

# Corporate Strategy to Achieve Our Long-Term

## Key Indicators and Growth Policies

AEON MALL aims to become a world-class global commercial developer, raising overseas revenues to 35 percent of total sales and achieving ¥100 billion in operating income by the year 2025.

### Long-Term Vision/Medium-Term Management Plan

#### Vision for 2025

- (1) Build a portfolio of multiple business models, rather than rely on domestic malls as a single source of profit generation.
- (2) Become a leading global commercial developer with consolidated operating income of ¥100.0 billion.
- (3) Conduct floor space expansions and renovations in Japan to become the dominant mall in each area.
- (4) Target overseas operating income of ¥35.0 billion (operating margin 20%) across 70 malls, operating at the same level of efficiency and scale as our domestic operations.

**Numerical Targets**

- Operating Revenue: **¥500 billion**
- Operating Income: **¥100 billion**

• Operating Revenue

• Operating Income

#### Medium-Term Management Plan (FY2017 to FY2019)

**Numerical Targets**

- Operating Revenue: **¥326 billion**
- Operating Income: **¥62 billion**

**Priority Measures**

- (1) Capture Growth Opportunities in Asia
- (2) Develop Latent Sources of Domestic Demand
- (3) Become the Overwhelmingly Dominant Mall in Each Region
- (4) Capture Urban Growth Opportunities
- (5) Implement Optimal Financing Mix and Build Organizational Structures That Support Growth

#### • Operating Income Component Ratio

Operating Income Component Ratio	FY2016	FY2019 (Plan)	FY20205 (Plan)
Urban Shopping Centers	2.7%	0.8%	5.0%
Japanese Malls	105.8%	87.1%	60.0%
Overseas Business	-8.5%	12.1%	35.0%

#### • Performance Indicator

		FY2016	FY2019 (Plan)	FY20205 (Plan)
Efficiency	ROIC	4.4%	4.5%	6% or higher
Safety	Net Debt-Equity Ratio	1.0 times	1.2 times	Around 1.0 times

\* Management indicators do not include an additional 115.0 billion in lease obligations as a result of applying IFRS No.16.

# Vision

## Medium-Term Management Plan Growth Policies

### ● Growth Policies

(1) Capture Growth Opportunities in Asia	<ul style="list-style-type: none"> <li>I. Reap benefits of rising brand penetration (via area-dominant strategy)</li> <li>II. Develop and manage superior malls</li> <li>III. Implement measures to increase operating revenues</li> <li>IV. Promote local management</li> </ul>
(2) Develop Latent Sources of Domestic Demand	<ul style="list-style-type: none"> <li>I. Happiness Mall Project</li> <li>II. Promote localization</li> </ul>
(3) Become the Overwhelmingly Dominant Mall in Each Region	<ul style="list-style-type: none"> <li>I. Conduct floor expansions and implement effective revitalization measures</li> <li>II. Propose new discoveries</li> <li>III. Open new malls in untapped territory</li> <li>IV. Develop new formats</li> <li>V. Improve employee satisfaction for tenants</li> </ul>
(4) Capture Urban Growth Opportunities	<ul style="list-style-type: none"> <li>I. Establish branding for new OPA               <ul style="list-style-type: none"> <li>•Renovate existing stores and engage in strategic S&amp;B/refining</li> <li>•Develop new format in urban locations</li> <li>•Open new stores in urban area</li> </ul> </li> </ul>
(5) Implement Optimal Financing Mix and Build Organizational Structures That Support Growth	<ul style="list-style-type: none"> <li>I. Secure financing to support growth business models</li> <li>II. Promote management diversity</li> <li>III. Engage in ESG initiatives</li> </ul>

### ● Business Environment and AEON MALL Initiatives

	Business Environment	AEON MALL Initiatives (Business Opportunities)
Chinese Business	<ul style="list-style-type: none"> <li>•Slowdown in economic growth rate</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>New tenants in areas with promising mall business growth; sustained growth by leveraging activation expertise developed in Japan to raise value of existing malls</b></li> </ul>
ASEAN Business	<ul style="list-style-type: none"> <li>•Response to rapidly developing markets</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>Capture overwhelming market share through leading-edge malls designed for market needs of the future</b></li> </ul>
Overseas Business	<ul style="list-style-type: none"> <li>•Changes in competitive environment overseas</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>Leverage mall management and operations expertise acquired in Japan to develop competitive malls</b></li> </ul>
Japanese Malls	<ul style="list-style-type: none"> <li>•Growth of e-commerce (brick-and-mortar vs online)</li> <li>•Changes in demographics due to population decline</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>Impact of e-commerce is limited in light of the range of functions and daily needs goods offered by brick-and-mortar</b></li> <li>▶ <b>Expand floor space to secure area dominance among competing brick-and-mortar businesses</b></li> </ul>
Urban Shopping Centers	<ul style="list-style-type: none"> <li>•Weakness in fashion-store building format due to apparel sales slump</li> </ul>	<ul style="list-style-type: none"> <li>▶ <b>Conduct complete renovations existing stores to improve earnings capacity</b></li> </ul>

\* For more about our medium-term management plan for FY2017 through FY2019, see [https://www.aeonmall.com/en/ir/pdf/manegemant\\_plan.pdf](https://www.aeonmall.com/en/ir/pdf/manegemant_plan.pdf).

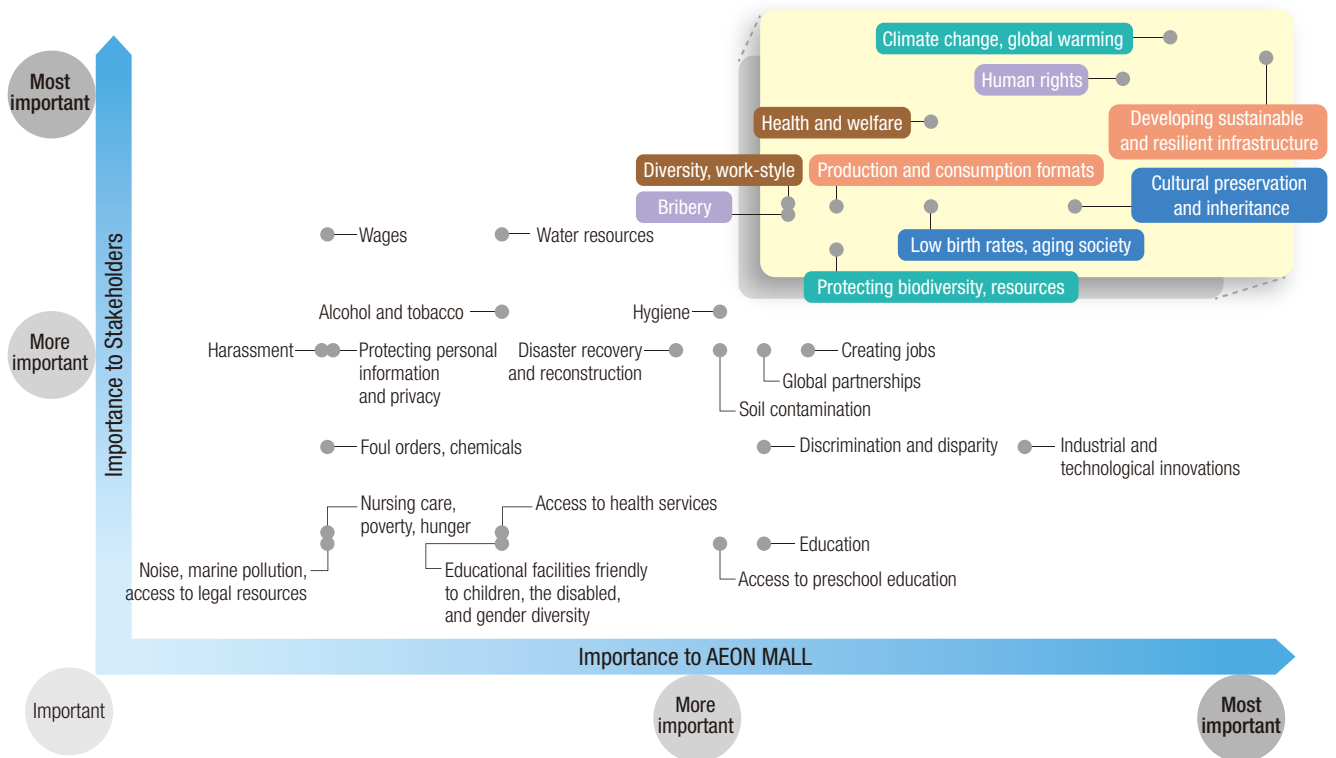
# Corporate Strategy to Achieve Our Long-Term Vision

## Materiality

AEON MALL uses materiality analysis to identify factors that have a significant influence on value creation over the medium and long term.

We intend to design strategies and policies to address these factors and set key performance indicators to measure execution in the future.

### Materiality Matrix



### The Materiality Analysis Process

#### Step 1 Identify Topics

We identified relevant social issues by referencing sources including DJSI, FTSE, GRI, generally accepted industry issues, etc. The AEON MALL Group defined 34 topics related to our business in Japan and overseas, reflecting SDGs and issues specific to Japanese society.

\*1 Sustainability stock index selected by S&P Down Jones Indices (U.S.) and RobecoSAM (Switzerland)



















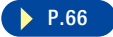
\*2 Based in London, the FTSE calculates and manages stock indices.

#### Step 2 Importance to Stakeholders

We used the SASB\* and other guidelines, as well as categories used by ESG benchmarking organizations, to assess importance to stakeholders.

\* U.S.-based Sustainability Accounting Standards Board

## Measures Addressing Materiality

Materiality	Related SDGs	Medium-Term Management Plan Growth Policies	Related Pages
<b>Developing Community and Social Infrastructure</b> <ul style="list-style-type: none"> <li>Developing sustainable and resilient infrastructure</li> <li>Production and consumption formats</li> </ul>	 	Safe, secure, and pleasant facilities Malls that reflect the unique character of a community Town planning for disaster prevention Expansion of public functions Encouraging acceptance and use of electric vehicles (EV) Encouraging the use of public transportation	
<b>Building Bridges to Local Communities</b> <ul style="list-style-type: none"> <li>Cultural preservation and inheritance</li> <li>Low birth rates, aging society</li> </ul>	 	Happiness Mall initiatives Hyper-Localization to boost local appeal AEON Yume-Mirai Nursery School	
<b>The Environment</b> <ul style="list-style-type: none"> <li>Climate change, global warming</li> <li>Protecting biodiversity, resources</li> </ul>	    	Responding to climate change and global warming AEON Hometown Forest Project (biodiversity) Recycling waste products	
<b>Diversity and Work-Style Reform</b> <ul style="list-style-type: none"> <li>Health and welfare</li> <li>Diversity, work-style</li> </ul>	  	Globalization of Human Resources Nadeshiko Brand Improving Employee Satisfaction for Tenant Employees	
<b>Accountability in Business</b> <ul style="list-style-type: none"> <li>Human rights</li> <li>Bribery</li> </ul>	 	Human Rights Policies, Systems, and Training Initiatives to Prevent Corruption	

### Step 3 Importance to AEON MALL

We used our management philosophy and medium-term management plan to ascertain the importance of these topics to AEON MALL.

### Step 4 Confirm Relevance

Finally, we confirmed the relevance (materiality analysis process and results) of these topics from the standpoint of our outside independent directors and in consideration of the unique AEON MALL business model. We revised group-wide materiality based on these opinions, and then confirmed the topics in a meeting of the CSR Council.

\* AEON MALL engages in business localized to the communities we serve, and we believe solving community social issues is part of our mission as a business. The AEON MALL CSR Council, chaired by the president of our company, meets monthly to ensure we make progress toward our ideal of Creating Shared Value (CSV), conducting business integrated with the principles of CSR. The council discusses details and progress related to four materialities, represented by *E* (environment), *S* (social), *G* (governance), and *C* (communication).

# Our Profit Model

To achieve the AEON MALL medium- to long-term business plan, we plan to grow our earnings capacity and increase corporate value, while improving investment efficiency and maximizing cash flow. We work to build a sound and strong financial foundation to support our growth strategy.

## Mall Operations Profit Structure

Most of AEON MALL's operating revenue is derived from the rental income paid by our mall tenants. Real estate rental income consists of a fixed rental income and a commission rental income, which fluctuates according to the retail sales of tenant specialty stores. With commission rental income, AEON MALL operating income also increases as the retail sales of tenant specialty stores increases.

In many cases, minimum guaranteed retail sales are set on a monthly or yearly basis for commission rent. This way, minimum rent is guaranteed, even if the tenant is temporarily unable to exceed a certain level of retail sales.

Operating costs, which are the expenses directly related to mall management and operations, include personnel expenses for full-time mall employees, facilities maintenance

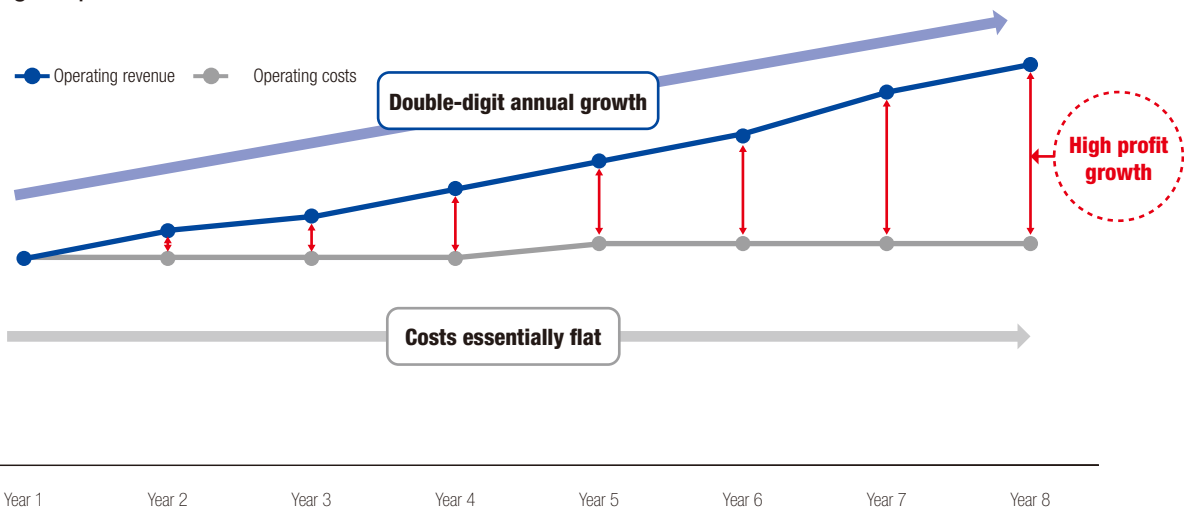
expenses and utilities for mall facilities, rent paid to the owners of the mall land and buildings, and depreciation and amortization expenses for facilities. The expenses that make up the highest proportion relative to operating income are rent and depreciation and amortization expenses.

In China, on the other hand, government-affiliated developers handle the development of roads and towns as a whole. AEON MALL serves as a master lessee recruiting tenants for our commercial facilities. While we receive rental income from tenants, the burden of operating costs is significant. Typically, malls take several years to become profitable. However, since the greatest portion of operating costs consists of real estate costs, expenses do not increase significantly. Operating revenue will grow for several years stemming from commission rental income and revisions in rent fees tied to increases in sales.

### Japanese operating revenue and expense structure



### Overseas gross profits



Looking at future economic growth, we are constructing spacious facilities with large parking lots on par with those in Japan. At present, real estate costs are high, leading to low profit levels. However, these facilities enjoy high growth rates and growing operating revenues. Costs consist largely of real estate costs that remain flat over time, resulting in high profit growth.

## Financial Strategy for Stronger Profit Structure

In recent years, construction costs have remained high in Japan, making it difficult to improve the efficiency of new stores. Given these circumstances, AEON MALL reduced the number of new mall openings to one in FY2019. If construction costs continue to remain high, we will limit new location openings to around two or three per year.

Meanwhile, we have studied properties that lend themselves to expansion of floor space. We are conducting floor space expansions at a rate of three or four malls per year. AEON MALL facilities feature flat parking lots, zoned at the time of construction to accommodate future mall expansion. In Japan, a process of elimination for malls has begun. Mall-opening strategies for specialty store operators is shifting from growth via numbers to a priority on efficiency. AEON MALL has a track record of creating malls that are the overwhelmingly dominant malls in their regions. Specialty store operators know that AEON MALL facilities attract customers and that we can increase retail floor area and remodel malls, while also generating sales growth through synergistic effects derived from attracting other tenants.

Overseas, our plans call for 70 malls by 2025. We will focus on area-dominant store openings in four areas: Beijing/Tianjin/Shandong; Jiangsu/Zhejiang; Hubei; and Guangdong. In ASEAN, we will focus on Vietnam, Indonesia, and

Cambodia. We recorded net operating income in our Overseas business for the first time in FY2018. We are now at a stage where increasing profits here will be the driver of growth for the company. At the same time, the weight of our overseas assets will continue to increase. In China, our basic approach will be to lease assets. In ASEAN, as well, we will create leasing schemes similar to those we use in China.

In support of this strategy, the AEON MALL three-year plan for FY2017-2019 calls for ¥575 billion in capital investment. A total ¥445 billion of this spending will be in Japan (¥275 billion for new malls, ¥150 billion for existing malls, ¥20 billion for OPA). We will invest ¥130 billion overseas (¥30 billion in China and ¥100 billion in ASEAN).

We intend to procure ¥270 billion of these funds from our operating cash flow, with another ¥15 billion from funds on hand for a total of ¥285 billion. The remainder will be covered with debt and REITs. The company will maintain a net debt-equity ratio of approximately one times.

For AEON MALL, a one times net debt-equity ratio is an important indicator of our discipline. Although we recorded a negative free cash flow this year, our overseas operations will begin generating a cash flow in FY2019. Accordingly, we anticipate free cash flow will turn positive during the course of our next medium-term management plan (FY2020 to FY2022).

## Use of WACC at AEON MALL

We consider internal rate of return to be the equivalent of net present value. Accordingly, we deem any investment in which internal rate of return exceeds the cost of capital to be a proper investment. When investing overseas, we use the weighted average cost of capital (WACC) and an overseas risk premium to make investment decisions, balanced by country

risk considerations.

We calculate WACC according to the weighted average of borrowing cost and cost of shareholders' equity. Shareholders' equity cost is the anticipated yield required by investors when issuing shares. We use the Capital Asset Pricing Model to calculate the investor's anticipated yield for the market price as of the closing date of our fiscal year.

# Building on Our Strengths

Several AEON MALL Group directors shared their views on the strengths of their divisions and the supporting AEON Group strategies.

## Maximizing Potential as a Developer

### Kaoru Iwamoto

Vice President, Development Officer



One of our greatest strengths as a retail business that integrates general financing and services is our ability to develop properties leveraging the AEON Group brand, infrastructure, and assets. Further, we can adopt the best practices from China and ASEAN into our Japanese businesses, while at the same time extending our expertise in Japan to those regions. This integration of overseas and Japanese expertise is a major advantage. In 2018, we combined our overseas planning functions into the Development Division, generating greater synergies through closer coordination between Japan and overseas. Another competitive strength is our ability to create new businesses completely in-house, as we tend to avoid outsourcing.

The mission of the Development Division is location selection. Our area strategy calls for tailoring our content to specific communities. To achieve this strategy, we will train our staff with greater skills to produce new ideas from the planning

stages to completion. To improve training requires a more stable system that uses manuals and other standard practices. Human resources strategy will be a key for brick-and-mortar businesses to win in this digital era. We also intend to improve our decision-making practices to reflect the type of speed required by landowners, governments, and others in the community. And, in terms of the environment and society, we will continue to obtain environmental certifications and create spaces that foster community-building in response to lower birthrates and aging demographics.

Our key policies over the medium and long term consist of leveraging the urban assets of the AEON Group. We see multi-use commercial complexes as a key growth area. Here, office workers will become repeat, steady customers for shopping, dining, and entertainment in the same facilities. We intend to recruit talent from outside the company as one means to achieve this goal.

## Attracting Customers Through Economies of Scale From 153 Malls Across Japan

### Akio Mishima

Managing Director, General Manager of Sales Division



Our mission is to maximize revenues and profits through more customer traffic. And, our greatest advantage here is the 153 malls we own and operate throughout Japan. This is a strength unique among developers in our space. Another advantage is how AEON MALL strives to localize our malls to the needs and preferences of the local community. This creates an advantage in our ability to combine goods and services organically in a fun space via a BtoBtoC business model. Specific instances of this localization include our Happiness Mall initiatives, carefully planned special customer events, points programs, and more. The Sales Division consists of more than 1,500 employees. We divide this large organization into smaller areas overseen by a division general manager. I believe this size and structure offer another advantage to AEON MALL over the competition.

In the future, we intend to raise our presence as part of the community infrastructure, using AEON MALL spaces for

disaster-relief, early voting, and other public benefits. In times of disaster, AEON MALL can be a location to safely evacuate, offering confidence and safety. We can offer nursery school and other support to facilitate work-style improvement among employees of our tenants.

We can foster deeper ties to our communities by proving ourselves an indispensable part of the local infrastructure, integrating brick-and-mortar with e-commerce and other digital technologies to create a hybrid virtual-real space. AEON MALL plans to offer even faster support to our tenants, rolling out QR code-based cashless payment systems and planning sales promotion activities that correspond to major developments such as consumption tax increases.



## Cultural Integration and an Overwhelming Sense of Scale

### Mitsuhiro Fujiki

Managing Director, General Manager of Leasing Division



One important mission of the Leasing Division is to find outstanding tenants. We strive to find new business partners and create stronger communities with our tenants as part of our responsibility for the real estate operations of a shopping mall development company. At the same time, another important part of our job is to go out and gain a sense for what is happening “now” in society. Leasing Division staff must go out and talk with people, observe behavior, and get a personal sense of the community. Staff in charge of restaurants must go out and eat. Staff in charge of fashion must read voraciously, go window shopping, and research the latest trends. We have to be sensitive to the newest developments and information out in the world. And, perhaps most of all, we must challenge ourselves always to try something new. This is the type of organization to which the Leasing Division aspires.

Our relationship with the nearly 8,000 tenants of the AEON Group is our strength. This major asset represents an

overwhelming scale only dreamed of by our competitors. Our advantage is the sheer number of malls located in areas from Hokkaido in the north to Okinawa in the south. AEON MALL is home to people with a wide variety of backgrounds. This diversity and variety helps us expand our perceptions.

Presently, our target is the second-generation baby boomers and their families, a wider cross-section of the population pyramid. Today, the most fashion-conscious age group is the group in their 50s, just entering our target zone. We hope to exploit this trend for further growth. At the same time, we plan to strengthen our strategy to raise added value and create a smoother cycle between the consumption of goods and the consumption of services. Here, we aim to capture a larger volume area of the market for seniors.

## Using Digital Technology for Outstanding Brick-and-Mortar Experiences

### Akiko Nakarai

Director, General Manager of Digital Promotion Management Department



We promote digital advancements along three vectors: (1) Developing an omnichannel approach to commerce; (2) Raising customer satisfaction through stress-free environments; and (3) Improving labor productivity. As Japan’s online business begins to reach a saturation point, we are working with platform providers to combine digital technologies with real-world AEON MALL assets. Meanwhile, we are making progress in our online business overseas in various ASEAN countries. One strength of digital promotion at AEON MALL is our access to 1.2 billion records of consumer transaction data in Japan, which we can use to create future business opportunities. Another strength is our access to partnerships, leveraging assets and relationships throughout the AEON Group.

Malls of the future must offer systems and digital-based conveniences, including maps, cashless transactions, highly

visible electronic signage, and stress-free cash register transactions. We are already conducting proof-of-concept tests for QR code-based cashless transactions, other digital infrastructure, and personal mobility.

Other important future topics include creating a digital network across the AEON Group for easy access by and convenience to customers. We plan to utilize our storehouse of data to identify the most appropriate services in this respect. As of the end of 2018, nearly every AEON MALL has been outfitted with Wi-Fi equipment, allowing online access throughout Japan. Looking ahead to 2020, we intend to welcome the opportunities offered by inbound tourist traffic to provide stress-free online environments for customers from overseas, adding to the excitement and enjoyment of their experience in ways unique to AEON MALL.