & Real Estate Trade” business stood at 9,564, with sales per store amounting to 56,089 yen and monthly sales totaling 536 million yen.

As for the number of properties by area, NEXT's share of the total number of residential properties as of March 31, 2011 stood at 6.8% in Greater Tokyo, 7.7% in Kinki and 4.2% in Tokai, pointing to a steady share gain that has been achieved. On the other hand, our share was 2.7% in Kita-kanto, 2.4% in Shikoku, 2.1% in Chugoku, 2.0% in Hokkaido/Tohoku, 1.8% in Kyushu/Okinawa and 1.6% in Hokuriku/Koshinetsu, meaning that we need to develop our business in these regions in the coming years.

Examining the trend of P/L by segment for the year ended March 31, 2011, real estate information services operating profit stood at 2,173 million yen, representing a year-on-year decline of 11.6%, as sales slowed due to a decline in inquiries. The local information business posted an operating loss of 314 million yen (a deterioration of 323 million yen year on year), while "Others" posted an operating loss of 128 million yen (a deterioration of 34 million yen year on year).

In the real estate information services business in the fiscal year under review, we launched multilingual services for English and Chinese speakers as well as smart phone-based services. The provision of smart phone-based services also started in the local information business in the year, for which a growing number of users and word of mouth referrals have been achieved. In "Others," we launched the "MONEYMO” and “eQOL Skincare” services as new business initiatives. Regarding the pursuit of our overseas business operations, we are currently in the process of selecting local partners in China and ASEAN countries.

As for the consolidated balance sheets, cash decreased by 1,781 million yen, mainly due to the payment of corporate tax and dividends, the payment of security deposit and construction cost for the new office in Shinagawa, capital increase by NFS Co., Ltd. and the acquisition of shares in Willnic Co., Ltd. In other current assets, advance money decreased by 278 million yen as a result of the sale of shares in NFS Co., Ltd, and allowances for uncollectible receivables declined by 134 million yen. In addition, advance receipts decreased by 510 million yen and performance guarantee allowances declined by 141 million yen.

The main reason for the change in tangible fixed assets was an increase of 518 million yen in building fixtures resulting from the head office relocation. The main reasons for the change in intangible fixed assets included an increase of 103 million yen due to a revamp of Lococom and an increase of 216 million yen due to the acquisition of shares in Littel Co., Ltd., as well as a security deposit and guarantee money totaling 405 million yen for the lease of office space for the head office.

◆Maximize the number of inquiries while maintaining the number of properties on the "HOME'S Rental & Real Estate Trade" website

As our top priorities for the year ending March 31, 2012, we aim to enhance sales in real estate information services by maximizing the number of users and inquiries while maintaining the number of properties on the "HOME'S Rental & Real Estate Trade" website. In the local information business, we aim to attain profitability for "Lococom" as early as possible by changing its business model while seeking to achieve profitability on a single-month basis.

For the year ending March 31, 2012, we forecast 11,739 million yen in consolidated sales, an increase of 9.3% year on year, 1,372 million yen in consolidated operating profit, a decline of 21.6% year on year, and 773 million yen in consolidated net income, a decrease of 30.1% year on year. Our forecast is predicated on growing sales; mainly in "Lococom" and new businesses. In the "HOME'S Rental & Real Estate Trade" business, we expect to post 6,596 million yen in sales, a decline of 7.1% year on year. In the year ending March 31, 2012, the number of properties posted on the "HOME'S Rental & Real Estate Trade" website is projected to remain more or less unchanged from the level recorded in the year ended March 31, 2011 and the number of affiliated stores is anticipated to show a small year-on-year increase.

Consolidated operating profit for the year ending March 31, 2012 is forecast to decline 21.6% year on year (a decline of 377 million yen) despite a 9.3% year-on-year gain (an increase of 1,001 million yen year on year) in consolidated sales for the fiscal year. That is mainly attributable to a projected increase of 921 million yen in other SG&A expenses, consisting chiefly of a 580 million yen increase in annual office rent, as well as a projected increase of 107 million yen in advertising costs. Consolidated net income for the year ending March 31, 2012 is forecast at 773 million yen compared with 1,107 million yen for the year ended March 31, 2011. We expect to pay 620 yen for the FY03/2012 dividend compared with 590 yen for the FY03/2011 dividend, and the FY03/2012 dividend ratio is likely to be 15.0% compared with 10.0% for the year ended March 31, 2011.

Q&As

1. What are the benefits of the head office relocation you have made?

The problem with our previous head office in Harumi, Minato Ward was its inconvenient location in terms of public transport, hampering sales efficiency and efforts to flexibly expand the capacity for a larger number of staff. Following a simulation-based examination of the scenario of improved sales efficiency and higher per-tsubo rent, we decided to target improved sales efficiency by relocating the head office to Shinagawa (Konan, Minato Ward), an area with a train station serviced by the Shinkansen express and with good access to Haneda Airport. Equipped with a capacity for up to 1,000 persons, the new head office in Shinagawa can accommodate an expanded number of employees.

2. **Your earnings forecast shows a high sales growth rate for "Lococom" and new businesses, but this forecast seems to have a very high risk. Please tell us how you will be able to achieve this earnings forecast.**

We are well aware that, as new businesses, they are subject to high risk. We hope you will understand that we at NEXT have strong determination and will achieve the forecast sales. Having said that, please keep in mind that risk is inevitable.

3. **You have achieved an increased number of properties posted on your website thanks to a shift to the pay-per-inquiry-based fee structure. According to your analysis, what is the ultimate cause of your failure to achieve the projected sales?**

In terms of future growth for NEXT, in order to develop our real estate website into the top property search website with total dominance within a certain period, we must target increased growth rates by pursuing our operations with a clear focus on the information quantity, quality and search website usability required by the website user, instead of continuing to pursue growth based on the pay-per-posting-based fee structure that has been generating annual growth rates of 3 to 5% or so to date. Thus, in our view, the move to implement the migration to the pay-per-service-based fee structure was the right management decision for achieving that goal. This is true from the perspective of differentiating our services from those offered by our competitors. One regrettable thing this time was the fact that the number of inquiries did not grow as much as anticipated, which was presumably due to a lower-than-expected percentage of website users actually making an inquiry. Another likely reason is the decreased service fee charge rate caused by a larger-than-expected number of fee charge exclusion requests made by affiliated stores. Currently, some improvements are being observed as a result of the steps we have taken in connection with several metrics pointing to fewer-than-expected inquiry placements. Nevertheless, the improvement will continue to remain gradual rather than rapid.

4. **Please explain the potential market in China and your future local partners there.**

The potential market in China is huge, with annual new housing starts totaling 6 million according to experts. We are now continuing to approach multiple local companies in the country in an effort to find our partner there. Given that our potential partners differ from one another in terms of corporate strength, we seek to identify a partner company whose business model can operate in good harmony with our own. Since the potential tie-up format differs from one party to another, we will bear that in mind during the ongoing process of plan formulation.