

Highlights of Major Retail Groups' Financial Results for Fiscal Year Ended February 2023

The following are Japan Credit Rating Agency, Ltd. (JCR)'s perception of the current status and highlights for rating concerning the financial results for the fiscal year ended February 2023 (FY2022) and earnings forecasts for FY2023 of Japan's two major retail groups: Seven & i Holdings Co., Ltd. ("Seven & i," security code: 3382) and AEON CO., LTD. ("AEON," security code: 8267).

1. Industry Trend

In FY2022, same-store sales of chain stores increased for the third consecutive year, up 1.0% year-on-year (up 3.1% year-on-year in FY2021), according to Japan Chain Stores Association. By product category, sales of foods were down 0.8% year-on-year due to a decline in demand for eating at home as a result of the easing of restrictions on activities and restrained buying due to price hikes. On the other hand, sales of apparel, which had fallen sharply due to the COVID-19 pandemic, rose 5.7% year-on-year. Sales of household goods also rose 6.4% year-on-year, and both sectors saw increased sales on the back of travel and other opportunities to go out. However, high prices are still continuing, and future trends in consumer confidence require caution.

In the retail industry, performance trends are different by business category. Department stores and shopping centers are improving their performance with a recovery in their ability to attract customers. Convenience stores (CVS) are also seeing growth in the number of customers and average sales per customer, and average daily sales are increasing. Among general merchandise stores (GMS), although sales of apparel, which had fallen in the wake of the COVID-19 pandemic, increased, many companies saw their operating income squeezed by higher SG&A expenses due to rising electricity rates and other factors. In addition, many supermarket (SM) companies saw their performance deteriorate due to a decline in demand for eating at home and increases in utilities and labor costs.

Both Seven & i and AEON are developing group strategies for future growth. Seven & i is seeking to grow its Domestic and Overseas CVS operations based on its strength in food. Along with vendors, 7-Eleven, Inc. ("SEI") plans to build and expand plants in the US to develop and expand sales of fresh foods. SEI also plans to transfer manufacturing technology from Japan to the existing plants to supply high-quality products. Seven Eleven Japan Co., Ltd. ("SEJ") plans to continue strengthening its "food" domain, centered on Seven Premium private brand (PB) products. Ito-Yokado Co, Ltd. ("IY") has completely withdrawn from its own apparel business and is working to develop process centers and other infrastructure in its food business. At the same time, it is continuing to select and concentrate its businesses through a review of its business portfolio, and following the sale of Sogo & Seibu Co., Ltd. announced in November 2022, it announced the sale of Barneys Japan in April 2023.

Based on an exclusive partnership agreement in Japan with Ocado Solutions, a subsidiary of the British online supermarket company Ocado Group plc, AEON in summer of 2023 will launch an online market "Green Beans" that will be based on a customer fulfillment center that will introduce cutting-edge AI and robotics functions. To strengthen the foundation of its SM operations in the Tokyo metropolitan area, in April 2023, AEON concluded a basic agreement with its equity-method affiliate Inageya Co., Ltd. and consolidated subsidiary United Supermarket Holdings Inc. (U.S.M.H.) for a business integration to realize the "1 trillion yen SM concept in the Kanto region." AEON plans to acquire up to 51% of Inageya's voting rights in November 2023 (17% at the end of September 2022), making it a consolidated subsidiary. After that, AEON plans to integrate Inageya and U.S.M.H. in November 2024.

2. Financial Results

Both Seven & i and AEON increased revenue and profit in FY2022. Seven & i posted an operating income of 506.5 billion yen (up 30.7% year-on-year), the second consecutive increase. By segment, the Superstore operations and Financial Services posted lower operating income, but the performance was driven by the Overseas CVS operations, resulting in a record income for the first time in three fiscal years. SEJ, Domestic CVS operations, increased its operating income for the first time in three fiscal years. SEJ strengthened its lineup of high-value-added products, changed the layout of its sales floors to increase

the number of items it handles, and held various fairs to encourage customers to visit its stores, resulting in the success. SEI, Overseas CVS operations, also posted higher operating income thanks to greater synergy effects with the Speedway business (acquired in May 2021) and higher merchandise sales at existing stores. Sogo & Seibu returned to profitability in operating income for the first time in three fiscal years, thanks to higher sales of apparel and other merchandise in reaction to store operating restrictions imposed until the previous fiscal year. IY, on the other hand, posted its second consecutive year of operating income decline due partly to higher utilities costs, despite higher same-store sales including those of tenants.

AEON's operating income also increased for the second consecutive year to 209.7 billion yen (up 20.3% year-on-year). By segment, the GMS and the Services & Specialty Store segments, which had been in the red for two consecutive fiscal years through the previous fiscal year, returned to profitability, and the International segment and the Developer segments posted higher operating income. The core of the GMS operations, AEON Retail, benefited from higher apparel sales, improved gross profit margin, and cost reductions at stores and headquarters. In the Services & Specialty Store operations, many group companies posted higher profits thanks to a recovery in attracting customers. On the other hand, the SM operations posted a profit decline for the second consecutive year due to lower same-store sales at core companies and higher SG&A expenses, including utilities costs.

Looking at the financial situations at the end of FY2022, Seven & i's equity ratio declined to 32.9% (34.1% at the end of FY2021). This was largely due to an increase in right-of-use assets and lease obligations resulting from the application of "Accounting Standards Updates No. 2016-02, Leases (Topic 842)" in its Overseas CVS operations. AEON's equity ratio was 8.0% (8.2% at the end of FY2021) and 14.5% (14.9% at the end of FY2021) excluding the Financial Services. Excluding the Financial Services, the interest-bearing debt (long- and short-term borrowings, CP, corporate bonds, lease obligations, accounts payable-installment purchase, etc.) continue to increase.

Capital investments in FY2022 at Seven & i were 431.9 billion yen (down 1.7% year-on-year), almost unchanged from the previous year. While the investments in the Overseas CVS operations increased 5.7% year-on-year, those in the Domestic CVS operations decreased 3.9% year-on-year due to decreased investments in existing stores at SEJ, and those in the Superstore operations decreased 12.1% year-on-year due to restrained investment at IY. The Overseas and Domestic CVS operations, which are positioned as a growth area, accounted for 65.9% of the total (63.3% in the previous year). AEON's capital investments were 370.8 billion yen (up 5.2% year-on-year) due to an increase in the digital and logistics fields, on which AEON is focusing. The weight of investments in digital and logistics increased, with domestic stores accounting for 56% (58% in the previous year), overseas stores for 14% (16% in the previous year), and digital and logistics for 30% (26% in the previous year).

3. Highlights for Rating

Both Seven & i and AEON are forecasting higher revenue and profit for FY2023. Seven & i plans to achieve a record-high operating income of 513.0 billion yen (up 1.3% year-on-year). In the Overseas CVS operations, although gasoline revenues are expected to decline, it anticipates an increase in income due to higher sales of original products, including fresh foods, and the accompanying rise in the gross profit margin of merchandise. In the Domestic CVS operations, it also plans an increase in same-store sales with expanded sales of Seven Premium and continued implementation of sales promotion events. On the other hand, IY is expected to post an operating loss due to upfront costs associated with the centering of online supermarkets and an increase in DX expenses aimed at improving productivity.

AEON plans an operating income of 220.0 billion yen (up 4.9% year-on-year), a record high, surpassing the 215.5 billion yen in FY2019 before the occurrence of the COVID-19 pandemic. Although results by segment are not disclosed, it expects profit growth in all segments.

There are concerns that consumer confidence will deteriorate due to rising prices and energy costs, and SG&A expenses, including labor and utilities costs, are also expected to increase. Both groups have already implemented various measures, but will need to step up their efforts in the future. Seven & i is working on renewing Seven Premium to increase the added value, and is expanding its lineup of products that balance value and price. As productivity improvement measures, SEJ is working to reduce the burden of store operations by introducing self-checkout and smartphone cash registers. SEI has established a Cost Leadership Committee and is implementing a fundamental review of its cost structure, including optimization of personnel. AEON kept the prices of most of its PB products TOPVALU unchanged, and made progress in making existing customers repeat customers and attracting new customers. AEON also worked on repositioning TOPVALU as a "new value-creation brand," Gurinai as an "organic and natural ingredient-focused brand," and BESTPRICE as a "satisfying quality brand" aimed at providing the best prices in each region to respond comprehensively to customers' diverse needs. To improve productivity,

it is reducing the workload of store operations by introducing self-checkout systems and utilizing process centers.

Efforts to integrate stores with the Internet and those for digitalization are important for the future growth, and JCR will closely monitor the progress of these efforts and their results. Seven & i is strengthening its delivery service, and SEJ is aggressively expanding the number of stores handling the service in preparation for a nationwide development within FY2024. As mentioned above, AEON plans to launch its online market "Green Beans" in summer of 2023.

Both companies plan to increase capital investments in FY2023: 453.1 billion yen (increase by 21.1 billion yen from a year earlier) for Seven & i and 400-450 billion yen (increase by 29.1 to 79.1 billion yen from a year earlier) for AEON. Seven & i's Domestic and Overseas CVS operations account for 64.0% of the total, and there is no change in the priority allocation of investments to these two operations. Looking at the breakdown of AEON's investment plan, the percentage for domestic stores will decline to 50% (56% in the previous year), while overseas stores will account for 20% (14% in the previous year) and digital and logistics will account for 30% (30% in the previous year), indicating an increased weight of investment in growth areas. Both companies are expected to continue to invest for future growth.

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(Chart 1) Consolidated Financial Results of Two Major Retail Groups

(Unit: JPY100mn)

Company	FY	Operating Revenue	Operating Income	Ordinary Income	Net Income Attributable to Owners of Parent
Seven & i (3382)	2021	87,497	3,876	3,585	2,107
	2022	118,113	5,065	4,758	2,809
	2023 (forecast)	111,540	5,130	4,800	2,850
AEON (8267)	2021	87,159	1,743	1,670	65
	2022	91,168	2,097	2,036	213
	2023 (forecast)	94,000	2,200	2,100	250

*Figures for FY2022 and FY2023 (forecast) are the figures after application of "Accounting Standards for Revenue Recognition."

(Source: Prepared by JCR based on financial materials of above companies for Charts 1 through 4)

(Chart 2) Operating Income of Two Major Retail Groups by Segment

(Unit: JPY 100 mn)

	Seven & i (3382)		AEON (8267)	
	FY2021	FY2022	FY2021	FY2022
GMS*	187	121	-20	140
Domestic CVS	2,233	2,320	-	-
Overseas CVS	1,598	2,897	-	-
SM	-	-	305	228
DS	-	-	27	36
Health & Wellness	-	-	419	448
Financial Services	375	371	617	603
Developer	-	-	388	452
Department and Specialty Store**	-81	34	-30	102
International	-	-	55	128
Others	-1	-4	-1	-54
Adjustment	-436	-674	-18	10
Total	3,876	5,065	1,743	2,097

*Superstore operations (including SM and others) for Seven & i

** Services & Specialty Store for AEON

(Chart 3) Consolidated Financial Position of Two Major Retail Groups

(Unit: JPY 100 mn, %)

Company	FY-end	Equity Capital	Interest-bearing debt*	Equity Ratio (%)
Seven & i (3382)	2021	29,809	28,987	34.1
	2022	34,745	29,757	32.9
AEON (8267)	2021	9,574	32,909	8.2
	2022	9,925	34,831	8.0

* Total of long- and short-term borrowings and corporate bonds for Seven & i, Total of long- and short-term borrowings, corporate bonds, CP, lease obligations, accounts payable-installment purchase, etc. for AEON

(Chart 4) Capital Expenditures of Two Major Retail Groups

(Unit: JPY100mn)

Company	FY	Capital Expenditure
Seven & i (3382)	2021	4,396
	2022	4,319
AEON (8267)	2021	3,525
	2022	3,708

<Reference>

Issuer: Seven & i Holdings Co., Ltd.

Long-term Issuer Rating: AA Outlook: Stable

Issuer: AEON CO., LTD.

Long-term Issuer Rating: A Outlook: Stable

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