Moving from Brand to Organizational Integration

I became president in September 2016, a little over a year and a half ago. During this time, the whole Company has made a concerted effort to integrate Circle K and Sunkus stores under the FamilyMart brand. Converted stores are seeing significant increases in daily sales and customers. Moreover, we have integrated manufacturing and logistics at the same time. As a result, our expansion of the convenience store network is creating economies of scale that are growing the earnings of the whole chain, and we plan to complete integration by November 2018. We have been able to proceed successfully with this 5,000-store brand conversion thanks to the tireless efforts of franchised stores, suppliers, and personnel as well as the know-how and business partner networks developed through previous initiatives, and the general mobilization of the capabilities of our organization and personnel. As well as being proud of our employees, I am genuinely thankful to everyone involved.

Our next task is to rebuild the head office’s support system for franchised stores. I feel that making brand integration our first priority has given rise to a range of issues with respect to optimization of the head office organization and personnel assignment. In fiscal 2018, under our new One FamilyMart slogan, we will achieve “real” integration that coalesces personnel as well as brands and infrastructure, and we will establish an environment that allows us to maximize our support for franchised stores as important partners.

Stepping Up Efforts through a Results-Oriented Organization

As we advance brand integration, enhancing the quality of our store network in Japan, which has reached 17,000 stores, has become a pressing management task for the near term. We aim to change course significantly by transitioning from scale expansion to the stepped-up pursuit of quality and the innovation and decision-making of individual stores. Furthermore, we will consider “localizing” supervisors who work in frontline operations supporting franchised stores so that supervisors can participate in store development with a stronger sense of ownership. Through marketing that reflects demand in retail zones and store management that accords with local communities, we aim to create convenience stores that earn the overwhelming trust and endorsement of customers and grow while contributing to local communities.

As part of these efforts, we renewed FamilyMart’s organization at the beginning of fiscal 2018. Aiming to establish a group of autonomous organizations with their own goals and responsibilities, we changed from a chain of command directly under the control of the president to a system in which each division has overall control of important functions. The new system also clarifies key performance indicators. Under this system, we will accelerate efforts to heighten the quality of our stores.

Aiming to Be Rooted in Local Communities

Being rooted in local communities is the guiding principle of FamilyMart’s medium-to-long-term growth scenario. As Japan’s population declines, competition in the retail industry is becoming challenging. In addition, e-commerce businesses are increasing the pace of their forays into the retail industry. Our existing approach of rolling out homogeneous products and services cannot win against such fierce competition. By being deeply rooted in each local community and responding flexibly to its distinctive consumer behavior and events, stores will become indispensable and achieve significant differentiation. With this in mind, we will create systems that support the innovation and decision-making of individual stores. Furthermore, we will consider “localizing” supervisors who work in frontline operations supporting franchised stores so that supervisors can participate in store development with a stronger sense of ownership. Through marketing that reflects demand in retail zones and store management that accords with local communities, we aim to create convenience stores that are deeply rooted in local communities and to Japan.

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Raising the Value of the Entire Chain by Strengthening Support for Franchised Stores

Overview of Business Conditions
In Japan, there are nearly 60,000 convenience stores, with three major chains accounting for nearly 90% of them. Due to fiercer competition, both companies in an expanding e-commerce market and with other business formats, convenience store operators need to increase the competitiveness of their stores by leveraging store networks as infrastructure and expanding and improving their capabilities. Also, in response to the decline in Japan’s population, chains urgently need to increase work efficiency and reduce workloads if they are to sustain long business hours and high-quality store operations.

In Japan, there are nearly 60,000 convenience stores, with three major chains accounting for nearly 90% of them. Due to the current fiscal year onward we expect lower impairment loss risk because we brought forward measures to mitigate this issue. In fiscal 2019 and beyond, we will continue developing highly profitable stores.

Opening Quality Stores
Through management integration, we established a network with the second largest number of stores in Japan. As Japan’s population trends downward, the number of convenience stores is approaching a saturation point in the country’s retail zones. Mindful of these business conditions, we will give first priority to establishing a quality store network. For new store openings, our basic policy will be to continue stringent selection of high-quality stores that promise stable earnings.

Strengthening Support for Franchised Stores
As a measure to heighten the competitiveness of individual stores, we are moving forward with a build-and-scrap (B&S) strategy. This entails relocating existing stores to stores with locations and sales floor areas that suit retail zones. The B&S strategy relocated 110 stores in fiscal 2014. In fiscal 2017, this number had risen steeply to 315, or more than half of all store openings. The benefits of the B&S strategy, daily sales are at least 15% up for establishing these spaces in even more stores.

Building Competitiveness through Strategic Store Openings
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FamilyMart has begun reforming store operations in earnest to increase their efficiency. In fiscal 2017, in addition to the short-term measures of simplifying work manuals and reducing sales promotion items, we introduced next-generation point-of-sale (POS) cash registers and invested in IT. As a result, we reduced store work by six hours. In fiscal 2018, we will eliminate the need for inspections of products when they are delivered and introduce larger, labor-saving store fixtures and food preparation equipment. Also, we plan to introduce about 1,000 self-checkout cash registers. Through these additional measures to increase work efficiency, we expect to reduce store work hours by another 3.5 hours. FamilyMart will actively invest to improve store operations and to establish environments that enable store staff to focus on strengthening the differentiating features of brick-and-mortar stores, such as customer service and high-quality store management.

**Accelerating Reform of Store Operations**
- Simplifying manuals
- Eliminating need for product inspections
- Introducing next-generation POS cash registers
- Introducing self-checkout cash registers
- Reducing workloads by introducing new fixtures

**Enabling Head Office to Support Stores**
- Helping to hire and train store staff
- Assisting with store staff retention
- Having head office employees support store operation

**Support Systems for Franchised Stores**
- New franchise contract
- Support for management of multiple stores
- Senior Citizen Franchisee System

FamilyMart has established a range of systems that allow franchisees to manage their convenience stores with peace of mind. Since September 2016, we have been switching over to a new franchise contract. Under this new contract, the head office reduces the financial burden of store operations by subsidizing a certain percentage of utility costs and losses on unsold ready-to-eat items and giving each franchised store ¥1.2 million per year as assistance for store management.

**Main Points of Change in New Franchise Contract**

<table>
<thead>
<tr>
<th>Old contract</th>
<th>New contract</th>
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</thead>
<tbody>
<tr>
<td><strong>Product disposal costs</strong></td>
<td>Franchisee responsibility</td>
</tr>
<tr>
<td>Head office offsets portion of product loss</td>
<td></td>
</tr>
<tr>
<td><strong>Support for utility bills</strong></td>
<td>Franchisee responsibility</td>
</tr>
<tr>
<td>Head office pays 90% of portion, less than ¥3.6 million annually</td>
<td></td>
</tr>
<tr>
<td><strong>Store management support</strong></td>
<td>N/A</td>
</tr>
<tr>
<td>¥1.2 million per year</td>
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FamiJOB, on the FamilyMart website. In addition, during sales promotions and other busy periods, head office employees help with store operations. To date, 2,200 employees have taken part in this system.
**STRATEGY**

**FamilyMart UNY Holdings Integrated Report 2018**

2019, nearly all of our stores will have new coffee machines equipped with the latest functions, thereby enabling us to offer higher-value products. For example, customers will be able to order a richer flavored coffee by adding beans or a smooth cappuccino finely blended with milk. In addition, the machines’ drip brewing process ensures that all of the beverages have a rich, refreshing flavor. We expect that these machines will boost coffee beverage sales by at least 10%.

**Developing and Increasing the Efficiency of Supply Chains**

As it continues renewing rice balls, noodles, sandwiches, and other mainstay products, FamilyMart will emphasize ingredients, preparation methods, and appearance. To realize tastiness that surpasses that of specialty store offerings, we will carefully select ingredients and introduce the latest food preparation equipment as needed. Further, through such measures as increasing our selection of health-focused products, we will provide an extensive product lineup that caters to diverse customer needs.

The use of self-service coffee machines has become firmly established among convenience store customers in Japan. By the end of fiscal 2019, nearly all of our stores will have new coffee

**Heightening the Quality of Ready-to-Eat Items**

By advancing structural reform in ready-to-eat items, we are continuing to market ready-to-eat items that have even greater value and appeal. This structural reform has two aims: rationalizing supply chains through the development and optimization of production and distribution bases and enhancing the quality of ready-to-eat items.

In fiscal 2018, we are progressing with an integration of production and distribution bases that includes Circle K and Sunkus while transitioning to a phase of enhancing product appeal even further. In efforts to raise the quality of ready-to-eat items, we aim to renew mainstay products and develop distinctive, attractive products. To these ends, since fiscal 2015 at plants that produce ready-to-eat items we have been collaborating with producers of ready-to-eat items to invest in renovation measures that are compliant with HACCP* principles, as well as invest in food preparation equipment that enables the manufacture of differentiated products.

**Strategic Planning**

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**Discovering New Potential for Stores**

Amid increasing interest in health, we decided to enter the fitness business to cater to customers who want a convenient place to work out. We have begun establishing Fit & Go gyms, which are open 24 hours a day year round. Other initiatives to add to store functions that meet everyday needs will include the launch of laundromat services through Famima Laundry. Also, we are considering the introduction of an in-store key delivery service that caters to the growing demand for vacation rentals. Through such initiatives, we will continue discovering new possibilities for combining existing stores with highly compatible businesses to create store formats that have added functions and as such go beyond merchandising.

**Introducing the Don Quijote Way to Convenience Stores**

In June 2018, we began the joint trial development of convenience stores that incorporate Don Quijote’s product lineup, sales floors, and management methods. We introduced special product shelves that are much higher than normal shelves, and the stores carry approximately 5,000 items, of which 2,800 are Don Quijote items, such as daily necessities, confectioneries, and processed foods. Through this joint trial, we will provide the kind of shopping fun that only brick-and-mortar stores can offer.

**Creating Next-Generation Stores**

In June 2017, FamilyMart announced a business alliance with ITOCHU Corporation and LINE Corporation. The alliance is premised on using LINE’s various services to cooperatively develop new products, technologies, and services. We are considering incorporating the company’s services in a wide range of store operations, such as the establishment of communication with customers that reflects their needs and purchase history, the improvement of payment equipment and other store equipment, the enhancement of customer convenience, and the mitigation of the workloads of store staff.

The merits of utilizing leading-edge technology in the CVS business are not limited to increases in the efficiency of store openings and operations. As well as using the technology of Google LLC to incorporate AI in store development, we are exploring ways of enhancing marketing efficiency through digital advertising. By capitalizing on the distinctive advantages that brick-and-mortar stores and points of contact with customers give it, FamilyMart will embrace state-of-the-art technology to create a new generation of stores.